THE TIMKEN COMPANY

# 2014 ANNUAL REPORT

# FINANCIAL SUMMARY

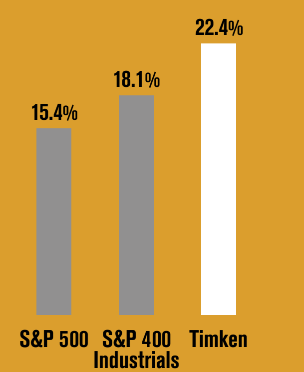
**CONTINUING OPERATIONS**

(Dollars in Millions)

| OPERATING DATA | 2014 | 2013 |
|---|---|---|
| Net Sales | $ 3,076.2 | $ 3,035.4 |
| Gross Profit | 898.0 | 868.4 |
| Adjusted EBIT* | 375.6 | 329.2 |
| Adjusted EBIT Margin* | 12.2% | 10.8% |
| Net Cash Provided by Operating Activities | 281.5 | 292.8 |
| Capital Expenditures | 126.8 | 133.6 |
| Free Cash Flow* | 154.7 | 159.2 |
| **SHAREHOLDER RETURNS** | | |
| Adjusted EPS* | 2.55 | 2.06 |
| Dividends | 1.00 | 0.92 |
| **KEY RATIOS** | | |
| Net Debt to Capital* | 12.9% | 1.7% |
| Adjusted Return on Invested Capital* | 11.5% | 9.7% |

**TOTAL SHAREHOLDER RETURNS****

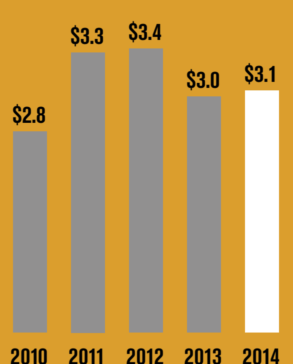
5-Year Annualized, Ending Dec. 31, 2014



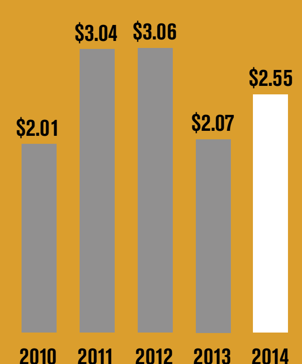

**DIVIDENDS PER SHARE**


**REVENUE**

Dollars in Billions




**ADJUSTED EARNINGS PER SHARE***




*See Appendix on last page for reconciliations to the most comparable GAAP equivalents.

***Total Shareholder Return* for the Company was calculated on an annualized basis, assumes quarterly reinvestment of dividends and takes into account the value of TimkenSteel common shares distributed in the Spinoff on June 30, 2014.

## TO OUR VALUED SHAREHOLDERS:

The Timken Company of 2014 stands as a different company than it was just a year ago. We have concluded a period of strategic realignment, the core of which was the multi-year reshaping of our portfolio and the spinoff of our steel business. We have emerged a stronger, more focused Timken, performing at higher levels for customers and shareholders alike.

We are focused on the fundamentals. That means a decisive management team, operational excellence, global growth and solid margins. We are committed to our customers and to identifying and solving their most complex friction management and power transmission needs.

For the year, Timken revenues were $3.1 billion, up modestly from 2013. We fell short in achieving our aspirations for top-line growth, yet the company's profitability and overall performance improved significantly over 2013. Operating margins were 12.2 percent, with adjusted EBIT of $376 million. We increased adjusted earnings per share by 23 percent over 2013 by improving our mix and reducing our cost structure. We returned $360 million of capital to our shareholders through dividends and share repurchases. Our 92 years of uninterrupted quarterly dividend payouts remains one of the longest on the New York Stock Exchange. Our cash flow and balance sheet are strong. Our global pensions are essentially fully funded and we continue to take actions designed to reduce risk in this area. Company shares closed up for the year at $42.68, representing share price growth of 8.3 percent and a market capitalization increase of $110 million compared to 2013.

# A FUNDAMENTAL FOCUS



## Stronger and leaner than before, we have more to achieve together.

In 2014, our Process Industries business grew sales 10 percent over 2013 and has now achieved a compound growth rate of 12 percent since the 2009 recession. The business delivered an EBIT margin of nearly 20 percent and is well-positioned to continue its growth trajectory at this level of performance. This year we also concluded the final stages of our Mobile Industries portfolio changes. As a result of this seven-year process, Mobile Industries is generating excellent returns and is now positioned to begin to grow. To spur better performance within Aerospace, we integrated it within our Mobile Industries business. While still early, we have already begun to see improvements from this segment reorganization.

Midyear, we spun off our steel business as an independent company. Doing so allowed us to fully focus on our global bearings and power transmission business. We completed this work on time and within our planned budget, all without interruption to our core business or customers.

During the year, we transitioned leadership and quickly developed a cohesive, action-oriented and aligned management team who shares a clear vision of our priorities: excellence, growth and knowledge-based product leadership. The team launched several new growth initiatives, improved operating margins and delivered solid returns to shareholders.

We also pursued a number of strategic acquisitions, introduced new products, expanded existing product lines and won new business. We launched DeltaX, a multi-year initiative to accelerate growth that includes redesigning our product management, engineering and business systems resources. This drives product development to commercialization more efficiently, so we can better meet customer needs.

We invested in talent to expand our geographic reach in 2014, adding key resources to our sales and marketing teams. To serve our customers in a more coordinated and efficient way, we also opened our new World Headquarters in North Canton, Ohio. This facility brings our product and business management teams together with engineering, research and product development, allowing us to engage collaboratively and more easily share complex product knowledge.

Many have contributed to our success this year and we thank you – our shareholders, directors, customers, communities and especially Timken associates – for your support. Stronger and leaner than before, we have more to achieve together.

Sincerely,

Richard G. Kyle
President & Chief Executive Officer
March 2, 2015

# FOCUSED LEADERSHIP



## Strong + Ready

An exceptionally strong executive leadership team sharpens Timken know-how with deep experience across specialties – from manufacturing to finance to technology. Each member of this team brings a seasoned understanding of our proven engineering approach, the customers we serve and where we must win. They are focused on a singular destination: reliable global growth across our diversified markets, driven by operational excellence.

## Aligned + Driven

With company strategy clearly articulated, the Timken leadership team manages for disciplined execution across businesses, operations, markets and geographies. This year the team invested in sales initiatives to advance organic growth meaningfully in the future and positioned Timken to continue 2014's progress in sectors such as wind energy and in emerging markets such as China. Combined, their efforts provide the fuel for Timken to deliver future growth and value. Whether at the edges of space or at the borders of an emerging economy, the Timken leadership team is focused on engineering what comes next.

## Clear + Decisive

Markets emerge larger than ever. Needs develop faster than ever. Customers demand solutions sooner than ever. Winning in this environment requires moving at the speed of opportunity. This is where the Timken team thrives – in the midst of complexity. Throughout 2014, Timken leadership set clear priorities, took more decisive actions and moved with greater velocity. We did this because our customers value it, our shareholders expect it and our mission demands it.

## Winning in this environment requires moving at the speed of opportunity.

With CEO Richard Kyle, company officers Philip Fracassa, executive vice president and CFO; Christopher Coughlin, executive vice president and group president; and William Burkhart, executive vice president, general counsel and secretary, work together to turn the promise of Timken into the performance shareholders expect.

JOHN M. TIMKEN, JR.
Chairman, Board of Directors,
The Timken Company

The Timken Company of the future came sharply into focus in 2014. We see exciting times ahead, filled with opportunities to prove and realize our full value. We have reached this important time because of the remarkable leadership and vision of those who preceded us. Both Jim Griffith, who retired as president and CEO midyear, and former Chairman Ward J. "Tim" Timken, Jr., as much as anyone in Timken history, set a course for what this company can truly be and the value we can create.

We recognize and thank former Directors Phillip Cox and Diane Creel, who assumed seats on the new steel company board. And we welcome our newest Directors Maria Crowe, Christopher Mapes and Ajita Rajendra, who bring an enormous wealth of experience and fresh perspective to our boardroom.

Our Board of Directors is energized by the work that lies ahead. The world through which we now navigate is more complex and connected than ever, making it more unpredictable. The Timken Company, though, is steady, strong and sure. What we know today will change what we make tomorrow, ensuring we remain a vital part of industry around the world. We will continue to be guided by our founding vision and philosophy, removing friction and smoothing the progress of business.

John M. Timken, Jr.
Chairman

## BOARD OF DIRECTORS

JOHN A. LUKE, JR.
Chairman and Chief Executive Officer,
MeadWestvaco Corporation

JACQUELINE F. WOODS
Retired President, AT&T Ohio

WARD J. TIMKEN, JR.
Chairman, Chief Executive Officer & President,
TimkenSteel Corporation

FRANK C. SULLIVAN
Chairman and Chief Executive Officer,
RPM International Inc.

JOSEPH W. RALSTON
Retired General, USAF;
Vice Chairman, The Cohen Group

JOHN M. TIMKEN, JR.
Chairman, Board of Directors,
The Timken Company

RICHARD G. KYLE
President and Chief Executive Officer,
The Timken Company

AJITA G. RAJENDRA
Chairman, President and Chief Executive Officer,
A. O. Smith Corporation

JOHN P. REILLY
Retired Chairman, President and Chief Executive
Officer, Figgie International

CHRISTOPHER L. MAPES
Chairman, President and Chief Executive Officer,
Lincoln Electric Holdings, Inc.

MARIA A. CROWE
President of Manufacturing Operations,
Eli Lilly and Company

Vikram Bedekar, the first industrial engineer to win the prestigious F.W. Taylor Medal for his research in materials science, performs an atomic-level microstructure analysis, which helps enhance bearing life.

# THE WORLD IN FOCUS

ANSWERING THE RIGHT CHALLENGES

by

CREATING THE RIGHT PRODUCTS

and

OPENING THE RIGHT MARKETS

through

LEVERAGING THE RIGHT CHANNELS

thus

DELIVERING VALUE AND GROWTH WORLDWIDE.

# EXCELLENCE WORLDWIDE



## A PRODUCT STRATEGY THAT BEGINS WITH CUSTOMERS

At Timken, success means capturing strategic opportunities by understanding our customers' needs, applying our know-how and delivering value. Our growth plan is to expand our served market space by accelerating our product development rate to offer a full line of premium industrial bearings. This plan also includes strategic bolt-on acquisitions with a focus on bearings, industrial services and power transmission components.

Our proven legacy in highly engineered bearings and related products – across their entire life cycle – is the bedrock of fulfilling our strategy. We are the leading authority on tapered roller bearings, leveraging our expertise in tribology, metallurgy and power transmission to diversify our portfolio to meet our customers' needs. Today, Timken engineers, manufactures and markets bearings, transmissions, gearboxes, chain and related products, and offers a spectrum of rebuild and repair services around the world.

### Growing Our Portfolio Beyond Tapered Roller Bearings

Timken is the leading authority on tapered roller bearings. Today we are leveraging our No. 1 global market position in tapered roller bearings and our engineering know-how and technology to expand our bearing and power transmission offering. For example, through a combination of organic and inorganic growth initiatives, we have expanded our bearing housed units line. Timken now markets among the broadest range of bearing housed units in the industry, and in 2014 complemented that line with the acquisition of Revolvo Ltd.

## Extending Our Services

Timken Power Systems (TPS) grew out of the marriage of the legacy Timken bearings services business and the company's acquisition of Philadelphia Gear in 2011. Since then, the gears and services business has achieved significant growth through a combination of geographic expansion and strategic acquisitions, including the purchase of the Schulz Group in 2014.

Today, TPS can service everything within our target industrial customer's mission-critical drive train, including switch gears, electric motors and generators, gearboxes, bearings, couplings and control panels. TPS provides end users and select OEMs with comprehensive repair solutions, parts, new drives and engineering expertise through a growing network of regional service and manufacturing centers. Using state-of-the-art machining technologies, ISO-certified business processes and advanced diagnostics to deliver engineered solutions, TPS aspires to continue outgrowing end markets. We believe we are well-positioned to achieve this growth, given our extensive product brand portfolio representing a broad range of equipment expertise.

## Building a Formidable Global Footprint

We are forging ahead in emerging markets, extending our value proposition and injecting talent in new geographies to win globally. Customers value our reliable and efficient products and services because they deliver real-world solutions for complex needs. This approach is reaping benefits, evidenced by a 12 percent year-over-year increase in emerging market revenues.

### 2014 Revenue: $3.1 Billion

| | |
|---|---|
| North America | 57% |
| Europe, Middle East and Africa | 18% |
| Asia-Pacific | 17% |
| Latin America | 8% |

## Record Year for Wind

2014 was a record year for our wind energy business as we doubled revenues over the previous year. We achieved these results by translating the investments we have made in research and manufacturing into new sales.

We have a solid strategy of developing and delivering new products in accelerated time frames. We also took our wear-resistant bearing technologies into the aftermarket, offering a technical solution to operators plagued with problems in the field. Finally, we attained a leadership position with the key OEM design centers.

Our efforts, combined with a strong wind market in Asia, propelled the business to new heights.

# A GLOBAL STRATEGY TO DRIVE GROWTH

## Timken is strategically and operationally aligned to capitalize on global macro trends, including urbanization and infrastructure development.

Serving our customers locally makes global operations critically important to attaining our growth aspirations. Through the course of the year, we deployed additional talent and expanded our sales and marketing infrastructure in fast-growing areas of the Middle East, Northern Africa, Southeast Asia and Latin America. We also bolstered our presence in Germany, a critical design center for heavy industries and vehicles. Our growing reach ensures efficient, knowledge-based service and increased value for customers. Over the past five years, we have achieved a 52 percent increase in emerging markets sales.

Going forward, we are targeting growth in international sales with a focus on emerging markets. The company is strategically and operationally aligned to capitalize on global macro trends that include urbanization, infrastructure development and sustainability. We stand ready to capture significant upside from the resulting global demand in power generation, agriculture, construction and mining – core resources that fuel developing economies.

### ASIA

Regional growth drivers in Asia are significant and infrastructure development – including growth in rail, steel and mining – presents real opportunity for Timken. Our investments over the last few years in the region, which bring us to 4,600 associates and eight manufacturing plants and service centers, give us greater traction in those key markets. For example, in 2014, driven by wind energy demand and aftermarket growth, increased market penetration and new customer acquisition, we grew our China sales more than 20 percent.

# A BUSINESS STRATEGY FOR TODAY AND TOMORROW

### LEED GOLD CERTIFICATION

Our new World Headquarters received LEED Gold certification from the U.S. Green Building Council for our adherence to green design and practices.

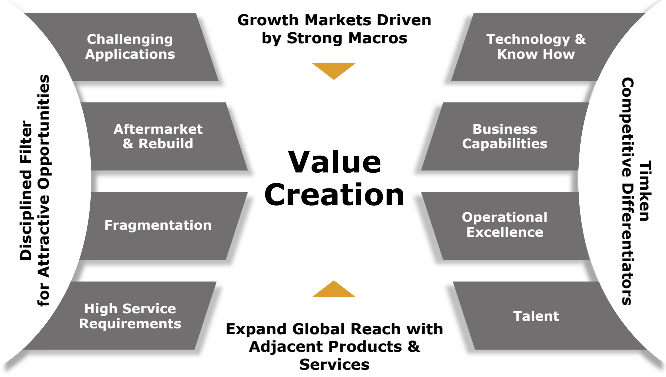
Along with natural lighting, outdoor gardens, and special parking for energy-efficient vehicles and car poolers, the 240,000-square-foot building incorporates high-efficiency heating and cooling components that save up to 32 percent on energy usage. At Timken, we are committed to our core values, whether by serving our customers with integrity, taking an active role in our local communities or furthering environmental sustainability.

Timken performs with excellence, every day and in every way. It is who we are and how we work. We challenge ourselves and our thinking, reimagining the future and executing our strategy in new ways. We see the most attractive opportunities surrounding challenging performance criteria, significant aftermarket sales and service prospects, market fragmentation at the OEM and end-user level, and high customer service requirements. To these complexities, we bring our technology, our operational excellence, our business capabilities and above all, our talent. These assets stand as formidable competitive differentiators that drive value for Timken customers and shareholders.

Our business model, coupled with our strategy, serves as our filter for business development and investment. It also drives the Timken team in advancing the key attributes of Timken success: integrity and hard work. Our team understands that refining processes and approaches creates new value, that speed of decision-making is of paramount importance, and that we must be disciplined in prioritizing our efforts to fuel growth.

## The world changes and we change with it.

### The Timken Business Model




The Timken team's leadership, dedication and professionalism make the difference. We extend our brands in new ways to new places and for new benefits. We win new business. We remain a respected industry voice. We partner in our local communities and protect the environment. And we continue to invest in people, recruiting and developing engineers, operators and other disciplined professionals who know how to make the world work better.

The world changes and we change with it. We remain committed to our stakeholders – and to use our know-how for their benefit.

### Manufacturing Excellence

Our passion to deliver is supported by a disciplined focus on continuous improvement and lean manufacturing. For example, in 2014, we removed $60 million in costs through initiatives focused on our manufacturing and supply chain efforts. While we did this, we upheld our industry-leading on-time delivery and stock-in rates. These initiatives require extensive collaboration across the enterprise. A leaner Timken offers more value for customers and shareholders, and our efforts to be more efficient will continue to drive improvements to the bottom line.


# BUILDING A STRONGER TIMKEN, TOGETHER.

## Executive Leadership Team

**RICHARD G. KYLE**
President and Chief Executive Officer

**WILLIAM R. BURKHART**
Executive Vice President, General Counsel and Secretary

**CHRISTOPHER A. COUGHLIN**
Executive Vice President and Group President

**PHILIP D. FRACASSA**
Executive Vice President and Chief Financial Officer

**RICHARD M. BOYER**
Vice President, Operations

**MICHAEL J. CONNORS**
Vice President, Aftermarket

**AJAY K. DAS**
Vice President, Quality

**KARI L. GROH**
Vice President, Communications and Public Relations

**HANS LANDIN**
Vice President, Power Transmission

**J. RON MENNING**
Senior Vice President, Strategy and Development

**J. TED MIHAILA**
Senior Vice President and Corporate Controller

**AMANDA J. MONTGOMERY**
Vice President, Industrial Bearings

**RONALD J. MYERS**
Vice President, Human Resources

**DOUGLAS C. NELSON**
Vice President, Compensation and Benefits

**ERIK A. PAULHARDT**
Vice President, Marketing

**CARL D. RAPP**
Vice President, Power Systems

**SANDRA L. RAPP**
Vice President, Information Technology

**ANDREAS ROELLGEN**
Vice President, Process Industries and Managing Director, Europe

**BRIAN J. RUEL**
Vice President, Mobile Industries

**DOUGLAS H. SMITH**
Vice President, Tapered Roller Bearings

**PETER M. SPROSON**
President, China

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

# FORM 10-K

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

For the fiscal year ended December 31, 2014

OR

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

For the transition period from _____________ to _____________

Commission file number: 1-1169

TIMKEN

**THE TIMKEN COMPANY**
(Exact name of registrant as specified in its charter)

| | |
|---|---|
| **Ohio**<br>(State or other jurisdiction of incorporation or organization) | **34-0577130**<br>(I.R.S. Employer Identification No.) |
| **4500 Mt. Pleasant St., N.W., North Canton, Ohio**<br>(Address of principal executive offices) | **44720-5450**<br>(Zip Code) |

**234.262.3000**
(Registrant's telephone number, including area code)

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

| Title of each class | Name of each exchange on which registered |
|---|---|
| Common Stock, without par value | New York Stock Exchange |

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

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act.
Yes ☒ No ☐

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

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

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

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

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

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).
Yes ☐ No ☒

As of June 30, 2014, the aggregate market value of the registrant's common shares held by non-affiliates of the registrant was $5,811,740,662 based on the closing sale price as reported on the New York Stock Exchange.

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date.

| Class | Outstanding at January 31, 2015 |
|---|---|
| Common Shares, without par value | 88,214,403 shares |

DOCUMENTS INCORPORATED BY REFERENCE

| Document | Parts Into Which Incorporated |
|---|---|
| Proxy Statement for the Annual Meeting of Shareholders to be held on or about May 7, 2015 (Proxy Statement) | Part III |

# THE TIMKEN COMPANY

## INDEX TO FORM 10-K REPORT

# PART I.

## ITEM 1. BUSINESS

**GENERAL:**

As used herein, the term "Timken" or the "Company" refers to The Timken Company and its subsidiaries unless the context otherwise requires. Timken engineers, manufactures and markets bearings, transmissions, gearboxes, chain and related products and offers a spectrum of power system rebuild and repair services around the world. The Company's growing product and services portfolio features many strong industrial brands, such as Timken, Fafnir, Philadelphia Gear, Drives and Interlube.

The Company was founded in 1899 by Henry Timken, who received two patents on the design of a tapered roller bearing. Timken later became, and continues to be, the world's largest manufacturer of tapered roller bearings, leveraging its expertise to develop a full portfolio of industry-leading products and services. Timken built its reputation as a global leader by applying its knowledge of metallurgy, friction management and mechanical power transmission to increase the reliability and efficiency of its customers' equipment across a diverse range of industries. Today, the Company's global footprint consists of 61 manufacturing facilities/service centers, 12 technology and engineering centers and 23 distribution centers and warehouses, supported by a team comprised of approximately 16,000 employees. Timken operates in 28 countries and territories around the globe.

For nearly 100 years, the Company also made and marketed steel within its steel business. However, on June 30, 2014, the Company announced that it had completed the tax-free spinoff of its steel business (the Spinoff) into a separate independent publicly traded company, TimkenSteel Corporation (TimkenSteel). The Company's Board of Directors declared a distribution of all outstanding common shares of TimkenSteel through a dividend. At the close of business on June 30, 2014, the Company's shareholders received one common share of TimkenSteel for every two common shares of the Company they held as of the close of business on June 23, 2014. The steel business has been reclassified to discontinued operations for all periods presented.

**INDUSTRY SEGMENTS AND GEOGRAPHICAL FINANCIAL INFORMATION:**

Information required by this Item is incorporated herein by reference to *Note 15 – Segment Information* in the Notes to the Consolidated Financial Statements.

**MAJOR CUSTOMERS:**

The Company sells products and services to a diverse customer base globally, including customers in the following market sectors: industrial equipment, construction, agriculture, rail, aerospace and defense, automotive, heavy truck and energy. No single customer accounts for 5% or more of total net sales.

**PRODUCTS:**

Timken manufactures and manages global supply chains for multiple product lines including anti-friction bearings and mechanical power transmission products designed to operate in demanding environments. The Company leverages its technical knowledge, research expertise, and production and engineering capabilities across all of its products and end markets to deliver high-performance products and services to its customers. Differentiation in these product lines is achieved by either: (1) product type or (2) the targeted applications utilizing the product.

**Bearings:**

The Timken® bearing portfolio features a broad range of anti-friction bearing products, including tapered, spherical and cylindrical roller bearings; thrust and ball bearings; and housed units. Timken is a leading authority on tapered roller bearings, and leverages its position by applying engineering know-how and technology across its entire bearing portfolio.

Selection and development of bearings for customer applications and demand for high reliability require sophisticated engineering and analytical techniques. Deep knowledge of friction management combined with high precision tolerances, proprietary internal geometries and quality materials provide Timken bearings with high load-carrying capacity, excellent friction-reducing qualities and long service lives. The uses for bearings are diverse and can be found in transportation applications that include passenger cars and trucks, heavy trucks, helicopters, airplanes and trains. Ranging in size from precision bearings the size of a pencil eraser to those roughly three meters in diameter, Timken components are also used in a wide variety of industrial applications: paper and steel mills, mining, oil and gas extraction and production, machine tools, gear drives, health and positioning control, wind turbines and food processing.

***Tapered Roller Bearings.*** Timken tapered roller bearings can increase power density and can include customized geometries, engineered surfaces and specialized sealing solutions. The Company's tapered roller bearing line comes in thousands of combinations in single-, double- and four-row configurations. Tapered roller designs permit ready absorption of both radial and axial load combinations, which makes them particularly well-adapted to reducing friction where shafts, gears or wheels are used.

***Spherical and Cylindrical Roller Bearings.*** Timken also produces spherical and cylindrical roller bearings that are used in large gear drives, rolling mills and other industrial and infrastructure development applications. These products are sold worldwide to original equipment manufacturers and industrial distributors serving major end-market sectors, including construction and mining, natural resources, defense, pulp and paper production, rolling mills and general industrial goods.

***Ball Bearings.*** Timken radial, angular and precision ball bearings are used by customers in a variety of market sectors, including aerospace, agriculture, construction, health, machine tool and general industries. Radial ball bearings are designed to tolerate relatively high-speed operation under a range of load conditions. Bearings consist of an inner and outer ring with a cage containing a complement of precision balls. Angular contact ball bearings are designed for a combination of radial and axial loading. Precision ball bearings are manufactured to tight tolerances and come in miniature and instrument, thin section and ball screw support designs.

***Housed Units.*** Timken markets among the broadest range of bearing housed units in the industry. These products deliver durable, heavy-duty components designed to protect spherical, tapered and ball bearings in debris-filled, contaminated or high-moisture environments. Common housed unit applications include material handling and processing equipment.

**Mechanical Power Transmission:**

***Chains.*** Timken manufactures precision Drives® roller chain, pintle chain, agricultural conveyor chain, engineering class chain and oil field roller chain. These highly engineered products are used in a wide range of mobile and industrial machinery applications, including agriculture, oil and gas, aggregate and mining, primary metals, forest products and other heavy industries. These products are also utilized in the food and beverage and packaged goods sectors, which often require high-end, specialty products, including stainless-steel and corrosion-resistant roller chain.

***Lubrication Systems.*** The Company offers 27 formulations of grease, leveraging its knowledge of tribology and anti-friction bearings to enable smooth equipment operation. Interlube® automated lubrication delivery systems dispense precise amounts of Timken grease, saving users from having to manually apply lubrication. These multifaceted delivery systems are used by the commercial vehicle, construction, mining, and heavy and general industries.

***Aerospace Products.*** The Company's portfolio of parts, systems and services for the aerospace market sector includes products used in helicopters and fixed-wing aircraft for the military and commercial aviation industries. Timken designs, manufactures and tests a wide variety of power transmission and drive train components, including bearings, transmissions, turbine engine components, gears and rotor-head assemblies and housings. In addition to original equipment, Timken provides a wide range of aftermarket products, including replacement parts for gas turbine engines, transmissions and fuel controls, gearboxes and accessory systems in helicopters and fixed-wing aircraft. Other parts include airfoils (such as blades, vanes, rotors and diffusers), nozzles and other precision flight-critical components.

***Industrial Gearboxes.*** The Company's Philadelphia Gear® line of low- and high-speed gear drive designs are used in large-scale industrial applications. These gear drive configurations are custom-made to meet user specifications, offering a wide-array of size, footprint and gear arrangements. Low-speed drives are commonly used in crushing and pulverizing equipment, cooling towers, conveyors and pumps. High-speed drives are typically used by power generation, oil and gas, marine and pipeline industries.

***Other Products.*** The Company also offers a full line of seals, couplings, augers and other mechanical power transmission components. Timken industrial sealing solutions come in a variety of types and material options that are used in manufacturing, food processing, mining, power generation, chemical processing, primary metals, pulp and paper, and oil and gas industry applications. Timken couplings, another mechanical power transmission component, are commonly found in gear drives, motors and pump applications. The Company also designs and manufactures Drives helicoid and sectional augers for agricultural applications, like conveying, digging and combines.

**Services:**

***Power Systems.*** Timken services components in the industrial customer's drive train, including switch gears, electric motors and generators, gearboxes, bearings, couplings and central panels. The Company's Philadelphia Gear services for gear drive applications include onsite technical services; inspection, repair and upgrade capabilities; and manufacturing of parts to OEM specifications. In addition, the Company's Wazee, Smith Services, Schulz, Standard Machine and H&N brands provide customers with services that include motor and generator rewind and repair and uptower wind turbine maintenance and repair. Timken power systems commonly serves customers in the power, wind energy, hydro and fossil fuel, water management, paper, mining and general manufacturing sectors.

***Bearing Repair.*** Timken bearing repair services return worn bearings to like-new specifications, which increases bearing service life and can often restore bearings in less time than required to manufacture new. Bearing remanufacturing is available for any bearing type or brand - including competitor products - and is well-suited to heavy industrial applications such as paper, metals, mining, power generation and cement; railroad locomotives, passenger cars and freight cars; and aerospace engines and gearboxes.

Services accounted for approximately 7% of the Company's net sales for the year ended December 31, 2014.

### SALES AND DISTRIBUTION:

Timken products are sold principally by its own internal sales organizations. A portion of each segment's sales are made through authorized distributors.

Customer collaboration is central to the Company's sales strategy. Therefore, Timken goes where its customers need them, with sales engineers primarily working in close proximity to customers rather than at production sites. In some cases, Timken may co-locate with a customer at their facility to ensure optimized collaboration. The Company's sales force constantly updates the team's training and knowledge regarding all friction management products and market sector trends, and Timken employees assist customers during development and implementation phases and provide ongoing service and support.

The Company has a joint venture in North America focused on joint logistics and e-business services. This joint venture, CoLinx, LLC, includes five equity members: Timken, SKF Group, the Schaeffler Group, Rockwell Automation and Gates Corporation. The e-business service focuses on information and business services for authorized distributors in the Process Industries segment.

Timken has entered into individually negotiated contracts with some of its customers. These contracts may extend for one or more years and, if a price is fixed for any period extending beyond current shipments, customarily include a commitment by the customer to purchase a designated percentage of its requirements from Timken. Timken does not believe that there is any significant loss of earnings risk associated with any given contract.

**COMPETITION:**

The anti-friction bearing business is highly competitive in every country where Timken sells products. Timken competes primarily based on total value, including price, quality, timeliness of delivery, product design and the ability to provide engineering support and service on a global basis. The Company competes with domestic manufacturers and many foreign manufacturers of anti-friction bearings, including SKF Group, the Schaeffler Group, NTN Corporation, JTEKT Corporation and NSK Ltd.

**JOINT VENTURES:**

Investments in affiliated companies accounted for under the equity method were approximately $1.8 million and $1.6 million, respectively, at December 31, 2014 and 2013. The amount at December 31, 2014 was reported in other non-current assets on the Consolidated Balance Sheets.

**BACKLOG:**

The following table provides the backlog of orders of the Company's domestic and overseas operations at December 31, 2014 and 2013:

| | December 31, | |
|---|---|---|
| (Dollars in millions) | **2014** | 2013 |
| Segment: | | |
| Mobile Industries | **$ 719.2** | $ 945.1 |
| Process Industries | **569.9** | 370.8 |
| Total Company | **$ 1,289.1** | $ 1,315.9 |

Approximately 90% of the Company's backlog at December 31, 2014 is scheduled for delivery in the succeeding twelve months. Actual shipments depend upon customers' ever-changing production schedules. Accordingly, Timken does not believe that its backlog data and comparisons thereof, as of different dates, reliably indicate future sales or shipments.

**RAW MATERIALS:**

The principal raw material used by the Company to make anti-friction bearings is special bar quality (SBQ) steel. SBQ steel is produced around the world by various suppliers. SBQ steel is purchased in bar, tube and wire forms. The primary inputs to SBQ steel include scrap metal, iron ore, alloys, energy and labor. The availability and price of SBQ steel are subject to changes in supply and demand, commodity prices for ferrous scrap, ore, alloy, electricity, natural gas, transportation fuel, and labor costs. The Company manages price variability of commodities by using surcharge mechanisms on some of its contracts with its customers that provides for partial recovery of these cost increases in the price of bearing products.

Any significant increase in the cost of steel could materially affect the Company's earnings. Disruptions in the supply of SBQ steel could temporarily impair the Company's ability to manufacture bearings for its customers, or require the Company to pay higher prices in order to obtain SBQ, which could affect the Company's revenues and profitability. The availability of bearing quality tubing is relatively limited, and the Company is taking steps to diversify its processes to limit its exposure to this particular form of SBQ steel. Overall, the Company believes that the number of suppliers of SBQ steel is adequate to support the needs of global bearing production, and, in general, the Company is not dependent on any single source of supply.

**RESEARCH:**

Timken operates a network of technology and engineering centers to support its global customers with sites in North America, Europe and Asia. This network develops and delivers innovative friction management and mechanical power transmission solutions and technical services. Timken's largest technical center is located in North Canton, Ohio, near Timken's world headquarters. Other sites in the United States include Mesa, Arizona; Manchester, Connecticut; Fulton, Illinois; Keene and Lebanon, New Hampshire; and King of Prussia, Pennsylvania. Within Europe, the Company has technology facilities in Plymouth, England; Colmar, France; and Ploiesti, Romania. In Asia, Timken operates technology and engineering facilities in Bangalore, India and Shanghai, China.

Expenditures for research and development amounted to approximately $38.8 million, $39.3 million and $45.7 million in 2014, 2013 and 2012, respectively. Of these amounts, approximately $0.3 million, $0.4 million and $0.8 million were funded by others in 2014, 2013 and 2012, respectively.

**ENVIRONMENTAL MATTERS:**

The Company continues its efforts to protect the environment and comply with environmental protection laws. Additionally, it has invested in pollution control equipment and updated plant operational practices. The Company is committed to implementing a documented environmental management system worldwide and to becoming certified under the ISO 14001 standard where appropriate to meet or exceed customer requirements. As of the end of 2014, 16 of the Company's plants had obtained ISO 14001 certification.

The Company believes it has established appropriate reserves to cover its environmental expenses and has a well-established environmental compliance audit program for its domestic and international units. This program measures performance against applicable laws, as well as against internal standards that have been established for all units worldwide. It is difficult to assess the possible effect of compliance with future requirements that differ from existing ones.

The Company and certain of its U.S. subsidiaries previously have been and could in the future be identified as potentially responsible parties for investigation and remediation at off-site disposal or recycling facilities under the Comprehensive Environmental Response, Compensation and Liability Act (CERCLA), known as the Superfund, or state laws similar to CERCLA. In general, such claims for investigation and remediation have also been asserted against numerous other entities.

Management believes any ultimate liability with respect to pending actions will not materially affect the Company's operations, cash flows or consolidated financial position. The Company is also conducting environmental investigation and/or remediation activities at a number of current or former operating sites. The costs of such investigation and remediation activities, in the aggregate, are not expected to be material to the operations or financial position of the Company.

New laws and regulations, stricter enforcement of existing laws and regulations, the discovery of previously unknown contamination or the imposition of new clean-up requirements may require Timken to incur costs or become the basis for new or increased liabilities that could have a materially adverse effect on the Company's business, financial condition or results of operations.

**PATENTS, TRADEMARKS AND LICENSES:**

Timken owns numerous U.S. and foreign patents, trademarks and licenses relating to certain products. While Timken regards these as important, it does not deem its business as a whole, or any industry segment, to be materially dependent upon any one item or group of items.

**EMPLOYMENT:**

At December 31, 2014, Timken had approximately 16,000 employees. Approximately 3% of Timken's U.S. employees are covered under collective bargaining agreements.

**AVAILABLE INFORMATION:**

The Company uses its Investor Relations website at www.timken.com/investors as a channel for routine distribution of important information, including news releases, analyst presentations and financial information. The Company posts filings as soon as reasonably practicable after they are electronically filed with, or furnished to, the Securities and Exchange Commission (the SEC), including its annual, quarterly and current reports on Forms 10-K, 10-Q and 8-K; its proxy statements; and any amendments to those reports or statements. All such postings and filings are available on the Company's website free of charge. In addition, this website allows investors and other interested persons to sign up to automatically receive e-mail alerts when the Company posts news releases and financial information on the Company's website. The SEC also maintains a web site, www.sec.gov, which contains reports, proxy and information statements and other information regarding issuers that file electronically with the SEC. The content on any website referred to in this Annual Report on Form 10-K is not incorporated by reference into this Annual Report unless expressly noted.

## ITEM 1A. RISK FACTORS

*The following are certain risk factors that could affect our business, financial condition and results of operations. The risks that are highlighted below are not the only ones that we face. These risk factors should be considered in connection with evaluating forward-looking statements contained in this Annual Report on Form 10-K because these factors could cause our actual results and financial condition to differ materially from those projected in forward-looking statements. If any of the following risks actually occur, our business, financial condition or results of operations could be negatively affected.*

**RISK RELATING TO OUR BUSINESS:**

***The bearing industry is highly competitive, and this competition results in significant pricing pressure for our products that could affect our revenues and profitability.***

The global bearing industry is highly competitive. We compete with domestic manufacturers and many foreign manufacturers of anti-friction bearings, including SKF Group, the Schaeffler Group, NTN Corporation, JTEKT Corporation and NSK Ltd. The bearing industry is also capital intensive and profitability is dependent on factors such as labor compensation and productivity and inventory management, which are subject to risks that we may not be able to control. Due to the competitiveness within the bearing industry, we may not be able to increase prices for our products to cover increases in our costs. In many cases we face pressure from our customers to reduce prices, which could adversely affect our revenues and profitability. In addition, our customers may choose to purchase products from one of our competitors rather than pay the prices we seek for our products, which could adversely affect our revenues and profitability.

***Our business is capital intensive, and if there are downturns in the industries that we serve, we may be forced to significantly curtail or suspend operations with respect to those industries, which could result in our recording asset impairment charges or taking other measures that may adversely affect our results of operations and profitability.***

Our business operations are capital intensive, and we devote a significant amount of capital to certain industries. If there are downturns in the industries that we serve, we may be forced to significantly curtail or suspend our operations with respect to those industries, including laying-off employees, recording asset impairment charges and other measures, which may adversely affect our results of operations and profitability.

***Weakness in global economic conditions or in any of the industries or geographic regions in which we or our customers operate, as well as the cyclical nature of our customers' businesses generally or sustained uncertainty in financial markets, could adversely impact our revenues and profitability by reducing demand and margins.***

Our results of operations may be materially affected by the conditions in the global economy generally and in global capital markets. There has been extreme volatility in the capital markets and in the end markets and geographic regions in which we and our customers operate, which has negatively affected our revenues. Our revenues may also be negatively affected by changes in customer demand, additional changes in the product mix and negative pricing pressure in the industries in which we operate. Margins in those industries are highly sensitive to demand cycles, and our customers in those industries historically have tended to delay large capital projects, including expensive maintenance and upgrades, during economic downturns. As a result, our revenues and earnings are impacted by overall levels of industrial production.

***Our results of operations may be materially affected by the conditions in the global financial markets or in any of the geographic regions in which we operate. If an end user cannot obtain financing to purchase our products, either directly or indirectly contained in machinery or equipment, demand for our products will be reduced, which could have a material adverse effect on our financial condition and earnings.***

If a customer becomes insolvent or files for bankruptcy, our ability to recover accounts receivable from that customer would be adversely affected and any payment we received during the preference period prior to a bankruptcy filing may be potentially recoverable by the bankruptcy estate. Furthermore, if certain of our customers liquidate in bankruptcy, we may incur impairment charges relating to obsolete inventory and machinery and equipment. In addition, financial instability of certain companies in the supply chain could disrupt production in any particular industry. A disruption of production in any of the industries where we participate could have a material adverse effect on our financial condition and earnings.

***Any change in raw material prices or the availability or cost of raw materials could adversely affect our results of operations and profit margins.***

We require substantial amounts of raw materials, including steel, to operate our business. Our supply of raw materials could be interrupted for a variety of reasons, including availability and pricing. Prices for raw materials necessary for production have fluctuated significantly in the past and could do so in the future. We generally attempt to manage these fluctuations by passing along increased raw material prices to our customers in the form of price increases; however, we may be unable to increase the price of our products due to pricing pressure, contract terms or other factors. Additionally, certain of our long term customer contracts contain raw material surcharge mechanisms, which are generally tied to a market index or indexes. The index or indexes may be ineffective in mitigating our exposure to changes in raw material costs, which could adversely impact our revenue and profit margins.

Moreover, future disruptions in the supply of our raw materials could impair our ability to manufacture our products for our customers or require us to pay higher prices in order to obtain these raw materials from other sources. Any significant increase in the prices for such raw materials could adversely affect our results of operations and profit margins.

***Warranty, recall, quality or product liability claims could materially adversely affect our earnings.***

In our business, we are exposed to warranty and product liability claims. In addition, we may be required to participate in the recall of a product. If we fail to meet customer specifications for their products, we may be subject to product quality costs and claims. A successful warranty or product liability claim against us, or a requirement that we participate in a product recall, could have a material adverse effect on our earnings.

***We may incur further impairment and restructuring charges that could materially affect our profitability.***

We have taken $187.7 million in impairment and restructuring charges during the last five years. Changes in business or economic conditions, or our business strategy, may result in additional restructuring programs and may require us to take additional charges in the future, which could have a material adverse effect on our earnings.

***Environmental laws and regulations impose substantial costs and limitations on our operations and environmental compliance may be more costly than we expect.***

We are subject to the risk of substantial environmental liability and limitations on our operations due to environmental laws and regulations. We are subject to extensive federal, state, local and foreign environmental, health and safety laws and regulations concerning matters such as air emissions, wastewater discharges, solid and hazardous waste handling and disposal and the investigation and remediation of contamination. The risks of substantial costs and liabilities related to compliance with these laws and regulations are an inherent part of our business, and future conditions may develop, arise or be discovered that create substantial environmental compliance or remediation liabilities and costs.

Compliance with environmental, health and safety legislation and regulatory requirements may prove to be more limiting and costly than we anticipate. To date, we have committed significant expenditures in our efforts to achieve and maintain compliance with these requirements at our facilities, and we expect that we will continue to make significant expenditures related to such compliance in the future. From time to time, we may be subject to legal proceedings brought by private parties or governmental authorities with respect to environmental matters, including matters involving alleged noncompliance with or liability under environmental, health and safety laws, property damage or personal injury. New laws and regulations, including those which may relate to emissions of greenhouse gases, stricter enforcement of existing laws and regulations, the discovery of previously unknown contamination or the imposition of new clean-up requirements could require us to incur costs or become the basis for new or increased liabilities that could have a material adverse effect on our business, financial condition or results of operations.

