INTERNATIONAL BUSINESS MACHINES CORP
Form 10-Q
April 28, 2015

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, DC 20549

FORM 10 - Q

QUARTERLY REPORT PURSUANT TO SECTION 13 or 15(d)

OF THE SECURITIES EXCHANGE ACT OF 1934

FOR THE QUARTER ENDED MARCH 31, 2015

1-2360

(Commission file number)

INTERNATIONAL BUSINESS MACHINES CORPORATION

(Exact name of registrant as specified in its charter)

New York	**13-0871985**
(State of incorporation)	(IRS employer identification number)
Armonk , New York	**10504**
(Address of principal executive offices)	(Zip Code)

914-499-1900

(Registrant’s telephone number)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section l3 or l5(d) of the Securities Exchange Act of 1934 during the preceding l2 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 ý 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 (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes ý No

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 ý	Accelerated filer
Non-accelerated filer (Do not check if a smaller reporting company)	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 ý

The registrant had 984,734,067 shares of common stock outstanding at March 31, 2015.

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Part I - Financial Information

Item 1. Consolidated Financial Statements:

INTERNATIONAL BUSINESS MACHINES CORPORATION
AND SUBSIDIARY COMPANIES

CONSOLIDATED STATEMENT OF EARNINGS
(UNAUDITED)

	Three Months Ended March 31,			
(Dollars in millions except per share amounts)		**2015**		**2014***
Revenue:				
Services	$	12,366	$	13,982
Sales		6,757		7,736
Financing		467		517
Total revenue		19,590		22,236
Cost:				
Services		8,278		9,101
Sales		1,625		2,229
Financing		235		278
Total cost		10,138		11,608
Gross profit		9,452		10,627
Expense and other (income):				
Selling, general and administrative		5,362		6,272
Research, development and engineering		1,298		1,402
Intellectual property and custom development income		(173)		(207)
Other (income) and expense		(143)		(127)
Interest expense		108		105
Total expense and other (income)		6,451		7,444
Income from continuing operations before income taxes		3,001		3,183
Provision for income taxes		585		653
Income from continuing operations	$	2,415	$	2,530
Loss from discontinued operations, net of tax		(88)		(146)
Net income	$	2,328	$	2,384
Earnings/(loss) per share of common stock:				
Assuming dilution:				
Continuing operations	$	2.44	$	2.43
Discontinued operations		(0.09)		(0.14)
Total	$	2.35	$	2.29
Basic:				
Continuing operations	$	2.45	$	2.44
Discontinued operations		(0.09)		(0.14)
Total	$	2.36	$	2.30

Weighted-average number of common shares outstanding: (millions)				
Assuming dilution		992.3		1,041.8
Basic		988.1		1,035.2
Cash dividend per common share	$	1.10	$	0.95

* Reclassified to reflect discontinued operation presentation.

(Amounts may not add due to rounding.)
(The accompanying notes are an integral part of the financial statements.)

**INTERNATIONAL BUSINESS MACHINES CORPORATION
AND SUBSIDIARY COMPANIES**

**CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME
(UNAUDITED)**

	Three Months Ended March 31,	
(Dollars in millions)	**2015**	**2014**
Net income	$ 2,328	$ 2,384
Other comprehensive income/(loss), before tax:		
Foreign currency translation adjustments	(452)	(61)
Net changes related to available-for-sale securities:		
Unrealized gains/(losses) arising during the period	32	0
Reclassification of (gains)/losses to net income	0	4
Total net changes related to available-for-sale securities	32	4
Unrealized gains/(losses) on cash flow hedges:		
Unrealized gains/(losses) arising during the period	619	88
Reclassification of (gains)/losses to net income	(249)	(1)
Total unrealized gains/(losses) on cash flow hedges	370	87
Retirement-related benefit plans:		
Prior service costs/(credits)	5	1
Net (losses)/gains arising during the period	(77)	32
Curtailments and settlements	4	4
Amortization of prior service (credits)/costs	(26)	(29)
Amortization of net (gains)/losses	835	649
Total retirement-related benefit plans	740	656
Other comprehensive income/(loss), before tax	690	687
Income tax (expense)/benefit related to items of other comprehensive income	(657)	(241)
Other comprehensive income/(loss)	33	446
Total comprehensive income/(loss)	$ 2,361	$ 2,830

(Amounts may not add due to rounding.)

(The accompanying notes are an integral part of the financial statements.)

**INTERNATIONAL BUSINESS MACHINES CORPORATION
AND SUBSIDIARY COMPANIES**

**CONSOLIDATED STATEMENT OF FINANCIAL POSITION
(UNAUDITED)**

ASSETS

(Dollars in millions)	**At March 31, 2015**	**At December 31, 2014**
Assets:		
Current assets:		
Cash and cash equivalents	$ 8,796	$ 8,476
Marketable securities	8	0
Notes and accounts receivable - trade (net of allowances of $354 in 2015 and $336 in 2014)	8,806	9,090
Short-term financing receivables (net of allowances of $484 in 2015 and $452 in 2014)	16,303	19,835
Other accounts receivable (net of allowances of $41 in 2015 and $40 in 2014)	2,740	2,906
Inventories, at lower of average cost or market:		
Finished goods	371	430
Work in process and raw materials	1,599	1,674
Total inventories	1,970	2,103
Deferred taxes	1,805	2,044
Prepaid expenses and other current assets	5,890	4,967
Total current assets	46,316	49,422
Property, plant and equipment	38,303	39,034
Less: Accumulated depreciation	27,793	28,263
Property, plant and equipment — net	10,509	10,771
Long-term financing receivables (net of allowances of $125 in 2015 and $126 in 2014)	9,820	11,109
Prepaid pension assets	2,690	2,160
Deferred taxes	4,374	4,808
Goodwill	29,871	30,556
Intangible assets — net	2,991	3,104
Investments and sundry assets	5,466	5,603
Total assets	$ 112,037	$ 117,532

(Amounts may not add due to rounding.)

(The accompanying notes are an integral part of the financial statements.)