***The Company may be subject to risks relating to its information technology systems.***

The Company relies on information technology systems to process, transmit and store electronic information and manage and operate its business. A breach in security could expose the Company and its customers and suppliers to risks of misuse of confidential information, manipulation and destruction of data, production downtimes and operations disruptions, which in turn could adversely affect the Company's reputation, competitive position, business or results of operations.

***The global nature of our business exposes us to foreign currency fluctuations that may affect our asset values, results of operations and competitiveness.***

We are exposed to the risks of currency exchange rate fluctuations because a significant portion of our net sales, costs, assets and liabilities, are denominated in currencies other than the U.S. dollar. These risks include a reduction in our asset values, net sales, operating income and competitiveness.

For those countries outside the United States where we have significant sales, devaluation in the local currency would reduce the value of our local inventory as presented in our Consolidated Financial Statements. In addition, a stronger U.S. dollar would result in reduced revenue, operating profit and shareholders' equity due to the impact of foreign exchange translation on our Consolidated Financial Statements. Fluctuations in foreign currency exchange rates may make our products more expensive for others to purchase or increase our operating costs, affecting our competitiveness and our profitability.

Changes in exchange rates between the U.S. dollar and other currencies and volatile economic, political and market conditions in emerging market countries have in the past adversely affected our financial performance and may in the future adversely affect the value of our assets located outside the United States, our gross profit and our results of operations.

***Global political instability and other risks of international operations may adversely affect our operating costs, revenues and the price of our products.***

Our international operations expose us to risks not present in a purely domestic business, including primarily:

- changes in tariff regulations, which may make our products more costly to export or import;
- difficulties establishing and maintaining relationships with local original equipment manufacturers (OEMs), distributors and dealers;
- import and export licensing requirements;
- compliance with a variety of foreign laws and regulations, including unexpected changes in taxation and environmental or other regulatory requirements, which could increase our operating and other expenses and limit our operations;
- disadvantages of competing against companies from countries that are not subject to U.S. laws and regulations, including the Foreign Corrupt Practices Act (FCPA);
- difficulty in staffing and managing geographically diverse operations; and
- tax exposures related to cross-border intercompany transfer pricing and other tax risks unique to international operations.

These and other risks may also increase the relative price of our products compared to those manufactured in other countries, reducing the demand for our products in the markets in which we operate, which could have a material adverse effect on our revenues and earnings.

***The funded status of our defined benefit and other postretirement plans has caused and may in the future cause a significant reduction in our shareholders' equity.***

We recorded a decrease in shareholders' equity related to pension and postretirement benefit liabilities in 2014 primarily due to a decrease in discount rates and changes in mortality assumptions, and in the future, we may be required to record charges related to pension and other postretirement liabilities as a result of asset returns, discount rate changes or other actuarial adjustments. These charges may be significant and would cause a reduction in our shareholders' equity.

***The funded status of our pension plans may require additional contributions, which may divert funds from other uses.***

The funded status of our pension plans may require us to make additional contributions to such plans. We made cash contributions of approximately $21 million, $121 million and $326 million in 2014, 2013 and 2012, respectively, to our defined benefit pension plans and currently expect to make cash contributions of approximately $15 million in 2015 to such plans. However, we cannot predict whether changing economic conditions, the future performance of assets in the plans or other factors will lead us or require us to make contributions in excess of our current expectations, diverting funds we would otherwise apply to other uses.

***Our defined benefit plans' assets and liabilities are substantial and expenses and contributions related to those plans are affected by factors outside our control, including the performance of plan assets, interest rates, actuarial data and experience, and changes in laws and regulations.***

Our defined benefit pension plans had assets with an estimated value of approximately $1.8 billion and liabilities with an estimated value of approximately $1.7 billion, both as of December 31, 2014. Our future expense and funding obligations for the defined benefit pension plans depend upon a number of factors, including the level of benefits provided for by the plans, the future performance of assets set aside in trusts for these plans, the level of interest rates used to determine the discount rate to calculate the amount of liabilities, actuarial data and experience and any changes in government laws and regulations. In addition, if the various investments held by our pension trusts do not perform as expected or the liabilities increase as a result of discount rates and other actuarial changes, our pension expense and required contributions would increase and, as a result, could materially adversely affect our business. Due to the value of our defined benefit plan assets and liabilities, even a minor decrease in interest rates, to the extent not offset by contributions or asset returns, could increase our obligations under such plans. We may be legally required to make contributions to the pension plans in the future in excess of our current expectations, and those contributions could be material.

***Work stoppages or similar difficulties could significantly disrupt our operations, reduce our revenues and materially affect our earnings.***

A work stoppage at one or more of our facilities could have a material adverse effect on our business, financial condition and results of operations. Also, if one or more of our customers were to experience a work stoppage, that customer would likely halt or limit purchases of our products, which could have a material adverse effect on our business, financial condition and results of operations.

***We are subject to a wide variety of domestic and foreign laws and regulations that could adversely affect our results of operations, cash flow or financial condition.***

We are subject to a wide variety of domestic and foreign laws and regulations, and legal compliance risks, including securities laws, tax laws, employment and pension-related laws, competition laws, U.S. and foreign export and trading laws, and laws governing improper business practices. We are affected by new laws and regulations, and changes to existing laws and regulations, including interpretations by courts and regulators.

In addition, we could be adversely affected by violations of the FCPA and similar worldwide anti-bribery laws as well as export controls and economic sanction laws. The FCPA and similar anti-bribery laws in other jurisdictions generally prohibit companies and their intermediaries from making improper payments to non-U.S. officials for the purpose of obtaining or retaining business. Our policies mandate compliance with these laws. We operate in many parts of the world that have experienced governmental corruption to some degree and, in certain circumstances, strict compliance with anti-bribery laws may conflict with local customs and practices. We cannot assure you that our internal controls and procedures will always protect us from the improper acts committed by our employees or agents. If we are found to be liable for FCPA, export control or sanction violations, we could suffer from criminal or civil penalties or other sanctions, including loss of export privileges or authorization needed to conduct aspects of our international business, which could have a material adverse effect on our business.

Compliance with the laws and regulations described above or with other applicable foreign, federal, state, and local laws and regulations currently in effect or that may be adopted in the future could materially adversely affect our competitive position, operating results, financial condition and liquidity.

***If we are unable to attract and retain key personnel our business could be materially adversely affected.***

Our business substantially depends on the continued service of key members of our management. The loss of the services of a significant number of members of our management could have a material adverse effect on our business. Our future success will also depend on our ability to attract and retain highly skilled personnel, such as engineering, finance, marketing and senior management professionals. Competition for these employees is intense, and we could experience difficulty from time to time in hiring and retaining the personnel necessary to support our business. If we do not succeed in retaining our current employees and attracting new high quality employees, our business could be materially adversely affected.

***We may not realize the improved operating results that we anticipate from past and future acquisitions and we may experience difficulties in integrating acquired businesses.***

We seek to grow, in part, through strategic acquisitions and joint ventures, which are intended to complement or expand our businesses, and expect to continue to do so in the future. These acquisitions involve challenges and risks. In the event that we do not successfully integrate these acquisitions into our existing operations so as to realize the expected return on our investment, our results of operations, cash flow or financial condition could be adversely affected.

***Our operating results depend in part on continued successful research, development and marketing of new and/or improved products and services, and there can be no assurance that we will continue to successfully introduce new products and services.***

The success of new and improved products and services depends on their initial and continued acceptance by our customers. Our businesses are affected, to varying degrees, by technological change and corresponding shifts in customer demand, which could result in unpredictable product transitions or shortened life cycles. We may experience difficulties or delays in the research, development, production, or marketing of new products and services which may prevent us from recouping or realizing a return on the investments required to bring new products and services to market. The end result could be a negative impact on our operating results.

**RISKS RELATING TO THE SPINOFF OF TIMKENSTEEL:**

***We may not realize the potential benefits from the Spinoff.***

We may not realize the potential financial, operational, managerial or other benefits that we expect from the recently completed Spinoff, or may not realize the potential benefits in a timely fashion. Additionally, the Company's operational and financial profile has changed as a result of the Spinoff. As a result, the Company's diversification of revenue sources has decreased, and it is possible that the Company's results of operations, cash flows, working capital and financing requirements may be subject to increased volatility. If we do not realize the potential benefits of the Spinoff, it could have a material adverse effect on our financial condition.

***Potential indemnification liabilities to TimkenSteel pursuant to the separation and distribution agreement could materially and adversely affect our business, financial condition, results of operations and cash flows.***

In connection with the Spinoff, we entered into a separation and distribution agreement, an employee matters agreement and a tax sharing agreement, all with TimkenSteel, which provide for, among other things, the principal corporate transactions required to effect the spinoff, certain conditions to the Spinoff and provisions governing the relationship between the Company and TimkenSteel with respect to and resulting from the Spinoff. Among other things, the separation and distribution agreement provides for indemnification obligations designed to make us financially responsible for substantially all liabilities that may exist relating to our continuing business operations, whether incurred prior to or after the spinoff, as well as those obligations of TimkenSteel assumed by us pursuant to the separation and distribution agreement. If we are required to indemnify TimkenSteel under the circumstances set forth in the separation and distribution agreement, we could be subject to substantial liabilities.

The employee matters agreement generally provides that each of the Company and TimkenSteel has responsibility for its own employees and compensation plans, subject to certain exceptions as described in the agreement. The tax sharing agreement generally governs the Company's and TimkenSteel's respective rights, responsibilities and obligations after the Spinoff with respect to taxes for any tax period ending on or before the distribution date, as well as tax periods beginning before and ending after the distribution date. Generally, TimkenSteel will be liable for all pre-spinoff U.S. federal income taxes, foreign income taxes and non-income taxes attributable to TimkenSteel's business, and all other taxes attributable to TimkenSteel, paid after the spinoff. In addition, the tax sharing agreement will address the allocation of liability for taxes that are incurred as a result of restructuring activities undertaken to effectuate the Spinoff. The tax sharing agreement will also provide that TimkenSteel is liable for taxes incurred by the Company that arise as a result of TimkenSteel's taking or failing to take, as the case may be, certain actions that result in the Spinoff failing to meet the requirements of a tax-free distribution under Section 355 of the Code.

Pursuant to the separation and distribution agreement, the employee matters agreement and the tax sharing agreement, TimkenSteel will agree to indemnify us for certain liabilities related to its steel business operations. However, third parties could seek to hold us responsible for any of the liabilities that TimkenSteel has agreed to retain, and there can be no assurance that the indemnity from TimkenSteel will be sufficient to protect us against the full amount of such liabilities, or that TimkenSteel will be able to fully satisfy its indemnification obligations. In particular, if TimkenSteel is unable to pay any prior period taxes for which it is responsible, the Company could be required to pay the entire amount of such taxes. Other provisions of federal law establish similar liability for other matters, including laws governing tax-qualified pension plans as well as other contingent liabilities. Moreover, even if we ultimately succeed in recovering from TimkenSteel any amounts for which we are held liable, we may be temporarily required to bear these losses ourselves. If TimkenSteel is unable to satisfy its indemnification obligations, the underlying liabilities could have a material adverse effect on our business, financial condition, results of operations and cash flows.

***If the Spinoff does not qualify as a tax-free transaction, the Company and its shareholders could be subject to substantial tax liabilities.***

The Spinoff was conditioned on our receipt of an opinion from Covington & Burling LLP, special tax counsel to the Company, that the distribution of TimkenSteel common shares in the spinoff qualified as tax-free (except for cash received by shareholders in lieu of fractional shares) to the Company, TimkenSteel and the Company's shareholders for U.S. federal income tax purposes under Sections 355 and 368(a)(1)(D) and related provisions of the Code. The opinion relied on, among other things, various assumptions and representations as to factual matters made by the Company and TimkenSteel, which, if inaccurate or incomplete in any material respect, could jeopardize the conclusions reached by such counsel in its opinion. We are not aware of any facts or circumstances that would cause the assumptions or representations that were relied on in the opinion of counsel to be inaccurate or incomplete in any material respect. The opinion is not binding on the Internal Revenue Service, or IRS, or the courts, and there can be no assurance that the qualification of the Spinoff as a transaction under Sections 355 and 368(a) of the Code will not be challenged by the IRS or by others in court, or that any such challenge would not prevail. If the Spinoff is determined to be taxable for U.S. federal income tax purposes, the Company and its shareholders that are subject to U.S. federal income tax could incur significant U.S. federal income tax liabilities, as each U.S. holder of the Company's common shares that received TimkenSteel common shares in the Spinoff would generally be treated as having received a taxable distribution of property in an amount equal to the fair market value of the TimkenSteel common shares received.

***Certain members of our Board of Directors and management may have actual or potential conflicts of interest because of their ownership of shares of TimkenSteel or their relationships with TimkenSteel following the spinoff.***

Certain members of our Board of Directors and management own shares of TimkenSteel and/or options to purchase shares of TimkenSteel, which could create, or appear to create, potential conflicts of interest when our directors and executive officers are faced with decisions that could have different implications for us and TimkenSteel. Two of our directors, Ward J. Timken, Jr. and John P. Reilly, are also directors of TimkenSteel and, in the case of Mr. Timken, Chairman, President and Chief Executive Officer of TimkenSteel. This may create, or appear to create, potential conflicts of interest if these directors are faced with decisions that could have different implications for TimkenSteel then the decisions have for us.

## ITEM 1B. UNRESOLVED STAFF COMMENTS

None.

## ITEM 2. PROPERTIES

Timken has manufacturing facilities at multiple locations in the United States and in a number of countries outside the United States. The aggregate floor area of these facilities worldwide is approximately 9,823,917 square feet, all of which, except for approximately 1,876,974 square feet, is owned in fee. The facilities not owned in fee are leased. The buildings occupied by Timken are principally made of brick, steel, reinforced concrete and concrete block construction. All buildings are in satisfactory operating condition to conduct business.

Timken's Mobile Industries segment's manufacturing facilities and service centers in the United States are located in Bucyrus and New Philadelphia, Ohio; Mesa, Arizona; Los Alamitos, California; Manchester and New Haven, Connecticut; Carlyle, Illinois; Keene and Lebanon, New Hampshire; Iron Station, North Carolina; Gaffney and Honea Path, South Carolina; Pulaski and Knoxville, Tennessee; and Ogden, Utah. These facilities, including warehouses at plant locations and a technology center in North Canton, Ohio have an aggregate floor area of 3,809,836 square feet.

Timken's Mobile Industries segment's manufacturing plants and service centers outside the United States are located in Benoni, South Africa; Villa Carcina, Italy; Colmar, France; Cheltenham, Northampton, Plymouth, and Wolverhampton, England; Belo Horizonte, Curtiba, and Sorocaba, Brazil; Jamshedpur, India; Sosnowiec, Poland; St. Thomas, Canada; and Yantai, China. These facilities, including warehouses at plant locations, have an aggregate floor area of 2,536,359 square feet.

Timken's Process Industries segment's manufacturing plants and service centers in the United States are located in Canton and Niles, Ohio; Hueytown, Alabama; Sante Fe Springs, California; Broomfield and Denver, Colorado; New Castle, Delaware; Fulton and Mokena, Illinois; Mishawaka, Indiana; Lenexa, Kansas; Augusta and Portland, Maine; Randleman, and Rutherfordton, North Carolina; Union, South Carolina; Altavista, Virginia; Ferndale and Pasco, Washington; Princeton, West Virginia; and Casper and Rock Springs, Wyoming. These facilities, including warehouses at plant locations and a technology center in North Canton, Ohio have an aggregate floor area of 1,773,950 square feet.

Timken's Process Industries segment's manufacturing plants and service centers outside the United States are located in Chengdu, Xiangtan and Wuxi, China; Chennai and Durg, India; Dudley, England; Saskatoon and Prince George, Canada; and Ploiesti, Romania. These facilities, including warehouses at plant locations have an aggregate floor area of 1,703,772 square feet.

In addition to the manufacturing and distribution facilities discussed above, Timken owns or leases warehouses and distribution facilities in the United States, France, Mexico, Singapore, Argentina, Australia, and China.

The extent to which the Company uses its properties varies by property and from time to time. The Company believes that its capacity levels are adequate for its present and anticipated future needs. Most of the Company's manufacturing facilities remain capable of handling additional volume increases.

## ITEM 3. LEGAL PROCEEDINGS

The Company is involved in various claims and legal actions arising in the ordinary course of business. In the opinion of management, the ultimate disposition of these matters will not have a material adverse effect on the Company's consolidated financial position or results of operations.

In October 2014, the Brazilian government antitrust agency announced that it had opened an investigation of alleged antitrust violations in the bearing industry. The Company's Brazilian subsidiary, Timken do Brasil Comercial Importadora Ltda, was included in the investigation. While the Company is unable to predict the ultimate length, scope or results of the investigation, management believes that the outcome will not have a material effect on the Company's consolidated financial position; however, any such outcome may be material to the results of operations of any particular period in which costs, if any, are recognized. Based on current facts and circumstances, the low end of the range for potential penalties, if any, would be immaterial to the Company.

## ITEM 4. MINE SAFETY DISCLOSURES

Not applicable.

## ITEM 4A. EXECUTIVE OFFICERS OF THE REGISTRANT

The executive officers are elected by the Board of Directors normally for a term of one year and until the election of their successors. All executive officers have been employed by Timken or by a subsidiary of the Company during the past five-year period. The executive officers of the Company as of March 2, 2015 are as follows:

| Name | Age | Current Position and Previous Positions During Last Five Years | |
|---|---|---|---|
| William R. Burkhart | 49 | 2014 | Executive Vice President, General Counsel and Secretary |
| | | 2000 | Senior Vice President and General Counsel |
| Christopher A. Coughlin | 54 | 2014 | Executive Vice President, Group President |
| | | 2012 | Group President |
| | | 2011 | President – Process Industries |
| | | 2010 | President – Process Industries & Supply Chain |
| Philip D. Fracassa | 47 | 2014 | Executive Vice President, Chief Financial Officer |
| | | 2012 | Senior Vice President – Planning and Development |
| | | 2010 | Senior Vice President and Controller – B&PT |
| Richard G. Kyle | 49 | 2014 | President and Chief Executive Officer; Director |
| | | 2013 | Chief Operating Officer – B&PT; Director |
| | | 2012 | Group President |
| | | 2011 | President – Mobile Industries & Aerospace |
| | | 2009 | President – Mobile Industries |
| J. Ted Mihaila | 60 | 2006 | Senior Vice President and Controller |

# PART II.

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

The Company's common shares are traded on the New York Stock Exchange under the symbol "TKR." The estimated number of record holders of the Company's common shares at December 31, 2014 was 4,733. The estimated number of beneficial shareholders at December 31, 2014 was 44,217.

The following table provides information about the high and low sales prices for the Company's common shares and dividends paid for each quarter for the last two fiscal years.

| | **2014** | | | 2013 | | |
|---|---|---|---|---|---|---|
| | Stock prices | | Dividends | Stock prices | | Dividends |
| | High | Low | per share | High | Low | per share |
| First quarter | **$ 61.37** | **$ 52.51** | **$ 0.25** | $ 58.50 | $ 47.67 | $ 0.23 |
| Second quarter | **$ 69.51** | **$ 57.69** | **$ 0.25** | $ 59.44 | $ 50.22 | $ 0.23 |
| Third quarter | **$ 49.96** | **$ 42.34** | **$ 0.25** | $ 64.35 | $ 55.00 | $ 0.23 |
| Fourth quarter | **$ 44.30** | **$ 37.62** | **$ 0.25** | $ 61.57 | $ 50.22 | $ 0.23 |

At the close of business on June 30, 2014, the Company's shareholders received one common share of TimkenSteel for every two common shares of the Company they held as of the close of business on June 23, 2014. On June 30, 2014, the last trading day before the Spinoff became effective, the closing price of our common shares, trading "regular way" (that is with an entitlement to common shares of TimkenSteel distributed in the Spinoff), was $67.84. On July 1, 2014, the first trading day after the Spinoff, the opening price of our common shares was $48.56 per share and the opening price of TimkenSteel common shares was $39.55 per share. These stock prices were as quoted on the New York Stock Exchange.

**ISSUER PURCHASES OF COMMON SHARES:**

The following table provides information about purchases of its common shares by the Company during the quarter ended December 31, 2014.

| Period | Total number of shares purchased (1) | Average price paid per share (2) | Total number of shares purchased as part of publicly announced plans or programs | Maximum number of shares that may yet be purchased under the plans or programs (3) |
|---|---|---|---|---|
| 10/1/2014 – 10/31/2014 | **150** | **$ 42.68** | **—** | **8,997,807** |
| 11/1/2014 – 11/30/2014 | **30** | **43.64** | **—** | **8,997,807** |
| 12/1/2014 – 12/31/2014 | **100,036** | **43.54** | **100,000** | **8,897,807** |
| Total | **100,216** | **$ 43.54** | **100,000** | **8,897,807** |

(1) Of the shares purchased in October, November and December, 150, 30 and 36, respectively, represent common shares of the Company that were owned and tendered by employees to exercise stock options, and to satisfy withholding obligations in connection with the exercise of stock options and vesting of restricted shares.

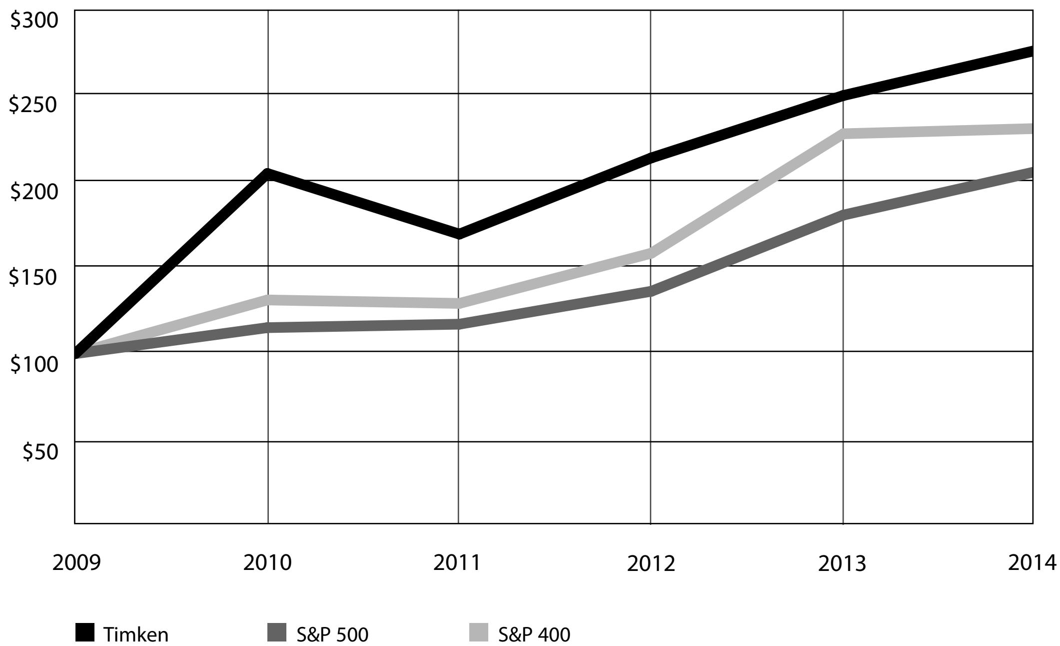
(2) For shares tendered in connection with the vesting of restricted shares, the average price paid per share is an average calculated using the daily high and low of the Company's common shares as quoted on the New York Stock Exchange at the time of vesting. For shares tendered in connection with the exercise of stock options, the price paid is the real-time trading share price at the time the options are exercised.

(3) On February 10, 2012, the Board of Directors of the Company approved a share purchase plan pursuant to which the Company may purchase up to ten million of its common shares in the aggregate. On June 13, 2014, the Board of Directors of the Company authorized an additional ten million common shares for repurchase under this plan. This share purchase plan expires on December 31, 2015. The Company may purchase shares from time to time in open market purchases or privately negotiated transactions. The Company may make all or part of the purchases pursuant to accelerated share repurchases or Rule 10b5-1 plans.

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

**COMPARISON OF FIVE-YEAR CUMULATIVE TOTAL RETURN***

Among The Timken Company, S&P 500 and S&P 400 Industries




*Total return assumes reinvestment of dividends. Fiscal years ending December 31.

| | 2010 | 2011 | 2012 | 2013 | **2014** |
|---|---|---|---|---|---|
| Timken | $ 204 | $ 169 | $ 213 | $ 249 | **$ 275** |
| S&P 500 | 115 | 117 | 136 | 180 | **205** |
| S&P 400 Industrials | 131 | 129 | 158 | 227 | **230** |

The line graph compares the cumulative total shareholder returns over five years for The Timken Company, the S&P 500 Stock Index and the S&P 400 Industrials Index. The graph assumes, in each case, an initial investment of $100 on January 1, 2010, in Timken common shares, S&P 500 Index and S&P 400 Industrials Index, based on market prices at the end of each fiscal year through and including December 31, 2014, and reinvestment of dividends (and taking into account the value of the TimkenSteel common shares distributed in the Spinoff).

## ITEM 6. SELECTED FINANCIAL DATA

# SUMMARY OF OPERATIONS AND OTHER COMPARATIVE DATA

| (Dollars in millions, except per share and per employee data) | 2014 | 2013 | 2012 | 2011 | 2010 |
|---|---|---|---|---|---|
| **Statements of Income** | | | | | |
| Net sales | **$3,076.2** | $3,035.4 | $3,359.5 | $3,333.6 | $2,798.6 |
| Gross profit | **898.0** | 868.4 | 1,028.0 | 1,018.0 | 803.9 |
| Selling, general and administrative expenses | **542.5** | 546.6 | 554.5 | 540.6 | 484.8 |
| Impairment and restructuring charges | **113.4** | 8.7 | 29.5 | 14.4 | 21.7 |
| Operating income | **208.4** | 305.9 | 444.0 | 463.0 | 297.4 |
| Other income (expense), net | **19.9** | 6.7 | 102.0 | (0.4) | 4.2 |
| Interest expense, net | **24.3** | 22.5 | 28.2 | 31.2 | 34.5 |
| Income from continuing operations | **149.3** | 175.5 | 331.5 | 280.8 | 179.2 |
| Income from discontinued operations, net of income taxes | **24.0** | 87.5 | 164.4 | 175.8 | 97.8 |
| Net income attributable to The Timken Company | **$ 170.8** | $ 262.7 | $ 495.5 | $ 454.3 | $ 274.8 |
| **Balance Sheets** | | | | | |
| Inventories, net | **$ 585.5** | $ 582.6 | $ 611.5 | $ 669.6 | $ 602.4 |
| Property, plant and equipment, net | **780.5** | 855.8 | 834.1 | 868.6 | 880.3 |
| Total assets | **3,001.4** | 4,477.9 | 4,244.2 | 4,327.4 | 4,180.4 |
| Total debt: | | | | | |
| Short-term debt | **7.4** | 18.6 | 14.3 | 22.0 | 22.4 |
| Current portion of long-term debt | **0.6** | 250.7 | 9.6 | 5.8 | 9.5 |
| Long-term debt | **522.1** | 176.4 | 424.9 | 448.6 | 443.0 |
| Total debt | **$ 530.1** | $ 445.7 | $ 448.8 | $ 476.4 | $ 474.9 |
| Net debt (cash) | | | | | |
| Total debt | **530.1** | 445.7 | 448.8 | 476.4 | 474.9 |
| Less: cash and cash equivalents and restricted cash | **(294.1)** | (399.7) | (601.5) | (468.4) | (877.1) |
| Net debt (cash): (1) | **$ 236.0** | $ 46.0 | $ (152.7) | $ 8.0 | $ (402.2) |
| Total liabilities | **1,412.3** | 1,829.3 | 1,997.6 | 2,284.9 | 2,238.6 |
| Shareholders' equity | **$1,589.1** | $2,648.6 | $2,246.6 | $2,042.5 | $1,940.7 |
| Capital: | | | | | |
| Net debt (cash) | **236.0** | 46.0 | (152.7) | 8.0 | (402.2) |
| Shareholders' equity | **1,589.1** | 2,648.6 | 2,246.6 | 2,042.5 | 1,940.7 |
| Net debt (cash) + shareholders' equity (capital) | **$1,825.1** | $2,694.6 | $2,093.9 | $2,050.5 | $1,538.5 |
| **Other Comparative Data** | | | | | |
| Income from continuing operations / Net sales | **4.9%** | 5.8% | 9.9% | 8.4% | 6.4% |
| Net income attributable to The Timken Company / Net sales | **5.6%** | 8.7% | 14.7% | 13.6% | 9.8% |
| Return on equity (2) | **9.4%** | 6.6% | 14.8% | 13.7% | 9.2% |
| Net sales per employee (3) | **$ 188.2** | $ 181.6 | $ 192.0 | $ 189.9 | $ 169.3 |
| Capital expenditures | **126.8** | 133.6 | 118.3 | 105.5 | 72.1 |
| Depreciation and amortization | **137.0** | 142.4 | 149.6 | 146.7 | 143.7 |
| Capital expenditures / Net sales | **4.1%** | 4.4% | 3.5% | 3.2% | 2.6% |
| Dividends per share | **$ 1.00** | $ 0.92 | $ 0.92 | $ 0.78 | $ 0.53 |
| Basic earnings per share – continuing operations (4) | **$ 1.62** | $ 1.84 | $ 3.41 | $ 2.84 | $ 1.84 |
| Diluted earnings per share – continuing operations (4) | **$ 1.61** | $ 1.82 | $ 3.38 | $ 2.81 | $ 1.82 |
| Basic earnings per share (5) | **$ 1.89** | $ 2.76 | $ 5.11 | $ 4.65 | $ 2.83 |
| Diluted earnings per share (5) | **$ 1.87** | $ 2.74 | $ 5.07 | $ 4.59 | $ 2.81 |
| Net debt (cash) to capital (1) | **12.9%** | 1.7% | (7.3)% | 0.4% | (26.1)% |
| Number of employees at year-end (6) | **16,345** | 16,717 | 17,500 | 17,558 | 16,534 |
| Number of shareholders (7) | **44,217** | 52,218 | 50,783 | 44,238 | 39,118 |

(1) The Company presents net debt (cash) because it believes net debt (cash) is more representative of the Company's financial position than total debt due to the amount of cash and cash equivalents.

(2) Return on equity is defined as income from continuing operations divided by ending shareholders' equity.

(3) Based on average number of employees employed during the year.

(4) Based on average number of shares outstanding during the year.

(5) Based on average number of shares outstanding during the year and includes discontinued operations for all periods presented.

(6) Adjusted to exclude employees from the former Steel segment (which was spunoff in June 2014) for all periods.

(7) Includes an estimated count of shareholders having common shares held for their accounts by banks, brokers and trustees for benefit plans.

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

(Dollars in millions, except per share data)

## OVERVIEW

**INTRODUCTION:**

The Timken Company engineers, manufactures and markets bearings, transmissions, gearboxes, chain and related products and offers a spectrum of power system rebuild and repair services around the world. The Company's growing product and services portfolio features many strong industrial brands, such as Timken, Fafnir, Philadelphia Gear, Drives and Interlube. Timken today applies its deep knowledge of metallurgy, tribology and power transmission across the broad spectrum of bearings and related systems to improve the reliability and efficiency of machinery and equipment all around the world. Known for its quality products and collaborative technical sales model, Timken focuses on providing value to diverse markets worldwide through both original equipment manufacturers (OEMs) and aftermarket channels. With approximately 16,000 people operating in 28 countries, Timken makes the world more productive and keeps industry in motion. Beginning in the fourth quarter of 2014, the Company began operating under two segments: (1) Mobile Industries and (2) Process Industries. Refer to *Note 15 – Segment Information* for additional information on the resegmentation of the Company's business segments. The following further describes these business segments:

- ***Mobile Industries*** offers an extensive portfolio of bearings, seals, lubrication devices and systems, as well as power transmission components, engineered chain, augers and related products and maintenance services, to OEMs of: off-highway equipment for the agricultural, construction and mining markets; on-highway vehicles including passenger cars, light trucks, and medium- and heavy-duty trucks; and rail cars, locomotives, rotor craft and fixed-wing aircraft. Beyond service parts sold to OEMs, aftermarket sales to individual end users, equipment owners, operators and maintenance shops are handled through the Company's extensive network of authorized automotive and heavy-truck distributors, and include hub units, specialty kits and more. Mobile Industries also provides power transmission systems and flight-critical components for civil and military aircraft, which include bearings, helicopter transmission systems, rotor-head assemblies, turbine engine components, gears and housings.
- ***Process Industries*** supplies industrial bearings and assemblies, power transmission components such as gears and gearboxes, couplings, seals, lubricants, chains and related products and services to OEMs and end users in industries that place heavy demands on operating equipment they make or use. This includes; metals, mining, cement and aggregate production; coal and wind power generation; oil and gas; pulp and paper in applications including printing presses; and cranes, hoists, drawbridges, wind energy turbines, gear drives, drilling equipment, coal conveyors, health and critical motion control equipment, marine equipment and food processing equipment. This segment also supports aftermarket sales and service needs through its global network of authorized industrial distributors. In addition, the Company's industrial services group offers end users a broad portfolio of maintenance support and capabilities that include repair and service for bearings and gearboxes as well as electric motor rewind, repair and services.

For nearly 100 years, the Company also made and marketed steel within its steel business. However, on June 30, 2014, the Company announced that it had completed the Spinoff into a separate independent publicly traded company, TimkenSteel. The Company's Board of Directors declared a distribution of all outstanding common shares of TimkenSteel through a dividend. At the close of business on June 30, 2014, the Company's shareholders received one common share of TimkenSteel for every two common shares of the Company they held as of the close of business on June 23, 2014. The steel business has been reclassified to discontinued operations for all periods presented.

Currently, the Company focuses its strategy on creating value that leads to growth and sustained levels of profitability. The Company works to create value by:

- Expanding in new and existing markets by applying the Timken team's knowledge of metallurgy, friction management and mechanical power transmission to create value for our customers. Using a highly collaborative technical selling model, the Company places particular emphasis on creating unique solutions for challenging and/or demanding applications. The Company intends to grow in attractive market sectors, emphasizing those spaces that are highly fragmented, demand high service and value the reliability and efficiency offered by the Company's products. The Company also targets those applications that offer significant aftermarket demand, thereby providing product and services revenue throughout the equipment's lifetime.
- Performing with excellence, driving for exceptional results with a passion for superior execution, the Company embraces a continuous improvement culture that is charged with lowering costs, eliminating waste, increasing efficiency, encouraging organizational agility and building greater brand equity. As part of this effort, the Company may also reposition underperforming product lines and segments and divest non-strategic assets.

The following items highlight certain of the Company's more significant strategic accomplishments in 2014:

- On November 30, 2014, the Company completed the acquisition of the assets of Revolvo Ltd. (Revolvo), a specialty bearing company based in Dudley, United Kingdom (U.K.). Revolvo makes and markets ball and roller bearings for industrial applications in process and heavy industries. Revolvo's split roller bearing housed units are widely used by mining, power generation, food and beverage, pulp and paper, metals, cements, marine and waste-water end users. Revolvo had full-year 2014 sales of approximately $9 million.
- On September 8, 2014, the Company announced plans to eliminate its Aerospace segment leadership positions and integrate substantially all aerospace business activities into Mobile Industries under the direction of its Group President. The Company also announced plans to close its aerospace engine overhaul business, located in Mesa, Arizona. The Company subsequently sold the aerospace engine overhaul assets in November 2014. In addition, the Company announced plans to evaluate strategic alternatives for its aerospace MRO parts business, also located in Mesa, and close its aerospace bearing facility located in Wolverhampton, U.K., which is expected to close in early 2016. The Company began reporting the aerospace business results primarily within the Mobile Industries segment starting with the fourth quarter of 2014.
- In June 2014, the Company announced that it was committing $60 million to the DeltaX initiative, a multi-year investment to improve the Company's concept-to-commercialization efforts. DeltaX will integrate technology and tools designated to enable the Company to be more agile and competitive. The Company will replace its traditional functional infrastructure with a more product-focused infrastructure, supported by new customer-facing systems. DeltaX is intended to help the Company to execute on its strategy to grow, delivering to the market place much faster and more efficently those products that customers value. As part of the $60 million DeltaX initiative, the XSell project will leverage the SAP infrastructure deployed throughout our global operations. It will provide the global sales team with new customer relationship management capabilities, as well as more consistent, mobility-enabled sales processes and business tools.
- On June 13, 2014, the Company's Board of Directors authorized the Company to purchase an additional 10 million of its common shares. The total number of shares that remained authorized for repurchase was 8.9 million shares at December 31, 2014.
- On April 28, 2014, the Company completed the acquisition of assets from Schulz Group (Schulz). Based in New Haven, Connecticut, Schulz provides electric motor and generator repairs, motor rewinds, custom controls and panels, systems integration, pump services, machine rebuilds, hydro services and diagnostics for a broad range of commercial and industrial applications. Schulz had full-year 2013 sales of approximately $18 million and employed 125 associates.

## RESULTS OF OPERATIONS

***2014 compared to 2013***

**OVERVIEW:**

| | **2014** | 2013 | $ Change | % Change |
|---|---|---|---|---|
| Net sales | **$ 3,076.2** | $ 3,035.4 | $ 40.8 | 1.3 % |
| Income from continuing operations | **149.3** | 175.5 | (26.2) | (14.9)% |
| Income from discontinued operations | **24.0** | 87.5 | (63.5) | (72.6)% |
| Income attributable to noncontrolling interest | **2.5** | 0.3 | 2.2 | NM |
| Net income attributable to The Timken Company | **$ 170.8** | $ 262.7 | $ (91.9) | (35.0)% |
| Diluted earnings per share: | | | | |
| Continuing operations | **$ 1.61** | $ 1.82 | $ (0.21) | (11.5)% |
| Discontinued operations | **0.26** | 0.92 | (0.66) | (71.7)% |
| Diluted earnings per share | **$ 1.87** | $ 2.74 | $ (0.87) | (31.8)% |
| Average number of shares—diluted | **91,224,328** | 95,823,728 | — | (4.8)% |

On January 29, 2015, the Company furnished a Current Report on Form 8-K to the Securities and Exchange Commission that included an earnings release issued that same day reporting results for the fourth quarter and full year of 2014, which was furnished as Exhibit 99.1 thereto (the Earning Release). For the twelve months ended December 31, 2014, the Earnings Release reported: (a) income from continuing operations of $147.0 million, or $1.58 per diluted share; (b) income from discontinued operations of $21.7 million, or $0.24 per diluted share; (c) net income of $168.7 million; and (d) net income attributable to The Timken Company of $166.2 million. Between the issuance of the Earnings Release and the filing of this Annual Report on Form 10-K, the Company adjusted an entry in its provision for income taxes for the three and twelve months ended December 31, 2014, reducing the provision for income taxes and increasing net income by $4.6 million, or $0.05 per diluted share.

The Company reported net sales for 2014 of approximately $3.1 billion, compared to approximately $3.0 billion in 2013, a 1.3% increase. The increase in sales was primarily due to higher volume in the Process Industries segment, partially offset by decreased volume in the Mobile Industries segment. The lower volume in the Mobile Industries segment was primarily driven by planned program exits that concluded in 2013. In 2014, diluted earnings per share from continuing operations was $1.61, compared to $1.82 in 2013. The Company's net income from continuing operations in 2014, compared to 2013, was lower due to higher impairment and restructuring charges, the impact of planned program exits that concluded at the end of 2013, and pension settlement charges, partially offset by the impact of higher volume, lower manufacturing cost and the gain on the sale of real estate in Sao Paulo, Brazil (Sao Paulo). Income from continuing operations also benefited from a lower effective tax rate. Impairment and restructuring charges primarily related to goodwill impairment for two of the Company's aerospace reporting units within the Mobile Industries segment. Discontinued operations related to Company's former steel business that was spun off on June 30, 2014. Income from discontinued operations was lower in 2014 compared to 2013 as a result of separation costs incurred as a result of the Spinoff.

**OUTLOOK:**

The Company expects sales to increase approximately 1% in 2015 compared to 2014, primarily driven by higher demand in the light vehicle, wind energy, marine and industrial aftermarket sectors, offset in large part by the impact of currency-rate changes. The Company's earnings are expected to be lower in 2015 compared to 2014, primarily due to non-cash charges related to the settlement of certain U.S. pension obligations, partially offset by lower impairment and restructuring charges and the impact of higher demand. On January 22, 2015, the Company entered into an agreement pursuant to which the Timken-Latrobe-MPB-Torrington Retirement Plan (the Plan) purchased a group annuity contract from Prudential Insurance Company of America (Prudential) to pay future pension benefits for approximately 5,000 U.S. Timken retirees. The Company has transferred approximately $600 million of the Company's pension obligations and approximately $635 million of the pension assets to Prudential. The Company expects to incur pension settlement charges of approximately $220 million during the first quarter of 2015 in connection with this group annuity purchase.

The Company expects to generate cash from continuing operations of approximately $345 million in 2015, an increase of approximately $65 million, or 23%, compared to 2014, as the Company anticipates higher income from continuing operations, excluding non-cash impairment and pension settlement charges. Pension contributions are expected to be approximately $15 million in 2015, compared to $21.1 million in 2014. The Company expects capital expenditures of approximately 4% of sales in 2015, compared to 4.2% of sales in 2014.

## THE STATEMENTS OF INCOME

### SALES BY SEGMENT:

| | 2014 | 2013 | $ Change | % Change |
|---|---|---|---|---|
| Mobile Industries | **$ 1,685.4** | $ 1,775.8 | $ (90.4) | (5.1)% |
| Process Industries | **1,390.8** | 1,259.6 | 131.2 | 10.4 % |
| Total Company | **$ 3,076.2** | $ 3,035.4 | $ 40.8 | 1.3 % |

Net sales for 2014 increased $40.8 million, or 1.3%, compared to 2013, primarily due to higher volume of approximately $150 million, driven by increases in the Process Industries' wind energy and industrial aftermarket sectors and the Mobile Industries' rail market sector, as well as the benefit of acquisitions of $25 million. These factors were partially offset by planned program exits in the Mobile Industries segment that concluded in 2013 of approximately $110 million and the impact of foreign currency of approximately $30 million.

### GROSS PROFIT:

| | 2014 | 2013 | $ Change | Change |
|---|---|---|---|---|
| Gross profit | **$ 898.0** | $ 868.4 | $ 29.6 | 3.4 % |
| Gross profit % to net sales | **29.2%** | 28.6% | — | 60 bps |
| Rationalization expenses included in cost of products sold | **$ 3.6** | $ 5.9 | $ (2.3) | (39.0)% |

Gross profit increased in 2014 compared to 2013, primarily due to lower manufacturing costs of approximately $30 million and the impact of higher sales volume and mix, including the impact of planned program exits, of approximately $10 million. These factors were partially offset by inventory valuation adjustments of approximately $20 million.

### SELLING, GENERAL AND ADMINISTRATIVE EXPENSES:

| | 2014 | 2013 | $ Change | Change |
|---|---|---|---|---|
| Selling, general and administrative expenses | **$ 542.5** | $ 546.6 | $ (4.1) | (0.8)% |
| Selling, general and administrative expenses % to net sales | **17.6%** | 18.0% | — | (40) bps |

The decrease in selling, general and administrative expenses of $4.1 million in 2014 compared to 2013 was primarily due to the benefit of cost reduction initiatives of approximately $25 million, partially offset by higher expense related to incentive compensation plans of approximately $15 million and the impact of acquisitions of approximately $5 million.

**IMPAIRMENT AND RESTRUCTURING CHARGES:**

| | 2014 | 2013 | $ Change |
|---|---|---|---|
| Impairment charges | $ 98.9 | $ 0.1 | $ 98.8 |
| Severance and related benefit costs | 10.7 | 9.2 | 1.5 |
| Exit costs | 3.8 | (0.6) | 4.4 |
| Total | $ 113.4 | $ 8.7 | $ 104.7 |

Impairment and restructuring charges of $113.4 million in 2014 were primarily due to goodwill and other intangible impairment charges of $96.2 million for two of the Company's aerospace reporting units within the Mobile Industries segment that were recorded in 2014. Impairment and restructuring charges for 2013 were primarily due to severance and related benefit costs of approximately $6 million due to cost-reduction initiatives relating to reductions in headcount in the bearings and power transmission business and the recognition of severance and related benefits of approximately $3 million related to the closure of the manufacturing facility in St. Thomas, Ontario, Canada (St. Thomas). Refer to *Note 11 – Impairment and Restructuring Charges* in the Notes to the Consolidated Financial Statements for additional discussion.

**PENSION SETTLEMENT CHARGES:**

| | 2014 | 2013 | $ Change |
|---|---|---|---|
| Pension Settlement Charges | $ 33.7 | $ 7.2 | $ 26.5 |

Pension settlement charges recorded in 2014 were primarily the result of the settlement of approximately $110 million of the Company's pension obligations related to its defined benefit pension plan in the United States as a result of the lump sum distributions to new retirees and certain deferred vested plan participants in 2014. Pension settlement charges in 2013 primarily related to the settlement of pension obligations for the Company's Canadian defined pension plans as a result of the closure of the Company's manufacturing facility in St. Thomas.

**INTEREST INCOME (EXPENSE):**

| | 2014 | 2013 | $ Change | % Change |
|---|---|---|---|---|
| Interest (expense) | $ (28.7) | $ (24.4) | $ (4.3) | 17.6 % |
| Interest income | 4.4 | 1.9 | 2.5 | 131.6 % |

Interest expense for 2014 increased compared to 2013 primarily due to higher average debt and lower capitalized interest. Interest income increased for 2014 compared to 2013 primarily due to interest income recognized on the deferred payments related to the sale of the Company's former manufacturing site in Sao Paulo.

**OTHER INCOME (EXPENSE):**

| | 2014 | 2013 | $ Change | % Change |
|---|---|---|---|---|
| Gain on sale of real estate | $ 22.6 | $ 5.4 | $ 17.2 | 318.5 % |
| Other income (expense), net | (2.7) | 1.3 | (4.0) | 307.7 % |
| Total | $ 19.9 | $ 6.7 | $ 13.2 | 197.0 % |

During 2014, the Company recognized a gain of $22.6 million, compared to $5.4 million in 2013, related to the sale of its former manufacturing site in Sao Paulo. Refer to *Note 7 – Property, Plant and Equipment* for additional information on the gain.

The Company reported other expense, net in 2014 compared to other income, net in 2013 primarily due to higher charitable donations in 2014. The Company also incurred higher foreign currency exchange losses in 2014 compared to 2013.

**INCOME TAX EXPENSE:**

| | **2014** | 2013 | $ Change | Change |
|---|---|---|---|---|
| Income tax expense | **$ 54.7** | $ 114.6 | $ (59.9) | (52.3)% |
| Effective tax rate | **26.8%** | 39.5% | — | (1,270) bps |

The effective tax rate on pretax income for 2014 was favorable relative to the U.S. federal statutory rate primarily due to U.S. foreign tax credits, earnings in certain foreign jurisdictions where the effective tax rate is less than 35%, the U.S. manufacturing deduction, the U.S. research tax credit and certain discrete tax benefits. These factors were partially offset by U.S. taxation of foreign income, losses at certain foreign subsidiaries where no tax benefit could be recorded, non-deductible intangible asset impairment charges recorded in the Mobile Industries segment and U.S. state and local taxes.

The effective tax rate on pretax income for 2013 was unfavorable relative to the U.S. federal statutory rate primarily due to U.S. taxation of foreign income including cash repatriation, losses at certain foreign subsidiaries where no tax benefit could be recorded and U.S. state and local taxes. These factors were partially offset by earnings in certain foreign jurisdictions where the effective tax rate is less than 35%, U.S. foreign tax credits, the U.S. manufacturing deduction and certain discrete U.S. tax benefits.

The change in the effective tax rate in 2014 compared to 2013 was primarily due to lower U.S. taxation of foreign income, lower losses at certain foreign subsidiaries where no tax benefit could be recorded and lower U.S. state and local taxes, partially offset by lower U.S. foreign tax credits, lower U.S. manufacturing deduction, non-deductible intangible asset impairment charges recorded in the Mobile Industries segment and the net effect of other discrete items.

**DISCONTINUED OPERATIONS:**

| | **2014** | 2013 | $ Change | Change |
|---|---|---|---|---|
| Net sales | **$ 786.2** | $ 1,305.8 | $ (519.6) | (39.8)% |
| Income before income taxes | **40.0** | 127.1 | (87.1) | (68.5)% |
| Income taxes | **16.0** | 39.6 | (23.6) | (59.6)% |
| Operating results, net of tax | **$ 24.0** | $ 87.5 | $ (110.7) | (72.6)% |

On June 30, 2014, the Company completed the Spinoff. The operating results, net of tax, included one-time transaction costs in connection with the separation of the two companies of $57.1 million and $13.0 million during 2014 and 2013, respectively. These costs included consulting and professional fees associated with preparing for and executing the Spinoff, as well as lease cancellation fees. For further discussion, please refer to *Note 2 – Spinoff Transaction* in the Notes to the Consolidated Financial Statements.

## BUSINESS SEGMENTS

The primary measurement used by management to measure the financial performance of each segment is earnings before interest and taxes (EBIT). Refer to *Note 15 – Segment Information* in the Notes to the Consolidated Financial Statements for the reconciliation of EBIT by segment to consolidated income before income taxes. Effective October 1, 2014, the Company began operating under new reportable segments. The Company's two reportable segments are: Mobile Industries and Process Industries. Results of the Company's former Aerospace segment are now primarily included in the Mobile Industries segment. In addition, the Company made adjustments to the allocation of certain selling, general and administrative expenses and certain foreign currency exchange gains or losses for all prior periods presented to better reflect the Company's operating model and new cost structure following the Spinoff and the elimination of the former Aerospace segment.

The presentation of segment results below includes a reconciliation of the changes in net sales for each segment reported in accordance with U.S. GAAP to net sales adjusted to remove the effects of acquisitions made in 2014 and 2013 and changes in foreign currency exchange rates. The effects of acquisitions and currency exchange rates on net sales are removed to allow investors and the Company to meaningfully evaluate the percentage change in net sales on a comparable basis from period to period. During the first quarter of 2013, the Company completed the acquisition of Interlube Systems Ltd. (Interlube). Results for Interlube are reported in the Mobile Industries segment. During the second quarter of 2013, the Company completed the acquisition of Hamilton Gear Ltd., d/b/a Standard Machine (Standard Machine), as well as substantially all of the assets of Smith Services, Inc. (Smith Services). During the second quarter of 2014, the Company acquired the assets of Schulz. During the fourth quarter of 2014, the Company acquired the assets of Revolvo. Results for Standard Machine, Smith Services, Schulz and Revolvo are reported in the Process Industries segment.

**MOBILE INDUSTRIES SEGMENT:**

| | **2014** | 2013 | $ Change | Change |
|---|---|---|---|---|
| Net sales | **$ 1,685.4** | $ 1,775.8 | $ (90.4) | (5.1)% |
| EBIT | **$ 65.6** | $ 193.7 | $ (128.1) | (66.1)% |
| EBIT margin | **3.9%** | 10.9% | — | (700) bps |

| | **2014** | 2013 | $ Change | % Change |
|---|---|---|---|---|
| Net sales | **$ 1,685.4** | $ 1,775.8 | $ (90.4) | (5.1)% |
| Less: Acquisitions | **3.6** | — | 3.6 | NM |
| Currency | **(17.1)** | — | (17.1) | NM |
| Net sales, excluding the impact of acquisitions and currency | **$ 1,698.9** | $ 1,775.8 | $ (76.9) | (4.3)% |

The Mobile Industries segment's net sales, excluding the impact of acquisitions and currency-rate changes, decreased 4.3% in 2014 compared to 2013, primarily due to lower volume of approximately $80 million. The lower volume was primarily driven by a reduction in sales to the light vehicle sector due to planned program exits that concluded in 2013 of approximately $110 million. In addition, heavy truck volume declined approximately $15 million, aerospace aftermarket volume declined approximately $5 million and aerospace original equipment volume declined approximately $5 million. These factors were partially offset by higher volume in the rail market sector of approximately $65 million. EBIT decreased in 2014 compared to 2013, primarily due to the impact of the aerospace business impairment and restructuring charges of approximately $125 million and the impact of lower sales volume and mix, including planned program exits of approximately $35 million. These factors were partially offset by the sale of real estate in Sao Paulo of approximately $25 million.

Sales for the Mobile Industries segment are expected to be flat to down approximately 2% in 2015 compared to 2014, reflecting organic growth primarily from the light vehicle market sector, offset by the impact of currency rate changes and a decline in the agriculture market sector. EBIT for the Mobile Industries segment is expected to increase in 2015 compared to 2014 as a result of lower impairment and restructuring charges and lower material costs, offset by the sale of real estate in Sao Paulo.

**PROCESS INDUSTRIES SEGMENT:**

| | 2014 | 2013 | $ Change | Change |
|---|---|---|---|---|
| Net sales | **$ 1,390.8** | $ 1,259.6 | $ 131.2 | 10.4 % |
| EBIT | **$ 267.1** | $ 189.3 | $ 77.8 | 41.1 % |
| EBIT margin | **19.2%** | 15.0% | — | 420 bps |

| | 2014 | 2013 | $ Change | % Change |
|---|---|---|---|---|
| Net sales | **$ 1,390.8** | $ 1,259.6 | $ 131.2 | 10.4 % |
| Less: Acquisitions | **16.0** | — | 16.0 | NM |
| Currency | **(13.3)** | — | (13.3) | NM |
| Net sales, excluding the impact of acquisitions and currency | **$ 1,388.1** | $ 1,259.6 | $ 128.5 | 10.2 % |

The Process Industries segment's net sales, excluding the impact of acquisitions and currency-rate changes, increased 10.2% for 2014 compared to 2013, primarily due to an increase in volume of approximately $120 million and favorable pricing of approximately $5 million. The higher volume was primarily due to higher demand in the wind energy market sector of approximately $75 million and higher demand from the industrial aftermarket of approximately $35 million. EBIT in 2014 increased compared to 2013 primarily due to the impact of higher volume of approximately $60 million and lower material and manufacturing costs of approximately $35 million, partially offset by unfavorable sales mix of approximately $15 million and higher selling, general and administrative expenses of approximately $10 million.

Sales for the Process Industries segment are expected to increase approximately 2% to 4% in 2015 compared to 2014, driven by organic growth in the industrial aftermarket, targeted original equipment sectors, including wind energy and military marine, and the benefit of acquisitions, partially offset by the impact of currency rate changes. EBIT for the Process Industries segment is expected to increase in 2015 compared to 2014 due to increased volume.

**CORPORATE:**

| | 2014 | 2013 | $ Change | Change |
|---|---|---|---|---|
| Corporate expenses | **$ 71.4** | $ 70.4 | $ 1.0 | 1.4 % |
| Corporate expenses % to net sales | **2.3%** | 2.3% | — | — |

Corporate expenses increased in 2014 compared to 2013 primarily due to higher expense related to incentive compensation plans and foreign currency exchange losses, which were partially offset by cost reduction initiatives.

## RESULTS OF OPERATIONS:

***2013 compared to 2012***

**OVERVIEW:**

| | 2013 | 2012 | $ Change | % Change |
|---|---|---|---|---|
| Net sales | **$ 3,035.4** | $ 3,359.5 | $ (324.1) | (9.6)% |
| Income from continuing operations | **175.5** | 331.5 | (156.0) | (47.1)% |
| Income from discontinued operations | **87.5** | 164.4 | (76.9) | (46.8)% |
| Income attributable to noncontrolling interest | **0.3** | 0.4 | (0.1) | (25.0)% |
| Net income attributable to The Timken Company | **$ 262.7** | $ 495.5 | $ (232.8) | (47.0)% |
| Diluted earnings per share: | | | | |
| Continuing operations | **$ 1.82** | $ 3.38 | $ (1.56) | (46.2)% |
| Discontinued operations | **0.92** | 1.69 | (0.77) | (45.6)% |
| Diluted earnings per share | **$ 2.74** | $ 5.07 | $ (2.33) | (46.0)% |
| Average number of shares – diluted | **95,823,728** | 97,602,481 | — | (1.8)% |

The Company reported net sales for 2013 of approximately $3.0 billion, compared to approximately $3.4 billion in 2012, a 9.6% decrease. The sales decrease reflected lower volume across most market sectors, and the effect of currency rate changes, partially offset by favorable pricing and the impact of acquisitions. The Company's net income from continuing operations for 2013, compared to 2012, was lower due to the impact of lower volume, unfavorable sales mix and higher manufacturing costs, partially offset by lower selling, general and administrative expenses, favorable pricing and lower restructuring charges. In addition, net income from continuing operations for 2013 was lower due to the U.S. Continued Dumping and Subsidy Offset Act (CDSOA) receipts, net of expense, of $108.0 million ($68.0 million after tax, or approximately $0.69 per diluted share), received in 2012.

## THE STATEMENTS OF INCOME

**SALES BY SEGMENT:**

| | 2013 | 2012 | $ Change | % Change |
|---|---|---|---|---|
| Mobile Industries | **$ 1,775.8** | $ 1,987.4 | $ (211.6) | (10.6)% |
| Process Industries | **1,259.6** | 1,372.1 | (112.5) | (8.2)% |
| Total Company | **$ 3,035.4** | $ 3,359.5 | $ (324.1) | (9.6)% |

Net sales for 2013 decreased $324.1 million, or 9.6%, compared to 2012, primarily due to lower volume of approximately $315 million across most market sectors. In addition, the decrease in sales reflected planned program exits that concluded at the end of 2013 of approximately $90 million and the effect of currency rate changes of approximately $10 million, partially offset by the impact of prior-year acquisitions of $70 million and favorable pricing of $30 million.

**GROSS PROFIT:**

| | 2013 | 2012 | $ Change | Change |
|---|---|---|---|---|
| Gross profit | **$ 868.4** | $ 1,028.0 | $ (159.6) | (15.5)% |
| Gross profit % to net sales | **28.6%** | 30.6% | — | (200) bps |
| Rationalization expenses included in cost of products sold | **$ 5.9** | $ 8.3 | $ (2.4) | (28.9)% |

Gross profit decreased in 2013 compared to 2012, primarily due to the impact of lower sales volume of approximately $130 million, higher manufacturing costs of approximately $40 million and the impact of planned program exits that concluded at the end of 2013 of approximately $35 million, partially offset by favorable pricing of approximately $30 million and the impact from prior-year acquisitions of approximately $15 million.

### SELLING, GENERAL AND ADMINISTRATIVE EXPENSES:

| | 2013 | 2012 | $ Change | Change |
|---|---|---|---|---|
| Selling, general and administrative expenses | **$ 546.6** | $ 554.5 | $ (7.9) | (1.4)% |
| Selling, general and administrative expenses % to net sales | **18.0%** | 16.5% | — | 150 bps |

The decrease in selling, general and administrative expenses of $7.9 million in 2013 compared to 2012 was primarily due to lower expenses related to incentive compensation plans of approximately $30 million, partially offset by the full year impact of acquisitions of approximately $15 million.

### IMPAIRMENT AND RESTRUCTURING CHARGES:

| | 2013 | 2012 | $ Change |
|---|---|---|---|
| Impairment charges | **$ 0.1** | $ 6.6 | $ (6.5) |
| Severance and related benefit costs | **9.2** | 18.4 | (9.2) |
| Exit costs | **(0.6)** | 4.5 | (5.1) |
| Total | **$ 8.7** | $ 29.5 | $ (20.8) |

Impairment and restructuring charges of $8.7 million in 2013 were primarily due to severance and related benefit costs of approximately $6 million due to cost-reduction initiatives relating to reductions in headcount in the bearings and power transmission business. In addition, impairment and restructuring charges for 2013 included the recognition of severance and related benefits of approximately $3 million related to the closure of the manufacturing facility in St. Thomas. Impairment and restructuring charges of $29.5 million in 2012 were primarily due to the recognition of severance and related benefits, including approximately $10.7 million of pension curtailment charges, as well as impairment charges related to the closure of the manufacturing facility in St. Thomas and the recognition of environmental remediation costs at the former manufacturing facility in Sao Paulo. Refer to *Note 11 – Impairment and Restructuring Charges* in the Notes to the Consolidated Financial Statements for additional discussion.

### INTEREST INCOME AND (EXPENSE):

| | 2013 | 2012 | $ Change | % Change |
|---|---|---|---|---|
| Interest (expense) | **$ (24.4)** | $ (31.1) | $ 6.7 | (21.5)% |
| Interest income | **$ 1.9** | $ 2.9 | $ (1.0) | (34.5)% |

Interest expense for 2013 decreased compared to 2012 primarily due to lower average debt and higher capitalized interest. Interest income decreased for 2013 compared to 2012 primarily due to lower invested cash balances.

### OTHER INCOME (EXPENSE):

| | 2013 | 2012 | $ Change | % Change |
|---|---|---|---|---|
| CDSOA receipts (expense), net | **$ (2.8)** | $ 108.0 | $ (110.8) | (102.6)% |
| Gain on sale of real estate in Sao Paulo | **5.4** | — | 5.4 | NM |
| Other income (expense) | **4.1** | (6.0) | 10.1 | (168.3)% |
| Total | **$ 6.7** | $ 102.0 | $ (95.3) | (93.4)% |

In 2013, the Company reported expenses in connection with CDSOA of $2.8 million. The Company reported CDSOA receipts, net of expense, of $108.0 million in 2012. Refer to *Note 20 – Continued Dumping and Subsidy Offset Act (CDSOA)* in the Notes to the Consolidated Financial Statements for additional information

In November 2013, the Company finalized the sale of its former manufacturing facility in Sao Paulo, resulting in a $5.4 million gain. The Company is recognizing the gain on the sale of this facility on the installment method. The Company recognized an additional gain of approximately $25 million in 2014 related to this transaction.

**INCOME TAX EXPENSE:**

| | 2013 | 2012 | $ Change | Change |
|---|---|---|---|---|
| Income tax expense | $ 114.6 | $ 186.3 | $ (71.7) | (38.5)% |
| Effective tax rate | 39.5% | 36.0% | — | 350 bps |

The effective tax rate on pretax income for 2013 was unfavorable relative to the U.S. federal statutory rate primarily due to U.S. taxation of foreign income including cash repatriation, losses at certain foreign subsidiaries where no tax benefit could be recorded, U.S. non-deductible items and U.S. state and local taxes. These factors were partially offset by discrete U.S. tax benefits, including certain settlements related to tax audits, U.S. foreign tax credits, earnings in certain foreign jurisdictions where the effective tax rate is less than 35%, the U.S. manufacturing deduction and the U.S research tax credit.

The effective tax rate for 2012 was slightly favorable relative to the U.S. federal statutory rate primarily due to earnings in certain foreign jurisdictions where the effective tax rate is less than 35%, U.S. Foreign tax credits, the U.S. manufacturing deduction and certain discrete U.S. tax benefits. These factors were partially offset by losses at certain foreign subsidiaries where no tax benefits could be recorded, U.S. state and local taxes and U.S. taxation of foreign income. The change in the effective tax rate in 2013 compared to 2012 was primarily due to U.S. taxation of foreign income, including U.S. taxation on cash repatriation, losses at certain foreign subsidiaries where no tax benefit could be recorded and higher U.S. state and local taxes, partially offset by U.S. foreign tax credits, higher U.S. manufacturing deduction and the net effect of other discrete items.

## BUSINESS SEGMENTS

The primary measurement used by management to measure the financial performance of each segment is EBIT. Refer to *Note 15 – Segment Information* in the Notes to the Consolidated Financial Statements for the reconciliation of EBIT by segment to consolidated income before income taxes.

The presentation of segment results below includes a reconciliation of the changes in net sales for each segment reported in accordance with U.S. GAAP to net sales adjusted to remove the effects of acquisitions and currency exchange rates. The effects of acquisitions and currency exchange rates on net sales are removed to allow investors and the Company to meaningfully evaluate the percentage change in net sales on a comparable basis from period to period. During the fourth quarter of 2012, the Company completed the acquisition of substantially all of the assets of Wazee Companies, LLC (Wazee). The acquisition of the assets of Wazee, which was completed on December 31, 2012, had no impact on the 2012 operating results. During the first quarter of 2013, the Company completed the acquisition of Interlube. Results for Interlube are reported in the Mobile Industries segment. During the second quarter of 2013, the Company completed the acquisition of Standard Machine, as well as substantially all of the assets of Smith Services. Results for Standard Machine, Smith Services and Wazee are reported in the Process Industries segment.

**MOBILE INDUSTRIES SEGMENT:**

| | 2013 | 2012 | $ Change | Change |
|---|---|---|---|---|
| Net sales | $ 1,775.8 | $ 1,987.4 | $ (211.6) | (10.6)% |
| EBIT | $ 193.7 | $ 245.2 | $ (51.5) | (21.0)% |
| EBIT margin | 10.9% | 12.3% | — | (140) bps |

| | 2013 | 2012 | $ Change | % Change |
|---|---|---|---|---|
| Net sales | $ 1,775.8 | $ 1,987.4 | $ (211.6) | (10.6)% |
| Less: Acquisitions | 27.0 | — | 27.0 | NM |
| Currency | (11.0) | — | (11.0) | NM |
| Net sales, excluding the impact of acquisitions and currency | $ 1,759.8 | $ 1,987.4 | $ (227.6) | (11.5)% |

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The Mobile Industries segment's net sales, excluding the impact of acquisitions and currency-rate changes, decreased 11.5% in 2013 compared to 2012, primarily due to lower volume of approximately $220 million, partially offset by favorable pricing of $10 million. The lower volume was led by a decrease in off-highway volume of approximately $105 million, and a decrease in heavy truck volume of approximately $30 million, driven by exited business. EBIT decreased in 2013 compared to 2012, primarily due to the impact of lower volume of approximately $80 million and higher manufacturing costs of approximately $35 million, partially offset by lower restructuring charges of approximately $15 million, lower raw material costs of approximately $15 million, lower selling, general and administrative expenses of approximately $10 million, favorable sale mix of approximately $10 million, favorable pricing of $10 million and a gain on the sale of the Company's former manufacturing facility in Sao Paulo of approximately $5 million. Restructuring charges related to the closure of the manufacturing facility in St. Thomas were lower in 2013 compared to 2012.

**PROCESS INDUSTRIES SEGMENT:**

| | **2013** | 2012 | $ Change | Change |
|---|---|---|---|---|
| Net sales | **$ 1,259.6** | $ 1,372.1 | $ (112.5) | (8.2)% |
| EBIT | **$ 189.3** | $ 261.8 | $ (72.5) | (27.7)% |
| EBIT margin | **15.0%** | 19.1% | — | (410) bps |

| | **2013** | 2012 | $ Change | % Change |
|---|---|---|---|---|
| Net sales | **$ 1,259.6** | $ 1,372.1 | $ (112.5) | (8.2)% |
| Less: Acquisitions | **58.8** | — | 58.8 | NM |
| Currency | **0.7** | — | 0.7 | NM |
| Net sales, excluding the impact of acquisitions and currency | **$ 1,200.1** | $ 1,372.1 | $ (172.0) | (12.5)% |

The Process Industries segment's net sales, excluding the effect of acquisitions and currency-rate changes, decreased 12.5% for 2013 compared to 2012, primarily due to lower volume of approximately $190 million, primarily offset by favorable pricing of $20 million. The lower volume was seen across all market sectors. EBIT decreased in 2013 compared to 2012 due to the impact of lower volume of approximately $80 million, the impact of higher manufacturing costs of approximately $20 million and unfavorable sales mix of approximately $15 million, partially offset by favorable pricing of approximately $20 million, lower selling, general and administrative expenses of approximately $10 million and lower material costs of approximately $10 million.

**CORPORATE:**

| | **2013** | 2012 | $ Change | Change |
|---|---|---|---|---|
| Corporate expenses | **$ 70.4** | $ 69.0 | $ 1.4 | 2.0 % |
| Corporate expenses % to net sales | **2.3%** | 2.1% | — | 20 bps |

Corporate expenses decreased in 2013 compared to 2012, primarily due to lower expense related to incentive compensation plans.

# THE BALANCE SHEETS

The following discussion is a comparison of the Consolidated Balance Sheets at December 31, 2014 and 2013.

**CURRENT ASSETS:**

| | December 31, | | | |
|---|---|---|---|---|
| | **2014** | 2013 | $ Change | % Change |
| Cash and cash equivalents | **$ 278.8** | $ 384.6 | $ (105.8) | (27.5)% |
| Restricted cash | **15.3** | 15.1 | 0.2 | 1.3 % |
| Accounts receivable, net | **475.7** | 444.0 | 31.7 | 7.1 % |
| Inventories, net | **585.5** | 582.6 | 2.9 | 0.5 % |
| Deferred income taxes | **49.9** | 56.2 | (6.3) | (11.2)% |
| Deferred charges and prepaid expenses | **25.2** | 26.8 | (1.6) | (6.0)% |
| Other current assets | **51.5** | 61.7 | (10.2) | (16.5)% |
| Current assets, discontinued operations | **—** | 366.5 | (366.5) | (100.0)% |
| Total current assets | **$ 1,481.9** | $ 1,937.5 | $ (455.6) | (23.5)% |

Cash and cash equivalents decreased primarily due to the Company's purchase of approximately 5.2 million of its common shares for an aggregate of $270.9 million during 2014. Accounts receivable, net increased as a result of higher sales in December 2014 compared to December 2013, partially offset by higher allowance for doubtful accounts of $3.6 million. Other current assets decreased primarily due to the liquidation of a portion of the Company's short-term investments of approximately $10 million. Current assets, discontinued operations at December 31, 2013 related to the Spinoff on June 30, 2014 and primarily included accounts receivable and inventory.

**PROPERTY, PLANT AND EQUIPMENT, NET:**

| | December 31, | | | |
|---|---|---|---|---|
| | **2014** | 2013 | $ Change | % Change |
| Property, plant and equipment | **$ 2,164.1** | $ 2,395.3 | $ (231.2) | (9.7)% |
| Less: allowances for depreciation | **(1,383.6)** | (1,539.5) | 155.9 | 10.1 % |
| Property, plant and equipment, net | **$ 780.5** | $ 855.8 | $ (75.3) | (8.8)% |

The decrease in property, plant and equipment, net in 2014 was primarily due to the reclassification of approximately $45 million of capitalized software from property, plant and equipment to intangible assets in 2014, and the impact of currency-rate changes of approximately $20 million. See *"Other Disclosures – Capital Expenditures"* for more information.

**OTHER ASSETS:**

| | December 31, | | | |
|---|---|---|---|---|
| | **2014** | 2013 | $ Change | % Change |
| Goodwill | **$ 259.5** | $ 346.1 | $ (86.6) | (25.0)% |
| Non-current pension assets | **176.2** | 223.5 | (47.3) | (21.2)% |
| Other intangible assets | **239.8** | 207.4 | 32.4 | 15.6 % |
| Other non-current assets | **63.5** | 58.4 | 5.1 | 8.7 % |
| Non-current assets, discontinued operations | **—** | 849.2 | (849.2) | (100.0)% |
| Total other assets | **$ 739.0** | $ 1,684.6 | $ (945.6) | (56.1)% |

The decrease in goodwill was primarily due to the impairment of two of the Company's aerospace reporting units in 2014. The decrease in non-current pension assets was primarily due to a decrease in the discount rate used to measure the Company's U.S. defined benefit pension plans, as well as the adoption of the new RP-2014 mortality tables. The increase in other intangible assets was primarily due to the reclassification of approximately $45 million of capitalized software from property, plant and equipment to other intangible assets, partially offset by current year amortization expense. Non-current assets, discontinued operations at December 31, 2013 related to the Spinoff and primarily included property, plant and equipment.

**CURRENT LIABILITIES:**

| | December 31, | | | |
|---|---|---|---|---|
| | **2014** | 2013 | $ Change | % Change |
| Short-term debt | **$ 7.4** | $ 18.6 | $ (11.2) | (60.2)% |
| Accounts payable | **143.9** | 139.9 | 4.0 | 2.9 % |
| Salaries, wages and benefits | **146.7** | 131.1 | 15.6 | 11.9 % |
| Income taxes payable | **80.2** | 106.7 | (26.5) | (24.8)% |
| Other current liabilities | **155.0** | 180.8 | (25.8) | (14.3)% |
| Current portion of long-term debt | **0.6** | 250.7 | (250.1) | (99.8)% |
| Current liabilities, discontinued operations | **—** | 152.3 | (152.3) | (100.0)% |
| Total current liabilities | **$ 533.8** | $ 980.1 | $ (446.3) | (45.5)% |

The decrease in short-term debt during 2014 was primarily due to lower borrowings under foreign lines of credit. Salaries, wages and benefits increased primarily due to the increase in accruals for incentive based compensation plans. The decrease in income taxes payable was primarily due to lower current year income tax expense compared to 2013, as well as higher taxes paid. The decrease in other current liabilities was primarily due to the recognition of deferred revenue related to the sale of the Company's former manufacturing site in Sao Paulo, as well as a reduction in accrued restructuring charges. The decrease in the current portion of long-term debt was primarily due to the Company's $250 million aggregate principal amount of fixed-rate 6.0% senior unsecured notes (2014 Notes) being repaid at maturity in September 2014. Current liabilities, discontinued operations at December 31, 2013 related to the Spinoff and primarily included accounts payable and other accruals.

**NON-CURRENT LIABILITIES:**

| | December 31, | | | |
|---|---|---|---|---|
| | **2014** | 2013 | $ Change | % Change |
| Long-term debt | **$ 522.1** | $ 176.4 | $ 345.7 | 196.0 % |
| Accrued pension cost | **165.9** | 159.0 | 6.9 | 4.3 % |
| Accrued postretirement benefits cost | **141.8** | 138.3 | 3.5 | 2.5 % |
| Deferred income taxes | **4.1** | 82.9 | (78.8) | (95.1)% |
| Other non-current liabilities | **44.6** | 55.9 | (11.3) | (20.2)% |
| Non-current liabilities, discontinued operations | **—** | 236.7 | (236.7) | (100.0)% |
| Total non-current liabilities | **$ 878.5** | $ 849.2 | $ 29.3 | 3.5 % |

The increase in long-term debt during 2014 was primarily due to the issuance of $350 million aggregate principal amount of fixed-rate 3.875% senior unsecured notes that mature on September 1, 2024 (2024 Notes). The increase in accrued pension cost was primarily due to a decrease in the discount rate used to measure the projected benefit obligation, as well as the adoption of the new RP-2014 mortality tables. The increase in accrued postretirement benefits cost was primarily due to a decrease in the discount rate used to measure the accumulated benefit obligation. The decrease in deferred income taxes related primarily to the reduction of pre-paid pension assets, impairment of intangible assets and depreciation of fixed assets. Non-current liabilities, discontinued operations at December 31, 2013 related to the Spinoff and primarily included long-term debt, accrued pension cost and accrued postretirement benefits cost.

**SHAREHOLDERS' EQUITY:**

| | December 31, | | | |
|---|---|---|---|---|
| | **2014** | 2013 | $ Change | % Change |
| Common stock | **$ 952.5** | $ 949.5 | $ 3.0 | 0.3 % |
| Earnings invested in the business | **1,615.4** | 2,586.4 | (971.0) | (37.5)% |
| Accumulated other comprehensive loss | **(482.5)** | (626.1) | 143.6 | (22.9)% |
| Treasury shares | **(509.2)** | (273.2) | (236.0) | (86.4)% |
| Noncontrolling interest | **12.9** | 12.0 | 0.9 | 7.5 % |
| Total equity | **$ 1,589.1** | $ 2,648.6 | $ (1,059.5) | (40.0)% |

Earnings invested in the business decreased in 2014 primarily due to the Spinoff. The decrease in accumulated other comprehensive loss was primarily due to a $228.4 million after-tax adjustment related to the Spinoff, partially offset by a pension and postretirement liability adjustment of $43.1 million and a foreign currency translation adjustment of $41.3 million. The pension and postretirement liability adjustment was primarily due to a decrease in the discount rate used to measure the pension and postretirement plan obligations, as well as the adoption of the new RP-2014 mortality tables, partially offset by higher than expected returns on plan assets, amortization of net actuarial losses and pension settlement charges. The foreign currency translation adjustment was due to the strengthening of the U.S. dollar against most other currencies. The increase in treasury shares was primarily due to the Company's purchase during 2014 of 5.2 million of its common shares for an aggregate of $270.9 million, partially offset by shares issued pursuant to stock compensation plans.

## CASH FLOWS

| | 2014 | 2013 | $ Change |
|---|---|---|---|
| Net cash provided by operating activities – continuing operations | **$ 281.5** | $ 292.8 | $ (11.3) |
| Net cash provided by operating activities – discontinued operations | **25.5** | 137.2 | (111.7) |
| Net cash provided by operating activities | **307.0** | 430.0 | (123.0) |
| Net cash used by investing activities – continuing operations | **(117.7)** | (184.1) | 66.4 |
| Net cash used by investing activities – discontinued operations | **(77.0)** | (191.9) | 114.9 |
| Net cash used by investing activities | **(194.7)** | (376.0) | 181.3 |
| Net cash used by financing activities – continuing operations | **(302.2)** | (249.3) | (52.9) |
| Net cash provided by financing activities – discontinued operations | **100.0** | — | 100.0 |
| Net cash used by financing activities | **(202.2)** | (249.3) | 47.1 |
| Effect of exchange rate changes on cash | **(15.9)** | (6.5) | (9.4) |
| (Decrease) in cash and cash equivalents | **$ (105.8)** | $ (201.8) | $ 96.0 |

Operating activities provided net cash of $307.0 million in 2014, compared to $430.0 million in 2013. The decrease in cash from operating activities was primarily due to lower cash provided by discontinued operations and higher cash used for income taxes and working capital items, partially offset by lower pension contributions and other postretirement benefit payments and an increase in income from continuing operations adjusted for impairment charges. Net cash provided by discontinued operations decreased to $25.5 million in 2014 from $137.2 million in 2013 primarily as a result of separation costs incurred to effect the Spinoff. Income taxes represented a use of cash of $15.3 million in 2014, after representing a source of cash of $67.5 million in 2013, as the Company incurred lower tax expense and paid higher taxes in 2014 compared to 2013. Net income from continuing operations decreased $30.7 million in 2014 compared to 2013, largely due to the impact from $98.9 million of impairment charges that were incurred in 2014. Pension and other postretirement benefit contributions and payments were $49.9 million in 2014, compared to $93.4 million in 2013.

The following chart displays the impact of working capital items on cash during 2014 and 2013:

| | 2014 | 2013 |
|---|---|---|
| Cash Provided (Used): | | |
| Accounts receivable | **$ (48.3)** | $ (4.6) |
| Inventories | **(26.8)** | 34.6 |
| Trade accounts payable | **8.0** | 0.9 |
| Other accrued expenses | **2.2** | (39.6) |

Investing activities used cash of $194.7 million in 2014 compared to $376.0 million in 2013. The decrease was primarily due to a $114.9 million decrease in investing activities from discontinued operations, a $42.5 million decrease in cash used for acquisitions, a $6.8 million decrease in cash used for capital expenditures, as well as a $18.9 million increase in cash from the disposal of property, plant and equipment primarily due to the sale of real estate in Sao Paulo and South Africa.

Net cash used by financing activities was $202.2 million and $249.3 million in 2014 and 2013, respectively. The decreased cash used by financing activities was primarily due to net cash provided by discontinued operations and a decrease in net borrowings, partially offset by increased purchases of common shares in 2014 and cash transferred to TimkenSteel. The Company purchased 5.2 million of its common shares for an aggregate of $270.9 million in 2014 after purchasing 3.4 million of its common shares for an aggregate of $189.2 million in 2013. In addition, the Company transferred cash of $46.5 million to TimkenSteel in connection with the Spinoff. Net cash from discontinued operations provided $100 million in the first six months of 2014 as TimkenSteel borrowed $100 million under its line of credit prior to the Spinoff. Net borrowings provided cash of $85.7 million in 2014 after using cash of $3.2 million in 2013.

## LIQUIDITY AND CAPITAL RESOURCES

Total debt was $530.1 million and $445.7 million at December 31, 2014 and 2013, respectively. Debt exceeded cash and cash equivalents by $236.0 million and $46.0 million at December 31, 2014 and 2013, respectively. The ratio of net debt to capital was 12.9% and 1.7% at December 31, 2014 and 2013, respectively.

Reconciliation of total debt to net debt and the ratio of net debt to capital:

**NET DEBT:**

| | December 31, | |
|---|---|---|
| | **2014** | 2013 |
| Short-term debt | **$ 7.4** | $ 18.6 |
| Current portion of long-term debt | **0.6** | 250.7 |
| Long-term debt | **522.1** | 176.4 |
| Total debt | **$ 530.1** | $ 445.7 |
| Less: Cash and cash equivalents | **278.8** | 384.6 |
| Restricted cash | **15.3** | 15.1 |
| Net debt | **$ 236.0** | $ 46.0 |

**RATIO OF NET DEBT TO CAPITAL:**

| | December 31, | |
|---|---|---|
| | **2014** | 2013 |
| Net debt | **$ 236.0** | $ 46.0 |
| Total equity | **1,589.1** | 2,648.6 |
| Capital (net debt + total equity) | **$ 1,825.1** | $ 2,694.6 |
| Ratio of net debt to capital | **12.9%** | 1.7% |

The Company presents net debt because it believes net debt is more representative of the Company's financial position than total debt due to the amount of cash and cash equivalents.

At December 31, 2014, approximately $130.9 million, or 46.9%, of the Company's cash and cash equivalents resided in jurisdictions outside the United States. Repatriation of these funds to the United States could be subject to domestic and foreign taxes and some portion may be subject to governmental restrictions. Part of the Company's strategy is to grow in attractive market sectors, many of which are outside the United States. This strategy may include making investments in facilities and equipment and potential new acquisitions. The Company plans to fund these investments, as well as meet working capital requirements, with cash and cash equivalents and unused lines of credit within the geographic location of these investments when possible.

On April 30, 2014, the Company amended its three-year Asset Securitization Agreement, reducing its aggregate borrowing availability from $200 million to $100 million. The Asset Securitization Agreement matures on November 30, 2015, is subject to certain borrowing base limitations and is secured by certain domestic trade receivables of the Company. At December 31, 2014, the Company had no outstanding borrowings under the Asset Securitization Agreement; however, certain borrowing base limitations reduced the availability under the Asset Securitization Agreement to $72.7 million.

The Company has a $500 million Senior Credit Facility that matures on May 11, 2016. At December 31, 2014, the Company had no outstanding borrowings under the Senior Credit Facility but had letters of credit outstanding totaling $8.6 million, which reduced the availability under the Senior Credit Facility to $491.4 million. Under the Senior Credit Facility, the Company has two financial covenants: a consolidated leverage ratio and a consolidated interest coverage ratio. At December 31, 2014, the Company was in full compliance with the covenants under the Senior Credit Facility. The maximum consolidated leverage ratio permitted under the Senior Credit Facility is 3.25 to 1.0. As of December 31, 2014, the Company's consolidated leverage ratio was 1.03 to 1.0. The minimum consolidated interest coverage ratio permitted under the Senior Credit Facility is 4.0 to 1.0. As of December 31, 2014, the Company's consolidated interest coverage ratio was 16.32 to 1.0.

The interest rate under the Senior Credit Facility is based on the Company's consolidated leverage ratio. In addition, the Company pays a facility fee based on the consolidated leverage ratio multiplied by the aggregate commitments of all of the lenders under the Senior Credit Facility.

Other sources of liquidity include short-term and long-term lines of credit for certain of the Company's foreign subsidiaries, which provide for borrowings up to $234.0 million in the aggregate. The majority of these lines are uncommitted. At December 31, 2014, the Company had borrowings outstanding of $7.4 million and guarantees of $5.8 million, which reduced the availability under these facilities to $220.8 million.