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INTERNATIONAL BUSINESS MACHINES CORPORATION
AND SUBSIDIARY COMPANIES

CONSOLIDATED STATEMENT OF FINANCIAL POSITION – (CONTINUED)
(UNAUDITED)

LIABILITIES AND EQUITY

(Dollars in millions)	At March 31, 2015	At December 31, 2014
Liabilities:		
Current liabilities:		
Taxes	$ 3,539	$ 5,084
Short-term debt	4,532	5,731
Accounts payable	6,314	6,864
Compensation and benefits	3,328	4,031
Deferred income	12,162	11,877
Other accrued expenses and liabilities	5,765	6,013
Total current liabilities	35,640	39,600
Long-term debt	34,295	35,073
Retirement and nonpension postretirement benefit obligations	17,211	18,261
Deferred income	3,811	3,691
Other liabilities	8,791	8,892
Total liabilities	99,747	105,518
Equity:		
IBM stockholders' equity:		
Common stock, par value $0.20 per share, and additional paid-in capital	52,928	52,666
Shares authorized: 4,687,500,000		
Shares issued: 2015 - 2,217,335,134		
2014 - 2,215,209,574		
Retained earnings	139,030	137,793
Treasury stock - at cost	(151,975)	(150,715)
Shares: 2015 - 1,232,601,067		
2014 - 1,224,685,815		
Accumulated other comprehensive income/(loss)	(27,842)	(27,875)
Total IBM stockholders' equity	12,141	11,868
Noncontrolling interests	148	146
Total equity	12,289	12,014
Total liabilities and equity	$ 112,037	$ 117,532

(Amounts may not add due to rounding.)

(The accompanying notes are an integral part of the financial statements.)

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INTERNATIONAL BUSINESS MACHINES CORPORATION
AND SUBSIDIARY COMPANIES

CONSOLIDATED STATEMENT OF CASH FLOWS
(UNAUDITED)

	Three Months Ended March 31,	
(Dollars in millions)	**2015**	**2014**
Cash flows from operating activities:		
Net income	$ 2,328	$ 2,384
Adjustments to reconcile net income to cash provided by operating activities		
Depreciation	670	802
Amortization of intangibles	298	339
Stock-based compensation	127	124
Net (gain)/loss on asset sales and other	352	(161)
Changes in operating assets and liabilities, net of acquisitions/divestitures	(165)	(162)
Net cash provided by operating activities	3,610	3,326
Cash flows from investing activities:		
Payments for property, plant and equipment	(857)	(849)
Proceeds from disposition of property, plant and equipment	47	74
Investment in software	(113)	(112)
Acquisition of businesses, net of cash acquired	(148)	(264)
Divestitures of businesses, net of cash transferred	19	391
Non-operating finance receivables — net	1,615	665
Purchases of marketable securities and other investments	(819)	(477)
Proceeds from disposition of marketable securities and other investments	816	608
Net cash provided by investing activities	560	35
Cash flows from financing activities:		
Proceeds from new debt	2,290	4,875
Payments to settle debt	(2,824)	(1,507)
Short-term borrowings/(repayments) less than 90 days — net	(776)	845
Common stock repurchases	(1,165)	(8,166)
Common stock transactions — other	161	270
Cash dividends paid	(1,088)	(990)
Net cash used in financing activities	(3,402)	(4,673)
Effect of exchange rate changes on cash and cash equivalents	(449)	5
Net change in cash and cash equivalents	319	(1,307)
Cash and cash equivalents at January 1	8,476	10,716
Cash and cash equivalents at March 31	$ 8,796	$ 9,409

(Amounts may not add due to rounding.)

(The accompanying notes are an integral part of the financial statements.)

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INTERNATIONAL BUSINESS MACHINES CORPORATION
AND SUBSIDIARY COMPANIES
CONSOLIDATED STATEMENT OF CHANGES IN EQUITY
(UNAUDITED)

(Dollars in millions)	Common Stock and Additional Paid-in Capital	Retained Earnings	Treasury Stock	Accumulated Other Comprehensive Income/(Loss)	Total IBM Stockholders' Equity	Non-Controlling Interests	Total Equity
Equity - January 1, 2015	$ 52,666	$ 137,793	$ (150,715)	$ (27,875)	$ 11,868	$ 146	$ 12,014
Net income plus other comprehensive income/(loss)							
Net income		2,328			2,328		2,328
Other comprehensive income/(loss)				33	33		33
Total comprehensive income/(loss)					$ 2,361		$ 2,361
Cash dividends paid – common stock		(1,088)			(1,088)		(1,088)
Common stock issued under employee plans (2,125,560 shares)	259				259		259
Purchases (363,779 shares) and sales (187,271 shares) of treasury stock under employee plans – net		(3)	(33)		(35)		(35)
Other treasury shares purchased, not retired (7,738,744 shares)			(1,227)		(1,227)		(1,227)
Changes in other equity	3				3		3
Changes in noncontrolling interests						3	3
Equity - March 31, 2015	$ 52,928	$ 139,030	$ (151,975)	$ (27,842)	$ 12,141	$ 148	$ 12,289

(Dollars in millions)	Common Stock and Additional Paid-in Capital	Retained Earnings	Treasury Stock	Accumulated Other Comprehensive Income/(Loss)	Total IBM Stockholders' Equity	Non-Controlling Interests	Total Equity
Equity - January 1, 2014	$ 51,594	$ 130,042	$ (137,242)	$ (21,602)	$ 22,792	$ 137	$ 22,929
Net income plus other comprehensive income/(loss)							
Net income		2,384			2,384		2,384
Other comprehensive income/(loss)				446	446		446
Total comprehensive income/(loss)					$ 2,830		$ 2,830
Cash dividends paid – common stock		(990)			(990)		(990)
Common stock issued under							

employee plans (3,105,227 shares)	333				333		333
Purchases (488,203 shares) and sales (328,673 shares) of treasury stock under employee plans – net		(5)	(46)		(51)		(51)
Other treasury shares purchased, not retired (45,153,202 shares)			(8,324)		(8,324)		(8,324)
Changes in other equity	16				16		16
Changes in noncontrolling interests						(4)	(4)
Equity - March 31, 2014	$ 51,943	$ 131,431	$ (145,612)	$ (21,156)	$ 16,607	$ 133	$ 16,740

(Amounts may not add due to rounding.)

(The accompanying notes are an integral part of the financial statements.)

Notes to Consolidated Financial Statements:

1. Basis of Presentation: The accompanying Consolidated Financial Statements and footnotes of the International Business Machines Corporation (IBM or the company) have been prepared in accordance with accounting principles generally accepted in the United States of America (GAAP). The financial statements and footnotes are unaudited. In the opinion of the company's management, these statements include all adjustments, which are only of a normal recurring nature, necessary to present a fair statement of the company's results of operations, financial position and cash flows.

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the amount of assets, liabilities, revenue, costs, expenses and other comprehensive income/(loss) that are reported in the Consolidated Financial Statements and accompanying disclosures. These estimates are based on management's best knowledge of current events, historical experience, actions that the company may undertake in the future and on various other assumptions that are believed to be reasonable under the circumstances. As a result, actual results may be different from these estimates. Refer to the company's 2014 Annual Report on pages 68 to 71 for a discussion of the company's critical accounting estimates.