The Company expects that any cash requirements in excess of cash on hand will be met by the committed funds available under its Asset Securitization Agreement and the Senior Credit Facility. Management believes it has sufficient liquidity to meet its obligations through at least the term of the Senior Credit Facility.

The Company expects to remain in compliance with its debt covenants. However, the Company may need to limit its borrowings under the Senior Credit Facility or other facilities in order to remain in compliance. As of December 31, 2014, the Company could have borrowed the full amounts available under the Senior Credit Facility and Asset Securitization Agreement, and would have still been in compliance with its debt covenants.

In August 2014, the Company issued $350 million of fixed-rate unsecured notes that mature in September 2024. The Company used a portion of the net proceeds from this issuance to repay the $250 million of fixed-rated unsecured notes that matured on September 15, 2014.

The Company expects to generate cash from continuing operations of approximately $345 million in 2015, an increase of approximately $65 million, or 23%, compared to 2014, as the Company anticipates higher income from continuing operations, excluding non-cash impairment and pension settlement charges. Pension contributions are expected to be approximately $15 million in 2015, compared to $21.1 million in 2014. The Company expects capital expenditures of approximately 4% of sales in 2015, compared to 4.2% of sales in 2014.

## CONTRACTUAL OBLIGATIONS

The Company's contractual debt obligations and contractual commitments outstanding as of December 31, 2014 were as follows:

**PAYMENTS DUE BY PERIOD:**

| Contractual Obligations | Total | Less than 1 Year | 1–3 Years | 3–5 Years | More than 5 Years |
|---|---|---|---|---|---|
| Interest payments | **$ 272.4** | **$ 25.8** | **$ 49.5** | **$ 48.4** | **$ 148.7** |
| Long-term debt, including current portion | **522.7** | **0.6** | **20.7** | **—** | **501.4** |
| Short-term debt | **7.4** | **7.4** | **—** | **—** | **—** |
| Operating leases | **96.3** | **28.6** | **37.9** | **19.5** | **10.3** |
| Purchase commitments | **44.8** | **16.0** | **7.3** | **21.5** | **—** |
| Retirement benefits | **1,736.9** | **206.9** | **353.0** | **362.7** | **814.3** |
| Total | **$ 2,680.5** | **$ 285.3** | **$ 468.4** | **$ 452.1** | **$ 1,474.7** |

The interest payments beyond five years primarily relate to medium-term notes that mature over the next 16 years.

Purchase commitments are defined as an agreement to purchase goods or services that are enforceable and legally binding on the Company. Included in purchase commitments above are certain obligations related to take or pay contracts, capital commitments, service agreements and utilities. Many of these commitments relate to take or pay contracts, in which the Company guarantees payment to ensure availability of products or services. These purchase commitments do not represent the entire anticipated purchases in the future, but represent only those items for which the Company is contractually obligated. The majority of the products and services purchased by the Company are purchased as needed, with no commitment.

Retirement benefits represent pension and health care payments, including lump sum distributions, expected to be paid to retirees or their beneficiaries over the next ten years. These payments are largely covered by pension and postretirement benefit plan assets. The table above does not reflect the group annuity contract purchased on January 22, 2015, which transferred approximately $600 million of pension obligations to Prudential. Refer to *Note 21 – Subsequent Events* in the Notes to the Consolidated Financial Statements for additional information.

During 2014, the Company made cash contributions of approximately $21.1 million to its global defined benefit pension plans. The Company currently expects to make contributions to its global defined benefit pension plans totaling approximately $15 million in 2015. Returns for the Company's global defined benefit pension plan assets in 2014 were 11.15%, above the expected rate of return of 7.25% due to broad increases in global equity markets. The higher returns positively impacted the funded status of the plans at the end of 2014 and are expected to result in lower pension expense in future years. Refer to *Note 13 – Retirement Benefit Plans* and *Note 14 – Postretirement Benefit Plans* in the Notes to the Consolidated Financial Statements for additional information.

The Company's 2012 common share purchase plan authorized the Company to buy, in the open market or in privately negotiated transactions, up to 10 million common shares, which are to be held as treasury shares and used for specified purposes. On June 13, 2014, the Company's Board of Directors authorized an additional 10 million common shares for repurchase under this plan. The authorization expires on December 31, 2015. During 2014, the Company purchased 5.2 million of its common shares for approximately $270.9 million in the aggregate under this plan. As of December 31, 2014, 8.9 million common shares remain authorized for purchase under this plan.

As disclosed in *Note 10 – Contingencies* and *Note 16 – Income Taxes* in the Notes to the Consolidated Financial Statements, the Company has exposure for certain legal and tax matters.

As of December 31, 2014, the Company had approximately $57.5 million of total gross unrecognized tax benefits. The Company anticipates a decrease in its unrecognized tax positions of $40 million to $45 million during the next 12 months. The anticipated decrease is primarily due to settlements with tax authorities. Future tax positions are not known at this time and therefore not included in the above summary of the Company's fixed contractual obligations. Refer to *Note 16 – Income Taxes* in the Notes to the Consolidated Financial Statements for additional information.

The Company does not have any off-balance sheet arrangements with unconsolidated entities or other persons.

## RECENTLY ADOPTED ACCOUNTING PRONOUNCMENTS

Information required for this Item is incorporated by reference to *Note 1 – Significant Accounting Policies* in the Notes to the Consolidated Financial Statements.

## CRITICAL ACCOUNTING POLICIES AND ESTIMATES

The Company's financial statements are prepared in accordance with accounting principles generally accepted in the United States. The preparation of these financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the periods presented. The following paragraphs include a discussion of some critical areas that require a higher degree of judgment, estimates and complexity.

**REVENUE RECOGNITION:**

The Company recognizes revenue when title passes to the customer. This occurs at the shipping point except for goods sold by certain foreign entities and certain exported goods, where title passes when the goods reach their destination. Selling prices are fixed based on purchase orders or contractual arrangements. Shipping and handling costs billed to customers are included in net sales and the related costs are included in cost of products sold in the Consolidated Statements of Income.

The Company recognizes a portion of its revenues on the percentage of completion method. In 2014 and 2013, the Company recognized approximately $50 million and $55 million, respectively, in net sales under the percentage-of-completion method.

**INVENTORY:**

Inventories are valued at the lower of cost or market, with approximately 48% valued by the last-in, first-out (LIFO) method and the remaining 52% valued by the first-in, first-out (FIFO) method. The majority of the Company's domestic inventories are valued by the LIFO method, and all of the Company's international inventories are valued by the FIFO method. An actual valuation of the inventory under the LIFO method can be made only at the end of each year based on the inventory levels and costs at that time. Accordingly, interim LIFO calculations are based on management's estimates of expected year-end inventory levels and costs. Because these are subject to many factors beyond management's control, annual results may differ from interim results as they are subject to the final year-end LIFO inventory valuation. The Company recognized an increase in its LIFO reserve of $0.4 million during 2014 compared to a decrease in its LIFO reserve of $3.8 million during 2013.

**GOODWILL:**

The Company tests goodwill and indefinite-lived intangible assets for impairment at least annually. The Company performs its annual impairment test as of October first, after the annual forecasting process is completed. Furthermore, goodwill is reviewed for impairment whenever events or changes in circumstances indicate that the carrying value may not be recoverable. Each interim period, management of the Company assesses whether or not an indicator of impairment is present that would necessitate that a goodwill impairment analysis be performed in an interim period other than during the fourth quarter.

The goodwill impairment analysis is a two-step process. Step one compares the carrying amount of the reporting unit to its estimated fair value. To the extent that the carrying value of the reporting unit exceeds its estimated fair value, step two is performed, where the reporting unit's carrying value of goodwill is compared to the implied fair value of goodwill. To the extent that the carrying value of goodwill exceeds the implied fair value of goodwill, impairment exists and must be recognized.

The Company reviews goodwill for impairment at the reporting unit level. The Mobile Industries segment has four reporting units and the Process Industries segment has two reporting units. The reporting units within the Mobile Industries segment are Mobile Industries, Aerospace Bearing, Aerospace Transmissions and Aerospace Aftermarket. The reporting units within the Process Industries segment are Process Industries and Industrial Services.

The Company prepares its goodwill impairment analysis by comparing the estimated fair value of each reporting unit, using an income approach (a discounted cash flow model), as well as a market approach, with its carrying value. The income approach and market approach are weighted in arriving at fair value based on the relative merits of the methods used and the quantity and quality of collected data to arrive at the indicated fair value.

During the third quarter of 2014, the Company determined there was an indicator for impairment for two of its three Aerospace reporting units, specifically Aerospace Transmissions and Aerospace Aftermarket, within its former Aerospace segment (now included in the Mobile Industries segment) as a result of declining sales forecasts and financial performance within the reporting units. The Company utilized currently updated forecasts for the income approach as part of the goodwill impairment analysis. As a result of the lower earnings and cash flow forecasts, the Company determined that the goodwill associated with the Aerospace Transmissions and the Aerospace Aftermarket reporting units could not support the carrying value of their goodwill. As a result, the Company recorded a pretax impairment charge of $86.3 million during the third quarter of 2014, which was reported in impairment and restructuring charges in the Consolidated Statement of Income. Refer to *Note 8 - Goodwill and Other Intangible Assets* in the Notes to the Consolidated Financial Statements for additional information.

During the fourth quarter of 2014, the Company completed its annual goodwill impairment testing with no further impairment identified.

The income approach requires several assumptions including future sales growth, EBIT (earnings before interest and taxes) margins and capital expenditures. The Company's reporting units each provide their forecast of results for the next three years. These forecasts are the basis for the information used in the discounted cash flow model. The discounted cash flow model also requires the use of a discount rate and a terminal revenue growth rate (the revenue growth rate for the period beyond the three years forecasted by the reporting units), as well as projections of future operating margins (for the period beyond the forecasted three years). During the fourth quarter of 2014, the Company used a discount rate for its reporting units of 10.5% to 13.0% and a terminal revenue growth rate of 3%.

The market approach requires several assumptions including sales and EBITDA (earnings before interest, taxes, depreciation and amortization) multiples for comparable companies that operate in the same markets as the Company's reporting units. During the fourth quarter of 2014, the Company used sales multiples of 0.75 to 1.80 for its reporting units. During the fourth quarter of 2014, the Company used EBITDA multiples of 6.0 to 9.0 for its reporting units.

As of December 31, 2014, the Company had $259.5 million of goodwill on its Consolidated Balance Sheet, of which $89.6 million was attributable to the Mobile Industries segment and $169.9 million was attributable to the Process Industries segment. See *Note 8 – Goodwill and Other Intangible Assets* in the Notes to Consolidated Financial Statements for the carrying amount of goodwill by segment.

The fair value of the Aerospace Bearing and Industrial Services reporting units was $225.3 million and $356.7 million, respectively, compared to their carrying value of $205.9 million and $294.8 million, respectively. The fair value of the Mobile Industries and Process Industries reporting units exceeded its carrying value by a significant amount. As a result, the Company did not recognize any goodwill impairment charges during the fourth quarter of 2014.

A 30 basis point increase in the discount rate would have resulted in the Aerospace Bearing reporting units failing step one of the goodwill impairment analysis, which would have required the completion of step two of the goodwill impairment analysis to arrive at a potential goodwill impairment loss. A 300 basis point increase in the discount rate would have resulted in the Industrial Services reporting unit failing step one of the goodwill impairment analysis. The projected cash flows could have declined by 4.2% for the Aerospace Bearing reporting unit and the fair value would have still exceeded its carrying value. The projected cash flows could have declined by as much as 29.3% for the Industrial Services reporting unit and the fair value would have still exceeded its carrying value.

In 2014, the income approach for the Aerospace Bearing and Industrial Services reporting units was weighted by 70% and the market approach was weighted by 30% in arriving at fair value. The 70/30 weighting was selected to give consideration for the fact that the metrics for the last twelve months for the Aerospace Bearing and Industrial Services reporting units were not reflective of expected performance and the discounted-cash flow model provided a more normalized view of future operating conditions for the Aerospace Bearing and Industrial Services reporting units. Had the Company used a 50/50 weighting, the Company would still have passed step one of the goodwill impairment test for the Aerospace Bearing and Industrial Services reporting units for the year ended December 31, 2014.

**RESTRUCTURING COSTS:**

The Company's policy is to recognize restructuring costs in accordance with Accounting Standards Codification (ASC) Topic 420, "Exit or Disposal Cost Obligations," and ASC Topic 712, "Compensation and Non-retirement Post-Employment Benefits." Detailed contemporaneous documentation is maintained and updated to ensure that accruals are properly supported. If management determines that there is a change in estimate, the accruals are adjusted to reflect this change.

**INCOME TAXES:**

The Company, which is subject to income taxes in the United States and numerous non-U.S. jurisdictions, accounts for income taxes in accordance with ASC Topic 740, "Income Taxes." Deferred tax assets and liabilities are recorded for the future tax consequences attributable to differences between financial statement carrying amounts of existing assets and liabilities and their respective tax bases, as well as net operating losses and tax credit carryforwards. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which temporary differences are expected to be recovered or settled. The Company records valuation allowances against deferred tax assets by tax jurisdiction when it is more likely than not that such assets will not be realized. In determining the need for a valuation allowance, the historical and projected financial performance of the entity recording the net deferred tax asset is considered along with any other pertinent information. Deferred tax assets relate primarily to pension and postretirement benefit obligations in the United States, which the Company believes are more likely than not to result in future tax benefits.

In the ordinary course of the Company's business, there are many transactions and calculations where the ultimate income tax determination is uncertain. The Company is regularly under audit by tax authorities. Accruals for uncertain tax positions are provided for in accordance with the requirements of ASC Topic 740. The Company records interest and penalties related to uncertain tax positions as a component of income tax expense.

Significant management judgment is required in determining the provision for income taxes, deferred tax assets and liabilities, valuation allowances against deferred tax assets, and accruals for uncertain tax positions.

**BENEFIT PLANS:**

The Company sponsors a number of defined benefit pension plans that cover eligible associates. The Company also sponsors several funded and unfunded postretirement plans that provide health care and life insurance benefits for eligible retirees and their dependents. These plans are accounted for in accordance with ASC Topic 715-30, "Defined Benefit Plans – Pension," and ASC Topic 715-60, "Defined Benefit Plans – Other Postretirement."

The measurement of liabilities related to these plans is based on management's assumptions related to future events, including discount rates, rates of return on pension plan assets, rates of compensation increases and health care cost trend rates. Management regularly evaluates these assumptions and adjusts them as required and appropriate. Other plan assumptions are also reviewed on a regular basis to reflect recent experience and the Company's future expectations. Actual experience that differs from these assumptions may affect future liquidity, expense and the overall financial position of the Company. While the Company believes that current assumptions are appropriate, significant differences in actual experience or significant changes in these assumptions may materially affect the Company's pension and other postretirement employee benefit obligations and its future expense and cash flow.

The discount rate is used to calculate the present value of expected future pension and postretirement cash flows as of the measurement date. The Company establishes the discount rate by constructing a notional portfolio of high-quality corporate bonds and matching the coupon payments and bond maturities to projected benefit payments under the Company's pension and postretirement welfare plans. The bonds included in the portfolio are generally non-callable. A lower discount rate will result in a higher benefit obligation; conversely, a higher discount rate will result in a lower benefit obligation. The discount rate is also used to calculate the annual interest cost, which is a component of net periodic benefit cost.

The expected rate of return on plan assets is determined by analyzing the historical long-term performance of the Company's pension plan assets, as well as the mix of plan assets between equities, fixed income securities and other investments, the expected long-term rate of return expected for those asset classes and long-term inflation rates. Short-term asset performance can differ significantly from the expected rate of return, especially in volatile markets. A lower-than-expected rate of return on pension plan assets will increase pension expense and future contributions.

**DEFINED BENEFIT PENSION PLANS:**

The Company recognized net periodic benefit cost of $54.6 million in 2014 for defined benefit pension plans, excluding the steel business spunoff on June 30, 2014, compared to $45.9 million in 2013. The increase in net periodic cost was primarily due to higher pension settlement charges and lower expected rate of return, partially offset by lower amortization of net actuarial losses. The higher pension settlement charges of $33.5 million for 2014, compared to $7.2 million for 2013, was the result of lump sum distributions in 2014 for retirees and a special lump sum offering to certain deferred vested participants. Pension settlement charges in 2013 related to the closure of the Company's manufacturing facility in St. Thomas. The lower expected return from plan assets for 2014, compared to 2013, was due to the impact of a 75 basis point reduction in the expected rate of return on pension plan assets. The lower amortization of net actuarial losses was primarily due to a 100 basis point reduction in the discount rate used to measure the defined benefit pension obligation from 4.0% at December 31, 2012 to 5.02% at December 31, 2013. The discount rate used to remeasure the defined benefit pension obligation as a result of the spinoff of TimkenSteel at April 30, 2014 was 4.68% also resulted in lower amortization compared to 2013. Net actuarial losses are amortized over the average remaining service period of participants in the defined benefit pension plans.

In 2015, the Company expects net periodic benefit cost to increase to approximately $273 million for defined benefit pension plans. The expected increase is primarily due to higher pension settlement charges and a lower expected rate of return on plan assets, partially offset by lower amortization of net actuarial losses and lower interest cost. Pension settlement charges are expected to increase approximately $210 million. The Company entered into an agreement on January 22, 2015 pursuant to which the Plan purchased a group annuity contract from Prudential to transfer approximately $600 million of its pension obligations related to one of its U.S. defined benefit pension plans. This is expected to result in a pension settlement charge of approximately $220 million. The lower expected return from plan assets for 2015 is primarily due to a 125 basis point reduction in the expected return on pension assets for 2014. The decrease in the expected rate of return is due to the Company's move to a higher level of debt securities, offset by a lower level of equity securities to maintain its overfunded status on U.S. pension plans.

Interest cost is expected to decrease in 2015, compared to 2014, primarily due to a decrease in the Company's discount rate used for expense purposes from 5.02% for the first four months of 2014 and 4.68% for the last eight months of 2014 compared to 4.20% for 2015. Amortization of net actuarial losses is expected to decrease as a result of the impact of pension settlement charges that were recorded in 2014 and will be recorded in 2015, as well as favorable asset returns over the last several years, partially offset by a reduction in the discount rate to measure the pension obligation from 4.68% at April 30, 2014 (the measurement date for the spinoff of the defined benefit pension plans related to TimkenSteel) to 4.20% at December 31, 2014 and the adoption of the new RP-2014 mortality tables. The weighted-average amortization period for the Company's global defined pension plans is approximately 11 years.

The Company expects to contribute approximately $15 million to its defined benefit pension plans in 2015 compared to $21.1 million in 2014.

The following table below presents a reconciliation of the cumulative net actuarial losses at December 31, 2009 and the cumulative net actuarial losses at December 31, 2014:

| | | |
|---|---|---|
| Net actuarial losses at December 31, 2009 | | $ 1,072.3 |
| Plus/minus actuarial (gains) and losses recognized: | | |
| Net actuarial gains recognized in 2010 | $ (51.1) | |
| Net actuarial losses recognized in 2011 | 404.6 | |
| Net actuarial losses recognized in 2012 | 263.1 | |
| Net actuarial gains recognized in 2013 | (376.3) | |
| Net actuarial losses recognized in 2014 | 161.2 | |
| | | 401.5 |
| Minus amortization of net actuarial losses: | | |
| Amortization of net actuarial losses in 2010 | $ (51.9) | |
| Amortization of net actuarial losses in 2011 | (56.0) | |
| Amortization of net actuarial losses in 2012 | (83.3) | |
| Amortization of net actuarial losses in 2013 | (116.8) | |
| Amortization of net actuarial losses in 2014 | (60.9) | |
| | | (368.9) |
| Curtailment loss recognized in 2012 | | (9.5) |
| Settlement loss recognized in 2013 | | (7.2) |
| Settlement loss recognized in 2014 | | (33.5) |
| Spinoff of TimkenSteel | | (347.4) |
| Foreign currency Impact | | (8.5) |
| Net actuarial losses at December 31, 2014 | | $ 698.8 |

During the period between December 31, 2009 and December 31, 2014, the Company recognized net actuarial losses totaling $401.5 million for defined benefit pension plans. These actuarial losses primarily occurred in 2011, 2012 and 2014, offset by gains in 2010 and 2013. In 2011, the net actuarial loss of $404.6 million was primarily due to a 75 basis point reduction in the Company's discount rate used to measure its defined benefit pension obligation. The change in the discount rate accounted for $234.1 million of the net actuarial loss. The remaining portion of the net actuarial loss for 2011 was due to lower than expected asset returns of $100.4 million and other changes in actuarial assumptions of $70.1 million.

In 2012, the net actuarial loss of $263.1 million was primarily due to a 100 basis point reduction in the Company's discount rate used to measure its defined benefit pension obligation. The change in the discount rate accounted for approximately $370 million of the net actuarial loss. Net actuarial losses as a result of the discount rate were partially offset by higher than expected asset returns of approximately $140 million (a net asset gain of $361.7 million on actual assets in 2012, or positive 13.8% on pension plan assets of $3.1 billion, compared to an expected return of $221.1 million, or 8.25%, in 2012). The remaining portion of the net actuarial loss for 2012 was due to other changes in actuarial assumptions.

In 2014, the net actuarial loss of $161.2 million was primarily due to a 82 basis point reduction in the Company's discount rate used to measure its defined benefit pension obligation, as well as the impact of adopting the new RP-2014 mortality tables for pension obligations. The change in the discount rate accounted for approximately $226 million of the net actuarial loss, and the change due to the adoption of the new RP-2014 mortality tables accounted for approximately $59 million. Net actuarial losses as a result of the discount rate and the adoption of the new mortality tables were partially offset by higher than expected asset returns of approximately $117 million (a net asset gain of $292.7 million on actual assets in 2014, or positive 11.2% on pension plan assets of $2.1 billion, compared to an expected return of $175.7 million, or 7.25%, in 2014). The remaining portion of the net actuarial loss for 2014 was due to other changes in actuarial assumptions.

In 2013, the net actuarial gain of $376.3 million was primarily due to a 102 basis point increase in the Company's discount rate used to measure its defined benefit pension obligation. The change in the discount rate accounted for approximately $320 million of the net actuarial gain. In addition to the change in the discount rate, higher than expected asset returns of approximately $100 million (a net asset gain of $334.0 million on actual assets in 2013, or positive 10.8% on pension plan assets of $3.3 billion, compared to an expected return of $232.0 million, or 8.0%, in 2013). The remaining portion of the net actuarial gain for 2013 was due to other changes in actuarial assumptions. The impact of these net actuarial losses for defined benefit pension plans, as well as net actuarial losses related to postretirement benefit plans and net prior service costs for defined benefit pension and postretirement plans, has increased total equity by $102.4 million after tax for the period between December 31, 2009 and December 31, 2014.

During this same time period, the Company contributed a total of $988.7 million to its global defined benefit pension plans, of which approximately $910.7 million was discretionary. As discussed above, the Company expects to contribute approximately $15 million to its global defined benefit pension plans in 2015. Despite the net actuarial losses recorded for the period between December 31, 2009 and December 31, 2014, only approximately $21 million of contributions was required in 2014. The contributions over the last five years, as well as favorable returns on pension assets, has contributed to the Company's U.S. defined benefit pension plans being overfunded and a lower requirement for the Company to contribute to its defined benefit pension plans. However, the effect of actuarial losses on future earnings and operating cash flow, as well as the impact from the lower interest rate to measure the Company's pension obligations is expected to be favorable in 2015, compared to 2014.

For expense purposes in 2014, the Company applied a discount rate of 5.02% for the first four months of 2014, and a discount rate of 4.68% for the last eight months of 2014 to its U.S. defined benefit pension plans as a result of a remeasurement of the U.S. defined benefit pension plans due to the spinoff of the plans related to TimkenSteel. For expense purposes for 2015, the Company has applied a discount rate of 4.20% for the defined benefit pension plans. For expense purposes in 2014, the Company applied an expected rate of return of 7.25% for the Company's U.S. pension plan assets. For expense purposes in 2015, the Company will apply an expected rate of return on plan assets of 6.00%. The reduction in expected rate of return on plan assets is due to the Company's move to a higher level of debt securities offset by a lower level of equity securities to maintain its overfunded status on U.S. pension plans.

The following table presents the sensitivity of the Company's U.S. projected pension benefit obligation (PBO), total equity and 2015 expense to the indicated increase/decrease in key assumptions:

| | +/– Change at December 31, 2015 | | | |
|---|---|---|---|---|
| | Change | PBO | Equity | 2014 Expense |
| Assumption: | | | | |
| Discount rate | +/– 0.25% | $ 48.4 | $ 48.4 | $ 3.0 |
| Actual return on plan assets | +/– 0.25% | N/A | 4.4 | 0.2 |
| Expected return on assets | +/– 0.25% | N/A | N/A | 4.1 |

In the table above, a 25 basis point decrease in the discount rate will increase the PBO by $48.4 million and decrease total equity by $48.4 million. The change in equity in the table above is reflected on a pre-tax basis. Defined benefit pension plans in the United States represent 80% of the Company's benefit obligation and 84% of the fair value of the Company's plan assets at December 31, 2014. The Company uses a combined U.S. federal and state statutory rate of approximately 37% to calculate the after tax impact on equity for U.S. plans. The Company uses the local statutory tax rate in effect to calculate the after tax impact on equity for all remaining non-U.S. plans. For some non-U.S. plans, a valuation allowance has been recorded against the tax benefits recorded in equity and, therefore, no tax benefits are recognized on an after tax basis.

**POSTRETIREMENT BENEFIT PLANS:**

The Company recognized net periodic benefit cost of $7.4 million in 2014 for postretirement benefit plans, excluding the steel business spun off on June 30, 2014, compared to $9.2 million in 2013. The decrease was primarily due to lower amortization of actuarial losses. The lower amortization of net actuarial losses was primarily due to a 79 basis point increase in the discount rate used to measure the defined benefit pension obligation from 3.80% at December 31, 2012 to 4.59% at December 31, 2013. The discount rate used to remeasure the defined benefit pension obligation as a result of the Spinoff at April 30, 2014 was 4.33% also resulted in lower amortization compared to 2013.

In 2015, the Company expects net periodic benefit cost to decrease to approximately $5 million for postretirement benefit plans. The expected decrease is primarily due to lower interest cost of approximately $1 million and a higher expected rate of return of approximately $1 million. The lower expected interest cost for 2014 is primarily due to a 64 basis point decrease in the Company's discount rate for expense purposes from 4.59% for 2014 to 3.95% for 2015. The higher expected return from plan assets for 2015 is primarily due to a 125 basis point increase in the expected return on pension assets for 2015.

For expense purposes in 2014, the Company applied a discount rate of 4.59% for the first four months of 2014, and a discount rate of 4.33% for the last eight months of 2014 to its postretirement benefit plans. For expense purposes in 2015, the Company will apply a discount rate of 3.95% to its postretirement benefit plans. For expense purposes in 2014, the Company applied an expected rate of return of 5.00% to the Voluntary Employee Beneficiary Association (VEBA) trust assets. For expense purposes in 2015, the Company will apply an expected rate of return of 6.25% to the VEBA trust assets.

The following table presents the sensitivity of the Company's accumulated other postretirement benefit obligation (ABO), total equity and 2015 expense to the indicated increase/decrease in key assumptions:

| | +/– Change at December 31, 2015 | | | |
|---|---|---|---|---|
| | Change | ABO | Equity | 2014 Expense |
| Assumption: | | | | |
| Discount rate | +/– 0.25% | $ 5.8 | $ 5.8 | $ 0.4 |
| Actual return on plan assets | +/– 0.25% | N/A | 0.3 | — |
| Expected return on assets | +/– 0.25% | N/A | N/A | 0.3 |

In the table above, a 25 basis point decrease in the discount rate will increase the ABO by $5.8 million and decrease equity by $5.8 million. The change in total equity in the table above is reflected on a pre-tax basis.

For measurement purposes for postretirement benefits, the Company assumed a weighted-average annual rate of increase in per capita cost (health care cost trend rate) for medical and prescription drug benefits of 7.0% for 2015, declining steadily for the next eight years to 5.0%; and 9.0% for HMO benefits for 2015, declining gradually for the next 16 years to 5.0%. The assumed health care cost trend rate may have a significant effect on the amounts reported. A one percentage point increase in the assumed health care cost trend rate would have increased the 2014 total service and interest cost components by $0.4 million and would have increased the postretirement obligation by $7.6 million. A one percentage point decrease would provide corresponding reductions of $0.3 million and $6.7 million, respectively.

**OTHER LOSS RESERVES:**

The Company has a number of loss exposures that are incurred in the ordinary course of business such as environmental claims, product liability, product warranty, litigation and accounts receivable reserves. Establishing loss reserves for these matters requires management's estimate and judgment with regards to risk exposure and ultimate liability or realization. These loss reserves are reviewed periodically and adjustments are made to reflect the most recent facts and circumstances.

## OTHER DISCLOSURES

**CAPITAL EXPENDITURES:**

The Company made capital expenditures of $126.8 million and $133.6 million in the years ended December 31, 2014 and December 31, 2013, respectively. These capital expenditures support on-going business needs, including facility maintenance, organic growth, continuous improvement and other business initiatives. The Company invested in the construction of a new building connected to its technology center in North Canton, Ohio, to serve as the Company's world headquarters subsequent to the Spinoff. The new building was completed in 2014, and the total cost was approximately $67 million.

**FOREIGN CURRENCY:**

Assets and liabilities of subsidiaries are translated at the rate of exchange in effect on the balance sheet date; income and expenses are translated at the average rates of exchange prevailing during the reporting period. Related translation adjustments are reflected as a separate component of accumulated other comprehensive loss. Foreign currency gains and losses resulting from transactions are included in the Consolidated Statements of Income.

The Company recognized a foreign currency exchange loss of $9.9 million, $9.1 million and $6.5 million for the years ended December 31, 2014, 2013 and 2012, respectively. For the year ended December 31, 2014, the Company recorded a negative non-cash foreign currency translation adjustment of $41.3 million that decreased shareholders' equity, compared to a negative non-cash foreign currency translation adjustment of $11.5 million that decreased shareholders' equity for the year ended December 31, 2013. The foreign currency translation adjustments for the year ended December 31, 2014 were negatively impacted by the strengthening of the U.S. dollar relative to most other currencies.

**TRADE LAW ENFORCEMENT:**

The U.S. government has an antidumping duty order in effect covering tapered roller bearings from China. The Company is a producer of these bearings, as well as ball bearings and other bearing types, in the United States. In 2012, the U.S. government extended this order for an additional five years. Antidumping duty orders covering ball bearings from Japan and the United Kingdom were sunset, as expected, by the U.S. Department of Commerce in March 2014, retroactive to September 2011.

**QUARTERLY DIVIDEND:**

On February 14, 2015, the Company's Board of Directors declared a quarterly cash dividend of $0.25 per common share. The quarterly dividend will be paid on March 6, 2015 to shareholders of record as of February 23, 2015. This will be the 371st consecutive dividend paid on the common shares of the Company.

**FORWARD-LOOKING STATEMENTS:**

Certain statements set forth in this Annual Report on Form 10-K and in the Company's 2014 Annual Report to Shareholders (including the Company's forecasts, beliefs and expectations) that are not historical in nature are "forward-looking" statements within the meaning of the Private Securities Litigation Reform Act of 1995. In particular, Management's Discussion and Analysis on pages 18 through 45 contains numerous forward-looking statements. Forward-looking statements generally will be accompanied by words such as "anticipate," "believe," "could," "estimate," "expect," "forecast," "outlook," "intend," "may," "possible," "potential," "predict," "project" or other similar words, phrases or expressions. You are cautioned not to place undue reliance on forward-looking statements, which speak only as of the date of this Annual Report on Form 10-K. The Company cautions readers that actual results may differ materially from those expressed or implied in forward-looking statements made by or on behalf of the Company due to a variety of factors, such as:

a) deterioration in world economic conditions, or in economic conditions in any of the geographic regions in which the Company conducts business, including additional adverse effects from the global economic slowdown, terrorism or hostilities. This includes: political risks associated with the potential instability of governments and legal systems in countries in which the Company or its customers conduct business, and changes in currency valuations;

b) the effects of fluctuations in customer demand on sales, product mix and prices in the industries in which the Company operates. This includes: the ability of the Company to respond to rapid changes in customer demand, the effects of customer bankruptcies or liquidations, the impact of changes in industrial business cycles, and whether conditions of fair trade continue in the U.S. markets;

c) competitive factors, including changes in market penetration, increasing price competition by existing or new foreign and domestic competitors, the introduction of new products by existing and new competitors, and new technology that may impact the way the Company's products are sold or distributed;

d) changes in operating costs. This includes: the effect of changes in the Company's manufacturing processes; changes in costs associated with varying levels of operations and manufacturing capacity; availability and cost of raw materials and energy; changes in the expected costs associated with product warranty claims; changes resulting from inventory management and cost reduction initiatives and different levels of customer demands; the effects of unplanned plant shutdowns; and changes in the cost of labor and benefits;

e) the success of the Company's operating plans, announced programs, initiatives and capital investments; the ability to integrate acquired companies; the ability of acquired companies to achieve satisfactory operating results, including results being accretive to earnings; and the Company's ability to maintain appropriate relations with unions that represent Company associates in certain locations in order to avoid disruptions of business;

f) unanticipated litigation, claims or assessments. This includes: claims or problems related to intellectual property, product liability or warranty, environmental issues, and taxes;

g) changes in worldwide financial markets, including availability of financing and interest rates, which affect: the Company's cost of funds and/or ability to raise capital; and customer demand and the ability of customers to obtain financing to purchase the Company's products or equipment that contain the Company's products;

h) the impact on the Company's pension obligations due to changes in interest rates, investment performance and other tactics designed to reduce risk;

i) retention of CDSOA distributions;

j) the Company's ability to realize the benefits of the Spinoff and avoid possible indemnification liabilities entered into with TimkenSteel in connection with the Spinoff;

k) the taxable nature of the Spinoff; and

l) those items identified under Item 1A. Risk Factors on pages 6 through 12.

Additional risks relating to the Company's business, the industries in which the Company operates or the Company's common shares may be described from time to time in the Company's filings with the Securities and Exchange Commission. All of these risk factors are difficult to predict, are subject to material uncertainties that may affect actual results and may be beyond the Company's control.

Readers are cautioned that it is not possible to predict or identify all of the risks, uncertainties and other factors that may affect future results and that the above list should not be considered to be a complete list. Except as required by the federal securities laws, the Company undertakes no obligation to publicly update or revise any forward-looking statement, whether as a result of new information, future events or otherwise.

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

**INTEREST RATE RISK:**

Changes in short-term interest rates related to several separate funding sources impact the Company's earnings. These sources are borrowings under the Asset Securitization Agreement, borrowings under the Senior Credit Facility and short-term bank borrowings by its international subsidiaries. If the market rates for short-term borrowings increased by one-percentage-point around the globe, the impact would be an increase in interest expense of $0.1 million annually, with a corresponding decrease in income from continuing operations before income taxes of the same amount. This amount was determined by considering the impact of hypothetical interest rates on the Company's borrowing cost and year-end debt balances by category.

**FOREIGN CURRENCY EXCHANGE RATE RISK:**

Fluctuations in the value of the U.S. dollar compared to foreign currencies, including the Euro, also impact the Company's earnings. The greatest risk relates to products shipped between the Company's European operations and the United States. Foreign currency forward contracts are used to hedge a portion of these intercompany transactions. Additionally, hedges are used to cover third-party purchases of product and equipment. As of December 31, 2014, there were $194.1 million of hedges in place. A uniform 10% weakening of the U.S. dollar against all currencies would have resulted in a charge of $16.6 million related to these hedges, which would have partially offset the otherwise favorable impact of the underlying currency fluctuation. In addition to the direct impact of the hedged amounts, changes in exchange rates also affect the volume of sales or foreign currency sales price as competitors' products become more or less attractive.

**COMMODITY PRICE RISK:**

In the ordinary course of business, the Company is exposed to market risk with respect to commodity price fluctuations, primarily related to our purchases of raw materials and energy, principally steel and natural gas. Whenever possible, the Company manages its exposure to commodity risks primarily through the use of supplier pricing agreements that enable the Company to establish the purchase prices for certain inputs that are used in our manufacturing and distribution business.

# CONSOLIDATED STATEMENTS OF INCOME

| | Year Ended December 31, | | |
|---|---|---|---|
| (Dollars in millions, except per share data) | **2014** | 2013 | 2012 |
| Net sales | **$ 3,076.2** | $ 3,035.4 | $ 3,359.5 |
| Cost of products sold | **2,178.2** | 2,167.0 | 2,331.5 |
| **Gross Profit** | **898.0** | 868.4 | 1,028.0 |
| Selling, general and administrative expenses | **542.5** | 546.6 | 554.5 |
| Impairment and restructuring charges | **113.4** | 8.7 | 29.5 |
| Pension settlement charges | **33.7** | 7.2 | — |
| **Operating Income** | **208.4** | 305.9 | 444.0 |
| Interest expense | **(28.7)** | (24.4) | (31.1) |
| Interest income | **4.4** | 1.9 | 2.9 |
| Gain on sale of real estate | **22.6** | 5.4 | — |
| Continued Dumping and Subsidy Offset Act (expenses) receipts, net | **(2.3)** | (2.8) | 108.0 |
| Other (expense) income, net | **(0.4)** | 4.1 | (6.0) |
| **Income From Continuing Operations Before Income Taxes** | **204.0** | 290.1 | 517.8 |
| Provision for income taxes | **54.7** | 114.6 | 186.3 |
| **Income From Continuing Operations** | **149.3** | 175.5 | 331.5 |
| Income from discontinued operations, net of income taxes | **24.0** | 87.5 | 164.4 |
| **Net Income** | **173.3** | 263.0 | 495.9 |
| Less: Net income attributable to noncontrolling interest | **2.5** | 0.3 | 0.4 |
| **Net Income Attributable to The Timken Company** | **$ 170.8** | $ 262.7 | $ 495.5 |
| **Amounts Attributable to The Timken Company's Common Shareholders:** | | | |
| Income from continuing operations, net of income taxes | **$ 146.8** | $ 175.2 | $ 331.1 |
| Income from discontinued operations, net of income taxes | **24.0** | 87.5 | 164.4 |
| **Net Income Attributable to The Timken Company** | **$ 170.8** | $ 262.7 | $ 495.5 |
| **Net Income per Common Share Attributable to The Timken Company Common Shareholders** | | | |
| Earnings per share – continuing operations | **$ 1.62** | $ 1.84 | $ 3.41 |
| Earnings per share – discontinued operations | **0.27** | 0.92 | 1.70 |
| **Basic earnings per share** | **$ 1.89** | $ 2.76 | $ 5.11 |
| Diluted earnings per share – continuing operations | **$ 1.61** | $ 1.82 | $ 3.38 |
| Diluted earnings per share – discontinued operations | **0.26** | 0.92 | 1.69 |
| **Diluted earnings per share** | **$ 1.87** | $ 2.74 | $ 5.07 |
| **Dividends per share** | **$ 1.00** | $ 0.92 | $ 0.92 |

See accompanying Notes to the Consolidated Financial Statements.

# CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

| (Dollars in millions) | Year Ended December 31, 2014 | 2013 | 2012 |
|---|---|---|---|
| Net Income | **$ 173.3** | $ 263.0 | $ 495.9 |
| Other comprehensive income, net of tax: | | | |
| Foreign currency translation adjustments | **(41.8)** | (19.0) | 10.5 |
| Unrealized loss on marketable securities | **—** | — | (0.8) |
| Pension and postretirement liability adjustment | **(43.1)** | 398.3 | (133.2) |
| Change in fair value of derivative financial instruments | **(0.4)** | 0.3 | (0.4) |
| Other comprehensive (loss) income, net of tax | **(85.3)** | 379.6 | (123.9) |
| **Comprehensive Income, net of tax** | **88.0** | 642.6 | 372.0 |
| Less: comprehensive income (loss) attributable to noncontrolling interest | **2.0** | (7.2) | 0.2 |
| **Comprehensive Income Attributable to The Timken Company** | **$ 86.0** | $ 649.8 | $ 371.8 |

See accompanying Notes to the Consolidated Financial Statements.

# CONSOLIDATED BALANCE SHEETS

| | December 31, | |
|---|---|---|
| (Dollars in millions) | **2014** | 2013 |
| **ASSETS** | | |
| **Current Assets** | | |
| Cash and cash equivalents | **$ 278.8** | $ 384.6 |
| Restricted cash | **15.3** | 15.1 |
| Accounts receivable, less allowances (2014 – $13.7 million; 2013 – $10.1 million) | **475.7** | 444.0 |
| Inventories, net | **585.5** | 582.6 |
| Deferred income taxes | **49.9** | 56.2 |
| Deferred charges and prepaid expenses | **25.2** | 26.8 |
| Other current assets | **51.5** | 61.7 |
| Current assets, discontinued operations | **—** | 366.5 |
| **Total Current Assets** | **1,481.9** | 1,937.5 |
| **Property, Plant and Equipment, Net** | **780.5** | 855.8 |
| **Other Assets** | | |
| Goodwill | **259.5** | 346.1 |
| Non-current pension assets | **176.2** | 223.5 |
| Other intangible assets | **239.8** | 207.4 |
| Other non-current assets | **63.5** | 58.4 |
| Non-current assets, discontinued operations | **—** | 849.2 |
| **Total Other Assets** | **739.0** | 1,684.6 |
| **Total Assets** | **$ 3,001.4** | $ 4,477.9 |
| **LIABILITIES AND EQUITY** | | |
| **Current Liabilities** | | |
| Short-term debt | **$ 7.4** | $ 18.6 |
| Current portion of long-term debt | **0.6** | 250.7 |
| Accounts payable, trade | **143.9** | 139.9 |
| Salaries, wages and benefits | **146.7** | 131.1 |
| Income taxes payable | **80.2** | 106.7 |
| Other current liabilities | **155.0** | 180.8 |
| Current liabilities, discontinued operations | **—** | 152.3 |
| **Total Current Liabilities** | **533.8** | 980.1 |
| **Non-Current Liabilities** | | |
| Long-term debt | **522.1** | 176.4 |
| Accrued pension cost | **165.9** | 159.0 |
| Accrued postretirement benefits cost | **141.8** | 138.3 |
| Deferred income taxes | **4.1** | 82.9 |
| Other non-current liabilities | **44.6** | 55.9 |
| Non-current liabilities, discontinued operations | **—** | 236.7 |
| **Total Non-Current Liabilities** | **878.5** | 849.2 |
| **Shareholders' Equity** | | |
| Class I and II Serial Preferred Stock without par value: | | |
| Authorized – 10,000,000 shares each class, none issued | **—** | — |
| Common stock without par value: | | |
| Authorized – 200,000,000 shares | | |
| Issued (including shares in treasury) (2014 – 98,375,135; 2013 – 98,375,135 shares) | | |
| Stated capital | **53.1** | 53.1 |
| Other paid-in capital | **899.4** | 896.4 |
| Earnings invested in the business | **1,615.4** | 2,586.4 |
| Accumulated other comprehensive loss | **(482.5)** | (626.1) |
| Treasury shares at cost (2014 – 9,783,375; 2013 – 5,252,441 shares) | **(509.2)** | (273.2) |
| **Total Shareholders' Equity** | **1,576.2** | 2,636.6 |
| Noncontrolling interest | **12.9** | 12.0 |
| **Total Equity** | **1,589.1** | 2,648.6 |
| **Total Liabilities and Equity** | **$ 3,001.4** | $ 4,477.9 |

See accompanying Notes to the Consolidated Financial Statements.

# CONSOLIDATED STATEMENTS OF CASH FLOWS

| | Year Ended December 31, | | |
|---|---|---|---|
| (Dollars in millions) | **2014** | 2013 | 2012 |
| **CASH PROVIDED (USED)** | | | |
| **Operating Activities** | | | |
| Net income attributable to The Timken Company | **$ 170.8** | $ 262.7 | $ 495.5 |
| Net income from discontinued operations | **(24.0)** | (87.5) | (164.4) |
| Net income attributable to noncontrolling interest | **2.5** | 0.3 | 0.4 |
| Adjustments to reconcile net income to net cash provided by operating activities: | | | |
| Depreciation and amortization | **137.0** | 142.4 | 149.6 |
| Impairment charges | **98.9** | 0.1 | 6.6 |
| (Gain) loss on sale of assets | **(20.2)** | (1.1) | 5.2 |
| Deferred income tax (benefit) provision | **(53.3)** | (33.0) | 91.6 |
| Stock-based compensation expense | **21.8** | 16.3 | 15.9 |
| Excess tax benefits related to stock-based compensation | **(7.1)** | (10.9) | (9.9) |
| Pension and other postretirement expense | **62.0** | 55.1 | 63.5 |
| Pension and other postretirement benefit contributions | **(49.9)** | (93.4) | (341.1) |
| Changes in operating assets and liabilities: | | | |
| Accounts receivable | **(48.3)** | (4.6) | 8.3 |
| Inventories | **(26.8)** | 34.6 | 57.6 |
| Accounts payable, trade | **8.0** | 0.9 | (36.0) |
| Other accrued expenses | **2.2** | (39.6) | (36.8) |
| Income taxes | **(15.3)** | 67.5 | 53.3 |
| Other, net | **23.2** | (17.0) | 28.1 |
| Net Cash Provided by Operating Activities – continuing operations | **281.5** | 292.8 | 387.4 |
| Net Cash Provided by Operating Activities – discontinued operations | **25.5** | 137.2 | 236.7 |
| **Net Cash Provided by Operating Activities** | **307.0** | 430.0 | 624.1 |
| **Investing Activities** | | | |
| Capital expenditures | **(126.8)** | (133.6) | (118.3) |
| Acquisitions, net of cash acquired of $0.4 million in 2013 | **(21.7)** | (64.2) | (20.7) |
| Proceeds from disposals of property, plant and equipment | **25.9** | 7.1 | 1.8 |
| Investments in short-term marketable securities, net | **4.9** | 5.5 | 14.3 |
| Other | **—** | 1.1 | 4.0 |
| Net Cash Used by Investing Activities – continuing operations | **(117.7)** | (184.1) | (118.9) |
| Net Cash Used by Investing Activities – discontinued operations | **(77.0)** | (191.9) | (178.8) |
| **Net Cash Used by Investing Activities** | **(194.7)** | (376.0) | (297.7) |
| **Financing Activities** | | | |
| Cash dividends paid to shareholders | **(90.3)** | (87.5) | (89.0) |
| Purchase of treasury shares | **(270.9)** | (189.2) | (112.3) |
| Proceeds from exercise of stock options | **16.8** | 13.1 | 13.8 |
| Excess tax benefits related to stock-based compensation | **7.1** | 10.9 | 9.9 |
| Proceeds from issuance of long-term debt | **346.2** | 1.9 | — |
| Deferred financing costs | **(3.2)** | — | — |
| Accounts receivable securitization financing borrowings | **90.0** | — | — |
| Accounts receivable securitization financing payments | **(90.0)** | — | — |
| Payments on long-term debt | **(250.7)** | (9.9) | (18.4) |
| Short-term debt activity, net | **(9.8)** | 4.8 | (7.7) |
| Cash transferred to TimkenSteel Corporation | **(46.5)** | — | — |
| Other | **(0.9)** | 6.6 | 3.6 |
| Net Cash Used by Financing Activities – continuing operations | **(302.2)** | (249.3) | (200.1) |
| Net Cash Provided (Used) by Financing Activities – discontinued operations | **100.0** | — | (8.5) |
| **Net Cash Used by Financing Activities** | **(202.2)** | (249.3) | (208.6) |
| Effect of exchange rate changes on cash | **(15.9)** | (6.5) | 3.8 |
| **(Decrease) Increase In Cash and Cash Equivalents** | **(105.8)** | (201.8) | 121.6 |
| Cash and cash equivalents at beginning of year | **384.6** | 586.4 | 464.8 |
| **Cash and Cash Equivalents at End of Year** | **$ 278.8** | $ 384.6 | $ 586.4 |

See accompanying Notes to the Consolidated Financial Statements.

# CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY

| | | The Timken Company Shareholders | | | | | |
|---|---|---|---|---|---|---|---|
| (Dollars in millions, except per share data) | Total | Stated Capital | Other Paid-In Capital | Earnings Invested in the Business | Accumulated Other Comprehensive Income (Loss) | Treasury Shares | Non-controlling Interest |
| Year Ended December 31, 2012 | | | | | | | |
| Balance at January 1, 2012 | $ 2,042.5 | $ 53.1 | $ 889.2 | $ 2,004.7 | $ (889.5) | $ (29.2) | $ 14.2 |
| Net income | 495.9 | | | 495.5 | | | 0.4 |
| Foreign currency translation adjustments | 10.5 | | | | 10.5 | | |
| Pension and postretirement liability adjustment (net of income tax of $55.3 million) | (133.2) | | | | (133.2) | | |
| Unrealized loss on marketable securities | (0.8) | | | | (0.6) | | (0.2) |
| Change in fair value of derivative financial instruments, net of reclassifications | (0.4) | | | | (0.4) | | |
| Dividends – $0.92 per share | (89.0) | | | (89.0) | | | |
| Excess tax benefit from stock compensation | 9.9 | | 9.9 | | | | |
| Stock-based compensation expense | 18.0 | | 18.0 | | | | |
| Stock purchased at cost | (112.3) | | | | | (112.3) | |
| Stock option exercise activity | 13.4 | | (21.9) | | | 35.3 | |
| Restricted shares (issued) surrendered | 0.2 | | (3.8) | | | 4.0 | |
| Shares surrendered for taxes | (8.1) | | | | | (8.1) | |
| Balance at December 31, 2012 | $ 2,246.6 | $ 53.1 | $ 891.4 | $ 2,411.2 | $ (1,013.2) | $ (110.3) | $ 14.4 |
| Year Ended December 31, 2013 | | | | | | | |
| Net income | 263.0 | | | 262.7 | | | 0.3 |
| Foreign currency translation adjustments | (19.0) | | | | (11.5) | | (7.5) |
| Pension and postretirement liability adjustment (net of income tax of $226.5 million) | 398.3 | | | | 398.3 | | |
| Change in fair value of derivative financial instruments, net of reclassifications | 0.3 | | | | 0.3 | | |
| Change in ownership of noncontrolling interest | 8.9 | | 1.3 | | | | 7.6 |
| Dividends declared to noncontrolling interest | (2.8) | | | | | | (2.8) |
| Dividends – $0.92 per share | (87.5) | | | (87.5) | | | |
| Excess tax benefit from stock compensation | 10.9 | | 10.9 | | | | |
| Stock-based compensation expense | 18.6 | | 18.6 | | | | |
| Stock purchased at cost | (189.2) | | | | | (189.2) | |
| Stock option exercise activity | 7.8 | | (22.0) | | | 29.8 | |
| Restricted shares (issued) surrendered | 1.0 | | (3.8) | | | 4.8 | |
| Shares surrendered for taxes | (8.3) | | | | | (8.3) | |
| Balance at December 31, 2013 | $ 2,648.6 | $ 53.1 | $ 896.4 | $ 2,586.4 | $ (626.1) | $ (273.2) | $ 12.0 |
| **Year Ended December 31, 2014** | | | | | | | |
| Net income | **173.3** | | | **170.8** | | | **2.5** |
| Foreign currency translation adjustments | **(41.8)** | | | | **(41.3)** | | **(0.5)** |
| Pension and postretirement liability adjustment (net of income tax of $23.9 million) | **(43.1)** | | | | **(43.1)** | | |
| Change in fair value of derivative financial instruments, net of reclassifications | **(0.4)** | | | | **(0.4)** | | |
| Dividends declared to noncontrolling interest | **(1.1)** | | | | | | **(1.1)** |
| Dividends – $1.00 per share | **(90.3)** | | | **(90.3)** | | | |
| Distribution of TimkenSteel | **(823.1)** | | | **(1,051.5)** | **228.4** | | |
| Excess tax benefit from stock compensation | **7.1** | | **7.1** | | | | |
| Stock-based compensation expense | **23.9** | | **23.9** | | | | |
| Stock purchased at cost | **(270.9)** | | | | | **(270.9)** | |
| Stock option exercise activity | **16.7** | | **(23.8)** | | | **40.5** | |
| Restricted shares (issued) surrendered | **0.9** | | **(4.2)** | | | **5.1** | |
| Shares surrendered for taxes | **(10.7)** | | | | | **(10.7)** | |
| Balance at December 31, 2014 | **$ 1,589.1** | **$ 53.1** | **$ 899.4** | **$ 1,615.4** | **$ (482.5)** | **$ (509.2)** | **$ 12.9** |

See accompanying Notes to the Consolidated Financial Statements.

# NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Dollars in millions, except per share data)

## NOTE 1 – SIGNIFICANT ACCOUNTING POLICIES

**PRINCIPLES OF CONSOLIDATION:**

The consolidated financial statements include the accounts and operations of the Company in which a controlling interest is maintained. Investments in affiliated companies that the Company does not control, and the activities of which it is not the primary beneficiary, are accounted for using the equity method. All significant intercompany accounts and transactions are eliminated upon consolidation.

**REVENUE RECOGNITION:**

The Company recognizes revenue when title passes to the customer. This occurs at the shipping point except for goods sold by certain foreign entities and certain exported goods, where title passes when the goods reach their destination. Selling prices are fixed based on purchase orders or contractual arrangements. Shipping and handling costs billed to customers are included in net sales and the related costs are included in cost of products sold in the Consolidated Statements of Income.

The Company recognizes a portion of its revenues on the percentage-of-completion method measured on the cost-to-cost basis. In 2014 and 2013, the Company recognized approximately $50 million and $55 million, respectively, in net sales under the percentage-of-completion method.

**CASH EQUIVALENTS:**

The Company considers all highly liquid investments with a maturity of three months or less when purchased to be cash equivalents.

**RESTRICTED CASH:**

Cash of $15.3 million and $15.1 million at December 31, 2014 and 2013, respectively, was restricted for use for workers compensation claims.

**ALLOWANCE FOR DOUBTFUL ACCOUNTS:**

The Company maintains an allowance for doubtful accounts, which represents an estimate of the losses expected from the accounts receivable portfolio, to reduce accounts receivable to their net realizable value. The allowance is based upon historical trends in collections and write-offs, management's judgment of the probability of collecting accounts and management's evaluation of business risk. The Company extends credit to customers satisfying pre-defined credit criteria. The Company believes it has limited concentration of credit risk due to the diversity of its customer base.

**INVENTORIES:**

Inventories are valued at the lower of cost or market. The majority of domestic inventories are valued by the LIFO method and the balance of the Company's inventories is valued by the FIFO method.

**INVESTMENTS:**

Short-term investments are investments with maturities between four months and one year and are valued at amortized cost, which approximates fair value. The Company held short-term investments as of December 31, 2014 and 2013 with a fair value and cost basis of $8.4 million and $13.9 million, respectively, which were included in other current assets on the Consolidated Balance Sheets.

**PROPERTY, PLANT AND EQUIPMENT:**

Property, plant and equipment, net is valued at cost less accumulated depreciation. Maintenance and repairs are charged to expense as incurred. The provision for depreciation is computed principally by the straight-line method based upon the estimated useful lives of the assets. The useful lives are approximately 30 years for buildings, three to ten years for computer software and three to 20 years for machinery and equipment.

The impairment of long-lived assets is evaluated when events or changes in circumstances indicate that the carrying amount of the asset or related group of assets may not be recoverable. If the expected future undiscounted cash flows are less than the carrying amount of the asset, an impairment loss is recognized at that time to reduce the asset to the lower of its fair value or its net book value.

Note 1 – Significant Accounting Policies (continued)

**GOODWILL AND OTHER INTANGIBLE ASSETS:**
Intangible assets subject to amortization are amortized on a straight-line method over their legal or estimated useful lives, with useful lives ranging from one to 20 years. Goodwill and indefinite-lived intangible assets not subject to amortization are tested for impairment at least annually. The Company performs its annual impairment test as of October 1, after the annual forecasting process is completed. Furthermore, goodwill and indefinite-lived intangible assets are reviewed for impairment whenever events or changes in circumstances indicate that the carrying values may not be recoverable in accordance with accounting rules related to goodwill and other intangible assets.

**PRODUCT WARRANTIES:**
The Company provides limited warranties on certain of its products. The Company accrues liabilities for warranties based upon specific claims and a review of historical warranty claim experience in accordance with accounting rules relating to contingent liabilities. The Company records and accounts for its warranty reserve based on specific claim incidents. Should the Company become aware of a specific potential warranty claim for which liability is probable and reasonably estimable, a specific charge is recorded and accounted for accordingly. Adjustments are made quarterly to the accruals as claim data and historical experience change.

**INCOME TAXES:**
The Company accounts for income taxes in accordance with ASC 740, "Income Taxes." Deferred tax assets and liabilities are recorded for the future tax consequences attributable to differences between financial statement carrying amounts of existing assets and liabilities and their respective tax bases, as well as net operating loss and tax credit carryforwards. The Company recognizes valuation allowances against deferred tax assets by tax jurisdiction when it is more likely than not that such assets will not be realized. Accruals for uncertain tax positions are provided for in accordance with ASC 740-10. The Company recognizes interest and penalties related to uncertain tax positions as a component of income tax expense.

**FOREIGN CURRENCY:**
Assets and liabilities of subsidiaries, other than those located in highly inflationary countries, are translated at the rate of exchange in effect on the balance sheet date; income and expenses are translated at the average rates of exchange prevailing during the year. The related translation adjustments are reflected as a separate component of accumulated other comprehensive loss. Gains and losses resulting from foreign currency transactions and the translation of financial statements of subsidiaries in highly inflationary countries are included in the Consolidated Statements of Income. The Company realized foreign currency exchange losses of $9.9 million, $9.1 million and $6.5 million in 2014, 2013 and 2012, respectively.

**PENSION AND OTHER POSTRETIREMENT BENEFITS:**
The Company recognizes an overfunded status or underfunded status (i.e., the difference between the fair value of plan assets and the benefit obligations) as either an asset or a liability for its defined benefit pension and postretirement benefit plans on the Consolidated Balance Sheets, with a corresponding adjustment to accumulated other comprehensive loss, net of tax. The adjustment to accumulated other comprehensive loss represents the current year net unrecognized actuarial gains and losses and unrecognized prior service costs. These amounts will be recognized in future periods as net periodic benefit cost.

**STOCK-BASED COMPENSATION:**
The Company recognizes stock-based compensation expense based on the grant date fair value of the stock-based awards over their required vesting period. Stock options are issued with an exercise price equal to the opening market price of Timken common shares on the date of grant. The fair value of stock options is determined using a Black-Scholes option pricing model, which incorporates assumptions regarding the expected volatility, the expected option life, the risk-free interest rate and the expected dividend yield. The fair value of stock-based awards that will settle in Timken common shares, other than stock options, is based on the opening market price of Timken common shares on the grant date. The fair value of stock-based awards that will settle in cash are remeasured at each reporting period until settlement of the awards.

Note 1 – Significant Accounting Policies (continued)

**EARNINGS PER SHARE:**

Unvested restricted shares provide for the payment of nonforfeitable dividends. The Company considers these awards as participating securities. Earnings per share are computed using the two-class method. Basic earnings per share are computed by dividing net income less undistributed earnings allocated to unvested restricted shares by the weighted-average number of common shares outstanding during the year. Diluted earnings per share are computed by dividing net income less undistributed earnings allocated to unvested restricted shares by the weighted-average number of common shares outstanding, adjusted for the dilutive impact of outstanding stock-based awards.

**DERIVATIVE INSTRUMENTS:**

The Company recognizes all derivatives on the Consolidated Balance Sheets at fair value. Derivatives that are not designated as hedges must be adjusted to fair value through earnings. If the derivative is designated and qualifies as a hedge, depending on the nature of the hedge, changes in the fair value of the derivatives are either offset against the change in fair value of the hedged assets, liabilities or firm commitments through earnings or recognized in other comprehensive loss until the hedged item is recognized in earnings. The Company's holdings of forward foreign currency exchange contracts qualify as derivatives pursuant to the criteria established in derivative accounting guidance, and the Company has designated certain of those derivatives as hedges.

**RECENT ACCOUNTING PRONOUNCEMENTS:**

In May 2014, the Financial Accounting Standards Board (FASB) issued ASU 2014-09, "Revenue from Contracts with Customers (Topic 606)." ASU 2014-09 introduces a new five-step revenue recognition model in which an entity should recognize revenue to depict the transfer of 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. ASU 2014-09 also requires disclosures sufficient to enable users to understand the nature, amount, timing, and uncertainty of revenue and cash flows arising from contracts with customers, including qualitative and quantitative disclosures about contracts with customers, significant judgments and changes in judgments and assets recognized from the costs to obtain or fulfill a contract. This new accounting guidance is effective for annual periods beginning after December 15, 2016, including interim periods within that reporting period. The Company is currently evaluating the impact of adopting ASU 2014-09 on the Company's results of operations or financial condition.

In April 2014, the FASB issued ASU 2014-08, "Presentation of Financial Statements (Topic 205) and Property, Plant and Equipment (Topic 360)." ASU 2014-08 amends the requirements for reporting discontinued operations and requires additional disclosures about discontinued operations. Under the new guidance, only disposals representing a strategic shift in operations or that have a major effect on the Company's operations and financial results should be presented as discontinued operations. ASU 2014-08 also requires expanded disclosures about discontinued operations that will provide financial statement users with more information about the assets, liabilities, income, and expenses of discontinued operations. This new accounting guidance is effective for annual periods beginning after December 15, 2014. The Company is currently evaluating the impact of adopting ASU 2014-08 on the Company's results of operations or financial condition.

In July 2013, the FASB issued ASU 2013-11, Income Taxes (Topic 740): "Presentation of an Unrecognized Tax Benefit When a Net Operating Loss Carryforward, a Similar Tax Loss, or a Tax Credit Carryforward Exists." ASU 2013-11 clarifies guidance and eliminates diversity in practice on the presentation of unrecognized tax benefits when a net operating loss carryforward, a similar tax loss, or a tax credit carryforward exists at the reporting date. This accounting guidance is effective for the Company for annual and interim reporting periods beginning after December 15, 2013. The adoption of this accounting guidance did not have a material impact on the Company's results of operations or financial condition.

**USE OF ESTIMATES:**

The preparation of financial statements in conformity with U.S. generally accepted accounting principles requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. These estimates and assumptions are reviewed and updated regularly to reflect recent experience.

Note 1 – Significant Accounting Policies (continued)

**RECLASSIFICATIONS:**

Certain amounts reported in the 2013 Consolidated Financial Statements for amounts related to the Company's former steel business have been reclassified to discontinued operations to reflect the Spinoff. In addition, certain amounts reported in the 2013 Consolidated Financial Statements for segment results have been reclassified to conform to the new segment presentation.

## NOTE 2 – SPINOFF TRANSACTION

On June 30, 2014, the Company completed the separation of its steel business through the Spinoff, creating a new independent publicly traded company, TimkenSteel. The Company's Board of Directors declared a distribution of all outstanding common shares of TimkenSteel through a dividend. At the close of business on June 30, 2014, the Company's shareholders received one common share of TimkenSteel for every two common shares of the Company they held as of the close of business on June 23, 2014.

In connection with the Spinoff, the Company and TimkenSteel entered into certain transitional relationships, including a commercial supply agreement for TimkenSteel to supply the Company with certain steel products and other relationships described in the section of this Annual Report on Form 10-K titled *"Risks Relating to the Spinoff of TimkenSteel."*

The operating results, net of tax, included one-time transaction costs of approximately $57 million and $13 million for 2014 and 2013, respectively, in connection with the separation of the two companies. These costs consisted of consulting and professional fees associated with preparing for and executing the Spinoff, as well as lease cancellation fees. In addition to the one time transaction costs, the Company incurred approximately $15 million of capital expenditures related to the Spinoff.

The following table presents the results of operations for TimkenSteel that have been reclassified to discontinued operations for all periods presented:

| | **Year Ended December 31,** | | |
|---|---|---|---|
| | **2014** | 2013 | 2012 |
| Net Sales | **$ 786.2** | $ 1,305.8 | $ 1,627.5 |
| Cost of goods sold | **642.0** | 1,082.2 | 1,289.2 |
| Gross profit | **144.2** | 223.6 | 338.3 |
| Selling, administrative and general expenses | **46.4** | 80.5 | 89.4 |
| Separation costs | **57.1** | 13.0 | — |
| Interest expense, net | **0.8** | — | — |
| Other (income) expense, net | **(0.1)** | 3.0 | 0.7 |
| Income before income taxes | **40.0** | 127.1 | 248.2 |
| Income tax expense | **16.0** | 39.6 | 83.8 |
| Income from discontinued operations | **$ 24.0** | $ 87.5 | $ 164.4 |

## Note 2 – Spinoff Transaction (continued)

The following table presents the carrying value of assets and liabilities immediately preceding the Spinoff on June 30, 2014.

| | 2014 |
|---|---|
| **ASSETS** | |
| Cash and cash equivalents | **$ 46.5** |
| Accounts receivable, net | **178.9** |
| Inventories, net | **238.2** |
| Deferred income taxes | **20.2** |
| Other current assets | **4.0** |
| Property, plant, and equipment, net | **751.6** |
| Goodwill | **12.6** |
| Non-current pension assets | **83.5** |
| Other intangible assets | **11.2** |
| Other non-current assets | **2.6** |
| **Total assets, discontinued operations** | **$ 1,349.3** |
| **LIABILITIES** | |
| Accounts payable, trade | **$ 132.8** |
| Salaries, wages and benefits | **52.0** |
| Income taxes payable | **0.1** |
| Other current liabilities | **15.9** |
| Long-term debt | **130.2** |
| Accrued pension cost | **24.5** |
| Accrued postretirement benefits cost | **68.3** |
| Deferred income taxes | **91.7** |
| Other non-current liabilities | **10.7** |
| **Total liabilities, discontinued operations** | **$ 526.2** |

## Note 2 – Spinoff Transaction (continued)

The following table presents the carrying value of assets and liabilities for the steel business at December 31, 2013.

| | 2013 |
|---|---|
| **ASSETS** | |
| Cash and cash equivalents | $ — |
| Accounts receivable, net | 122.7 |
| Inventories, net | 227.3 |
| Deferred income taxes | 13.6 |
| Other current assets | 2.9 |
| Property, plant, and equipment, net | 702.2 |
| Goodwill | 12.6 |
| Non-current pension assets | 119.1 |
| Other intangible assets | 11.7 |
| Other non-current assets | 3.6 |
| **Total assets, discontinued operations** | $ 1,215.7 |
| **LIABILITIES** | |
| Accounts payable, trade | $ 82.6 |
| Salaries, wages and benefits | 52.0 |
| Income taxes payable | 0.4 |
| Other current liabilities | 17.3 |
| Long-term debt | 30.2 |
| Accrued pension cost | 20.0 |
| Accrued postretirement benefits cost | 95.7 |
| Deferred income taxes | 84.1 |
| Other non-current liabilities | 6.7 |
| **Total liabilities, discontinued operations** | $ 389.0 |

# NOTE 3 – ACQUISITIONS AND DIVESTITURES

**ACQUISITIONS:**

On November 30, 2014, the Company completed the acquisition of the assets of Revolvo, a specialty bearing company based in Dudley, U.K., for $9.7 million. Revolvo makes and markets ball and roller bearings for industrial applications in process and heavy industries. Revolvo's split roller bearing housed units are widely used by mining, power generation, food and beverage, pulp and paper, metals, cement, marine and waste-water end users. Revolvo had full-year 2014 sales of approximately $9 million. The Company reported the results for Revolvo in the Process Industries segment.

On April 28, 2014, the Company completed the acquisition of assets from Schulz for $12.0 million in cash. Schulz provides electric motor and generator repairs, motor rewinds, custom controls and panels, systems integration, pump services, machine rebuilds, hydro services and diagnostics for a broad range of commercial and industrial applications. Schulz serves customers nationwide in the commercial nuclear power market sector, as well as regionally in the hydro and fossil fuel market sectors, water management, paper and general manufacturing sectors in the New England and Mid-Atlantic regions. Based in New Haven, Connecticut, Schulz employs 125 associates and had 2013 sales of approximately $18 million. The Company reported the results for Schulz in the Process Industries segment.

On May 13, 2013, the Company completed the acquisition of Standard Machine, which provides new gearboxes, gearbox service and repair, open gearing, large gear fabrication, machining and field technical services to end users in Canada and the western United States, for $37.0 million in cash, including cash acquired of approximately $0.1 million that was subject to a post-closing indebtedness adjustment. Based in Saskatoon, Saskatchewan, Canada, Standard Machine employs 125 people and serves a wide variety of industrial sectors including mining, oil and gas, and pulp and paper. The results of operations of Standard Machine were included in the Company's Consolidated Statements of Income for the period subsequent to the effective date of the acquisition and are reported in the Process Industries segment.

On April 11, 2013, the Company completed the acquisition of substantially all of the assets of Smith Services, an electric motor repair specialist, for $13.2 million. Based in Princeton, West Virginia, Smith Services employs approximately 140 people. The results of operations of Smith Services were included in the Company's Consolidated Statements of Income for the period subsequent to the effective date of the acquisition and are reported in the Process Industries segment.

On March 11, 2013, the Company completed the acquisition of Interlube, which makes and markets automated lubrication delivery systems and related components to end market sectors including commercial vehicles, construction, mining, and heavy and general industries, for $14.5 million, including cash acquired of approximately $0.3 million, that was subject to a post-closing indebtedness adjustment. Based in Plymouth, U.K., Interlube employs about 90 people. The results of operations of Interlube were included in the Company's Consolidated Statements of Income for the period subsequent to the effective date of the acquisition and are reported in the Mobile Industries segment.

On December 31, 2012, the Company completed the acquisition of the assets of Wazee, a leading regional provider of motor, generator, wind turbine and industrial crane services to diverse end-markets including oil and gas, wind, agriculture, material handling and construction, for $20.1 million in cash. Based in Denver, Colorado, Wazee employs over 100 people. The results of operations of Wazee were included in the Company's Consolidated Statements of Income for the period subsequent to the effective date of the acquisition and are reported in the Process Industries segment. In addition to the Wazee acquisition, the Company purchased the remaining interest in its joint venture in Curitiba, Brazil.

Pro forma results of these operations have not been presented because the effects of the acquisitions were not significant to the Company's income from operations or total assets in 2014, 2013 or 2012, respectively.

Note 3 – Acquisitions and Divestitures (continued)

The purchase price allocations, net of cash acquired, and any subsequent purchase price adjustments for acquisitions in 2014, 2013 and 2012 are presented below:

| | **2014** | 2013 | 2012 |
|---|---|---|---|
| Assets: | | | |
| Accounts receivable, net | **$ 5.0** | $ 10.6 | $ 4.7 |
| Inventories, net | **5.5** | 12.7 | 2.3 |
| Other current assets | **0.2** | 0.4 | 0.3 |
| Property, plant and equipment, net | **2.9** | 19.5 | 3.0 |
| Goodwill | **3.3** | 18.1 | 7.1 |
| Other intangible assets | **8.3** | 13.0 | 7.7 |
| Total assets acquired | **$ 25.2** | $ 74.3 | $ 25.1 |
| Liabilities: | | | |
| Accounts payable, trade | **$ 2.3** | $ 3.3 | $ 2.3 |
| Salaries, wages and benefits | **—** | 1.4 | 0.3 |
| Other current liabilities | **0.7** | 0.9 | 1.8 |
| Other non-current liabilities | **0.5** | 4.5 | — |
| Total liabilities assumed | **$ 3.5** | $ 10.1 | $ 4.4 |
| Net assets acquired | **$ 21.7** | $ 64.2 | $ 20.7 |

The amounts for 2014 in the table above represent the preliminary purchase price allocation for current year acquisitions.

The following table summarizes the preliminary purchase price allocation for identifiable intangible assets acquired in 2014:

| | Purchase Price Allocation | |
|---|---|---|
| | | Weighted-Average Life |
| Trade name | **$ 1.0** | **6 years** |
| Technology / Know-how | **4.1** | **17 years** |
| All customer relationships | **3.0** | **16 years** |
| Non-compete agreements | **0.2** | **5 years** |
| Total intangible assets | **$ 8.3** | |

The following table summarizes the final purchase price allocation for identifiable intangible assets acquired in 2013:

| | Purchase Price Allocation | |
|---|---|---|
| | | Weighted-Average Life |
| Trade name | $ 1.1 | 13 years |
| Technology / Know-how | 5.2 | 18 years |
| All customer relationships | 6.4 | 20 years |
| Non-compete agreements | 0.3 | 4 years |
| Total intangible assets | $ 13.0 | |

**DIVESTITURES:**

On December 31, 2012, the Company completed the sale of its interest in Advanced Green Components, LLC (AGC) to Machinery Tec Masters Corporation. The Company received $2.2 million in cash proceeds for AGC. The Company recognized a pretax loss on divestiture of $2.0 million, and the loss was reflected in other (expense) income, net in the Consolidated Statement of Income.

## NOTE 4 – EARNINGS PER SHARE

The following table sets forth the reconciliation of the numerator and the denominator of basic earnings per share and diluted earnings per share for the years ended December 31:

| | 2014 | 2013 | 2012 |
|---|---|---|---|
| Numerator: | | | |
| Net income from continuing operations attributable to The Timken Company | **$ 146.8** | $ 175.2 | $ 331.1 |
| Less: undistributed earnings allocated to nonvested stock | **—** | (0.2) | (1.5) |
| Net income from continuing operations available to common shareholders for basic earnings per share and diluted earnings per share | **$ 146.8** | $ 175.0 | $ 329.6 |
| Denominator: | | | |
| Weighted-average number of shares outstanding – basic | **90,367,345** | 94,989,561 | 96,671,613 |
| Effect of dilutive securities: | | | |
| Stock options and awards – based on the treasury stock method | **856,983** | 834,167 | 930,868 |
| Weighted-average number of shares outstanding, assuming dilution of stock options and awards | **91,224,328** | 95,823,728 | 97,602,481 |
| Basic earnings per share from continuing operations | **$ 1.62** | $ 1.84 | $ 3.41 |
| Diluted earnings per share from continuing operations | **$ 1.61** | $ 1.82 | $ 3.38 |

The exercise prices for certain stock options that the Company has awarded exceed the average market price of the Company's common shares. Such stock options are antidilutive and were not included in the computation of diluted earnings per share. The antidilutive stock options outstanding were 523,252, 382,525 and 879,413 during 2014, 2013 and 2012, respectively.

## NOTE 5 – ACCUMULATED OTHER COMPREHENSIVE INCOME (LOSS)

The following tables present details about components of accumulated other comprehensive income (loss) for the years ended December 31, 2014 and December 31, 2013 respectively:

| | Foreign currency translation adjustments | Pension and postretirement liability adjustments | Change in fair value of derivative financial instruments | Total |
|---|---|---|---|---|
| Balance at December 31, 2013 | **$ 37.5** | **$ (663.2)** | **$ (0.4)** | **$ (626.1)** |
| Other comprehensive (loss) income before reclassifications, before income tax | **(41.8)** | **(166.0)** | **0.7** | **(207.1)** |
| Amounts reclassified from accumulated other comprehensive income (loss), before income tax | **—** | **99.0** | **(0.8)** | **98.2** |
| Income tax expense (benefit) | **—** | **23.9** | **(0.3)** | **23.6** |
| Net current period other comprehensive (loss) net of income taxes | **(41.8)** | **(43.1)** | **(0.4)** | **(85.3)** |
| Non-controlling interest | **0.5** | **—** | **—** | **0.5** |
| Distribution of TimkenSteel | **3.1** | **225.3** | **—** | **228.4** |
| Net current period comprehensive (loss) income, net of income taxes and non-controlling interest | **(38.2)** | **182.2** | **(0.4)** | **143.6** |
| **Balance at December 31, 2014** | **$ (0.7)** | **$ (481.0)** | **$ (0.8)** | **$ (482.5)** |

| | Foreign currency translation adjustments | Pension and postretirement liability adjustments | Change in fair value of derivative financial instruments | Total |
|---|---|---|---|---|
| Balance, December 31, 2012 | $ 49.0 | $ (1,061.5) | $ (0.7) | $ (1,013.2) |
| Other comprehensive (loss) income before reclassifications, before income tax | (19.0) | 494.2 | 0.7 | 475.9 |
| Amounts reclassified from accumulated other comprehensive income (loss), before income tax | — | 130.6 | (0.4) | 130.2 |
| Income tax expense | — | (226.5) | — | (226.5) |
| Net current period other comprehensive (loss) income, net of income taxes | (19.0) | 398.3 | 0.3 | 379.6 |
| Non-controlling interest | 7.5 | — | — | 7.5 |
| Net current period comprehensive (loss) income, net of income taxes and non-controlling interest | (11.5) | 398.3 | 0.3 | 387.1 |
| Balance at December 31, 2013 | $ 37.5 | $ (663.2) | $ (0.4) | $ (626.1) |

Other comprehensive (loss) income before reclassifications, before income tax includes the effect of foreign currency. The reclassification of the pension and postretirement liability adjustment was included in costs of products sold and selling, general and administrative expenses on the Consolidated Statements of Income. The reclassification of the change in fair value of derivative financial instruments was included in other income (expense), net on the Consolidated Statements of Income.

## NOTE 6 – INVENTORIES

The components of inventories at December 31, 2014 and 2013 were as follows:

| | 2014 | 2013 |
|---|---|---|
| Manufacturing supplies | **$ 25.0** | $ 26.8 |
| Raw materials | **51.3** | 62.3 |
| Work in process | **291.3** | 199.2 |
| Finished products | **302.7** | 312.7 |
| Subtotal | **$ 598.3** | $ 601.0 |
| Allowance for surplus and obsolete inventory | **(12.8)** | (18.4) |
| Total Inventories, net | **$ 585.5** | $ 582.6 |

Inventories valued on the FIFO cost method were 52% and the remaining 48% were valued by the LIFO method. If all inventories had been valued at FIFO, inventories would have been $199.7 million and $199.3 million greater at December 31, 2014 and 2013, respectively. The Company recognized an increase in its LIFO reserve of $0.4 million during 2014, compared to a decrease in its LIFO reserve of $3.8 million during 2013.

During the third quarter of 2014, the Company recorded an inventory valuation adjustment of $18.7 million related to its former Aerospace segment. The Company recorded this adjustment during the third quarter of 2014 as a result of the announcement of a plan to exit the engine overhaul business, as well as other product lines, and lower than expected future sales. The Company disposed of the related inventory during the fourth quarter of 2014.

## NOTE 7 – PROPERTY, PLANT AND EQUIPMENT

The components of property, plant and equipment, net at December 31, 2014 and 2013 were as follows:

| | 2014 | 2013 |
|---|---|---|
| Land and buildings | **$ 428.8** | $ 382.3 |
| Machinery and equipment | **1,735.3** | 2,013.0 |
| Subtotal | **$ 2,164.1** | $ 2,395.3 |
| Less allowances for depreciation | **(1,383.6)** | (1,539.5) |
| Property, Plant and Equipment, net | **$ 780.5** | $ 855.8 |

Total depreciation expense was $115.5 million, $124.7 million and $131.8 million in 2014, 2013 and 2012, respectively. At December 31, 2013, property, plant and equipment, net included $63.3 million of capitalized software. Depreciation expense for capitalized software was $13.7 million, $23.1 million and $21.5 million in 2014, 2013 and 2012, respectively.

During the middle of 2014, the Company transferred approximately $45 million of capitalized software from property, plant and equipment to intangible assets. The Company did not reclassify prior year amounts to conform to the current year presentation because management of the Company determined the amount was immaterial to the 2013 Consolidated Balance Sheet.

In November 2013, the Company finalized the sale of its former manufacturing facility in Sao Paulo. The Company expects to receive approximately $33 million over a twenty-four month period, of which $20.6 million was received as of December 31, 2014. The total costs of this transaction, including the net book value of the real estate and broker's commissions, were approximately $3 million. The Company began recognizing the gain on the sale of this site using the installment method. In the fourth quarter of 2013, the Company recognized a gain of $5.4 million ($5.4 million after tax). In the first quarter of 2014, the Company changed to the full accrual method of recognizing the gain after it had received 25% of the total sales value. As a result, the Company recognized the remaining gain of $22.6 million ($19.5 million after tax) related to this transaction during the first quarter of 2014. During 2014, the Company also recorded interest income of $2.1 million on deferred payments related to this transaction.

Note 7 – Property, Plant and Equipment (continued)

During the third quarter of 2014, the Company classified assets of the aerospace engine overhaul business, located in Mesa, Arizona, as assets held for sale. In connection with this classification, the Company recorded an impairment charge of $1.2 million. In November 2014, the Company sold the assets of the aerospace engine overhaul business for $7.4 million and recorded an immaterial loss.

## NOTE 8 – GOODWILL AND OTHER INTANGIBLE ASSETS

**GOODWILL:**

The Company tests goodwill and indefinite-lived intangible assets for impairment at least annually. The Company performs its annual impairment test as of October 1 after the annual forecasting process is completed. Furthermore, goodwill and indefinite-lived intangible assets are reviewed for impairment whenever events or changes in circumstances indicate that the carrying value may not be recoverable.

The Company reviews goodwill for impairment at the reporting unit level. The Mobile Industries segment has four reporting units and the Process Industries segment has two reporting units.

Changes in the carrying value of goodwill were as follows:

Year ended December 31, 2014:

| | Mobile Industries | Process Industries | Total |
|---|---|---|---|
| Beginning Balance | **$ 176.7** | **$ 169.4** | **$ 346.1** |
| Acquisitions | **—** | **3.3** | **3.3** |
| Impairment | **(86.3)** | **—** | **(86.3)** |
| Other | **(0.8)** | **(2.8)** | **(3.6)** |
| Ending Balance | **$ 89.6** | **$ 169.9** | **$ 259.5** |

The change related to acquisitions reflects the results of a preliminary purchase price allocation for the acquisition of Schulz completed on April 28, 2014 and Revolvo on November 30, 2014. The goodwill acquired from Schulz of $2.9 million is tax-deductible and will be amortized over 15 years. The goodwill acquired from Revolvo of $0.4 million is tax-deductible and is estimated to be amortized over approximately 15 years. "Other" primarily included foreign currency translation adjustments for 2014. Refer to *Note 3 – Acquisitions and Divestitures* for additional information on the acquisitions listed above.

During the third quarter of 2014, the Company reviewed goodwill for impairment for two of its reporting units within the Company's former Aerospace segment (now included in the Mobile Industries segment) as a result of declining sales forecasts and financial performance within the segment. The Company utilizes both an income approach and a market approach in testing goodwill for impairment. The Company utilized updated forecasts for the income approach as part of the goodwill impairment review. As a result of the lower earnings and cash flow forecasts, the Company determined that the Aerospace Transmissions and the Aerospace Aftermarket reporting units could not support the carrying value of their goodwill. As a result, the Company recorded a pretax impairment loss of $86.3 million during the third quarter of 2014, which was reported in impairment and restructuring charges in the Consolidated Statement of Income.

In 2013 and 2012, no goodwill impairment losses were recorded.

## Note 8 – Goodwill and Other Intangible Assets (continued)

Year ended December 31, 2013:

| | Mobile Industries | Process Industries | Total |
|---|---|---|---|
| Beginning Balance | $ 171.9 | $ 154.4 | $ 326.3 |
| Acquisitions | 4.3 | 13.8 | 18.1 |
| Other | 0.5 | 1.2 | 1.7 |
| Ending Balance | $ 176.7 | $ 169.4 | $ 346.1 |

Acquisitions in 2013 primarily relate to the purchase price allocation for Interlube completed on March 11, 2013, Smith Services completed on April 11, 2013 and Standard Machine completed on May 13, 2013. "Other" includes foreign currency translation adjustments for 2013. The goodwill acquired from Smith Services of $1.7 million is tax-deductible and will be amortized over 15 years.