On October 20, 2014, the company announced a definitive agreement to divest its Microelectronics business and manufacturing operations to GLOBALFOUNDRIES. The assets and liabilities of the Microelectronics business are reported as held for sale at March 31, 2015. The operating results of the Microelectronics business have been reported as discontinued operations. Prior periods have been reclassified to conform to this presentation to allow for a meaningful comparison of continuing operations. Refer to Note 9, "Acquisitions/Divestitures," for additional information on the transaction. In addition, in the first quarter of 2015, the company renamed its Systems & Technology segment to Systems Hardware.

Interim results are not necessarily indicative of financial results for a full year. The information included in this Form 10-Q should be read in conjunction with the company's 2014 Annual Report.

Noncontrolling interest amounts in income of $1.2 million and $(0.5) million, net of tax, for the three months ended March 31, 2015 and 2014, respectively, are included in the Consolidated Statement of Earnings within the other (income) and expense line item.

Within the financial statements and tables presented, certain columns and rows may not add due to the use of rounded numbers for disclosure purposes. Percentages presented are calculated from the underlying whole-dollar amounts. Certain prior year amounts have been reclassified to conform to the current year presentation. This is annotated where applicable.

2. Accounting Changes: In April 2015, the Financial Accounting Standards Board (FASB) issued guidance which requires debt issuance costs related to a recognized debt liability to be presented in the balance sheet as a direct deduction from the carrying amount of that debt liability, consistent with debt discounts. The guidance is effective January 1, 2016 with early adoption permitted. The guidance is a change in financial statement presentation only and will not have a material impact in the consolidated financial results. At March 31, 2015, the company had approximately $80 million in debt issuance costs included in investments and sundry assets in the Consolidated Statement of Financial Position.

In May 2014, the FASB issued guidance on the recognition of revenue from contracts with customers. Revenue recognition will depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. The guidance also requires disclosures regarding the nature, amount, timing and uncertainty of revenue and cash flows arising from contracts with customers. The guidance permits two methods of adoption: retrospectively to each prior reporting period presented, or retrospectively with the cumulative effect of initially applying the guidance recognized at the date of initial application. The guidance is effective January 1, 2017 and early adoption is not permitted. The company is currently evaluating the impact of the new guidance and the method of adoption.

In April 2014, the FASB issued guidance that changed the criteria for reporting a discontinued operation. Only disposals of a component that represents a strategic shift that has (or will have) a major effect on an entity's operations and financial results is a discontinued operation. The guidance also requires expanded disclosures about discontinued operations and disposals of a significant part of an entity that does not qualify for discontinued operations reporting. The guidance was effective January 1, 2015. The impact to the company will be dependent on any transaction that is within the scope of the new guidance.

In July 2013, the FASB issued guidance regarding the presentation of an unrecognized tax benefit when a net operating loss carryforward, a similar tax loss, or a tax credit carryforward exists. Under certain circumstances, unrecognized tax benefits should be presented in the financial statements as a reduction to a deferred tax asset for a net operating loss

Notes to Consolidated Financial Statements – (continued)

carryforward, a similar tax loss, or a tax credit carryforward. The guidance was effective January 1, 2014. The guidance was a change in financial statement presentation only and did not have a material impact in the consolidated financial results.

In March 2013, the FASB issued guidance on when foreign currency translation adjustments should be released to net income. When a parent entity ceases to have a controlling financial interest in a subsidiary or group of assets that is a business within a foreign entity, the parent is required to release any related cumulative translation adjustment into net income. Accordingly, the cumulative translation adjustment should be released into net income only if the sale or transfer results in the complete or substantially complete liquidation of the foreign entity in which the subsidiary or group of assets had resided. The guidance was effective January 1, 2014 and did not have a material impact in the consolidated financial results.

In February 2013, the FASB issued guidance for the recognition, measurement and disclosure of obligations resulting from joint and several liability arrangements for which the total amount of the obligation within the scope of the guidance is fixed at the reporting date. Examples include debt arrangements, other contractual obligations and settled litigation matters. The guidance requires an entity to measure such obligations as the sum of the amount that the reporting entity agreed to pay on the basis of its arrangement among its co-obligors plus additional amounts the reporting entity expects to pay on behalf of its co-obligors. The guidance was effective January 1, 2014 and did not have a material impact in the consolidated financial results.

3. Financial Instruments:

Fair Value Measurements

Accounting guidance defines fair value 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. Under this guidance, the company is required to classify certain assets and liabilities based on the following fair value hierarchy:

- Level 1—Quoted prices (unadjusted) in active markets for identical assets or liabilities that can be accessed at the measurement date;
- Level 2—Inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly or indirectly; and
- Level 3—Unobservable inputs for the asset or liability.

The guidance requires the use of observable market data if such data is available without undue cost and effort.

When available, the company uses unadjusted quoted market prices in active markets to measure the fair value and classifies such items as Level 1. If quoted market prices are not available, fair value is based upon internally developed models that use current market-based or independently sourced market parameters such as interest rates and currency rates. Items valued using internally generated models are classified according to the lowest level input or value driver that is significant to the valuation.

The determination of fair value considers various factors including interest rate yield curves and time value underlying the financial instruments. For derivatives and debt securities, the company uses a discounted cash flow analysis using discount rates commensurate with the duration of the instrument.

In determining the fair value of financial instruments, the company considers certain market valuation adjustments to the "base valuations" calculated using the methodologies described below for several parameters that market participants would consider in determining fair value:

- Counterparty credit risk adjustments are applied to financial instruments, taking into account the actual credit risk of a counterparty as observed in the credit default swap market to determine the true fair value of such an instrument.

- Credit risk adjustments are applied to reflect the company's own credit risk when valuing all liabilities measured at fair value. The methodology is consistent with that applied in developing counterparty credit risk adjustments, but incorporates the company's own credit risk as observed in the credit default swap market.

As an example, the fair value of derivatives is derived utilizing a discounted cash flow model that uses observable market inputs such as known notional value amounts, yield curves, spot and forward exchange rates as well as discount rates. These inputs relate to liquid, heavily traded currencies with active markets which are available for the full term of the derivative.

Notes to Consolidated Financial Statements – (continued)

Certain financial assets are measured at fair value on a nonrecurring basis. These assets include equity method investments that are recognized at fair value at the measurement date to the extent that they are deemed to be other-than-temporarily impaired. Certain assets that are measured at fair value on a recurring basis can be subject to nonrecurring fair value measurements. These assets include available-for-sale equity investments that are deemed to be other-than-temporarily impaired. In the event of an other-than-temporary impairment of a financial investment, fair value is measured using a model described above.

Non-financial assets such as property, plant and equipment, land, goodwill and intangible assets are also subject to nonrecurring fair value measurements if they are deemed to be impaired. The impairment models used for nonfinancial assets depend on the type of asset. In the third quarter of 2014, the company recorded an impairment on certain assets that were initially reported as held for sale at September 30, 2014. See note 9, "Acquisitions/Divestitures," for additional information. There were no material impairments of non-financial assets for the three months ended March 31, 2015 and 2014, respectively.

Accounting guidance permits the measurement of eligible financial assets, financial liabilities and firm commitments at fair value, on an instrument-by-instrument basis, that are otherwise not permitted to be accounted for at fair value under other accounting standards. This election is irrevocable. The company has not applied the fair value option to any eligible assets or liabilities.

The following tables present the company's financial assets and financial liabilities that are measured at fair value on a recurring basis at March 31, 2015 and December 31, 2014.

Notes to Consolidated Financial Statements – (continued)

(Dollars in millions)								
At March 31, 2015		**Level 1**		**Level 2**		**Level 3**		**Total**
Assets:								
Cash equivalents (1)								
Time deposits and certificates of deposit	$	—	$	4,503	$	—	$	4,503
Commercial paper		—		500		—		500
Money market funds		1,311		—		—		1,311
U.S. government securities		—		530		—		530
Canadian government securities		—		237		—		237
Other securities		—		6		—		6
Total		1,311		5,775		—		7,086(6)
Debt securities - current (2)		—		8		—		8(6)
Debt securities - noncurrent (3)		1		8		—		9
Trading security investments (3)		49		—		—		49
Available-for-sale equity investments (3)		281		—		—		281
Derivative assets (4)								
Interest rate contracts		—		743		—		743
Foreign exchange contracts		—		1,230		—		1,230
Equity contracts		—		18		—		18
Total		—		1,991		—		1,991(7)
Total assets	**$**	1,642	$	7,782	$	—	$	9,424(7)
Liabilities:								
Derivative liabilities (5)								
Foreign exchange contracts	$	—	$	172	$	—	$	172
Equity contracts		—		10		—		10
Interest rate contracts		—		0		—		0
Total liabilities	**$**	—	$	181	$	—	$	181(7)

(1) Included within cash and cash equivalents in the Consolidated Statement of Financial Position.

(2) Commercial paper and certificates of deposit reported as marketable securities in the Consolidated Statement of Financial Position.

(3) Included within investments and sundry assets in the Consolidated Statement of Financial Position.

(4) The gross balances of derivative assets contained within prepaid expenses and other current assets, and investments and sundry assets in the Consolidated Statement of Financial Position at March 31, 2015 were $1,204 million and $787 million respectively.

(5) The gross balances of derivative liabilities contained within other accrued expenses and liabilities, and other liabilities in the Consolidated Statement of Financial Position at March 31, 2015 were $164 million and $18 million, respectively.

(6) Available-for-sale securities with carrying values that approximate fair value.

(7) If derivative exposures covered by a qualifying master netting agreement had been netted in the Consolidated Statement of Financial Position, the total derivative asset and liability positions would have been reduced by $141 million each.

Notes to Consolidated Financial Statements – (continued)

(Dollars in millions) **At December 31, 2014**	**Level 1**	**Level 2**	**Level 3**	**Total**
Assets:				
Cash equivalents (1)				
Time deposits and certificates of deposit	$ —	$ 3,517	$ —	$ 3,517
Commercial paper	—	764	—	764
Money market funds	662	—	—	662
U.S government securities	—	410	—	410
Other securities	—	6	—	6
Total	662	4,697	—	5,359(5)
Debt securities - noncurrent (2)	1	8	—	9
Trading security investments (2)	74	—	—	74
Available-for-sale equity investments (2)	243	—	—	243
Derivative assets (3)				
Interest rate contracts	—	633	—	633
Foreign exchange contracts	—	775	—	775
Equity contracts	—	24	—	24
Total	—	1,432	—	1,432(6)
Total assets	**$** 980	$ 6,138	$ —	$ 7,118(6)
Liabilities:				
Derivative liabilities (4)				
Foreign exchange contracts	$ —	$ 177	$ —	$ 177
Equity contracts	—	19	—	19
Total liabilities	**$** —	$ 196	$ —	$ 196(6)

(1) Included within cash and cash equivalents in the Consolidated Statement of Financial Position.

(2) Included within investments and sundry assets in the Consolidated Statement of Financial Position.

(3) The gross balances of derivative assets contained within prepaid expenses and other current assets, and investments and sundry assets in the Consolidated Statement of Financial Position at December 31, 2014 were $751 million and $681 million, respectively.

(4) The gross balances of derivative liabilities contained within other accrued expenses and liabilities, and other liabilities in the Consolidated Statement of Financial Position at December 31, 2014 were $165 million and $31 million, respectively.

(5) Available-for-sale securities with carrying values that approximate fair value.

(6) If derivative exposures covered by a qualifying master netting agreement had been netted in the Consolidated Statement of Financial Position, the total derivative asset and liability positions would have been reduced by $97

million each.

There were no transfers between Levels 1 and 2 for the quarter ended March 31, 2015. During the year ended December 31, 2014, the company transferred trading security investments valued at $74 million from Level 2 to Level 1 due to the expiration of certain regulatory restrictions.

Financial Assets and Liabilities Not Measured at Fair Value

Short-Term Receivables and Payables

Notes and other accounts receivable and other investments are financial assets with carrying values that approximate fair value. Accounts payable, other accrued expenses and short-term debt (excluding the current portion of long-term debt) are financial liabilities with carrying values that approximate fair value. If measured at fair value in the financial statements, these financial instruments would be classified as Level 3 in the fair value hierarchy.

Loans and Long-term Receivables

Fair values are based on discounted future cash flows using current interest rates offered for similar loans to clients with similar credit ratings for the same remaining maturities. At March 31, 2015 and December 31, 2014, the difference between the carrying amount and estimated fair value for loans and long-term receivables was immaterial. If measured at fair value in the financial statements, these financial instruments would be classified as Level 3 in the fair value hierarchy.

Notes to Consolidated Financial Statements – (continued)

Long-Term Debt

Fair value of publicly-traded long-term debt is based on quoted market prices for the identical liability when traded as an asset in an active market. For other long-term debt for which a quoted market price is not available, an expected present value technique that uses rates currently available to the company for debt with similar terms and remaining maturities is used to estimate fair value. The carrying amount of long-term debt was $34,295 million and $35,073 million, and the estimated fair value was $36,844 million and $37,524 million at March 31, 2015 and December 31, 2014, respectively. If measured at fair value in the financial statements, long-term debt (including the current portion) would be classified as Level 2 in the fair value hierarchy.

Debt and Marketable Equity Securities

The company's cash equivalents and current debt securities are considered available-for-sale and recorded at fair value, which is not materially different from carrying value, in the Consolidated Statement of Financial Position.