**INTANGIBLES ASSETS:**

The following table displays intangible assets as of December 31:

| | **2014** | | | 2013 | | |
|---|---|---|---|---|---|---|
| | **Gross Carrying Amount** | **Accumulated Amortization** | **Net Carrying Amount** | Gross Carrying Amout | Accumulated Amortization | Net Carrying Amount |
| Intangible assets subject to amortization: | | | | | | |
| Customer relationships | **$ 160.1** | **$ 59.0** | **$ 101.1** | $ 160.4 | $ 49.3 | $ 111.1 |
| Know-how | **33.4** | **5.1** | **28.3** | 31.4 | 4.4 | 27.0 |
| Industrial license agreements | **0.1** | **0.1** | **—** | 0.1 | 0.1 | — |
| Land-use rights | **8.7** | **4.7** | **4.0** | 8.9 | 4.5 | 4.4 |
| Patents | **2.3** | **2.0** | **0.3** | 2.3 | 1.8 | 0.5 |
| Technology use | **37.0** | **11.9** | **25.1** | 44.4 | 17.2 | 27.2 |
| Trademarks | **5.4** | **3.0** | **2.4** | 4.6 | 2.7 | 1.9 |
| PMA licenses | **5.3** | **4.5** | **0.8** | 8.8 | 4.0 | 4.8 |
| Non-compete agreements | **3.5** | **3.2** | **0.3** | 3.2 | 2.8 | 0.4 |
| Software | **235.0** | **182.0** | **53.0** | — | — | — |
| | **$ 490.8** | **$ 275.5** | **$ 215.3** | $ 264.1 | $ 86.8 | $ 177.3 |
| Intangible assets not subject to amortization: | | | | | | |
| Tradename | **$ 15.8** | **$ —** | **$ 15.8** | $ 15.9 | $ — | $ 15.9 |
| FAA air agency certificates | **8.7** | **—** | **8.7** | 14.2 | — | 14.2 |
| | **$ 24.5** | **$ —** | **$ 24.5** | $ 30.1 | $ — | $ 30.1 |
| Total intangible assets | **$ 515.3** | **$ 275.5** | **$ 239.8** | $ 294.2 | $ 86.8 | $ 207.4 |

During the middle of 2014, the Company transferred approximately $45 million of capitalized software from property, plant and equipment to intangible assets. The Company did not reclassify prior year amounts to conform to the current year presentation because management of the Company determined the amount was immaterial to the 2013 Consolidated Balance Sheet.

In addition to recording an impairment loss related to goodwill, the Company recorded an impairment loss of $9.9 million related to intangible assets within the former Aerospace segment during the third quarter of 2014.

### Note 8 – Goodwill and Other Intangible Assets (continued)

Intangible assets acquired in 2014 were $4.9 million for the Schulz acquisition and $3.4 million for the Revolvo acquisition. Intangible assets subject to amortization acquired in 2014 were assigned useful lives of five to 20 years and had a weighted-average amortization period of 15.0 years. Intangible assets acquired in 2013 were $6.1 million for the Standard Machine acquisition, $0.7 million for the Smith Services acquisition and $6.2 million for the Interlube acquisition. Intangible assets subject to amortization acquired in 2013 were assigned useful lives of two to 20 years and had a weighted-average amortization period of 18.4 years.

Amortization expense for intangible assets was $21.5 million, $17.7 million and $17.8 million for the years ended December 31, 2014, 2013 and 2012, respectively. Amortization expense for intangible assets is estimated to be approximately: $17.5 million in 2015; $17.4 million in 2016; $17.3 million in 2017; $17.0 million in 2018; and $15.0 million in 2019.

## NOTE 9 – FINANCING ARRANGEMENTS

Short-term debt for the years ended December 31 was as follows:

| | **2014** | 2013 |
|---|---|---|
| Variable-rate lines of credit for certain of the Company's foreign subsidiaries with various banks with interest rates ranging from 0.51% to 5.13% and 0.87% to 4.86% at December 31, 2014 and 2013, respectively | **$ 7.4** | $ 18.6 |
| Short-term debt | **$ 7.4** | $ 18.6 |

The lines of credit for certain of the Company's foreign subsidiaries provide for borrowings up to $234.0 million. Most of these lines of credit are uncommitted. At December 31, 2014, the Company's foreign subsidiaries had borrowings outstanding of $7.4 million and guarantees of $5.8 million, which reduced the availability under these facilities to $220.8 million.

The weighted-average interest rate on short-term debt during the year was 3.1%, 3.2% and 3.2% in 2014, 2013 and 2012, respectively. The weighted-average interest rate on short-term debt outstanding at December 31, 2014 and 2013 was 1.39% and 4.6%, respectively.

On April 30, 2014, the Company amended its Asset Securitization Agreement, reducing its aggregate borrowing availability from $200 million to $100 million. This agreement matures on November 30, 2015. Under the terms of the Asset Securitization Agreement, the Company sells, on an ongoing basis, certain domestic trade receivables to Timken Receivables Corporation, a wholly-owned consolidated subsidiary that in turn uses the trade receivables to secure borrowings which are funded through a vehicle that issues commercial paper in the short-term market. Borrowings under the Asset Securitization Agreement are limited to certain borrowing base calculations. Any amounts outstanding under this Asset Securitization Agreement would be reported in short-term debt on the Company's Consolidated Balance Sheets. As of December 31, 2014 and 2013, there were no outstanding borrowings under the Asset Securitization Agreement. However, certain borrowing base limitations reduced the availability of the Asset Securitization Agreement to $72.7 million at December 31, 2014. The cost of this facility, which is the commercial paper rate plus program fees, is considered a financing cost and is included in interest expense in the Consolidated Statements of Income. The yield rate was 0.20%, 0.96% and 1.06%, at December 31, 2014, 2013 and 2012, respectively.

Note 9 – Financing Arrangements (continued)

Long-term debt for the years ended December 31 was as follows:

| | 2014 | 2013 |
|---|---|---|
| Fixed-rate Medium-Term Notes, Series A, mature at various dates through May 2028, with interest rates ranging from 6.74% to 7.76% | **$ 175.0** | $ 175.0 |
| Fixed-rate Senior Unsecured Notes, maturing on September 1, 2024, with an interest rate of 3.875% | **346.4** | — |
| Fixed-rate Senior Unsecured Notes, maturing on September 15, 2014, with an interest rate of 6.0% | **—** | 249.9 |
| Other | **1.3** | 2.2 |
| Total debt | **$ 522.7** | $ 427.1 |
| Less current maturities | **0.6** | 250.7 |
| Long-term debt | **$ 522.1** | $ 176.4 |

The Company has a $500 million Senior Credit Facility, which matures on May 11, 2016. At December 31, 2014, the Company had no outstanding borrowings under the Senior Credit Facility. Under the Senior Credit Facility, the Company has two financial covenants: a consolidated leverage ratio and a consolidated interest coverage ratio. At December 31, 2014, the Company was in full compliance with the covenants under the Senior Credit Facility.

On August 20, 2014, the Company issued the 2024 Notes. The Company used the net proceeds from the issuance of the 2024 Notes to repay the Company's 2014 Notes and for general corporate purposes.

The maturities of long-term debt for the five years subsequent to December 31, 2014 are as follows: 2015 – $0.6 million; 2016 – $15.7 million; 2017 – $5.0 million; 2018 – zero and 2019 – zero.

Interest paid was $34.4 million in 2014, $31.0 million in 2013 and $32.4 million in 2012. This differs from interest expense due to the timing of payments and interest capitalized of $1.6 million in 2014, $12.7 million in 2013 and $4.9 million in 2012.

The Company and its subsidiaries lease a variety of real property and equipment. Rent expense under operating leases amounted to $33.0 million, $35.6 million and $35.1 million in 2014, 2013 and 2012, respectively. At December 31, 2014, future minimum lease payments for noncancelable operating leases totaled $96.2 million and are payable as follows: 2015 – $28.5 million; 2016 – $21.5 million; 2017 – $16.4 million; 2018 – $11.2 million; 2019 – $8.3 million and $10.3 million thereafter.

## NOTE 10 – CONTINGENCIES

The Company and certain of its subsidiaries have been identified as potentially responsible parties for investigation and remediation under the Superfund or similar state laws with respect to certain sites. Claims for investigation and remediation have been asserted against numerous other entities, which are believed to be financially solvent and are expected to fulfill their proportionate share of the obligation.

The Company had an accrual of $1.5 million and $2.1 million for environmental matters that are probable and reasonably estimable as of December 31, 2014 and 2013, respectively. This accrual is recorded based upon the best estimate of costs to be incurred in light of the progress made in determining the magnitude of remediation costs, the timing and extent of remedial actions required by governmental authorities and the amount of the Company's liability in proportion to other responsible parties. Of the 2014 accrual, $0.6 million is included in the rollforward of the restructuring accrual as of December 31, 2014, discussed further in *Note 11 – Impairment and Restructuring Charges.*

In addition, the Company is subject to various lawsuits, claims and proceedings, which arise in the ordinary course of its business. The Company accrues costs associated with legal and non-income tax matters when they become probable and reasonably estimable. Accruals are established based on the estimated undiscounted cash flows to settle the obligations and are not reduced by any potential recoveries from insurance or other indemnification claims. Management believes that any ultimate liability with respect to these actions, in excess of amounts provided, will not materially affect the Company's Consolidated Financial Statements.

In October 2014, the Brazilian government antitrust agency announced that it had opened an investigation of alleged antitrust violations in the bearing industry. The Company's Brazilian subsidiary, Timken do Brasil Comercial Importadora Ltda, was included in the investigation. While the Company is unable to predict the ultimate length, scope or results of the investigation, management believes that the outcome will not have a material effect on the Company's consolidated financial position; however, any such outcome may be material to the results of operations of any particular period in which costs, if any, are recognized. Based on current facts and circumstances, the low end of the range for potential penalties, if any, would be immaterial to the Company.

Note 10 – Contingencies (continued)

**PRODUCT WARRANTIES:**

In addition to the contingencies above, the Company provides limited warranties on certain of its products. The following is a rollforward of the warranty reserves for 2014 and 2013:

| | **2014** | 2013 |
|---|---|---|
| Beginning balance, January 1 | **$ 4.2** | $ 4.3 |
| Expense (Income) | **(1.4)** | 4.7 |
| Payments | **(1.1)** | (4.8) |
| Ending balance, December 31 | **$ 1.7** | $ 4.2 |

The product warranty accrual for 2014 and 2013 was included in other current liabilities on the Consolidated Balance Sheets.

## NOTE 11 – IMPAIRMENT AND RESTRUCTURING CHARGES

Impairment and restructuring charges by segment were as follows:

Year ended December 31, 2014:

| | Mobile Industries | Process Industries | Corporate | Total |
|---|---|---|---|---|
| Impairment charges | **$ 98.2** | **$ 0.3** | **$ 0.4** | **$ 98.9** |
| Severance expense and related benefit costs | **9.3** | **1.4** | **—** | **10.7** |
| Exit costs | **2.0** | **1.8** | **—** | **3.8** |
| Total | **$ 109.5** | **$ 3.5** | **$ 0.4** | **$ 113.4** |

Year ended December 31, 2013:

| | Mobile Industries | Process Industries | Corporate | Total |
|---|---|---|---|---|
| Impairment charges | $ — | $ 0.1 | $ — | $ 0.1 |
| Severance expense and related benefit costs | 6.6 | 2.6 | — | 9.2 |
| Exit costs | (1.5) | 0.9 | — | (0.6) |
| Total | $ 5.1 | $ 3.6 | $ — | $ 8.7 |

Year ended December 31, 2012:

| | Mobile Industries | Process Industries | Corporate | Total |
|---|---|---|---|---|
| Impairment charges | $ 6.5 | $ 0.1 | $ — | $ 6.6 |
| Severance expense and related benefit costs | 16.8 | 1.6 | — | 18.4 |
| Exit costs | 4.2 | 0.3 | — | 4.5 |
| Total | $ 27.5 | $ 2.0 | $ — | $ 29.5 |

Note 11 – Impairment and Restructuring Charges (continued)

The following discussion explains the major impairment and restructuring charges recorded for the periods presented; however, it is not intended to reflect a comprehensive discussion of all amounts in the tables above.

**MOBILE INDUSTRIES:**

On September 8, 2014, the Company announced plans to restructure its Aerospace segment. In connection with the restructuring, the Company: 1) eliminated leadership positions and integrated substantially all aerospace activities into Mobile Industries under the direction of its Group President; 2) sold the assets of its aerospace engine overhaul business, located in Mesa, Arizona, prior to the end of the year; 3) evaluated strategic alternatives for its aerospace MRO parts business, also located in Mesa; and 4) plans to close its aerospace bearing facility located in Wolverhampton, U.K. by early 2016, rationalizing the capacity into existing facilities. In conjunction with this announcement, the Company reviewed goodwill for impairment for its three reporting units within the Aerospace segment as a result of declining sales forecasts and financial performance within the segment. As a result of that review, the Company recorded a pretax goodwill impairment charge of $86.3 million during the third quarter of 2014 related to its Aerospace Transmissions and Aerospace Aftermarket reporting units. In addition, the Company recorded an intangible asset impairment charge of $9.9 million, an impairment charge of $1.2 million for its engine overhaul business, which it classified as assets held for sale, and severance and related benefits of $0.3 million. During the fourth quarter of 2014, the Company recorded severance and related benefits of $3.7 million related to the planned closure of Wolverhampton. See *Note 17 – Fair Value* for additional information on the impairment charges for the Aerospace segment.

In May 2012, the Company announced the closure of its manufacturing facility in St. Thomas, which was expected to be completed in approximately one year, and was intended to consolidate bearing production from this plant with existing U.S. operations to better align the Company's manufacturing footprint and customer base. In connection with this closure, the Company also moved customer service for the Canadian market to its offices in Toronto. The Company completed the closure of this manufacturing facility on March 31, 2013. The closure of the St. Thomas manufacturing facility displaced 190 employees. The Company expects to incur pretax costs of approximately $55 million to $60 million in connection with this closure, of which approximately $20 million to $25 million is expected to be pretax cash costs. The Company has incurred pretax costs related to this closure of approximately $41.7 million as of December 31, 2014, including rationalization costs recorded in cost of products sold. During 2013, the Company recorded $1.1 million of severance and related benefits related to this closure. During 2012, the Company recorded $16.9 million of severance and related benefits, including a curtailment of pension benefits of $10.7 million, and impairment charges of $6.5 million, related to this closure.

In March 2007, the Company announced the closure of its manufacturing facility in Sao Paulo. The Company completed the closure of this manufacturing facility on March 31, 2010. Mobile Industries has incurred cumulative pretax expenses of approximately $55.2 million as of December 31, 2014 related to this closure. In 2013 and 2012, the Company recorded a favorable adjustment of $2.0 million and exit costs of $6.8 million, respectively, associated with the closure of this facility. The favorable adjustment for 2013 and exit costs for 2012 primarily related to environmental remediation costs.

In addition to the above charges, the Company incurred $2.9 million of severance and related benefit costs related to the rationalization of one of its facilities in Europe in 2014. The Company also recorded a favorable adjustment of $2.7 million during 2012 for environmental exit costs at the site of its former plant in Columbus, Ohio. The favorable adjustment was a result of the sale of the real estate at the site of this former plant during the first quarter of 2012. The buyer assumed responsibility for the environmental remediation as a result of the sale. The buyer was able to obtain funding from the State of Ohio to remediate the site.

**WORKFORCE REDUCTIONS:**

In 2013, the Company began the realignment of its organization to improve efficiency and reduce costs. During 2013, the Company recognized $5.9 million of severance and related benefit costs to eliminate approximately 180 positions. Of the $5.9 million charge for 2013, $3.4 million related to the Mobile Industries segment and $2.5 million related to the Process Industries segment.

Note 11 – Impairment and Restructuring Charges (continued)

**CONSOLIDATED RESTRUCTURING ACCRUAL:**

The following is a rollforward of the consolidated restructuring accrual for the years ended December 31:

| | **2014** | 2013 |
|---|---|---|
| Beginning balance, January 1 | **$ 10.8** | $ 17.6 |
| Expense | **14.5** | 8.7 |
| Payments | **(15.8)** | (15.5) |
| Ending balance, December 31 | **$ 9.5** | $ 10.8 |

The restructuring accrual at December 31, 2014 and 2013 was included in other current liabilities on the Consolidated Balance Sheets. At December 31, 2014 and 2013, the restructuring accrual included $0.6 million and $1.2 million, respectively, of environmental remediation costs. The Company adjusts environmental remediation accruals based on the best available estimate of costs to be incurred, the timing and extent of remedial actions required by governmental authorities and the amount of the Company's liability in proportion to other responsible parties.

## NOTE 12 – STOCK COMPENSATION PLANS

Under the Company's long-term incentive plan, the Company's common shares have been made available for grant, at the discretion of the Compensation Committee of the Board of Directors, to officers and key employees in the form of stock option awards. Stock option awards typically have a ten-year term and generally vest in 25% increments annually beginning on the first anniversary of the date of grant. In addition to stock option awards, the Company has granted restricted shares under the long-term incentive plan. Restricted shares typically vest in 25% increments annually beginning on the first year anniversary of the date of grant and are expensed over the vesting period.

Upon the Spinoff, outstanding long-term incentive awards were treated in a manner similar to that experienced by the Company's shareholders with respect to their common shares of the Company. As a result, common shares of the Company, as well as outstanding stock options, restricted stock units, restricted share, deferred share and performance share awards, were bifurcated such that common shares and the equity awards were split into shares or equity awards of both the Company and TimkenSteel. Individuals kept existing common shares of the Company and received one common share of TimkenSteel for every two common shares of the Company that they owned immediately prior to the Spinoff. Any unvested or vested but unexercised equity-based incentives held immediately prior to the Spinoff were treated in a similar manner.

Pre- and post-Spinoff stock option awards were intended to provide comparable value. The adjustment for each award was based on the average of the high and low stock prices on both June 30 and July 1, 2014. The strike price of each stock award was adjusted so that each participant's aggregate value was generally preserved.

In addition to the bifurcation of then-currently held stock, stock options, restricted stock units and restricted stock, the 2012 to 2014 strategic performance share award was scored upon the Spinoff based on results at that time and the award will be paid in March 2015. The award will be paid in cash.

The 2013 to 2015 strategic performance share measurement cycle also ended June 30, 2014, half way through the originally intended performance cycle. Performance for the first 18 months of the 2013-2015 performance cycle was scored as of June 30, 2014 and the earned amount, which was based on one-half of the original target number of strategic performance shares, will be paid in early 2016. The award will be paid in cash. In August 2014, a replacement grant covering the performance period from July 1, 2014 through December 31, 2015 was issued.

During 2014, 2013 and 2012, the Company recognized stock-based compensation expense of $13.7 million ($8.5 million after tax or $0.09 per diluted share), $12.1 million ($7.6 million after tax or $0.08 per diluted share) and $10.8 million ($6.8 million after tax or $0.07 per diluted share), respectively, for stock option awards.

The fair value of stock option awards granted during 2014, 2013 and 2012 was estimated at the date of grant using a Black-Scholes option-pricing method with the following assumptions:

Note 12 – Stock Compensation Plans (continued)

| | 2014 | 2013 | 2012 |
|---|---|---|---|
| Weighted-average fair value per option (pre-Spinoff) | **$ 23.09** | $ 21.17 | $ 20.16 |
| Risk-free interest rate | **1.64%** | 1.09% | 1.15% |
| Dividend yield | **1.75%** | 2.29% | 1.94% |
| Expected stock volatility | **50.96%** | 50.66% | 50.00% |
| Expected life – years | **5** | 6 | 6 |

Historical information was the primary basis for the selection of the expected dividend yield, expected volatility and the expected lives of the options. The dividend yield was calculated based upon the last dividend prior to the grant compared to the stock price on the dividend date. The risk-free interest rate was based upon yields of U.S. zero coupon issues with a term equal to the expected life of the option being valued. Forfeitures were estimated at 4%.

A summary of option activity for the year ended December 31, 2014 is presented below:

| | Number of Shares | Weighted-average Exercise Price | Weighted-average Remaining Contractual Term | Aggregate Intrinsic Value (millions) |
|---|---|---|---|---|
| Outstanding – beginning of year | **3,384,687** | **$ 40.50** | | |
| Granted – new awards | **602,905** | **56.87** | | |
| Exercised | **(764,001)** | **21.74**[(a)] | | |
| Canceled or expired | **(55,228)** | **48.16** | | |
| Outstanding – end of year | **3,168,363** | **$ 33.57** | **7 years** | **$ 28.9** |
| Options expected to vest | **3,117,761** | **$ 33.45** | **7 years** | **$ 28.8** |
| Options exercisable | **1,734,601** | **$ 28.49** | **5 years** | **$ 24.6** |

[(a)] Reflects the weighted average price at time of exercise with respect to pre- or post-Spinoff prices.

The total intrinsic value of options exercised during the years ended December 31, 2014, 2013 and 2012 was $21.5 million, $25.2 million and $28.2 million, respectively. Net cash proceeds from the exercise of stock options were $16.8 million, $13.1 million and $13.8 million, respectively. Income tax benefits were $5.9 million, $8.9 million and $8.1 million for the years ended December 31, 2014, 2013 and 2012, respectively.

In 2014, the Company issued 102,070 strategic performance shares and 431,785 time-vesting restricted stock units to officers and key employees. These strategic performance shares are performance-based restricted stock units that vest based on achievement of specified performance objectives and cliff-vest after 1.5 years. Strategic performance shares settle in either cash or shares, with 1,480 shares expected to settle in cash and 100,590 expected to settle in shares. Time-vesting restricted stock units vest on one of three schedules: 25% increments annually beginning on the first anniversary of the grant, cliff-vest after 3 years, or cliff-vest after 5 years. Time-vesting restricted stock units also settle in either cash or shares, with 11,729 time-vesting restricted stock units expected to settle in cash and 420,056 time-vesting restricted stock units expected to settle in common shares. For time-vesting restricted stock units that are expected to settle in cash, the Company has $15.3 million as of December 31, 2014, accrued on the Consolidated Balance Sheets. This is included in other non-current liabilities and salaries, wages and benefits for $5.3 million and $10.0 million, respectively.

A summary of restricted share activity, including restricted shares, deferred shares, strategic performance shares and strategic shares that will settle in common shares, for the year ended December 31, 2014 is as follows:

| | Number of Shares | Weighted-average Grant Date Fair Value |
|---|---|---|
| Outstanding – beginning of year | **397,052** | **$ 43.57** |
| Granted – new awards | **520,646** | **43.38** |
| Vested | **(171,135)** | **56.97** |
| Canceled or expired | **(59,533)** | **51.13** |
| Outstanding – end of year | **687,030** | **$ 35.21** |

FINANCIALS AND FOOTNOTES

Note 12 – Stock Compensation Plans (continued)

As of December 31, 2014, a total of 687,030 restricted shares have been awarded that have not yet vested. The Company distributed 171,135, 221,542 and 249,569 shares in 2014, 2013 and 2012, respectively, due to the vesting of these awards. The shares awarded in 2014, 2013 and 2012 totaled 520,912, 111,640 and 161,905, respectively. The Company recognized compensation expense of $10.1 million, $6.5 million and $7.2 million, for the years ended December 31, 2014, 2013 and 2012, respectively, relating to restricted shares.

As of December 31, 2014, the Company had unrecognized compensation expense of $27.4 million related to stock option awards and restricted shares. The unrecognized compensation expense is expected to be recognized over a total weighted-average period of two years. The number of shares available for future grants for all plans at December 31, 2014 was 3,537,197.

## NOTE 13 – RETIREMENT BENEFIT PLANS

The Company and its subsidiaries sponsor a number of defined benefit pension plans, which cover eligible employees, including certain employees in foreign countries. These plans are generally noncontributory. Pension benefits earned are generally based on years of service and compensation during active employment. The cash contributions for the Company's defined benefit pension plans were $21.1 million, $120.7 million, and $325.8 million in 2014, 2013 and 2012, respectively.

The following tables summarize the net periodic benefit cost information and the related assumptions used to measure the net periodic benefit cost for the years ended December 31:

| | U.S. Plans | | | International Plans | | |
|---|---|---|---|---|---|---|
| | **2014** | 2013 | 2012 | **2014** | 2013 | 2012 |
| Components of net periodic benefit cost: | | | | | | |
| Service cost | **$ 21.5** | $ 35.7 | $ 31.4 | **$ 2.4** | $ 2.8 | $ 3.3 |
| Interest cost | **98.3** | 116.2 | 131.3 | **17.7** | 18.5 | 19.8 |
| Expected return on plan assets | **(152.0)** | (207.6) | (197.8) | **(23.7)** | (24.4) | (23.3) |
| Amortization of prior service cost | **3.5** | 4.5 | 9.0 | **0.1** | — | 0.3 |
| Amortization of net actuarial loss | **55.6** | 109.2 | 76.9 | **5.3** | 7.6 | 6.4 |
| Pension curtailments and settlements | **32.7** | — | — | **0.8** | 7.2 | 11.6 |
| Less: discontinued operations | **(8.0)** | (24.2) | (19.4) | **0.4** | 0.4 | 0.4 |
| Net periodic benefit cost | **$ 51.6** | $ 33.8 | $ 31.4 | **$ 3.0** | $ 12.1 | $ 18.5 |

| Assumptions | **2014** | 2013 | 2012 |
|---|---|---|---|
| U.S. Plans: | | | |
| Discount rate | **4.68% / 5.02%** | 4.00% | 5.00% |
| Future compensation assumption | **2.00% to 3.00%** | 2.00% to 3.00% | 2.00% to 3.00% |
| Expected long-term return on plan assets | **7.25%** | 8.00% | 8.25% |
| International Plans: | | | |
| Discount rate | **3.25% to 9.75%** | 2.75% to 9.00% | 4.75% to 9.50% |
| Future compensation assumption | **2.30% to 8.00%** | 2.30% to 8.00% | 2.50% to 8.00% |
| Expected long-term return on plan assets | **3.00% to 8.50%** | 3.25% to 8.50% | 3.25% to 9.00% |

The discount rate assumption is based on current rates of high-quality long-term corporate bonds over the same period that benefit payments will be required to be made. The expected rate of return on plan assets assumption is based on the weighted-average expected return on the various asset classes in the plans' portfolio. The asset class return is developed using historical asset return performance as well as current market conditions such as inflation, interest rates and equity market performance.

For expense purposes in 2014, the Company applied a discount rate of 5.02% for the first four months of 2014, and a discount rate of 4.68% for the last eight months of 2014 to its U.S. defined benefit pension plans as a result of a remeasurement of the U.S. defined benefit pension plans due to the spinoff of the plans related to TimkenSteel. For expense purposes in 2015, the Company will apply a discount rate of 4.20% to its U.S. defined benefit pension plans.

For expense purposes in 2014, the Company applied an expected rate of return of 7.25% for the Company's U.S. pension plan assets. For expense purposes in 2015, the Company will apply an expected rate of return on plan assets of 6.00%. The reduction in expected rate of return on plan assets is due to the Company's move to a higher level of debt securities offset by a lower level of equity securities to maintain its overfunded status on U.S. pension plans.

## Note 13 – Retirement Benefit Plans (continued)

The following tables set forth the change in benefit obligation, change in plan assets, funded status and amounts recognized on the Consolidated Balance Sheets for the defined benefit pension plans as of December 31, 2014 and 2013:

| | U.S. Plans | | International Plans | |
|---|---|---|---|---|
| | **2014** | 2013 | **2014** | 2013 |
| Change in benefit obligation: | | | | |
| Benefit obligation at beginning of year | **$ 2,642.4** | $ 2,996.5 | **$ 491.1** | $ 499.8 |
| Service cost | **21.5** | 35.7 | **2.4** | 2.8 |
| Interest cost | **98.3** | 116.2 | **17.7** | 18.5 |
| Amendments | **—** | — | **0.3** | — |
| Actuarial losses (gains) | **239.6** | (274.0) | **38.7** | (0.4) |
| Employee contributions | **—** | — | **0.3** | 0.2 |
| International plan exchange rate change | **—** | — | **(29.5)** | 5.3 |
| Benefits paid | **(234.6)** | (232.0) | **(23.5)** | (35.1) |
| Spinoff of TimkenSteel | **(1,063.3)** | — | **(81.8)** | — |
| Benefit obligation at end of year | **$ 1,703.9** | $ 2,642.4 | **$ 415.7** | $ 491.1 |
| Change in plan assets: | | | | |
| Fair value of plan assets at beginning of year | **$ 2,870.0** | $ 2,698.4 | **$ 420.6** | $ 400.0 |
| Actual return on plan assets | **250.5** | 293.8 | **42.2** | 40.2 |
| Employee contributions | **—** | — | **0.3** | 0.2 |
| Company contributions / payments | **4.5** | 109.8 | **16.6** | 10.9 |
| International plan exchange rate change | **—** | — | **(21.2)** | 4.4 |
| Benefits paid | **(234.6)** | (232.0) | **(23.5)** | (35.1) |
| Spinoff of TimkenSteel | **(1,118.0)** | — | **(85.6)** | — |
| Fair value of plan assets at end of year | **1,772.4** | 2,870.0 | **349.4** | 420.6 |
| Funded status at end of year | **$ 68.5** | $ 227.6 | **$ (66.3)** | $ (70.5) |
| Amounts recognized on the Consolidated Balance Sheets: | | | | |
| Non-current assets | **$ 176.2** | $ 342.3 | **$ —** | $0.3 |
| Current liabilities | **(4.1)** | (4.8) | **(4.0)** | (1.7) |
| Non-current liabilities | **(103.6)** | (109.9) | **(62.3)** | (69.1) |
| | **$ 68.5** | $ 227.6 | **$ (66.3)** | $ (70.5) |
| Amounts recognized in accumulated other comprehensive loss: | | | | |
| Net actuarial loss | **$ 566.5** | $ 846.9 | **$ 132.3** | $ 142.2 |
| Net prior service cost | **11.9** | 18.5 | **0.7** | 0.5 |
| Accumulated other comprehensive loss | **$ 578.4** | $ 865.4 | **$ 133.0** | $ 142.7 |

Note 13 – Retirement Benefit Plans (continued)

| Changes in plan assets and benefit obligations recognized in accumulated other comprehensive loss (AOCL): | 2014 | 2013 | 2014 | 2013 |
|---|---|---|---|---|
| AOCL at beginning of year | **$ 865.4** | $ 1,339.2 | **$ 142.7** | $ 173.7 |
| Net actuarial loss (gain) | **141.0** | (360.1) | **20.2** | (16.2) |
| Prior service cost | **—** | — | **0.3** | — |
| Recognized net actuarial loss | **(55.6)** | (109.2) | **(5.3)** | (7.6) |
| Recognized prior service cost | **(3.5)** | (4.5) | **(0.1)** | — |
| Loss recognized due to curtailment | **(32.7)** | — | **(0.8)** | (7.2) |
| Foreign currency impact | **—** | — | **(9.8)** | — |
| TimkenSteel Spinoff | **(336.2)** | — | **(14.2)** | — |
| Total recognized in accumulated other comprehensive loss at December 31 | **$ 578.4** | $ 865.4 | **$ 133.0** | $ 142.7 |

Amounts recognized on the Consolidated Balance Sheet for 2013 include amounts related to the Company's former steel business.

The presentation in the above tables for amounts recognized in accumulated other comprehensive loss on the Consolidated Balance Sheets is before the effect of income taxes.

The following table summarizes assumptions used to measure the benefit obligation for the defined benefit pension plans at December 31:

| Assumptions | 2014 | 2013 |
|---|---|---|
| U.S. Plans: | | |
| Discount rate | **4.20%** | 5.02% |
| Future compensation assumption | **2.00% to 3.00%** | 2.00% to 3.00% |
| International Plans: | | |
| Discount rate | **1.50% to 8.75%** | 3.25% to 9.75% |
| Future compensation assumption | **2.20% to 8.00%** | 2.30% to 8.00% |

The Company adopted the new RP-2014 mortality tables for pension obligations for the Company's U.S. defined benefit pension plans. Company-specific experience was applied to these mortality tables. This change in assumption increased pension obligations by $59.0 million for 2014.

Defined benefit pension plans in the United States represent 80% of the benefit obligation and 84% of the fair value of plan assets as of December 31, 2014.

Certain of the Company's defined benefit pension plans were overfunded as of December 31, 2014. As a result, $176.2 million and $342.6 million at December 31, 2014 and 2013, respectively, are included in non-current pension assets on the Consolidated Balance Sheets. The current portion of accrued pension cost, which is included in salaries, wages and benefits on the Consolidated Balance Sheets, was $8.1 million and $6.5 million at December 31, 2014 and 2013, respectively. In 2014, the current portion of accrued pension cost relates to unfunded plans and represents the actuarial present value of expected payments related to the plans to be made over the next 12 months.

The accumulated benefit obligation at December 31, 2014 exceeded the market value of plan assets for several of the Company's pension plans. For these plans, the projected benefit obligation was $226.3 million, the accumulated benefit obligation was $213.8 million and the fair value of plan assets was $56.4 million at December 31, 2014.

The total pension accumulated benefit obligation for all plans was $2.1 billion and $3.0 billion at December 31, 2014 and 2013, respectively.

Investment performance increased the value of the Company's pension assets by 11.2%.

As of December 31, 2014 and 2013, the Company's defined benefit pension plans did not directly hold any of the Company's common shares.

Note 13 – Retirement Benefit Plans (continued)

The estimated net actuarial loss and prior service cost for the defined benefit pension plans that will be amortized from accumulated other comprehensive loss into net periodic benefit cost over the next fiscal year are $53.3 million and $2.9 million, respectively.

The Company recorded $33.7 million of pension settlement charges, including professional fees, in 2014. These pension settlement charges primarily related to the settlement of approximately $110 million of the Company's pension obligations related to its defined benefit pension plan in the U.S. as a result of the lump sum distributions for 2014 retirements and certain deferred vested plan participants.

**PLAN ASSETS:**

The Company's target allocation for pension plan assets, as well as the actual pension plan asset allocations as of December 31, 2014 and 2013, was as follows:

| | Current Target Allocation | Percentage of Pension Plan Assets at December 31, | |
|---|---|---|---|
| Asset Category | | **2014** | 2013 |
| Equity securities | 10% to 18% | **10%** | 43% |
| Debt securities | 70% to 78% | **77%** | 45% |
| Other | 9% to 15% | **13%** | 12% |
| Total | | **100%** | 100% |

The Company recognizes its overall responsibility to ensure that the assets of its various defined benefit pension plans are managed effectively and prudently and in compliance with its policy guidelines and all applicable laws. Preservation of capital is important; however, the Company also recognizes that appropriate levels of risk are necessary to allow its investment managers to achieve satisfactory long-term results consistent with the objectives and the fiduciary character of the pension funds. Asset allocations are established in a manner consistent with projected plan liabilities, benefit payments and expected rates of return for various asset classes. The expected rate of return for the investment portfolio is based on expected rates of return for various asset classes, as well as historical asset class and fund performance.

Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date (exit price). The FASB provides accounting rules that classify the inputs used to measure fair value into the following hierarchy:

Level 1 – Unadjusted quoted prices in active markets for identical assets or liabilities.

Level 2 – Unadjusted quoted prices in active markets for similar assets or liabilities, or unadjusted quoted prices for identical or similar assets or liabilities in markets that are not active, or inputs other than quoted prices that are observable for the asset or liability.

Level 3 – Unobservable inputs for the asset or liability.

Note 13 – Retirement Benefit Plans (continued)

The following table presents the fair value hierarchy for those investments of the Company's pension assets measured at fair value on a recurring basis as of December 31, 2014:

| | U.S. Pension Plans | | | | International Pension Plans | | | |
|---|---|---|---|---|---|---|---|---|
| | Total | Level 1 | Level 2 | Level 3 | Total | Level 1 | Level 2 | Level 3 |
| Assets: | | | | | | | | |
| Cash and cash equivalents | $ 55.3 | $ 0.8 | $ 54.5 | $ — | $ 25.5 | $ — | $ 25.5 | $ — |
| Government and agency securities | 505.9 | 496.4 | 9.5 | — | — | — | — | — |
| Corporate bonds – investment grade | 473.7 | — | 473.7 | — | 2.7 | — | 2.7 | — |
| Equity securities – U.S. companies | 22.7 | 22.7 | — | — | 30.2 | 30.2 | — | — |
| Equity securities – international companies | 16.3 | 16.3 | — | — | 26.6 | 25.7 | 0.9 | — |
| Asset backed securities | — | — | — | — | 3.4 | — | 3.4 | — |
| Common collective funds – domestic equities | 22.6 | — | 22.6 | — | 2.1 | — | 2.1 | — |
| Common collective funds – international equities | 27.4 | — | 27.4 | — | 60.6 | — | 60.6 | — |
| Common collective funds – fixed income | 379.5 | — | 379.5 | — | 108.9 | — | 108.9 | — |
| Common collective funds – other | — | — | — | — | 89.4 | — | 89.4 | — |
| Limited partnerships | 66.1 | — | — | 66.1 | — | — | — | — |
| Real estate partnerships | 112.6 | — | 84.8 | 27.8 | — | — | — | — |
| Risk parity | 90.3 | — | 90.3 | — | — | — | — | — |
| Total Assets | $ 1,772.4 | $ 536.2 | $ 1,142.3 | $ 93.9 | $ 349.4 | $ 55.9 | $ 293.5 | $ — |

The table below sets forth a summary of changes in the fair value of the level 3 assets by fund for the year ended December 31, 2014:

| | Limited Partnerships | Real Estate | Total |
|---|---|---|---|
| Beginning balance, January 1 | $ 78.8 | $ 21.1 | $ 99.9 |
| Purchases | 2.1 | 10.5 | 12.6 |
| Sales | (16.8) | (5.6) | (22.4) |
| Realized losses | (11.0) | (4.1) | (15.1) |
| Unrealized gains | 13.0 | 5.9 | 18.9 |
| Ending balance, December 31 | $ 66.1 | $ 27.8 | $ 93.9 |

Note 13 – Retirement Benefit Plans (continued)

The following table presents the fair value hierarchy for those investments of the Company's pension assets measured at fair value on a recurring basis as of December 31, 2013:

| | U.S. Pension Plans | | | | International Pension Plans | | | |
|---|---|---|---|---|---|---|---|---|
| | Total | Level 1 | Level 2 | Level 3 | Total | Level 1 | Level 2 | Level 3 |
| Assets: | | | | | | | | |
| Cash and cash equivalents | $ 345.8 | $ 3.3 | $ 342.5 | $ — | $ 18.1 | $ — | $ 18.1 | $ — |
| Government and agency securities | 188.4 | 175.0 | 13.4 | — | — | — | — | — |
| Corporate bonds – investment grade | 300.6 | — | 300.6 | — | 0.5 | — | 0.5 | — |
| Corporate bonds – non-investment grade | 110.1 | — | 110.1 | — | — | — | — | — |
| Equity securities – U.S. companies | 274.6 | 273.2 | 1.4 | — | 26.0 | 26.0 | — | — |
| Equity securities – international companies | 230.8 | 230.8 | — | — | 80.7 | 80.7 | — | — |
| Asset backed securities | 34.8 | — | 34.8 | — | 3.3 | — | 3.3 | — |
| Common collective funds – domestic equities | 180.9 | — | 180.9 | — | 14.8 | — | 14.8 | — |
| Common collective funds – international equities | 315.5 | — | 315.5 | — | 72.0 | — | 72.0 | — |
| Common collective funds – fixed income | 507.5 | — | 507.5 | — | 118.0 | — | 118.0 | — |
| Common collective funds – other | — | — | — | — | 87.2 | — | 87.2 | — |
| Limited partnerships | 78.8 | — | — | 78.8 | — | — | — | — |
| Real estate partnerships | 145.6 | — | 124.5 | 21.1 | — | — | — | — |
| Mutual funds – real estate | 156.6 | 155.9 | 0.7 | — | — | — | — | — |
| Total Assets | $ 2,870.0 | $ 838.2 | $ 1,931.9 | $ 99.9 | $ 420.6 | $ 106.7 | $ 313.9 | $ — |

The table below sets forth a summary of changes in the fair value of the level 3 assets by fund for the year ended December 31, 2013:

| | Limited Partnerships | Real Estate | Total |
|---|---|---|---|
| Beginning balance, January 1 | $ 79.9 | $ 16.3 | $ 96.2 |
| Purchases | 5.3 | 3.5 | 8.8 |
| Sales | (11.5) | (0.6) | (12.1) |
| Realized losses | (6.2) | (0.1) | (6.3) |
| Unrealized gains | 11.3 | 2.0 | 13.3 |
| Ending balance, December 31 | $ 78.8 | $ 21.1 | $ 99.9 |

Cash and cash equivalents are valued at redemption value. Government and agency securities are valued at the closing price reported in the active market in which the individual securities are traded. Certain corporate bonds are valued at the closing price reported in the active market in which the bond is traded. Equity securities (both common and preferred stock) are valued at the closing price reported in the active market in which the individual security is traded. Common collective funds are valued based on a net asset value per share. Asset-backed securities are valued based on quoted prices for similar assets in active markets. When such prices are unavailable, the plan trustee determines a valuation from the market maker dealing in the particular security.

Limited partnerships include investments in funds that invest primarily in private equity, venture capital and distressed debt. Limited partnerships are valued based on the ownership interest in the net asset value of the investment, which is used as a practical expedient to fair value, per the underlying investment fund, which is based upon the general partner's own assumptions about the assumptions a market participant would use in pricing the assets and liabilities of the partnership. Real estate investments include funds that invest in companies that primarily invest in commercial and residential properties, commercial mortgage-backed securities, debt and equity securities of real estate operating companies, and real estate investment trusts. Mutual funds – real estate are valued based on the closing price reported in the active market in which the individual security is traded. Other real estate investments are valued based on the ownership interest in the net asset value of the investment, which is used as a practical expedient to fair value per the underlying investment fund, which is based on appraised values and current transaction prices. Risk parity investments include funds that invest in diversified global asset classes (equities, bonds, inflation-linked bonds, and commodities) with leverage to balance risk and achieve consistent returns with lower volatility. Risk parity investments are valued based on the closing prices of the underlying securities in the active markets in which they are traded.