The following tables summarize the company's noncurrent debt and marketable equity securities which are considered available-for-sale and recorded at fair value in the Consolidated Statement of Financial Position.

(Dollars in millions) At March 31, 2015:	**Adjusted Cost**	**Gross Unrealized Gains**	**Gross Unrealized Losses**	**Fair Value**
Debt securities – noncurrent(1)	$ 6	$ 3	$ —	$ 9
Available-for-sale equity investments(1)	$ 278	$ 8	$ 5	$ 281

(1) Included within investments and sundry assets in the Consolidated Statement of Financial Position.

(Dollars in millions) At December 31, 2014:	**Adjusted Cost**	**Gross Unrealized Gains**	**Gross Unrealized Losses**	**Fair Value**
Debt securities – noncurrent(1)	$ 7	$ 3	$ —	$ 9
Available-for-sale equity investments(1)	$ 272	$ 2	$ 31	$ 243

(1) Included within investments and sundry assets in the Consolidated Statement of Financial Position.

During the fourth quarter of 2014, the company acquired equity securities in conjunction with the sale of the industry standard server business which are classified as available-for-sale securities. Gross unrealized gains related to available-for-sale securities of $26 million for the three months ended March 31, 2015 were recorded in the

Consolidated Statement of Financial Position.

Based on an evaluation of available evidence as of March 31, 2015 and December 31, 2014, the company believes that unrealized losses on debt and available-for-sale equity investments were temporary and did not represent a need for an other-than-temporary impairment.

Sales of debt and available-for-sale equity investments during the period were as follows:

(Dollars in millions) **For the three months ended March 31:**	**2015**	**2014**
Proceeds	$ 4	$ 14
Gross realized gains (before taxes)	0	—
Gross realized losses (before taxes)	0	4

Notes to Consolidated Financial Statements – (continued)

The after-tax net unrealized holding gains/(losses) on available-for-sale debt and marketable equity securities that have
been included in other comprehensive income/(loss) for the period and the after-tax net (gains)/losses reclassified from
accumulated other comprehensive income/(loss) to net income were as follows:

(Dollars in millions) For the three months ended March 31:	2015	2014
Net unrealized gains/(losses) arising during the period	$ 20	$ 0
Net unrealized (gains)/losses reclassified to net income*	0	3

* There were no writedowns for the three months ended March 31, 2015 and 2014, respectively.

The contractual maturities of substantially all available-for-sale debt securities are less than one year at March 31, 2015.

Derivative Financial Instruments

The company operates in multiple functional currencies and is a significant lender and borrower in the global markets. In the normal course of business, the company is exposed to the impact of interest rate changes and foreign currency fluctuations, and to a lesser extent equity and commodity price changes and client credit risk. The company limits these risks by following established risk management policies and procedures, including the use of derivatives, and, where cost effective, financing with debt in the currencies in which assets are denominated. For interest rate exposures, derivatives are used to better align rate movements between the interest rates associated with the company’s lease and other financial assets and the interest rates associated with its financing debt. Derivatives are also used to manage the related cost of debt. For foreign currency exposures, derivatives are used to better manage the cash flow volatility arising from foreign exchange rate fluctuations.

As a result of the use of derivative instruments, the company is exposed to the risk that counterparties to derivative contracts will fail to meet their contractual obligations. To mitigate the counterparty credit risk, the company has a policy of only entering into contracts with carefully selected major financial institutions based upon their overall credit profile. The company’s established policies and procedures for mitigating credit risk on principal transactions include reviewing and establishing limits for credit exposure and continually assessing the creditworthiness of counterparties. The right of set-off that exists under certain of these arrangements enables the legal entities of the company subject to the arrangement to net amounts due to and from the counterparty reducing the maximum loss from credit risk in the event of counterparty default.

The company is also a party to collateral security arrangements with most of its major derivative counterparties. These arrangements require the company to hold or post collateral (cash or U.S. Treasury securities) when the derivative fair values exceed contractually established thresholds. Posting thresholds can be fixed or can vary based on credit default swap pricing or credit ratings received from the major credit agencies. The aggregate fair value of all derivative instruments under these collateralized arrangements that were in a liability position at March 31, 2015 and December 31, 2014 was $10 million and $21 million, respectively, for which no collateral was posted at March 31, 2015 and December 31, 2014. Full collateralization of these agreements would be required in the event that the company's credit rating falls below investment grade or if its credit default swap spread exceeds 250 basis points, as applicable, pursuant to the terms of the collateral security arrangements. The aggregate fair value of derivative instruments in asset positions as of March 31, 2015 and December 31, 2014 was $1,991 million and $1,432 million, respectively. This amount represents the maximum exposure to loss at the reporting date if the counterparties failed to perform as contracted. This exposure was reduced by $141 million and $97 million at March 31, 2015 and December 31, 2014, respectively, of liabilities included in master netting arrangements with those counterparties. Additionally, at March 31, 2015 and December 31, 2014, this exposure was reduced by $734 million and $487 million of cash collateral, respectively, received by the company. At March 31, 2015 and December 31, 2014, the net exposure related to derivative assets recorded in the Consolidated Statement of Financial Position was $1,070 million and $817 million, respectively. At March 31, 2015 and December 31, 2014, the net exposure related to derivative liabilities recorded in the Consolidated Statement of Financial Position was $40 million and $99 million, respectively.

In the Consolidated Statement of Financial Position, the company does not offset derivative assets against liabilities in master netting arrangements nor does it offset receivables or payables recognized upon payment or receipt of cash collateral against the fair values of the related derivative instruments. No amount was recognized in other receivables at March 31, 2015 or December 31, 2014 for the right to reclaim cash collateral. The amount recognized in accounts payable for the obligation to return cash collateral totaled $734 million and $487 million at March 31, 2015 and December 31, 2014, respectively. The company restricts the use of cash collateral received to rehypothecation, and therefore reports it in prepaid expenses and other current assets in the Consolidated Statement of Financial Position. No amount was rehypothecated at

Notes to Consolidated Financial Statements – (continued)

March 31, 2015 and December 31, 2014. At March 31, 2015 and December 31, 2014, the company held $46 million and $31 million in non-cash collateral in U.S. Treasury securities, respectively.

The company may employ derivative instruments to hedge the volatility in stockholders' equity resulting from changes in currency exchange rates of significant foreign subsidiaries of the company with respect to the U.S. dollar. These instruments, designated as net investment hedges, expose the company to liquidity risk as the derivatives have an immediate cash flow impact upon maturity which is not offset by a cash flow from the translation of the underlying hedged equity. The company monitors this cash loss potential on an ongoing basis and may discontinue some of these hedging relationships by de-designating or terminating the derivative instrument in order to manage the liquidity risk. Although not designated as accounting hedges, the company may utilize derivatives to offset the changes in the fair value of the de-designated instruments from the date of de-designation until maturity.

In its hedging programs, the company uses forward contracts, futures contracts, interest-rate swaps, cross-currency swaps, and options depending upon the underlying exposure. The company is not a party to leveraged derivative instruments.

A brief description of the major hedging programs, categorized by underlying risk, follows.

Interest Rate Risk

Fixed and Variable Rate Borrowings

The company issues debt in the global capital markets, principally to fund its financing lease and loan portfolios. Access to cost-effective financing can result in interest rate mismatches with the underlying assets. To manage these mismatches and to reduce overall interest cost, the company uses interest-rate swaps to convert specific fixed-rate debt issuances into variable-rate debt (i.e., fair value hedges) and to convert specific variable-rate debt issuances into fixed-rate debt (i.e., cash flow hedges). At March 31, 2015 and December 31, 2014, the total notional amount of the company's interest rate swaps was $6.6 billion and $5.8 billion, respectively. The weighted-average remaining maturity of these instruments at March 31, 2015 and December 31, 2014 was approximately 7.8 years and 8.7 years, respectively.

Forecasted Debt Issuance

The company is exposed to interest rate volatility on future debt issuances. To manage this risk, the company may use forward starting interest-rate swaps to lock in the rate on the interest payments related to the forecasted debt issuance. These swaps are accounted for as cash flow hedges. The company did not have any derivative instruments relating to this program outstanding at March 31, 2015 and December 31, 2014.

At March 31, 2015 and December 31, 2014, net gains of approximately $1 million (before taxes) were recorded in accumulated other comprehensive income/(loss) in connection with cash flow hedges of the company's borrowings. Within these amounts, gains of less than $1 million are expected to be reclassified to net income within the next 12 months, providing an offsetting economic impact against the underlying transactions.

Foreign Exchange Risk

Long-Term Investments in Foreign Subsidiaries (Net Investment)

A large portion of the company's foreign currency denominated debt portfolio is designated as a hedge of net investment in foreign subsidiaries to reduce the volatility in stockholders' equity caused by changes in foreign currency exchange rates in the functional currency of major foreign subsidiaries with respect to the U.S. dollar. The company also uses cross-currency swaps and foreign exchange forward contracts for this risk management purpose. At March 31, 2015 and December 31, 2014, the total notional amount of derivative instruments designated as net investment hedges was $4.2 billion and $2.2 billion, respectively. The weighted-average remaining maturity of these instruments at March 31, 2015 and December 31, 2014 was approximately 0.2 years for both periods.

Anticipated Royalties and Cost Transactions

The company's operations generate significant nonfunctional currency, third-party vendor payments and intercompany payments for royalties and goods and services among the company's non-U.S. subsidiaries and with the parent company. In anticipation of these foreign currency cash flows and in view of the volatility of the currency markets, the company selectively employs foreign exchange forward contracts to manage its currency risk. These forward contracts are accounted

Notes to Consolidated Financial Statements – (continued)

for as cash flow hedges. The maximum length of time over which the company has hedged its exposure to the variability in future cash flows is four years. At March 31, 2015 and December 31, 2014, the total notional amount of forward contracts designated as cash flow hedges of forecasted royalty and cost transactions was $9.3 billion for both periods, with a weighted-average remaining maturity of 0.7 years for both periods.

At March 31, 2015 and December 31, 2014, in connection with cash flow hedges of anticipated royalties and cost transactions, the company recorded net gains of $972 million and net gains of $602 million (before taxes), respectively, in accumulated other comprehensive income/(loss). Within these amounts, $921 million of gains and $572 million of gains, respectively, are expected to be reclassified to net income within the next 12 months, providing an offsetting economic impact against the underlying anticipated transactions.

Foreign Currency Denominated Borrowings

The company is exposed to exchange rate volatility on foreign currency denominated debt. To manage this risk, the company employs cross-currency swaps to convert fixed-rate foreign currency denominated debt to fixed-rate debt denominated in the functional currency of the borrowing entity. These swaps are accounted for as cash flow hedges. The maximum length of time over which the company has hedged its exposure to the variability in future cash flows is approximately seven years. At March 31, 2015, and December 31, 2014, no amounts were outstanding under this program.

At March 31, 2015 and December 31, 2014, in connection with cash flow hedges of foreign currency denominated borrowings, the company recorded net losses of $2 million (before taxes) in accumulated other comprehensive income/(loss). Within these amounts, less than $1 million of losses are expected to be reclassified to net income within the next 12 months, providing an offsetting economic impact against the underlying exposure.

Subsidiary Cash and Foreign Currency Asset/Liability Management

The company uses its Global Treasury Centers to manage the cash of its subsidiaries. These centers principally use currency swaps to convert cash flows in a cost-effective manner. In addition, the company uses foreign exchange forward contracts to economically hedge, on a net basis, the foreign currency exposure of a portion of the company's nonfunctional currency assets and liabilities. The terms of these forward and swap contracts are generally less than one year. The changes in the fair values of these contracts and of the underlying hedged exposures are generally offsetting and are recorded in other (income) and expense in the Consolidated Statement of Earnings. At March 31, 2015 and December 31, 2014, the total notional amount of derivative instruments in economic hedges of foreign currency exposure was $11.2 billion and $13.1 billion, respectively.

Equity Risk Management

The company is exposed to market price changes in certain broad market indices and in the company's own stock primarily related to certain obligations to employees. Changes in the overall value of these employee compensation obligations are recorded in selling, general and administrative (SG&A) expense in the Consolidated Statement of Earnings. Although not designated as accounting hedges, the company utilizes derivatives, including equity swaps and futures, to economically hedge the exposures related to its employee compensation obligations. The derivatives are linked to the total return on certain broad market indices or the total return on the company's common stock, and are recorded at fair value with gains or losses also reported in SG&A expense in the Consolidated Statement of Earnings. At March 31, 2015 and December 31, 2014, the total notional amount of derivative instruments in economic hedges of these compensation obligations was $1.2 billion and $1.3 billion, respectively.

Other Risks

The company may hold warrants to purchase shares of common stock in connection with various investments that are deemed derivatives because they contain net share or net cash settlement provisions. The company records the changes in the fair value of these warrants in other (income) and expense in the Consolidated Statement of Earnings. The company did not have any warrants qualifying as derivatives outstanding at March 31, 2015 and December 31, 2014.

The company is exposed to a potential loss if a client fails to pay amounts due under contractual terms. The company may utilize credit default swaps to economically hedge its credit exposures. The swaps are recorded at fair value with gains and losses reported in other (income) and expense in the Consolidated Statement of Earnings. The company did not have any derivative instruments relating to this program outstanding at March 31, 2015 and December 31, 2014.