## CASH FLOWS:

| Employer Contributions to Defined Benefit Plans | |
|---|---|
| 2013 | $ 120.7 |
| 2014 | 21.1 |
| 2015 (planned) | 15.0 |

Future benefit payments, including lump sum distributions, are expected to be as follows:

| Benefit Payments | |
|---|---|
| 2015 | $ 178.9 |
| 2016 | 154.2 |
| 2017 | 147.1 |
| 2018 | 145.9 |
| 2019 | 169.4 |
| 2020–2024 | 716.8 |

## EMPLOYEE SAVINGS PLANS:

The Company sponsors defined contribution retirement and savings plans covering substantially all employees in the United States and employees at certain non-U.S. locations. The Company has contributed its common shares to certain of these plans based on formulas established in the respective plan agreements. At December 31, 2014, the plans held 3,984,363 of the Company's common shares with a fair value of $170.1 million. Company contributions to the plans, including performance sharing, were $26.1 million in 2014, $28.5 million in 2013 and $24.9 million in 2012. The Company paid dividends totaling $4.7 million in 2014, $5.5 million in 2013 and $6.3 million in 2012 to plans holding the Company's common shares. The Spinoff also resulted in a dividend of $81.9 million of TimkenSteel common shares in 2014 to plans holding the Company's common shares.

## NOTE 14 – POSTRETIREMENT BENEFIT PLANS

The Company and its subsidiaries sponsor several funded and unfunded postretirement plans that provide health care and life insurance benefits for eligible retirees and dependents. Depending on retirement date and employee classification, certain health care plans contain contribution and cost-sharing features such as deductibles, coinsurance and limitations on employer-provided subsidies. The remaining health care and life insurance plans are noncontributory.

The following tables summarize the net periodic benefit cost information and the related assumptions used to measure the net periodic benefit cost for the years ended December 31:

| | **2014** | 2013 | 2012 |
|---|---|---|---|
| Components of net periodic benefit cost: | | | |
| Service cost | **$ 1.3** | $ 2.9 | $ 2.5 |
| Interest cost | **16.7** | 21.7 | 28.4 |
| Expected return on plan assets | **(8.5)** | (11.1) | (10.6) |
| Amortization of prior service credit | **1.0** | (0.2) | (0.2) |
| Amortization of net actuarial loss | **—** | 2.3 | 2.5 |
| Less: discontinued operations | **(3.1)** | (6.4) | (9.0) |
| Net periodic benefit cost | **$ 7.4** | $ 9.2 | $ 13.6 |

| Assumptions: | **2014** | 2013 | 2012 |
|---|---|---|---|
| Discount rate | **4.33% / 4.59%** | 3.80% | 4.85% |
| Rate of return | **5.00%** | 5.00% | 5.00% |

The discount rate assumption is based on current rates of high-quality long-term corporate bonds over the same period that benefit payments will be required to be made. The expected rate of return on plan assets assumption is based on the weighted-average expected return on the various asset classes in the plans' portfolio. The asset class return is developed using historical asset return performance as well as current market conditions such as inflation, interest rates and equity market performance.

For expense purposes in 2014, the Company applied a discount rate of 4.59% for the first four months of 2014, and a discount rate of 4.33% for the last eight months of 2014 to its postretirement benefit plans. For expense purposes in 2015, the Company will apply a discount rate of 3.95% to its postretirement benefit plans.

For expense purposes in 2014, the Company applied an expected rate of return of 5.00% to the VEBA trust assets. For expense purposes in 2015, the Company will apply an expected rate of return of 6.25% to the VEBA trust assets.

## Note 14 – Postretirement Benefit Plans (continued)

The following tables set forth the change in benefit obligation, change in plan assets, funded status and amounts recognized on the Consolidated Balance Sheets of the postretirement benefit plans as of December 31, 2014 and 2013:

| | **2014** | 2013 |
|---|---|---|
| Change in benefit obligation: | | |
| Benefit obligation at beginning of year | **$ 515.6** | $ 639.2 |
| Service cost | **1.3** | 2.9 |
| Interest cost | **16.7** | 21.7 |
| Actuarial losses (gains) | **18.0** | (101.9) |
| International plan exchange rate change | **(0.1)** | — |
| Benefits paid | **(37.1)** | (46.3) |
| Spinoff of TimkenSteel | **(229.8)** | — |
| Benefit obligation at end of year | **$ 284.6** | $ 515.6 |
| Change in plan assets: | | |
| Fair value of plan assets at beginning of year | **$ 240.1** | $ 221.9 |
| Company contributions / payments | **49.4** | 37.3 |
| Return on plan assets | **12.2** | 27.2 |
| Benefits paid | **(37.1)** | (46.3) |
| Spinoff of TimkenSteel | **(143.9)** | — |
| Fair value of plan assets at end of year | **120.7** | 240.1 |
| Funded status at end of year | **$ (163.9)** | $ (275.5) |
| Amounts recognized on the Consolidated Balance Sheets: | | |
| Current liabilities | **$ (22.1)** | $ (41.6) |
| Non-current liabilities | **(141.8)** | (233.9) |
| | **$ (163.9)** | $ (275.5) |
| Amounts recognized in accumulated other comprehensive loss: | | |
| Net actuarial loss | **$ 18.5** | $ 5.5 |
| Net prior service cost | **3.0** | 7.8 |
| Accumulated other comprehensive loss | **$ 21.5** | $ 13.3 |
| Changes in plan assets and benefit obligations recognized in AOCL: | | |
| AOCL at beginning of year | **$ 13.3** | $ 133.3 |
| Net actuarial loss (gain) | **14.3** | (117.9) |
| Recognized net actuarial loss | **—** | (2.3) |
| Recognized prior service credit | **(1.0)** | 0.2 |
| Spinoff of TimkenSteel | **(5.1)** | — |
| Total recognized in accumulated other comprehensive loss at December 31 | **$ 21.5** | $ 13.3 |

Amounts recognized on the Consolidated Balance Sheet for 2013 include amounts related to the Company's former steel business.

The presentation in the above tables for amounts recognized in accumulated other comprehensive loss on the Consolidated Balance Sheets is before the effect of income taxes.

Note 14 – Postretirement Benefit Plans (continued)

The following table summarizes assumptions used to measure the benefit obligation for the postretirement benefit plans at December 31:

| Assumptions: | **2014** | 2013 |
|---|---|---|
| Discount rate | **3.95%** | 4.59% |

The current portion of accrued postretirement benefit cost, which is included in salaries, wages and benefits on the Consolidated Balance Sheets, was $22.1 million and $41.6 million at December 31, 2014 and 2013, respectively. In 2014, the current portion of accrued postretirement benefit cost related to unfunded plans and represented the actuarial present value of expected payments related to the plans to be made over the next 12 months.

The estimated net actuarial loss and prior service cost for the postretirement plans that will be amortized from accumulated other comprehensive loss into net periodic benefit cost over the next fiscal year are zero and $0.8 million of expense, respectively.

For measurement purposes, the Company assumed a weighted-average annual rate of increase in the per capita cost (health care cost trend rate) for medical benefits of 7.0% for 2015, declining gradually to 5.0% in 2023 and thereafter; and 7.0% for 2015, declining gradually to 5.0% in 2023 and thereafter for prescription drug benefits; and 9.0% for 2015, declining gradually to 5.0% in 2031 and thereafter for HMO benefits.

The assumed health care cost trend rate may have a significant effect on the amounts reported. A one percentage point increase in the assumed health care cost trend rate would have increased the 2014 total service and interest cost components by $0.4 million and would have increased the postretirement benefit obligation by $7.6 million. A one percentage point decrease would provide corresponding reductions of $0.3 million and $6.7 million, respectively.

The Medicare Prescription Drug, Improvement and Modernization Act of 2003 (the Medicare Act) provides for prescription drug benefits under Medicare Part D and contains a subsidy to plan sponsors who provide "actuarially equivalent" prescription plans. The Company's actuary determined that the prescription drug benefit provided by the Company's postretirement plan is considered to be actuarially equivalent to the benefit provided under the Medicare Act. In accordance with ASC Topic 715, "Compensation – Retirement Benefits," all measures of the accumulated postretirement benefit obligation or net periodic postretirement benefit cost in the financial statements or accompanying notes reflect the effects of the Medicare Act on the plan for the entire fiscal year. The 2014 expected subsidy was $2.7 million, of which $0.6 million was received prior to December 31, 2014.

**PLAN ASSETS:**

The Company's target allocation for the VEBA trust assets, as well as the actual VEBA trust asset allocation as of December 31, 2014 and 2013, was as follows:

| | Current Target Allocation | Percentage of VEBA Assets at December 31, | |
|---|---|---|---|
| Asset Category | | **2014** | 2013 |
| Equity securities | 45% to 55% | **51%** | 55% |
| Debt securities | 45% to 55% | **49%** | 45% |
| Total | | **100%** | 100% |

The Company recognizes its overall responsibility to ensure that the assets of its postretirement benefit plan are managed effectively and prudently and in compliance with its policy guidelines and all applicable laws.

Preservation of capital is important; however, the Company also recognizes that appropriate levels of risk are necessary to allow its investment managers to achieve satisfactory long-term results consistent with the objectives and the fiduciary character of the postretirement funds. Asset allocations are established in a manner consistent with projected plan liabilities, benefit payments and expected rates of return for various asset classes. The expected rate of return for the investment portfolio is based on expected rates of return for various asset classes, as well as historical asset class and fund performance.

Note 14 – Postretirement Benefit Plans (continued)

The following table presents the fair value hierarchy for those investments of the Company's VEBA trust assets measured at fair value on a recurring basis as of December 31, 2014:

| | Total | Level 1 | Level 2 | Level 3 |
|---|---|---|---|---|
| Assets: | | | | |
| Cash and cash equivalents | **$ 7.9** | **$ —** | **$ 7.9** | **$ —** |
| Common Collective fund – U.S. equities | **39.9** | **—** | **39.9** | **—** |
| Common Collective fund – international equities | **22.1** | **—** | **22.1** | **—** |
| Common Collective fund – fixed income | **50.8** | **—** | **50.8** | **—** |
| Total Assets | **$ 120.7** | **$ —** | **$ 120.7** | **$ —** |

The following table presents the fair value hierarchy for those investments of the Company's VEBA trust assets measured at fair value on a recurring basis as of December 31, 2013:

| | Total | Level 1 | Level 2 | Level 3 |
|---|---|---|---|---|
| Assets: | | | | |
| Cash and cash equivalents | $ 2.9 | $ — | $ 2.9 | $ — |
| Common Collective fund – U.S. equities | 82.7 | — | 82.7 | — |
| Common Collective fund – international equities | 49.7 | — | 49.7 | — |
| Common Collective fund – fixed income | 104.8 | — | 104.8 | — |
| Total Assets | $ 240.1 | $ — | $ 240.1 | $ — |

Cash and cash equivalents are valued at redemption value. Common collective funds are valued based on a net asset value per share, which is used as a practical expedient to fair value. When such prices are unavailable, the plan trustee determines a valuation from the market maker dealing in the particular security.

**CASH FLOWS:**

Employer Contributions to the VEBA Trust:

| | |
|---|---|
| 2013 | $ — |
| 2014 | 20.0 |
| 2015 (planned) | — |

Future benefit payments are expected to be as follows:

| | Gross | Expected Medicare Subsidies | Net Including Medicare Subsidies |
|---|---|---|---|
| 2015 | $ 29.8 | $ 1.8 | $ 28.0 |
| 2016 | 28.4 | 1.9 | 26.5 |
| 2017 | 27.2 | 2.0 | 25.2 |
| 2018 | 26.3 | 2.0 | 24.3 |
| 2019 | 25.1 | 2.0 | 23.1 |
| 2020–2024 | 107.1 | 9.6 | 97.5 |

## NOTE 15 – SEGMENT INFORMATION

Beginning in the fourth quarter of 2014, the Company began operating under two reportable segments: (1) Mobile Industries and (2) Process Industries. Prior to the fourth quarter of 2014 and after the Spinoff, the Company operated under three reportable segments: (1) Mobile Industries; (2) Process Industries; and (3) Aerospace. Results for the Company's former Aerospace segment are now primarily included in the Mobile Industries segment. Segment results for 2014, 2013 and 2012 have been reclassified to conform with the new presentation of segments. In addition, the Company also made adjustments to the allocation of certain selling, general and administrative expenses and certain foreign currency exchange gains or losses for all prior periods presented to better reflect the Company's operating model and new cost structure following the Spinoff and the elimination of the former Aerospace segment.

***Description of types of products and services from which each reportable segment derives its revenues:***

The Company's reportable segments are business units that target different industry sectors. Each reportable segment is managed separately to address specific customer needs in these diverse market segments.

Mobile Industries offers an extensive portfolio of bearings, seals, lubrication devices and systems, as well as power transmission components, engineered chain, augers and related products and maintenance services, to OEMs of: off-highway equipment for the agricultural, construction and mining markets; on-highway vehicles including passenger cars, light trucks and medium- and heavy-duty trucks; and rail cars and locomotives. Beyond service parts sold to OEMs, aftermarket sales to individual end users, equipment owners, operators and maintenance shops are handled through the Company's extensive network of authorized automotive and heavy-truck distributors, and include hub units, specialty kits and more. Mobile Industries also provides power transmission systems and flight-critical components for civil and military aircraft, which include bearings, helicopter transmission systems, rotor-head assemblies, turbine engine components, gears and housings, with a focus on the entire lifecycle of aircraft. Timken products are integrated into gas turbine engines and gearboxes, helicopter transmission systems, rotor systems, landing gear, instrumentation and guidance systems, for example. In addition to original equipment parts and systems, this segment also provides aftermarket products and services, including complete engine overhaul, aerospace bearing repair, component reconditioning and replacement parts.

Process Industries supplies industrial bearings and assemblies, power transmission components such as gears and gearboxes, couplings, seals, lubricants, chains and related products and services to OEMs and end users in industries that place heavy demands on operating equipment they make or use. This includes; metals, mining, cement and aggregate production; coal and wind power generation; oil and gas; pulp and paper in applications including printing presses; and cranes, hoists, drawbridges, wind energy turbines, gear drives, drilling equipment, coal conveyors, marine equipment and food processing equipment. This segment also supports aftermarket sales and service needs through its global network of authorized industrial distributors. In addition, the Company's industrial services group offers end users a broad portfolio of maintenance support and capabilities that include repair and service for bearings and gearboxes as well as electric motor rewind, repair and services. Additionally, this segment manufactures precision bearings, complex assemblies and sensors for manufacturers of health and critical motion control equipment.

***Measurement of segment profit or loss and segment assets:***

The Company evaluates performance and allocates resources based on return on capital and profitable growth. The primary measurement used by management to measure the financial performance of each segment is EBIT.

The accounting policies of the reportable segments are the same as those described in the summary of significant accounting policies.

***Factors used by management to identify the enterprise's reportable segments:***

Net sales by geographic area are reported by the destination of net sales, which is reflective of how the Company operates its segments. Long-lived assets by geographic area are reported by the location of the subsidiary.

Export sales from the United States and Canada are less than 10% of the Company's revenue. The Company's Mobile Industries and Process Industries segments have historically participated in the global bearing industry.

Note 15 – Segment Information (continued)

Timken's non-U.S. operations are subject to normal international business risks not generally applicable to domestic business. These risks include currency fluctuation, changes in tariff restrictions, difficulties in establishing and maintaining relationships with local distributors and dealers, import and export licensing requirements, difficulties in staffing and managing geographically diverse operations and restrictive regulations by foreign governments, including price and exchange controls.

**GEOGRAPHIC FINANCIAL INFORMATION:**

| | **2014** | 2013 | 2012 |
|---|---|---|---|
| Net sales: | | | |
| United States | **$ 1,623.6** | $ 1,663.0 | $ 1,885.4 |
| Canada & Mexico | **233.1** | 206.5 | 217.5 |
| South America | **145.0** | 142.9 | 152.2 |
| Europe / Middle East / Africa | **658.8** | 658.4 | 704.6 |
| Asia-Pacific | **415.7** | 364.6 | 399.8 |
| | **$ 3,076.2** | $ 3,035.4 | $ 3,359.5 |
| Long-lived assets: | | | |
| United States | **$ 443.5** | $ 497.1 | $ 484.5 |
| Canada & Mexico | **12.5** | 12.6 | 6.1 |
| South America | **1.4** | 2.1 | 4.5 |
| Europe / Middle East / Africa | **96.2** | 105.5 | 101.6 |
| Asia-Pacific | **226.9** | 238.5 | 237.4 |
| | **$ 780.5** | $ 855.8 | $ 834.1 |

Note 15 – Segment Information (continued)

**BUSINESS SEGMENT INFORMATION:**

The following tables provide segment financial information and a reconciliation of segment results to consolidated results:

| | **2014** | 2013 | 2012 |
|---|---|---|---|
| Net sales to external customers: | | | |
| Mobile Industries | **$ 1,685.4** | $ 1,775.8 | $ 1,987.4 |
| Process Industries | **1,390.8** | 1,259.6 | 1,372.1 |
| | **$ 3,076.2** | $ 3,035.4 | $ 3,359.5 |
| Segment EBIT: | | | |
| Mobile Industries | **$ 65.6** | $ 193.7 | $ 245.2 |
| Process Industries | **267.1** | 189.3 | 261.8 |
| Total EBIT, for reportable segments | **$ 332.7** | $ 383.0 | $ 507.0 |
| Unallocated corporate expenses | **(71.4)** | (70.4) | (69.0) |
| CDSOA receipts, net of expense | **—** | — | 108.0 |
| Pension settlement charges | **(33.0)** | — | — |
| Interest expense | **(28.7)** | (24.4) | (31.1) |
| Interest income | **4.4** | 1.9 | 2.9 |
| Income from continuing operations before income taxes | **$ 204.0** | $ 290.1 | $ 517.8 |

| | **2014** | 2013 | 2012 |
|---|---|---|---|
| Assets employed at year-end: | | | |
| Mobile Industries | **$ 1,373.8** | $ 1,579.3 | $ 1,466.2 |
| Process Industries | **1,209.6** | 1,157.4 | 1,072.5 |
| Corporate | **418.0** | 484.3 | 715.3 |
| Discontinued Operations | **—** | 1,256.9 | 990.7 |
| | **$ 3,001.4** | $ 4,477.9 | $ 4,244.7 |
| Capital expenditures: | | | |
| Mobile Industries | **$ 55.7** | $ 48.2 | $ 44.2 |
| Process Industries | **70.1** | 80.3 | 70.6 |
| Corporate | **1.0** | 5.1 | 3.5 |
| | **$ 126.8** | $ 133.6 | $ 118.3 |
| Depreciation and amortization: | | | |
| Mobile Industries | **$ 65.7** | $ 71.4 | $ 84.1 |
| Process Industries | **68.8** | 67.9 | 63.2 |
| Corporate | **2.5** | 3.1 | 2.3 |
| | **$ 137.0** | $ 142.4 | $ 149.6 |

Corporate assets include corporate buildings and cash and cash equivalents.

## NOTE 16 – INCOME TAXES

Income before income taxes, based on geographic location of the operations to which such earnings are attributable, is provided below. As the Company has elected to treat certain foreign subsidiaries as branches for U.S. income tax purposes, pretax income attributable to the United States shown below may differ from the pretax income reported in the Company's annual U.S. Federal income tax return.

Income before income taxes:

| | **2014** | 2013 | 2012 |
|---|---|---|---|
| United States | **$ 39.5** | $ 189.4 | $ 438.7 |
| Non-United States | **164.5** | 100.7 | 79.1 |
| Income from continuing operations before income taxes | **$ 204.0** | $ 290.1 | $ 517.8 |

The provision for income taxes consisted of the following:

| | **2014** | 2013 | 2012 |
|---|---|---|---|
| Current: | | | |
| Federal | **$ 61.1** | $ 96.8 | $ 58.9 |
| State and local | **2.8** | 11.5 | 2.1 |
| Foreign | **44.1** | 39.3 | 33.7 |
| | **$ 108.0** | $ 147.6 | $ 94.7 |
| Deferred: | | | |
| Federal | **$ (46.9)** | $ (35.7) | $ 73.9 |
| State and local | **(4.4)** | 1.8 | 17.6 |
| Foreign | **(2.0)** | 0.9 | 0.1 |
| | **$ (53.3)** | $ (33.0) | $ 91.6 |
| United States and foreign tax expense on income | **$ 54.7** | $ 114.6 | $ 186.3 |

The Company made net income tax payments of $111.6 million, $98.9 million and $93.0 million in 2014, 2013 and 2012, respectively.

The following table is the reconciliation between the provision for income taxes and the amount computed by applying the U.S. Federal income tax rate of 35% to income before taxes:

| | **2014** | 2013 | 2012 |
|---|---|---|---|
| Income tax at the U.S. federal statutory rate | **$ 71.4** | $ 101.5 | $ 181.2 |
| Adjustments: | | | |
| State and local income taxes, net of federal tax benefit | **(0.3)** | 8.4 | 12.1 |
| Tax on foreign remittances and U.S. tax on foreign income | **19.6** | 41.0 | 9.6 |
| Tax expense related to undistributed earnings of foreign subsidiaries | **(8.7)** | 8.7 | — |
| Foreign losses without current tax benefits | **4.3** | 9.5 | 16.2 |
| Foreign earnings taxed at different rates including tax holidays | **(15.7)** | (3.9) | (19.0) |
| U.S. domestic manufacturing deduction | **(6.6)** | (8.8) | (1.0) |
| U.S. foreign tax credit | **(15.1)** | (25.9) | (13.7) |
| U.S. research tax credit | **(1.0)** | (3.2) | 0.1 |
| Accruals and settlements related to tax audits | **12.8** | (10.8) | 4.1 |
| Other items, net | **(6.0)** | (1.9) | (3.3) |
| Provision for income taxes | **$ 54.7** | $ 114.6 | $ 186.3 |
| Effective income tax rate | **26.8%** | 39.5% | 36.0% |

## Note 16 – Income Taxes (continued)

In connection with various investment arrangements, the Company has been granted a "holiday" from income taxes for one affiliate in Asia for 2014, 2013 and 2012. These agreements began to expire at the end of 2010, with full expiration in 2018. In total, the agreements reduced income tax expense by $1.3 million in 2014, $0.7 million in 2013 and $1.0 million in 2012. These savings resulted in an increase to earnings per diluted share of approximately $0.01 in 2014, approximately $0.01 in 2013 and approximately $0.01 in 2012.

Income tax expense includes U.S. and international income taxes. The Company had undistributed earnings related to its international subsidiaries of $567.7 million and $577.9 million at December 31, 2014 and 2013, respectively. The Company has determined that U.S. earnings are sufficient to cover U.S. cash needs for operations and foreign earnings will be reinvested outside the U.S. to support global business growth initiatives. Accordingly, no provisions for U.S. income taxes have been made with respect to earnings of $486.7 million that are planned to be reinvested indefinitely outside the United States. The amount of U.S. income taxes that may be applicable to such earnings is $10.0 million if such earnings were repatriated, net of foreign tax credits.

The effect of temporary differences giving rise to deferred tax assets and liabilities at December 31, 2014 and 2013 was as follows:

| | **2014** | 2013 |
|---|---|---|
| Deferred tax assets: | | |
| Accrued postretirement benefits cost | **$ 91.4** | $ 88.0 |
| Accrued pension cost | **16.3** | 9.6 |
| Inventory | **0.7** | 12.0 |
| Other employee benefit accruals | **16.9** | 14.9 |
| Tax loss and credit carryforwards | **117.9** | 153.1 |
| Other, net | **60.0** | 44.6 |
| Valuation allowances | **(145.4)** | (177.0) |
| | **$ 157.8** | $ 145.2 |
| Deferred tax liabilities – principally depreciation and amortization | **(101.0)** | (140.9) |
| Net deferred tax (liabilities) assets | **$ 56.8** | $ 4.3 |

The Company has a U.S. foreign tax credit carryforward of $8.7 million that will begin to expire in 2023, and U.S. state and local credit carryforwards of $1.5 million, portions of which will expire in 2015. The Company also has U.S. state and local loss carryforwards with tax benefits totaling $0.5 million, portions of which will expire at the end of 2015. In addition, the Company has loss carryforwards in various non-U.S. jurisdictions with tax benefits totaling $107.3 million having various expiration dates, as well as tax credit carryforwards of $0.1 million. The Company has provided valuation allowances of $112.8 million against certain of these carryforwards. The majority of the non-U.S. loss carryforwards represent local country net operating losses for branches of the Company or entities treated as branches of the Company under U.S. tax law. Tax benefits have been recorded for these losses in the United States. The related local country net operating loss carryforwards are offset fully by valuation allowances. In addition to loss and credit carryforwards, the Company has provided valuation allowances of $32.6 million against other deferred tax assets.

As of December 31, 2014, the Company had $57.5 million of total gross unrecognized tax benefits. Included in this amount was $47.3 million of unrecognized tax benefits that would favorably impact the Company's effective income tax rate in any future periods if such benefits were recognized. As of December 31, 2014, the Company anticipates a decrease in its unrecognized tax positions of approximately $40.0 million to $45.0 million during the next 12 months. The anticipated decrease is primarily due to settlements with tax authorities and the expiration of various statutes of limitation. As of December 31, 2014, the Company had accrued $16.5 million of interest and penalties related to uncertain tax positions. The Company records interest and penalties related to uncertain tax positions as a component of income tax expense.

As of December 31, 2013, the Company had $49.5 million of total gross unrecognized tax benefits. Included in this amount was $35.8 million of unrecognized tax benefits that would favorably impact the Company's effective income tax rate in any future periods if such benefits were recognized. As of December 31, 2013, the Company had accrued $9.8 million of interest and penalties related to uncertain tax positions.

Note 16 – Income Taxes (continued)

The following table reconciles the Company's total gross unrecognized tax benefits for the years ended December 31, 2014 and 2013:

| | **2014** | 2013 |
|---|---|---|
| Beginning balance, January 1 | **$ 49.5** | $ 112.6 |
| Tax positions related to the current year: | | |
| Additions | **0.7** | 9.3 |
| Tax positions related to prior years: | | |
| Additions | **14.7** | 6.9 |
| Reductions | **(3.5)** | (1.4) |
| Settlements with tax authorities | **(3.0)** | (77.9) |
| Lapses in statutes of limitation | **(0.9)** | — |
| Ending balance, December 31 | **$ 57.5** | $ 49.5 |

During 2014, gross unrecognized tax benefits increased primarily due to net additions related to various current year and prior year tax matters, including certain U.S. federal taxes, U.S. state and local taxes and taxes related to the Company ' s international operations. These increases were partially offset by reductions related to prior year tax matters, including settlement of tax matters with government authorities and taxes related to the Company ' s international operations.

During 2013, gross unrecognized tax benefits decreased primarily due to net reductions related to various current year and prior year tax matters, including settlement of tax matters with government authorities and taxes related to the Company's international operations. These decreases were partially offset by additions related to prior year tax matters, including certain U.S. federal taxes, U.S. state and local taxes and taxes related to the Company ' s international operations.

As of December 31, 2014, the Company is subject to examination by the IRS for tax years 2012 to the present. The Company is also subject to tax examination in various U.S. state and local tax jurisdictions for tax years 2006 to the present, as well as various foreign tax jurisdictions, including Canada, France, Germany, Italy and India for tax years 2002 to the present. The current portion of the Company's unrecognized tax benefits was presented on the Consolidated Balance Sheets within income taxes payable, and the non-current portion was presented as a component of other non-current liabilities.

## NOTE 17 – FAIR VALUE

The following tables present the fair value hierarchy for those assets and liabilities on the Consolidated Balance Sheet measured at fair value on a recurring basis as of December 31, 2014 and 2013:

| | December 31, 2014 | | | |
|---|---|---|---|---|
| | Total | Level 1 | Level 2 | Level 3 |
| Assets: | | | | |
| Cash and cash equivalents | **$ 278.8** | **$ 155.6** | **$ 123.2** | **$ —** |
| Restricted cash | **15.3** | **—** | **15.3** | **—** |
| Short-term investments | **8.4** | **—** | **8.4** | **—** |
| Foreign currency hedges | **12.4** | **—** | **12.4** | **—** |
| Total Assets | **$ 314.9** | **$ 155.6** | **$ 159.3** | **$ —** |
| Liabilities: | | | | |
| Foreign currency hedges | **$ 0.3** | **$ —** | **$ 0.3** | **$ —** |
| Total Liabilities | **$ 0.3** | **$ —** | **$ 0.3** | **$ —** |

| | December 31, 2013 | | | |
|---|---|---|---|---|
| | Total | Level 1 | Level 2 | Level 3 |
| Assets: | | | | |
| Cash and cash equivalents | $ 384.6 | $ 320.4 | $ 64.2 | $ — |
| Restricted cash | 15.1 | — | 15.1 | — |
| Short-term investments | 13.9 | — | 13.9 | — |
| Foreign currency hedges | 0.9 | — | 0.9 | — |
| Total Assets | $ 414.5 | $ 320.4 | $ 94.1 | $ — |
| Liabilities: | | | | |
| Foreign currency hedges | $ 9.3 | $ — | $ 9.3 | $ — |
| Total Liabilities | $ 9.3 | $ — | $ 9.3 | $ — |

Cash and cash equivalents are highly liquid investments with maturities of three months or less when purchased and are valued at redemption value. Short-term investments are investments with maturities between four months and one year and are valued at amortized cost, which approximates fair value. The Company uses publicly available foreign currency forward and spot rates to measure the fair value of its foreign currency forward contracts.

The Company does not believe it has significant concentrations of risk associated with the counterparts to its financial instruments.

## Note 17 – Fair Value (continued)

The following table presents those assets measured at fair value on a nonrecurring basis for the year ended December 31, 2014 using Level 3 inputs:

| | Carrying Value | Fair Value Adjustment | Fair Value |
|---|---|---|---|
| **Long-lived assets held for sale:** | | | |
| Aerospace Overhaul business | **$ 8.0** | **$ (1.2)** | **$ 6.8** |
| Total long-lived assets held for sale | **$ 8.0** | **$ (1.2)** | **$ 6.8** |
| **Long-lived assets held and used:** | | | |
| Goodwill | **$ 92.5** | **$ (86.3)** | **$ 6.2** |
| Indefinite-lived intangible assets | **14.2** | **(5.5)** | **8.7** |
| Amortizable Intangible assets | **4.4** | **(4.4)** | **—** |
| Fixed assets | **1.5** | **(1.5)** | **—** |
| Total long-lived assets held and used | **$ 112.6** | **$ (97.7)** | **$ 14.9** |

During 2014, assets held for sale of $8.0 million and assets held and used of $112.6 million were written down to their fair value of $6.8 million and $14.9 million, respectively, and impairment charges of $1.2 million and $97.7 million, respectively, were included in earnings.

On September 8, 2014, the Company announced plans to restructure its Aerospace segment. In connection with the restructuring, the Company: 1) eliminated leadership positions and integrated substantially all aerospace activities into Mobile Industries under the direction of its Group President; 2) sold the assets of its aerospace engine overhaul business, located in Mesa, Arizona, prior to the end of the year; 3) evaluated strategic alternatives for its aerospace MRO parts business, also located in Mesa; and 4) plans to close its aerospace bearing facility located in Wolverhampton, U.K. by early 2016, rationalizing the capacity into existing facilities.

Assets held for sale of $8.0 million associated with the Company's aerospace engine overhaul business were written down to their fair value of $6.8 million, resulting in an impairment charge of $1.2 million. The fair value of these assets was based on the price that the Company expected to receive to sell these assets.

In conjunction with the above Aerospace announcement, the Company reviewed goodwill for impairment for its Aerospace Transmissions and Aerospace Aftermarket reporting units. Step one of the goodwill impairment test failed for both of these reporting units. Therefore, the Company conducted step two of the goodwill impairment test. The carrying value of goodwill for the Aerospace Transmissions reporting unit was $56.9 million, and the carrying value of the Aerospace Aftermarket reporting unit was $35.6 million. The implied fair value of goodwill for the Aerospace Transmissions reporting unit was $1.7 million, and the implied fair value of the Aerospace Aftermarket reporting unit was $4.5 million. As a result of the carrying value of goodwill for these two reporting units exceeding fair value, the Company recorded a pretax impairment charge of $86.3 million during the third quarter of 2014.

Indefinite-lived intangible assets that were classified as assets held and used associated with the Company's Aerospace Aftermarket reporting unit with a carrying value of $14.2 million were written down to their fair value of $8.7 million resulting in an impairment charge of $5.5 million. In conjunction with the above Aerospace announcement, the Company also reviewed indefinite-lived intangible assets within the Aerospace segment for impairment. The fair value for these intangible assets was based on a relief from royalty method.

Intangible assets that were classified as assets held and used associated with the Company's Aerospace Aftermarket reporting unit with a carrying value of $4.4 million were written down to their fair value of zero resulting in an impairment charge of $4.4 million. The fair value for these intangible assets was based on the price that would be received in a current transaction to sell the assets on a standalone basis.

Various items of property, plant and equipment, with a carrying value of $1.5 million, were written down to their fair value of zero, resulting in an impairment charge of $1.5 million. The fair value for these assets was based on the price that would be received in a current transaction to sell the assets on a standalone basis, considering the age and physical attributes of these items, as these assets had been idled.

Note 17 – Fair Value (continued)

During 2012, machinery and equipment associated with the manufacturing facility in St. Thomas with a carrying value of $10.4 million was written down to its fair value of $3.8 million, resulting in an impairment loss of $6.6 million. The fair value of these assets was based on the price that would be expected to be received in a current transaction to sell the assets on a standalone basis, considering the age and physical attributes of the equipment, compared to the cost of similar used equipment. The fair value of machinery and equipment was measured using Level 3 inputs.

**FINANCIAL INSTRUMENTS:**

The Company's financial instruments consist primarily of cash and cash equivalents, short-term investments, accounts receivable, net, accounts payable, trade, short-term borrowings and long-term debt. Due to their short-term nature, the carrying value of cash and cash equivalents, short-term investments, accounts receivable, net, accounts payable, trade and short-term borrowings are a reasonable estimate of their fair value. The fair value of the Company's long-term fixed-rate debt, based on quoted market prices, was $558.6 million and $474.5 million at December 31, 2014 and 2013, respectively. The carrying value of this debt was $521.4 million and $441.6 million at December 31, 2014 and 2013, respectively.

## NOTE 18 – DERIVATIVE INSTRUMENTS AND HEDGING ACTIVITIES

The Company is exposed to certain risks relating to its ongoing business operations. The primary risks managed by using derivative instruments are foreign currency exchange rate risk, commodity price risk and interest rate risk. Forward contracts on various foreign currencies are entered into in order to manage the foreign currency exchange rate risk on forecasted revenue denominated in foreign currencies. Other forward exchange contracts on various foreign currencies are entered into in order to manage the foreign currency exchange rate risk associated with certain of the Company's commitments denominated in foreign currencies. Forward contracts on various commodities are entered into in order to manage the price risk associated with forecasted purchases of natural gas used in the Company's manufacturing process. Interest rate swaps are entered into to manage interest rate risk associated with the Company's fixed and floating-rate borrowings.

The Company designates certain foreign currency forward contracts as cash flow hedges of forecasted revenues and certain interest rate hedges as fair value hedges of fixed-rate borrowings. The majority of the Company's natural gas forward contracts are not subject to any hedge designation as they are considered within the normal purchases exemption.

The Company does not purchase or hold any derivative financial instruments for trading purposes. As of December 31, 2014 and 2013, the Company had approximately $194 million and $517 million, respectively, of outstanding foreign currency forward contracts at notional value. *Refer to Note 17 – Fair Value* for the fair value disclosure of derivative financial instruments.

**CASH FLOW HEDGING STRATEGY:**

For certain derivative instruments that are designated as and qualify as cash flow hedges (*i.e.*, hedging the exposure to variability in expected future cash flows that is attributable to a particular risk), the effective portion of the gain or loss on the derivative instrument is reported as a component of other comprehensive income and reclassified into earnings in the same line item associated with the forecasted transaction and in the same period or periods during which the hedged transaction affects earnings. The remaining gain or loss on the derivative instrument in excess of the cumulative change in the present value of future cash flows of the hedged item, if any (*i.e.,* the ineffective portion), or hedge components excluded from the assessment of effectiveness, are recognized in the Consolidated Statement of Income during the current period.

To protect against a reduction in the value of forecasted foreign currency cash flows resulting from export sales over the next year, the Company has instituted a foreign currency cash flow hedging program. The Company hedges portions of its forecasted intra-group revenue or expense denominated in foreign currencies with forward contracts. When the dollar strengthens significantly against foreign currencies, the decline in the present value of future foreign currency revenue is offset by gains in the fair value of the forward contracts designated as hedges. Conversely, when the dollar weakens, the increase in the present value of future foreign currency cash flows is offset by losses in the fair value of the forward contracts.

**FAIR VALUE HEDGING STRATEGY:**

For derivative instruments that are designated and qualify as fair value hedges (*i.e.*, hedging the exposure to changes in the fair value of an asset or a liability or an identified portion thereof that is attributable to a particular risk), the gain or loss on the derivative instrument as well as the offsetting loss or gain on the hedged item attributable to the hedged risk are recognized in the same line item associated with the hedged item (*i.e.,* in "interest expense" when the hedged item is fixed-rate debt).

## NOTE 19 – RESEARCH AND DEVELOPMENT

The Company performs research and development under Company-funded programs and under contracts with the federal government and others. Expenditures committed to research and development amounted to $38.8 million, $39.3 million and $45.7 million in 2014, 2013 and 2012, respectively. Of these amounts, $0.3 million, $0.4 million and $0.8 million, respectively, were funded by others. Expenditures may fluctuate from year-to-year depending on special projects and needs.

## NOTE 20 – CONTINUED DUMPING AND SUBSIDY OFFSET ACT (CDSOA)

CDSOA provides for distribution of monies collected by U.S. Customs and Border Protection (U.S. Customs) from antidumping cases to qualifying domestic producers where the domestic producers have continued to invest in their technology, equipment and people. The Company reported CDSOA expense of $2.3 million and $2.8 million, in 2014 and 2013, respectively, and income of $108.0 million in 2012.

In September 2002, the World Trade Organization (WTO) ruled that CDSOA payments are not consistent with international trade rules. In February 2006, U.S. legislation was enacted that ended CDSOA distributions for dumped imports covered by antidumping duty orders entering the United States after September 30, 2007. Instead, any such antidumping duties collected would remain with the U.S. Treasury. Several countries have objected that this U.S. legislation is not consistent with WTO rulings, and were granted retaliation rights by the WTO, typically in the form of increased tariffs on some imported goods from the United States. The European Union and Japan have been retaliating in this fashion against the operation of U.S. law.

In 2006, the U.S. Court of International Trade (CIT) ruled, in two separate decisions, that the procedure for determining recipients eligible to receive CDSOA distributions was unconstitutional. In addition, several other court cases challenging various provisions of CDSOA were ongoing. As a result, from 2006 through 2010, U.S. Customs withheld a portion of the amounts that would otherwise have been distributed under CDSOA.

In February 2009, the U.S. Court of Appeals for the Federal Circuit reversed both of the 2006 decisions of the CIT. Later in December 2009, a plaintiff petitioned the U.S. Supreme Court to hear a further appeal, but the Supreme Court declined the petition, allowing the appellate court reversals to stand. At that time, several court cases challenging various provisions of the CDSOA were still unresolved, so U.S. Customs accepted the CIT's recommendation to continue to withhold CDSOA receipts related to 2006 through 2010 until January 2012.

U.S. Customs began distributing the withheld funds to affected domestic producers in early April 2012. In April 2012, the Company received CDSOA distributions of $112.8 million in the aggregate for amounts originally withheld from 2006 through 2010.

While some of the challenges to CDSOA have been resolved, others are still in litigation. Since there continue to be legal challenges to CDSOA, U.S. Customs has advised all affected domestic producers that it is possible that CDSOA distributions could be subject to clawback. Management of the Company believes that the likelihood of clawback is remote.

## NOTE 21 – SUBSEQUENT EVENTS

On January 22, 2015, the Company entered into an agreement pursuant to which the Plan purchased a group annuity contract from Prudential to pay future pension benefits for approximately 5,000 U.S. Timken retirees. The Company has transferred approximately $600 million of the Company's pension obligations and approximately $635 million of pension assets to Prudential. The Company expects to incur pension settlement charges of approximately $220 million during the first half of 2015 in connection with this group annuity purchase.