Notes to Consolidated Financial Statements – (continued)

The company is exposed to market volatility on certain investment securities. The company may utilize options or forwards to economically hedge its market exposure. The derivatives are recorded at fair value with gains and losses reported in other (income) and expense in the Consolidated Statement of Earnings. At March 31, 2015 and December 31, 2014, the total notional amount of derivative instruments in economic hedges of investment securities was less than $0.1 billion for both periods.

The following tables provide a quantitative summary of the derivative and non-derivative instrument-related risk management activity as of March 31, 2015 and December 31, 2014, as well as for the three months ended March 31, 2015 and 2014, respectively.

Fair Values of Derivative Instruments in the Consolidated Statement of Financial Position
As of March 31, 2015 and December 31, 2014

(Dollars in millions)	Fair Value of Derivative Assets			Fair Value of Derivative Liabilities		
	Balance Sheet Classification	3/31/2015	12/31/2014	Balance Sheet Classification	3/31/2015	12/31/2
Designated as hedging instruments:						
Interest rate contracts:	Prepaid expenses and other current assets	$ 5	$ 5	Other accrued expenses and liabilities	$ 0	$ [illegible]
	Investments and sundry assets	738	628	Other liabilities	0	[illegible]
Foreign exchange contracts:	Prepaid expenses and other current assets	966	632	Other accrued expenses and liabilities	43	[illegible]
	Investments and sundry assets	15	17	Other liabilities	15	[illegible]
Fair value of derivative assets		$ 1,724	$ 1,281	**Fair value of derivative liabilities**	$ 58	$ [illegible]
Not designated as hedging instruments:						
Foreign exchange contracts:	Prepaid expenses and other current assets	$ 214	$ 90	Other accrued expenses and liabilities	$ 111	$ [illegible]
	Investments and sundry assets	35	37	Other liabilities	3	[illegible]
Equity contracts:	Prepaid expenses and other current assets	18	24	Other accrued expenses and liabilities	10	[illegible]
	Investments and sundry assets	0	0	Other liabilities	0	[illegible]
Fair value of derivative assets		$ 267	$ 151	**Fair value of derivative liabilities**	$ 124	$ [illegible]
Total debt designated as hedging instruments:						

Short-term debt	N/A	N/A	$	$ —
Long-term debt	N/A	N/A	$ 6,416	$ 7,7
Total	$ 1,991	$ 1,432	$ 6,597	$ 7,9

N/A-not applicable

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Notes to Consolidated Financial Statements – (continued)

The Effect of Derivative Instruments in the Consolidated Statement of Earnings
For the three months ended March 31, 2015 and 2014

(Dollars in millions)		Gain (Loss) Recognized in Earnings			
	Consolidated Statement of Earnings Line Item	Recognized on Derivatives(1)		Attributable to Risk Being Hedged(2)	
For the three months ended March 31:		2015	2014	2015	2014
Derivative instruments in fair value hedges(4):					
Interest rate contracts	Cost of financing	$ 97	$ 48	$ (66)	$ (23)
	Interest expense	74	33	(51)	(15)
Derivative instruments not designated as hedging instruments(1):					
Foreign exchange contracts	Other (income) and expense	17	(34)	N/A	N/A
Interest rate contracts	Other (income) and expense	(1)	—	N/A	N/A
Equity contracts	SG&A expense	24	21	N/A	N/A
	Other (income) and expense	0	—	N/A	N/A
Total		$ 211	$ 68	$ (118)	$ (38)

	Gain (Loss) Recognized in Earnings and Other Comprehensive Income						
	Effective Portion Recognized in OCI		Consolidated Statement of Earnings Line Item	Effective Portion Reclassified from AOCI		(Ineffectiveness) and Amounts Excluded from Effectiveness Testing	
For the three months ended March 31:	2015	2014		2015	2014	2015	2014
Derivative instruments in cash flow hedges:							
Interest rate contracts	$ —	$ —	Interest expense	$ 0	$ —	$ —	$ —
Foreign exchange contracts	619	88	Other (income) and expense	160	29	0	0
			Cost of sales	50	(26)	—	—
			SG&A expense	40	(2)	—	—
Instruments in net investment hedges(3):							
Foreign exchange contracts	694	(26)	Interest expense	—	—	0	0

Total	$ 1,313	$ 62		$ 249	$ 1	$ 1	$ 0

N/A-not applicable

Note: OCI represents Other comprehensive income/(loss) in the Consolidated Statement of Comprehensive Income and AOCI represents Accumulated other comprehensive income/(loss) in the Consolidated Statement of Changes in Equity.

(1) The amount includes changes in clean fair values of the derivative instruments in fair value hedging relationships and the periodic accrual for coupon payments required under these derivative contracts.

(2) The amount includes basis adjustments to the carrying value of the hedged item recorded during the period and amortization of basis adjustments recorded on de-designated hedging relationships during the period.

(3) Instruments in net investment hedges include derivative and non-derivative instruments.

(4) For the three month period ended March 31, 2015, fair value hedges resulted in a gain of $2 million in ineffectiveness. There were no amounts recorded as ineffectiveness on fair value hedges for the three month period ended March 31, 2014.

Notes to Consolidated Financial Statements – (continued)

For the three months ending March 31, 2015 and 2014, there were no significant gains or losses recognized in earnings representing hedge ineffectiveness or excluded from the assessment of hedge effectiveness (for fair value hedges), or associated with an underlying exposure that did not or was not expected to occur (for cash flow hedges); nor are there any anticipated in the normal course of business.

4. Financing Receivables: The following table presents financing receivables, net of allowances for credit losses, including residual values.

(Dollars in millions)		At March 31, 2015		At December 31, 2014
Current:				
Net investment in sales-type and direct financing leases	$	3,560	$	3,781
Commercial financing receivables		6,026		8,423
Client loan and installment payment receivables (loans)		6,717		7,631
Total	$	16,303	$	19,835
Noncurrent:				
Net investment in sales-type and direct financing leases	$	4,081	$	4,449
Client loan and installment payment receivables (loans)		5,740		6,660
Total	$	9,820	$	11,109

Net investment in sales-type and direct financing leases relates principally to the company’s systems products and are for terms ranging generally from two to six years. Net investment in sales-type and direct financing leases includes unguaranteed residual values of $649 million and $671 million at March 31, 2015 and December 31, 2014, respectively, and is reflected net of unearned income of $491 million and $517 million, and net of the allowance for credit losses of $188 million and $165 million at those dates, respectively.

Commercial financing receivables, net of the allowance for credit losses of $13 million and $17 million at March 31, 2015 and December 31, 2014, respectively, relate primarily to inventory and accounts receivable financing for dealers and remarketers of IBM and OEM products. Payment terms for inventory and accounts receivable financing generally range from 30 to 90 days.

Client loan and installment payment receivables (loans), net of the allowance for credit losses of $408 million and $396 million at March 31, 2015 and December 31, 2014, respectively, are loans that are provided primarily to clients to finance the purchase of hardware, software and services. Payment terms on these financing arrangements are generally for terms up to seven years.

Client loan and installment payment receivables (loans) financing contracts are priced independently at competitive market rates. The company has a history of enforcing the terms of these financing agreements.

The company utilizes certain of its financing receivables as collateral for nonrecourse borrowings. Financing receivables pledged as collateral for borrowings were $596 million and $642 million at March 31, 2015 and December 31, 2014, respectively.

The company did not have any financing receivables held for sale as of March 31, 2015 and December 31, 2014.

Financing Receivables by Portfolio Segment

The following tables present financing receivables on a gross basis, excluding the allowance for credit losses and residual value, by portfolio segment and by class, excluding current commercial financing receivables and other miscellaneous current financing receivables at March 31, 2015 and December 31, 2014. The company determines its allowance for credit losses based on two portfolio segments: lease receivables and loan receivables, and further segments the portfolio into two classes: major markets and growth markets.

Notes to Consolidated Financial Statements – (continued)

(Dollars in millions) **At March 31, 2015**	**Major Markets**	**Growth Markets**	**Total**
Financing receivables:			
Lease receivables	$ 5,265	$ 1,840	$ 7,105
Loan receivables	8,911	3,953	12,864
Ending balance	$ 14,176	$ 5,793	$ 19,970
Collectively evaluated for impairment	$ 14,098	$ 5,332	$ 19,431
Individually evaluated for impairment	$ 78	$ 461	$ 539
<u>Allowance for credit losses:</u>			
Beginning balance at January 1, 2015			
Lease receivables	$ 32	$ 133	$ 165
Loan receivables	79	317	396
Total	$ 111	$ 450	$ 561
Write-offs	(1)	(1)	(1)
Provision	5	49	54
Other	(8)	(11)	(19)
Ending balance at March 31, 2015	$ 107	$ 488	$ 595
Lease receivables	$ 32	$ 156	$ 188
Loan receivables	$ 75	$ 332	$ 408
Collectively evaluated for impairment	$ 41	$ 39	$ 80
Individually evaluated for impairment	$ 66	$ 449	$ 515

(Dollars in millions) **At December 31, 2014**	**Major Markets**	**Growth Markets**	**Total**
Financing receivables:			
Lease receivables	$ 5,702	$ 1,943	$ 7,645
Loan receivables	10,049	4,639	14,687
Ending balance	$ 15,751	$ 6,581	$ 22,332
Collectively evaluated for impairment	$ 15,665	$ 6,156	$ 21,821
Individually evaluated for impairment	$ 86	$ 425	$ 511
<u>Allowance for credit losses:</u>			
Beginning balance at January 1, 2014			
Lease receivables	$ 42	$ 80	$ 123
Loan receivables	95	147	242
Total	$ 137	$ 228	$ 365
Write-offs	(18)	(6)	(24)
Provision	3	240	243
Other	(12)	(11)	(23)
Ending balance at December 31, 2014	$ 111	$ 450	$ 561
Lease receivables	$ 32	$ 133	$ 165
Loan receivables	$ 79	$ 317	$ 396
Collectively evaluated for impairment	$ 42	$ 39	$ 81
Individually evaluated for impairment	$ 69	$ 411	$ 480

When determining the allowances, financing receivables are evaluated either on an individual or a collective basis. For individually evaluated receivables, the company determines the expected cash flow for the receivable and calculates an estimate of the potential loss and the probability of loss. For those accounts in which the loss is probable, the company records a specific reserve. In addition, the company records an unallocated reserve that is determined by applying a reserve rate to its different portfolios, excluding accounts that have been specifically reserved. This reserve rate is based upon credit rating, probability of default, term, characteristics (lease/loan) and loss history.

Notes to Consolidated Financial Statements – (continued)

Financing Receivables on Non-Accrual Status

The following table presents the recorded investment in financing receivables which were on non-accrual status at March 31, 2015 and December 31, 2014.

(Dollars in millions)	At March 31, 2015	At December 31, 2014
Major markets	$ 13	$ 13
Growth markets	78	40
Total lease receivables	$ 91	$ 53
Major markets	$ 24	$ 27
Growth markets	137	151
Total loan receivables	$ 160	$ 178
Total receivables	$ 251	$ 231

Impaired Loans

The company considers any loan with an individually evaluated reserve as an impaired loan. Depending on the level of impairment, loans will also be placed on non-accrual status.

The following tables present impaired client loan receivables.

	At March 31, 2015		At December 31, 2014	
(Dollars in millions)	Recorded Investment	Related Allowance	Recorded Investment	Related Allowance
Major markets	$ 50	$ 47	$ 54	$ 47
Growth markets	331	320	299	293
Total	$ 381	$ 366	$ 353	$ 340

(Dollars in millions) For the three months ended March 31, 2015:	Average Recorded Investment	Interest Income Recognized	Interest Income Recognized on Cash Basis

Major markets	$	52	$	0	$	—
Growth markets		315		0		—
Total	$	367	$	0	$	—

(Dollars in millions) For the three months ended March 31, 2014:		Average Recorded Investment		Interest Income Recognized		Interest Income Recognized on Cash Basis
Major markets	$	77	$	0	$	—
Growth markets		134		0		—
Total	$	211	$	0	$	—

Notes to Consolidated Financial Statements – (continued)

Credit Quality Indicators

The company's credit quality indicators, which are based on rating agency data, publicly available information and information provided by customers, are reviewed periodically based on the relative level of risk. The resulting indicators are a numerical rating system that maps to Moody's Investors Service credit ratings as shown below. The company uses information provided by Moody's, where available, as one of many inputs in its determination of customer credit ratings.

The following tables present the gross recorded investment for each class of receivables, by credit quality indicator, at March 31, 2015 and December 31, 2014. Receivables with a credit quality indicator ranging from Aaa to Baa3 are considered investment grade. All others are considered non-investment grade. The credit quality indicators do not reflect mitigation actions that the company may take to transfer credit risk to third parties.

	Lease Receivables		Loan Receivables	
(Dollars in millions) At March 31, 2015:	**Major Markets**	**Growth Markets**	**Major Markets**	**Growth Markets**
Credit Rating:				
Aaa – Aa3	$ 541	$ 43	$ 916	$ 93
A1 – A3	1,233	151	2,086	