## NOTE 22 – QUARTERLY FINANCIAL DATA

(Unaudited)

| | | | 2014 | | |
|---|---|---|---|---|---|
| | 1st | 2nd | 3rd | 4th | Total |
| Net sales | **$ 736.8** | **$ 789.2** | **$ 788.0** | **$ 762.2** | **$ 3,076.2** |
| Gross profit [1] | **218.1** | **233.6** | **225.5** | **220.8** | **898.0** |
| Impairment and restructuring charges [2] | **3.2** | **5.4** | **99.4** | **5.4** | **113.4** |
| Pension settlement charges [3] | **0.7** | **—** | **—** | **33.0** | **33.7** |
| Income (loss) from continuing operations | **60.3** | **57.6** | **(10.2)** | **41.6** | **149.3** |
| Income (loss) from discontinued operations | **23.5** | **6.2** | **(11.0)** | **5.3** | **24.0** |
| Net income (loss) [4] | **83.8** | **63.8** | **(21.2)** | **46.9** | **173.3** |
| Net income attributable to noncontrolling interests | **0.3** | **1.1** | **0.7** | **0.4** | **2.5** |
| Net income (loss) attributable to The Timken Company | **83.5** | **62.7** | **(21.9)** | **46.5** | **170.8** |
| Net income (loss) per share – Basic: | | | | | |
| Income (loss) from continuing operations | **$ 0.64** | **$ 0.62** | **$ (0.12)** | **$ 0.46** | **$ 1.62** |
| Income (loss) from discontinuing operations | **0.26** | **0.07** | **(0.12)** | **0.06** | **0.27** |
| Total net income (loss) per share | **$ 0.90** | **$ 0.69** | **$ (0.24)** | **$ 0.52** | **$ 1.89** |
| Net income (loss) per share – Diluted: | | | | | |
| Income (loss) from continuing operations | **$ 0.64** | **$ 0.61** | **$ (0.12)** | **$ 0.46** | **$ 1.61** |
| Income (loss) from discontinued operations | **0.26** | **0.07** | **(0.12)** | **0.06** | **0.26** |
| Total net income (loss) per share | **$ 0.90** | **$ 0.68** | **$ (0.24)** | **$ 0.52** | **$ 1.87** |
| Dividends per share | **$ 0.25** | **$ 0.25** | **$ 0.25** | **$ 0.25** | **$ 1.00** |

| | | | 2013 | | |
|---|---|---|---|---|---|
| | 1st | 2nd | 3rd | 4th | Total |
| Net sales | $ 763.2 | $ 791.3 | $ 731.4 | $ 749.5 | $ 3,035.4 |
| Gross profit | 218.9 | 239.6 | 202.0 | 207.9 | 868.4 |
| Impairment and restructuring charges [5] | 1.2 | 1.5 | 2.2 | 3.8 | 8.7 |
| Pension settlement charges [6] | — | 5.2 | 1.5 | 0.5 | 7.2 |
| Income from continuing operations | 51.5 | 55.4 | 34.8 | 33.8 | 175.5 |
| Income from discontinued operations | 23.4 | 27.5 | 17.7 | 18.9 | 87.5 |
| Net income [7] | 74.9 | 82.9 | 52.5 | 52.7 | 263.0 |
| Net income (loss) attributable to noncontrolling interests | (0.2) | 0.1 | 0.3 | 0.1 | 0.3 |
| Net income attributable to The Timken Company | 75.1 | 82.8 | 52.2 | 52.6 | 262.7 |
| Net income per share – Basic: | | | | | |
| Income from continuing operations | $ 0.54 | $ 0.58 | $ 0.36 | $ 0.36 | $ 1.84 |
| Income from discontinuing operations | 0.24 | 0.28 | 0.19 | 0.20 | 0.92 |
| Total net income per share | $ 0.78 | $ 0.86 | $ 0.55 | $ 0.56 | $ 2.76 |
| Net income per share – Diluted: | | | | | |
| Income from continuing operations | $ 0.53 | $ 0.57 | $ 0.36 | $ 0.35 | $ 1.82 |
| Income from discontinued operations | 0.24 | 0.29 | 0.18 | 0.20 | 0.92 |
| Total net income per share | $ 0.77 | $ 0.86 | $ 0.54 | $ 0.55 | $ 2.74 |
| Dividends per share | $ 0.23 | $ 0.23 | $ 0.23 | $ 0.23 | $ 0.92 |

Earnings per share are computed independently for each of the quarters presented; therefore, the sum of the quarterly earnings per share may not equal the total computed for the year.

Note 22 – Quarterly Financial Data (continued)

(1) Gross profit for the third quarter of 2014 included an inventory valuation adjustment of $18.7 million related to the Company's Mobile Industries segment.

(2) Impairment and restructuring charges for the second quarter of 2014 included severance and related benefits of $2.8 million, exit costs of $1.8 million and impairment charges of $0.8 million. Impairment and restructuring charges for the third quarter of 2014 included impairment charges of $98.0 million, severance and related benefits of $1.3 million and exit costs of $0.1 million. The impairment charges primarily related to the impairment of goodwill and intangible assets for two of the Company's Aerospace reporting units. Impairment and restructuring charges for the fourth quarter of 2014 included severance and related benefits of $4.4 million and exits costs of $1.0 million.

(3) Pension settlement charges for the fourth quarter of 2014 primarily related to the settlement of approximately $110 million of pension obligation for one of the Company's U.S. defined benefit pension plans.

(4) Net income for the first quarter of 2014 included a gain of $22.6 million on the sale of real estate in Sao Paulo.

(5) Impairment and restructuring charges for the fourth quarter of 2013 included severance and related benefit costs of $5.6 million, impairment charges of $0.1 million and a favorable adjustment for exit costs of $1.9 million.

(6) Pension settlement charges for the second quarter of 2013 related to the settlement of pension obligations for one of the Company's Canadian defined benefit pension plans.

(7) Net income for the fourth quarter of 2013 included a gain of $5.4 million on the sale of real estate in Sao Paulo.

# REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

**To the Board of Directors and Shareholders of The Timken Company and subsidiaries**

We have audited the accompanying consolidated balance sheets of The Timken Company and subsidiaries as of December 31, 2014 and 2013, and the related consolidated statements of income, comprehensive income, shareholders' equity, and cash flows for each of the three years in the period ended December 31, 2014. Our audits also included the financial statement schedule listed in the Index at Item 15(a). These financial statements and schedule are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements and schedule based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of The Timken Company and subsidiaries at December 31, 2014 and 2013, and the consolidated results of their operations and their cash flows for each of the three years in the period ended December 31, 2014, in conformity with U.S. generally accepted accounting principles. Also, in our opinion, the related financial statement schedule, when considered in relation to the basic financial statements taken as a whole, presents fairly in all material respects the information set forth therein.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), The Timken Company's internal control over financial reporting as of December 31, 2014, based on criteria established in Internal Control-Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (2013 framework) and our report dated March 2, 2015 expressed an unqualified opinion thereon.

/s/ Ernst & Young LLP

Cleveland, Ohio

March 2, 2015

## ITEM 9. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE

Not applicable.

## ITEM 9A. CONTROLS AND PROCEDURES

As of the end of the period covered by this Annual Report on Form 10-K, the Company's management carried out an evaluation, under the supervision and with the participation of the Company's principal executive officer and principal financial officer, of the effectiveness of the design and operation of the Company's disclosure controls and procedures as defined in Exchange Act Rule 13a-15(e). Based upon that evaluation, the principal executive officer and principal financial officer concluded that the Company's disclosure controls and procedures were effective as of the end of the period covered by this Annual Report on Form 10-K.

There have been no changes during the Company's fourth quarter of 2014 in the Company's internal control over financial reporting that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

**REPORT OF MANAGEMENT ON INTERNAL CONTROL OVER FINANCIAL REPORTING**

The management of The Timken Company is responsible for establishing and maintaining adequate internal control over financial reporting for the Company. Timken's internal control system was designed to provide reasonable assurance regarding the preparation and fair presentation of published financial statements. Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

Timken management assessed the effectiveness of the Company's internal control over financial reporting as of December 31, 2014. In making this assessment, it used the criteria set forth by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). Based on this assessment under COSO's "Internal Control-Integrated Framework (2013 framework)," management believes that, as of December 31, 2014, Timken's internal control over financial reporting is effective.

Ernst & Young LLP, independent registered public accounting firm, has issued an audit report on our assessment of Timken's internal control over financial reporting as of December 31, 2014, which is presented below.

# REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

**The Board of Directors and Shareholders of The Timken Company and subsidiaries**

We have audited The Timken Company and subsidiaries' internal control over financial reporting as of December 31, 2014, based on criteria established in Internal Control-Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (2013 framework) (the COSO criteria). The Timken Company and subsidiaries' management is responsible for maintaining effective internal control over financial reporting, and for its assessment of the effectiveness of internal control over financial reporting included in the accompanying Report of Management on Internal Control Over Financial Reporting. Our responsibility is to express an opinion on the Company's internal control over financial reporting based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, testing and evaluating the design and operating effectiveness of internal control based on the assessed risk, and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, The Timken Company and subsidiaries maintained, in all material respects, effective internal control over financial reporting as of December 31, 2014, based on the COSO criteria.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheets of The Timken Company and subsidiaries as of December 31, 2014 and 2013 and the related consolidated statements of income, comprehensive income, shareholders' equity, and cash flows for each of the three years in the period ended December 31, 2014, and our report dated March 2, 2015 expressed an unqualified opinion thereon.

/s/ Ernst & Young LLP

Cleveland, Ohio

March 2, 2015

# ITEM 9B. OTHER INFORMATION

Not applicable.

# PART III.

## ITEM 10. DIRECTORS, EXECUTIVE OFFICERS AND CORPORATE GOVERNANCE

Required information is set forth under the captions "Election of Directors" and "Section 16(a) Beneficial Ownership Reporting Compliance" in the proxy statement filed in connection with the annual meeting of shareholders to be held on or about May 7, 2015 (the "Proxy Statement"), and is incorporated herein by reference. Information regarding the executive officers of the registrant is included in Part I hereof. Information regarding the Company's Audit Committee and its Audit Committee Financial Expert is set forth under the caption "Audit Committee" in the Proxy Statement, and is incorporated herein by reference.

The General Policies and Procedures of the Board of Directors of the Company and the charters of its Audit Committee, Compensation Committee and Nominating and Corporate Governance Committee are also available on the Company's website at www.timken.com/investors/governance and are available to any shareholder upon request to the General Counsel. The information on the Company's website is not incorporated by reference into this Annual Report on Form 10-K.

The Company has adopted a code of ethics that applies to all of its employees, including its principal executive officer, principal financial officer and principal accounting officer, as well as its directors. The Company's code of ethics, The Timken Company Standards of Business Ethics Policy, is available on its website at www.timken.com/investors/governance. The Company intends to disclose any amendment to, or waiver from, its code of ethics by posting such amendment or waiver, as applicable, on its website.

## ITEM 11. EXECUTIVE COMPENSATION

Required information is set forth under the captions "Compensation Discussion and Analysis," "2014 Summary Compensation Table," "2014 Grants of Plan-Based Awards," "Outstanding Equity Awards at 2014 Year-End," "2014 Option Exercises and Stock Vested," "Pension Benefits," "2014 Pension Benefits Table," "2014 Nonqualified Deferred Compensation," "Potential Payments Upon Termination or Change-in-Control," "Director Compensation," "Compensation Committee," and "Compensation Committee Report" in the Proxy Statement, and is incorporated herein by reference.

## ITEM 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT AND RELATED SHAREHOLDER MATTERS

Required information, including with respect to institutional investors owning more than 5% of the Company's common shares, is set forth under the caption "Beneficial Ownership of Common Stock" in the Proxy Statement, and is incorporated herein by reference.

Required information is set forth under the caption "Equity Compensation Plan Information" in the Proxy Statement, and is incorporated herein by reference.

## ITEM 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS, AND DIRECTOR INDEPENDENCE

Required information is set forth under the caption "Election of Directors" in the Proxy Statement, and is incorporated herein by reference.

## ITEM 14. PRINCIPAL ACCOUNTANT FEES AND SERVICES

Required information regarding fees paid to and services provided by the Company's independent auditor during the years ended December 31, 2014 and 2013 and the pre-approval policies and procedures of the Audit Committee of the Company's Board of Directors is set forth under the caption "Auditors" in the Proxy Statement, and is incorporated herein by reference.

# PART IV.

## ITEM 15. EXHIBITS AND FINANCIAL STATEMENT SCHEDULES

(a)(1) – Financial Statements are included in Part II, Item 8 of the Annual Report on Form 10-K.

(a)(2) – Schedule II – Valuation and Qualifying Accounts is submitted as a separate section of this report. Schedules I, III, IV and V are not applicable to the Company and, therefore, have been omitted.

(a)(3) Listing of Exhibits

***Exhibit***

(2.1) Separation and Distribution Agreement between The Timken Company and TimkenSteel Corporation, dated as of June 30, 2014 was filed on July 3, 2014 with Form 8-K (Commission File No. 1-1169) and is incorporated herein by reference.

(3.1) Amended Articles of Incorporation of The Timken Company, (effective May 31, 2013) were filed on July 31, 2013 with Form 10-Q (Commission File No. 1-1169) and are incorporated herein by reference.

(3.2) Amended Regulations of The Timken Company adopted on February 14, 2014, were filed on February 14, 2014 with Form 8-K (Commission File No. 1-1169) and are incorporated herein by reference.

(4.1) Second Amended and Restated Credit Agreement, dated as of May 11, 2011, by and among: The Timken Company together with certain of its subsidiaries as Guarantors; Bank of America, N.A. and KeyBank National Association as Co-Administrative Agents; KeyBank National Association as Paying Agent, L/C Issuer and Swing Line Lender; and the other Lenders party thereto, was filed on May 12, 2011 with Form 8-K (Commission File No. 1-1169) and is incorporated herein by reference.

(4.2) First Amendment to Credit Agreement and Waiver, dated as of November 6, 2013, by and among: The Timken Company, together with certain of its subsidiaries as Guarantors; Bank of America, N.A. and KeyBank National Association as Co-Administrative Agents and the other Lenders party thereto, was filed on February 28, 2014 with Form 10-K (Commission File No. 1-1169) and is incorporated herein by reference.

(4.3) Second Amendment to Credit Agreement, dated as of June 13, 2014, by and among: The Timken Company, together with certain of its subsidiaries as Guarantors; Bank of America, N.A. and KeyBank National Association as Co-Administrative Agents and the other Lenders party thereto, was filed on August 11, 2014 with Form 10-Q (Commission File No. 1-1169) and is incorporated herein by reference.

(4.4) Indenture dated as of July 1, 1990, between The Timken Company and Ameritrust Company of New York, was filed with Form S-3 dated July 12, 1990 (Registration No. 333-35773) and is incorporated herein by reference.

(4.5) First Supplemental Indenture, dated as of July 24, 1996, by and between The Timken Company and Mellon Bank, N.A. was filed on November 13, 1996 with Form 10-Q (Commission File No. 1-1169) and is incorporated herein by reference.

(4.6) Indenture, dated as of February 18, 2003, between The Timken Company and The Bank of New York, as Trustee, providing for Issuance of Notes in Series was filed on March 27, 2003 with Form 10-K (Commission File No. 1-1169) and is incorporated herein by reference.

(4.7) Indenture, dated as of August 20, 2014, by and between The Timken Company and The Bank of New York Mellon Trust Company, N.A., was filed on August 20, 2014 with Form 8-K (Commission File No. 1-1169) and is incorporated herein by reference.

(4.8) The Company is also a party to agreements with respect to other long-term debt in total amount less than 10% of the Registrant's consolidated total assets. The Registrant agrees to furnish a copy of such agreements upon request.

(4.9) Amended and Restated Receivables Purchase Agreement, dated as of November 30, 2012, by and among: Timken Receivables Corporation; The Timken Corporation; the Purchasers from time to time parties thereto; SunTrust Bank and the Bank of Tokyo-Mitsubishi UFJ, Ltd., New York Branch was filed on November 30, 2012 with Form 8-K (Commission File No. 1-1169) and is incorporated herein by reference.

## *List of Exhibits (continued)*

### *Exhibit*

(4.10) Second Amended and Restated Receivables Sale Agreement, dated as of November 10, 2010, between The Timken Corporation and Timken Receivables Corporation was filed on November 10, 2010 with Form 8-K (Commission File No. 1-1169) and is incorporated herein by reference.

(4.11) Receivables Sale Agreement, dated as of November 10, 2010, between MPB Corporation and Timken Receivables Corporation was filed on November 10, 2010 with Form 8-K (Commission File No. 1-1169) and is incorporated herein by reference.

(4.12) Amendment No. 1 to Second Amended and Restated Receivables Sale Agreement dated as of November 30, 2012 between The Timken Corporation and Timken Receivables Corporation was filed on November 30, 2012 with Form 8-K (Commission File No. 1-1169) and is incorporated herein by reference.

(4.13) Amendment No. 1 to Receivables Sale Agreement dated as of November 30, 2012 between MPB Corporation and Timken Receivables Corporation was filed on November 30, 2012 with Form 8-K (Commission File No. 1-1169) and is incorporated herein by reference.

(4.14) Amendment No. 1 to Amended and Restated Receivables Sale Agreement dated as of April 30, 2014 between Timken Receivables Corporation, The Timken Corporation, the Purchasers from time to time parties thereto and the Bank of Tokyo-Mitsubishi UFJ, Ltd., New York Branch was filed on May 1, 2014 with Form 8-K (Commission File No. 1-1169) and is incorporated herein by reference.

(4.15) Amendment No. 2 to Second Amended and Restated Receivables Sale Agreement dated as of April 30, 2014 between Timken Receivables Corporation and The TImken Corporation was filed on May 1, 2014 with Form 8-K (Commission File No. 1-1169) and is incorporated herein by reference.

## *Management Contracts and Compensation Plans*

### *Exhibit*

(10.1) The Timken Company 1996 Deferred Compensation Plan for officers and other key employees, amended and restated effective December 31, 2010, was filed on February 17, 2012 with Form 10-K (Commission File No. 1-1169) and is incorporated herein by reference.

(10.2) The Timken Company Director Deferred Compensation Plan, amended and restated effective December 31, 2008, was filed on February 25, 2010 with Form 10-K (Commission File No. 1-1169) and is incorporated herein by reference.

(10.3) Form of The Timken Company 1996 Deferred Compensation Plan Election Agreement, amended and restated as of January 1, 2008, was filed on February 25, 2010 with Form 10-K (Commission File No. 1-1169) and is incorporated herein by reference.

(10.4) Form of The Timken Company Director Deferred Compensation Plan Election Agreement, amended and restated as of January 1, 2008, was filed on February 25, 2010 with Form 10-K (Commission File No. 1-1169) and is incorporated herein by reference.

(10.5) The Timken Company Long-Term Incentive Plan for directors, officers and other key employees as amended and restated as of February 5, 2008 and approved by the shareholders on May 1, 2008 was filed on March 18, 2008 as Appendix A to the Registrant's Definitive Proxy Statement on Schedule 14A (Commission File No. 1-1169) and is incorporated herein by reference.

(10.6) The Timken Company 2011 Long-Term Incentive Plan for directors, officers and other key employees as approved by the shareholders on May 10, 2011 was filed on May 12, 2011 with Form 8-K (Commission File No. 1-1169) and is incorporated herein by reference.

*Management Contracts and Compensation Plans (continued)*

*Exhibit*

(10.7) Amended and Restated Supplemental Pension Plan of The Timken Company, amended and restated effective as of January 1, 2011, was filed on February 17, 2012 with Form 10-K (Commission File No. 1-1169) and is incorporated herein by reference.

(10.8) The Timken Company Senior Executive Management Performance Plan, as amended and restated as of February 8, 2010 and approved by shareholders May 11, 2010, was filed on May 12, 2010 with Form 8-K (Commission File No. 1-1169) and is incorporated herein by reference.

(10.9) Form of Amended and Restated Severance Agreement (for Executive Officers appointed prior to January 1, 2011) was filed on December 18, 2009 with Form 8-K (Commission File No. 1-1169) and is incorporated herein by reference.

(10.10) Form of Severance Agreement (for Executive Officers appointed on or after January 1, 2011 and other officers) as adopted on December 9, 2010 was filed on February 22, 2011 with Form 10-K (Commission File No. 1-1169) and is incorporated herein by reference.

(10.11) Amendment No. 1 to the Amended and Restated Severance Agreement (for Executive Officers appointed prior to January 1, 2011) as adopted on December 9, 2010 was filed on February 22, 2011 with Form 10-K (Commission File No. 1-1169) and is incorporated herein by reference.

(10.12) Form of Indemnification Agreement entered into with all Directors who are not Executive Officers of the Company was filed on July 31, 2013 with Form 10-Q (Commission File No. 1-1169) and is incorporated herein by reference.

(10.13) Form of Indemnification Agreement entered into with all Executive Officers of the Company who are not Directors of the Company was filed on July 31, 2013 with Form 10-Q (Commission File No. 1-1169) and is incorporated herein by reference.

(10.14) Form of Indemnification Agreement entered into with all Executive Officers of the Company who are also Directors of the Company was filed on July 31, 2013 with Form 10-Q (Commission File No. 1-1169) and is incorporated herein by reference.

(10.15) Form of Amended and Restated Employee Excess Benefits Agreement entered into with certain Executive Officers and certain key employees of the Company, was filed on February 26, 2009 with Form 10-K (Commission File No. 1-1169) and is incorporated herein by reference.

(10.16) Form of Amended and Restated Employee Excess Benefits Agreement entered into with the Chief Executive Officer and the President of Steel, was filed on February 26, 2009 with Form 10-K (Commission File No. 1-1169) and is incorporated herein by reference.

(10.17) Form of Employee Excess Benefits Agreement, entered into with all Executive Officers after January 1, 2011, was filed on August 4, 2011 with Form 10-Q (Commission File No. 1-1169) and is incorporated herein by reference.

(10.18) Form of Amendment No. 1 to The Amended and Restated Employee Excess Benefit Agreement, entered into with certain Executive Officers and certain key employees of the Company, was filed on September 2, 2009 with Form 8-K (Commission File No. 1-1169) and is incorporated herein by reference.

(10.19) Form of Amendment No. 1 to The Amended and Restated Employee Excess Benefits Agreement with all Executive Officers after January 1, 2011 and Form of Amendment No. 2 to the Amended and Restated Excess Benefits Agreement with certain Executive Officers and certain key employees of the Company, as adopted December 8, 2011, was filed on February 17, 2012 with Form 10-K (Commission File No. 1-1169) and is incorporated herein by reference.

(10.20) Form of Amendment No. 1 to The Amended and Restated Employee Excess Benefits Agreement entered into with the Chief Executive Officer and the President of Steel, as adopted December 8, 2011, was filed on February 17, 2012 with Form 10-K (Commission File No. 1-1169) and is incorporated herein by reference.

(10.21) Form of Amendment No. 2 to The Amended and Restated Employee Excess Benefits Agreement entered into with the Chief Executive Officer and the President of Steel, as adopted December 8, 2011, was filed on February 17, 2012 with Form 10-K (Commission File No. 1-1169) and is incorporated herein by reference.

### *Management Contracts and Compensation Plans (continued)*

***Exhibit***

(10.22) Form of Nonqualified Stock Option Agreement for nontransferable options without dividend credit, as adopted on April 17, 2001, was filed on May 14, 2001 with Form 10-Q (Commission File No. 1-1169) and is incorporated herein by reference.

(10.23) Form of Nonqualified Stock Option Agreement for Officers, as adopted on January 31, 2005, was filed on February 4, 2005 with Form 8-K (Commission File No. 1-1169) and is incorporated herein by reference.

(10.24) Form of Nonqualified Stock Option Agreement for Non-Employee Directors, as adopted on January 31, 2005, was filed on March 15, 2005 with Form 10-K (Commission File No. 1-1169) and is incorporated herein by reference.

(10.25) Form of Nonqualified Stock Option Agreement for Officers, as adopted on February 6, 2006, was filed on February 10, 2006 with Form 8-K (Commission File No. 1-1169) and is incorporated herein by reference.

(10.26) Form of Nonqualified Stock Option Agreement for Officers, as adopted on November 6, 2008, was filed on February 26, 2009 with Form 10-K (Commission File No. 1-1169) and is incorporated herein by reference.

(10.27) Form of Nonqualified Stock Option Agreement for Officers, as adopted on December 10, 2009, was filed on February 25, 2010 with Form 10-K (Commission File No. 1-1169), and is incorporated herein by reference.

(10.28) Form of Nonqualified Stock Option Agreement for Non-Employee Directors, as adopted on December 8, 2011, was filed on February 17, 2012 with Form 10-K (Commission File No. 1-1169) and is incorporated herein by reference.

(10.29) Form of Nonqualified Stock Option Agreement for transferable options for Officers, as adopted on December 8, 2011, was filed on February 17, 2012 with Form 10-K (Commission File No. 1-1169) and is incorporated herein by reference.

(10.30) Form of Nonqualified Stock Option Agreement for non-transferable options for Non-Officer Employees, as adopted on December 8, 2011, was filed on February 17, 2012 with Form 10-K (Commission File No. 1-1169) and is incorporated herein by reference.

(10.31) Form of Restricted Share Agreement for Non-Employee Directors, as adopted on January 31, 2005, was filed on March 15, 2005 with Form 10-K (Commission File No. 1-1169) and is incorporated herein by reference.

(10.32) Form of Restricted Shares Agreement, as adopted on November 6, 2008, was filed on February 17, 2012 with Form 10-K (Commission File No. 1-1169) and is incorporated herein by reference.

(10.33) Form of Restricted Share Agreement for Non-Employee Directors, as adopted on December 8, 2011, was filed on February 17, 2012 with Form 10-K (Commission File No. 1-1169) and is incorporated herein by reference.

(10.34) Form of Performance Unit Agreement, as adopted on February 4, 2008, was filed on February 7, 2008 with Form 8-K (Commission File No. 1-1169) and is incorporated herein by reference.

(10.35) Form of Performance Shares Agreement was filed on February 11, 2010 with Form 8-K (Commission File No. 1-1169) and is incorporated herein by reference.

(10.36) Form of Deferred Shares Agreement, as adopted on February 2, 2009, was filed on February 17, 2012 with Form 10-K (Commission File No. 1-1169) and is incorporated herein by reference.

(10.37) Form of Deferred Shares Agreement entered into with employees after January 1, 2012, as adopted on December 8, 2011, was filed on February 17, 2012 with Form 10-K (Commission File No. 1-1169) and is incorporated herein by reference.

(10.38) Form of Performance-Based Restricted Stock Unit Agreement entered into with key employees was filed on May 2, 2012 with Form 10-Q (Commission File No. 1-1169) and is incorporated herein by reference.

(10.39) Form of Time-Based Restricted Stock Unit Agreement entered into with key employees was filed on May 2, 2012 with Form 10-Q (Commission File No. 1-1169) and is incorporated herein by reference.

(10.40) Form of Time-Based Restricted Stock Unit Agreement (Cliff Vesting) entered into with key employees was filed on February 28, 2014 with Form 10-K (Commission File No. 1-1169) and is incorporated herein by reference.

***Management Contracts and Compensation Plans (continued)***

***Exhibit***

(10.41) Form of Associate Non-Compete Agreement entered into with key employees was filed on December 3, 2012 with Form 10-Q/A (Commission File No. 1-1169) and is incorporated herein by reference.

(10.42) Employee Matters Agreement between The Timken Company and TimkenSteel Corporation, dated June 30, 2014 was filed on July 3, 2014 with Form 8-K (Commission File No. 1-1169) and is incorporated herein by reference.

(10.43) Tax Sharing Agreement by and between The Timken Company and TimkenSteel Corporation, dated June 30, 2014 was filed on July 3, 2014 with Form 8-K (Commission File No. 1-1169) and is incorporated herein by reference.

(10.44) Transition Services Agreement between The Timken Company and TimkenSteel Corporation, dated June 30, 2014 was filed on July 3, 2014 with Form 8-K (Commission File No. 1-1169) and is incorporated herein by reference.

(10.45) Trademark License Agreement between The Timken Company and TimkenSteel Corporation, dated June 30, 2014 was filed on July 3, 2014 with Form 8-K (Commission File No. 1-1169) and is incorporated herein by reference.

(10.46) Noncompetition Agreement between The Timken Company and TimkenSteel Corporation, dated June 30, 2014 was filed on July 3, 2014 with Form 8-K (Commission File No. 1-1169) and is incorporated herein by reference.

(10.47) Registration Rights Agreement between The Timken Company and TimkenSteel Corporation, dated August 20, 2014 was filed on August 20, 2014 with Form 8-K (Commission File No. 1-1169) and is incorporated herein by reference.

***Listing of Exhibits (continued)***

(12) Computation of Ratio of Earnings to Fixed Charges.

(21) A list of subsidiaries of the Registrant.

(23) Consent of Independent Registered Public Accounting Firm.

(24) Power of Attorney.

(31.1) Principal Executive Officer's Certifications pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.

(31.2) Principal Financial Officer's Certifications pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.

(32) Certification pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

(101) Financial statements from the Annual Report on Form 10-K of The Timken Company for the year ended December 31, 2014, formatted in XBRL: (i) the Consolidated Statements of Income, (ii) the Consolidated Balance Sheets, (iii) the Consolidated Statements of Cash Flows, (iv) the Consolidated Statements of Shareholders' Equity and (v) the Notes to the Consolidated Financial Statements.

**SIGNATURES:**

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the Company has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

THE TIMKEN COMPANY

By: /s/ Richard G. Kyle

Richard G. Kyle
President, Chief Executive Officer and Director
(Principal Executive Officer)
Date: March 2, 2015

By: /s/ Philip D. Fracassa

Philip D. Fracassa
Executive Vice President and Chief Financial Officer
(Principal Financial Officer)
Date: March 2, 2015

By: /s/ J. Ted Mihaila

J. Ted Mihaila
Senior Vice President and Controller
(Principal Accounting Officer)
Date: March 2, 2015

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed by the following persons on behalf of the registrant and in the capacities and on the dates indicated.

By: /s/ Maria A. Crowe *

Maria A. Crowe, Director
Date: March 2, 2015

By: /s/ Richard G. Kyle *

Richard G. Kyle, Director
Date: March 2, 2015

By: /s/ John A. Luke, Jr.*

John A. Luke, Jr., Director
Date: March 2, 2015

By: /s/ Christopher L. Mapes*

Christopher L. Mapes, Director
Date: March 2, 2015

By: /s/ Ajita G. Rajendra*

Ajita G. Rajendra, Director
Date: March 2, 2015

By: /s/ Joseph W. Ralston *

Joseph W. Ralston, Director
Date: March 2, 2015

By: /s/ John P. Reilly *

John P. Reilly, Director
Date: March 2, 2015

By: /s/ Frank C. Sullivan *

Frank C. Sullivan, Director
Date: March 2, 2015

By: /s/ John M. Timken, Jr.*

John M. Timken, Jr., Director
Date: March 2, 2015

By: /s/ Ward J. Timken, Jr.*

Ward J. Timken, Jr., Director
Date: March 2, 2015

By: /s/ Jacqueline F. Woods *

Jacqueline F. Woods, Director
Date: March 2, 2015

* By: /s/ Philip D. Fracassa

Philip D. Fracassa, attorney-in-fact
By authority of Power of Attorney
filed as Exhibit 24 hereto
Date: March 2, 2015

## SCHEDULE II—VALUATION AND QUALIFYING ACCOUNTS

### THE TIMKEN COMPANY AND SUBSIDIARIES

| Allowance for uncollectible accounts: | 2014 | 2013 | 2012 |
|---|---|---|---|
| Balance at Beginning of Period | **$ 10.1** | $ 11.0 | $ 16.6 |
| Additions: | | | |
| Charged to Costs and Expenses (1) | **2.7** | 2.4 | 8.5 |
| Charged to Other Accounts (2) | **(0.5)** | — | (0.6) |
| Deductions (3) | **(1.4)** | 3.3 | 13.5 |
| Balance at End of Period | **$ 13.7** | $ 10.1 | $ 11.0 |

| Allowance for surplus and obsolete inventory: | 2014 | 2013 | 2012 |
|---|---|---|---|
| Balance at Beginning of Period | **$ 18.4** | $ 19.0 | $ 28.7 |
| Additions: | | | |
| Charged to Costs and Expenses (4) | **28.0** | 10.5 | 9.3 |
| Charged to Other Accounts (2) | **(5.7)** | 0.2 | 1.2 |
| Deductions (5) | **27.9** | 11.3 | 20.2 |
| Balance at End of Period | **$ 12.8** | $ 18.4 | $ 19.0 |

| Valuation allowance on deferred tax assets: | 2014 | 2013 | 2012 |
|---|---|---|---|
| Balance at Beginning of Period | **$ 177.0** | $ 164.0 | $ 162.4 |
| Additions | | | |
| Charged to Costs and Expenses (6) | **14.4** | 32.1 | 13.8 |
| Charged to Other Accounts (7) | **(10.0)** | (4.5) | 8.8 |
| Deductions (8) | **36.0** | 14.6 | 21.0 |
| Balance at End of Period | **$ 145.4** | $ 177.0 | $ 164.0 |

(1) Provision for uncollectible accounts included in expenses.

(2) Currency translation and change in reserves due to acquisitions, net of divestitures.

(3) Actual accounts written off against the allowance—net of recoveries.

(4) Provisions for surplus and obsolete inventory included in expenses. Higher Obsolete and Surplus Inventory expenses in 2014 were a result of an inventory adjustment of $18.7 million in the third quarter that was recorded as a result of the announcement to exit the engine overhaul business, as well as other product lines, and lower than expected future sales. The Company sold or disposed of this excess inventory during the fourth quarter of 2014

(5) Inventory items written off against the allowance.

(6) Increase in valuation allowance is recorded as a component of the provision for income taxes.

(7) Includes valuation allowances recorded against other comprehensive income/loss or goodwill.

(8) Amount primarily relates to the reversal of valuation allowances due to the realization of net operating loss carryforwards.

## EXHIBIT 31.1

**PRINCIPAL EXECUTIVE OFFICER'S CERTIFICATIONS**

**PURSUANT TO SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002**

I, Richard G. Kyle, certify that:

1. I have reviewed this annual report on Form 10-K of The Timken Company;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

   (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

   (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

   (c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

   (d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting: and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of registrant's board of directors (or persons performing the equivalent functions):

   (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

   (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: March 2, 2015

By: /s/ Richard G. Kyle

Richard G. Kyle
President and Chief Executive Officer
(Principal Executive Officer)

## EXHIBIT 31.2

**PRINCIPAL FINANCIAL OFFICER'S CERTIFICATIONS**

**PURSUANT TO SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002**

I, Philip D. Fracassa, certify that:

1. I have reviewed this annual report on Form 10-K of The Timken Company;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

   (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

   (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

   (c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

   (d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting: and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of registrant's board of directors (or persons performing the equivalent functions):

   (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

   (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: March 2, 2015

By: /s/ Philip D. Fracassa

Philip D. Fracassa
Executive Vice President and Chief Financial Officer
(Principal Financial Officer)

## EXHIBIT 32

### CERTIFICATION PURSUANT TO 18 U.S.C. SECTION 1350, AS ADOPTED PURSUANT TO SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

In connection with the Annual Report of The Timken Company (the "Company") on Form 10-K for the period ended December 31, 2014, as filed with the Securities and Exchange Commission on the date hereof (the "Report"), each of the undersigned officers of the Company certifies, pursuant to 18 U.S.C. 1350, as adopted pursuant to 906 of the Sarbanes-Oxley Act of 2002, that, to such officer's knowledge:

1. The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
2. The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company as of the dates and for the periods expressed in the Report.

Date: March 2, 2015

By: /s/ Richard G. Kyle

Richard G. Kyle
President and Chief Executive Officer
(Principal Executive Officer)

By: /s/ Philip D. Fracassa

Philip D. Fracassa
Executive Vice President and Chief Financial Officer
(Principal Financial Officer)

The foregoing certification is being furnished solely pursuant to 18 U.S.C. 1350 and is not being filed as part of the Report or as a separate disclosure document.

## APPENDIX: RECONCILIATION OF GAAP TO NON-GAAP MEASURES

| **Reconciliation of Adjusted EBIT and Margin** | **2014** | 2013 |
|---|---|---|
| Net sales | **$ 3,076.2** | $ 3,035.4 |
| Income from continuing operations, net of income taxes | **149.3** | 175.5 |
| Provision for income taxes | **54.7** | 114.6 |
| Interest expense | **28.7** | 24.4 |
| Interest income | **(4.4)** | (1.9) |
| Earnings Before Interest and Taxes (EBIT) (As Reported) | **228.3** | 312.6 |
| Gain on sale of real estate in Brazil | **(22.6)** | (5.4) |
| Charges for cost-reduction initiatives and plant rationalization costs | **14.6** | 14.8 |
| Aerospace impairment and restructuring charges | **121.6** | – |
| Pension settlement costs | **33.7** | 7.2 |
| Adjusted EBIT | **$ 375.6** | $ 329.2 |
| Adjusted EBIT Margin (% of net sales) | **12.2%** | 10.8% |

| **Reconciliation of Net Operating Profit after Taxes** | **2014** | 2013 |
|---|---|---|
| Adjusted EBIT | **$ 375.6** | $ 329.2 |
| Tax Rate | **33.0%** | 35.1% |
| Calculated Income Taxes | **123.9** | 115.7 |
| Net operating profit after taxes | **$ 251.7** | $ 213.5 |

| **Reconciliation of Adjusted Invested Capital** | **2014** | 2013 | 2012 |
|---|---|---|---|
| Total debt | **$ 530.1** | $ 445.7 | $ 448.8 |
| Total equity | **1,589.1** | 2,648.6 | 2,246.6 |
| Less: equity related to discontinued operations | **–** | 826.7 | 549.2 |
| Adjusted total equity | **1,589.1** | 1,821.9 | 1,697.4 |
| Adjusted invested capital (Total debt + Adjusted total equity) | **2,119.2** | 2,267.6 | 2,146.2 |
| Adjusted invested capital (two-point average) | **$ 2,193.4** | $ 2,206.9 | |

| **Calculation of Adjusted Return on Invested Capital**[1] | **2014** | 2013 |
|---|---|---|
| Net operating profit after taxes (NOPAT) | **$ 251.7** | $ 213.5 |
| Adjusted invested capital (two-point average) | **2,193.4** | 2,206.9 |
| Return on invested capital | **11.5%** | 9.7% |

| **Reconciliation of Free Cash Flow** | **2014** | 2013 |
|---|---|---|
| Net cash provided from operating activities – continuing operations | **$ 281.5** | $ 292.8 |
| Less: capital expenditures | **126.8** | 133.6 |
| Free cash flow | **$ 154.7** | $ 159.2 |

| **Reconciliation of Net Debt** | **2014** | 2013 |
|---|---|---|
| Short-term debt | **$ 8.0** | $ 269.3 |
| Long-term debt | **522.1** | 176.4 |
| Total debt | **530.1** | 445.7 |
| Less: Cash, cash equivalents and restricted cash | **294.1** | 399.7 |
| Net debt | **$ 236.0** | $ 46.0 |

| **Calculation of Net Debt to Capital**[2] | **2014** | 2013 |
|---|---|---|
| Net debt | **$ 236.0** | $ 46.0 |
| Total Equity | **1,589.1** | 2,648.6 |
| Total Capital | **1,825.1** | 2,694.6 |
| Ratio of net debt to capital | **12.9%** | 1.7% |

| **Reconciliation of GAAP EPS to Adjusted EPS** | **2014** | 2013 | 2012 | 2011 | 2010 |
|---|---|---|---|---|---|
| Diluted Earnings per Share (EPS) – Continuing Operations | **$ 1.61** | $ 1.82 | $ 3.38 | $ 2.81 | $ 1.82 |
| CDSOA receipts, net of expense | **–** | – | (1.11) | – | – |
| Pension settlement charges | **0.37** | 0.08 | – | – | – |
| Aerospace impairment and restructuring charges | **1.33** | – | – | – | – |
| Gain on sale of real estate in Brazil | **(0.25)** | (0.06) | – | – | – |
| Charges for cost-reduction initiatives and plant rationalization costs | **0.16** | 0.16 | 0.39 | 0.22 | 0.29 |
| Provision (benefit) for income taxes | **(0.67)** | 0.07 | 0.40 | 0.01 | (0.10) |
| Adjusted EPS – Continuing Operations | **$ 2.55** | $ 2.07 | $ 3.06 | $ 3.04 | $ 2.01 |

[1] The company uses NOPAT/Average Invested Capital as a type of ratio that indicates return on invested capital.

[2] Capital, used for the ratio of total debt to capital, is defined as total debt plus total shareholders' equity. Capital, used for the ratio of net debt to capital, is defined as total debt less cash and cash equivalents plus total shareholders' equity.

# SHAREHOLDER INFORMATION

## Corporate Offices

The Timken Company
4500 Mount Pleasant St. NW
North Canton, OH 44720-5450

234-262-3000
www.timken.com

## Stock Listing

Timken shares are traded on the New York Stock Exchange under the symbol TKR.

## Annual Meeting of Shareholders

May 7, 2015, 10 a.m.
Timken World Headquarters

Please direct meeting inquiries to:
William Burkhart
Executive Vice President,
General Counsel and Secretary

234-262-3000

## Independent Registered Public Accounting Firm

Ernst & Young LLP
950 Main Ave.
Suite 1800
Cleveland, OH 44113-7214

## Publications

The Annual Meeting Notice and Proxy Card are mailed to shareholders in March.

Copies of the Annual Report, Proxy Statement, Forms 10-K and 10-Q may be obtained from the company's website, **www.timken.com/investors,** or by written request at no charge from:

The Timken Company
Treasury/Shareholder Relations
WHQ-03
4500 Mount Pleasant St. NW
North Canton, OH 44720-5450

## Investor Relations

Steve Tschiegg
Director, Capital Markets and Investor Relations
The Timken Company
4500 Mount Pleasant St. NW
North Canton, OH 44720-5450

234-262-7446
steve.tschiegg@timken.com

## Shareholder Information

Dividends on common shares are generally payable in March, June, September and December.

The Timken Company offers an open enrollment dividend reinvestment and stock purchase plan through its transfer agent Wells Fargo. This program allows current shareholders and new investors the opportunity to purchase common shares without a broker.

Shareholders of record may increase their investment in the company by reinvesting their dividends at no cost. Shares held in the name of a broker must be transferred to the shareholder's name to permit reinvestment. Information and enrollment materials are available online or by contacting Wells Fargo.

Inquiries regarding dividend reinvestment, dividend payments, change of address or lost certificates should be directed to:

Wells Fargo
Shareowner Services
P.O. Box 64874
St. Paul, MN 55164-0856

800-468-9716 or
651-450-4064
www.shareowneronline.com


The Timken Company (NYSE: TKR; www.timken.com) engineers, manufactures and markets Timken® bearings, transmissions, motors, gearboxes, chain and related products, and offers a spectrum of powertrain rebuild and repair services. The leading authority on tapered roller bearings, Timken today applies its deep knowledge of metallurgy, tribology and power transmission across a variety of bearings and related systems to improve the reliability and efficiency of machinery and equipment all around the world.

6.5M 03-14:05 Order No. 10783 I 