

TENNECO INC
Form 10-K/A
August 14, 2007

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**UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549**

**FORM 10-K/A
(Amendment No. 1)**

(Mark One)

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

For the fiscal year ended December 31, 2006

OR

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

**Commission file number 1-12387
TENNECO INC.**

(Exact name of registrant as specified in its charter)

Delaware

(State or other jurisdiction of
incorporation or organization)

500 North Field Drive

Lake Forest, IL

(Address of principal executive offices)

76-0515284

(I.R.S. Employer
Identification No.)

60045

(Zip Code)

Registrant's telephone number, including area code: (847) 482-5000

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

Title of each class	Name of each Exchange on which registered
7.45% Debentures due 2025; 9.20% Debentures due 2012; 10.20% Debentures due 2008	New York Stock Exchange
Common Stock, par value \$.01 per share	New York, Chicago, and London Stock Exchanges
Preferred Share Purchase Rights	New York, Chicago, and London Stock Exchanges

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 Act. Yes No

Note Checking the box above will not relieve any registrant required to file reports pursuant to Section 13 or 15(d) of the Exchange Act from their obligations under those Sections.

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 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, or a non-accelerated filer. See definition of "accelerated filer and large accelerated filer" in Rule 12b-2 of the Exchange Act. (Check one):
 Large accelerated filer Accelerated filer Non-accelerated filer

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

State the aggregate market value of the voting and non-voting common equity held by non-affiliates computed by reference to the price at which the common equity was last sold, or the average bid and asked price of such common equity, as of the last business day of the registrant's most recently completed second fiscal quarter.

**Class of Common Equity and Number of Shares
 held by Non-affiliates at June 30, 2006**

Market Value held by Non-affiliates*

Common Stock, 43,758,681 shares

\$1,137,725,706

* Based upon the closing sale price on the New York Stock Exchange Composite Tape for the Common Stock on June 30, 2006.

INDICATE THE NUMBER OF SHARES OUTSTANDING OF EACH OF THE REGISTRANT'S CLASSES OF COMMON STOCK, AS OF THE LATEST PRACTICABLE DATE. Common Stock, par value \$.01 per share, 45,768,992 shares outstanding as of February 23, 2007.

Documents Incorporated by Reference:

Document	Part of the Form 10-K into which incorporated
Portions of Tenneco Inc.'s Definitive Proxy Statement for the Annual Meeting of Stockholders to be held May 8, 2007	Part III

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Explanatory Note

Overview

Tenneco Inc. is filing this Amendment No. 1 on Form 10-K/A to its Annual Report on Form 10-K for the year ended December 31, 2006, originally filed on March 1, 2007 (the Original Filing), to amend and restate our consolidated financial statements as of December 31, 2006 and 2005 and for each of the three years in the period ended December 31, 2006. The restatement is discussed in Note 4 to the consolidated financial statements.

Restatement

Subsequent to the Original Filing, an error in accounting for our interest rate swap agreements has been identified. In April 2004, we entered into three separate fixed-to-floating interest rate swaps with two financial institutions. These agreements swapped a total of \$150 million of our fixed 10.25% senior secured notes to floating interest rate debt at LIBOR plus an average spread of 5.68 percentage points. From the inception of the interest rate swaps, we applied the so-called short-cut method of fair value hedge accounting under Statement of Financial Accounting Standards (SFAS) No. 133, Accounting for Derivative Instruments and Hedging Activities. To qualify for the short-cut method of hedge accounting, the terms of an interest rate swap must be an exact match, or mirror image, of the terms of the debt it is hedging. When these conditions are met, a company can assume the changes in the value of the hedges and the underlying debt offset each other. Any unrealized gains and losses in fair value of the swap agreements are recorded as an offset to long-term debt thereby having no effect on earnings.

While we believed we had appropriately matched the terms of the swaps and the underlying debt, differences have subsequently been identified. One difference is between the 30-day notice period to terminate the swaps and the 30 to 60 day notice period to redeem the notes. Another difference relates to the fact that while the debt and swaps can both be redeemed before their maturity dates, the notes allow us to make redemptions in increments of \$1,000 while the interest rate swap agreements imply that they can only be redeemed in their full amounts.

As a result, we have determined that these transactions do not meet the requirements for hedge accounting treatment under SFAS No. 133 and we are correcting our past accounting for the swaps as hedges. Therefore, we are recording the changes in the fair value of the interest rate swaps as increases or decreases to interest expense in each period since we entered into them, instead of recording an offset for changes in the fair value of the underlying debt. The fair value of these swaps has been disclosed in the footnotes to our financial statements each quarter since the swaps inception.

The error did not change the underlying economics of the transaction and had no effect on our cash flow or liquidity.

In addition, we are correcting other errors as part of this restatement. We originally concluded these items, both individually and in the aggregate, were not material to our consolidated financial statements. Finally, as previously disclosed, we have conducted a detailed reconciliation of our deferred income tax balances. The restatement reflects the results of that reconciliation.

The following sections of this Form 10-K/A have been amended to reflect the restatement: Part I Item 1 Business, Item 1A Risk Factors, Part II Item 6 Selected Financial Data, Item 7 Management's Discussion and Analysis of Financial Condition and Results of Operations, Item 8 Financial Statements and Supplementary Data, and Item 9A Controls and Procedures; and Part IV Item 15 Exhibits and Financial Statement Schedules. For the convenience of the reader, this Amendment No. 1 includes, in their entirety, those items in the Original Filing not being amended and restated. Except to the extent relating to the restatement of our financial statements and other financial information described above, this Form 10-K/A continues to describe conditions as of the Original Filing, and does not update

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disclosures contained herein to reflect events that occurred at a later date. Accordingly, this Form 10-K/A should be read in conjunction with our filings made with the Securities and Exchange Commission subsequent to the filing of the Original Filing.

New certifications of the principal executive officer and principal financial officer are included as exhibits to this Amendment No. 1 on Form 10-K/A.

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CAUTIONARY STATEMENT FOR PURPOSES OF THE SAFE HARBOR PROVISIONS OF THE PRIVATE SECURITIES LITIGATION REFORM ACT OF 1995

This Annual Report contains forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995 concerning, among other things, the prospects and developments of the Company (as defined) and business strategies for our operations, all of which are subject to risks and uncertainties. These forward-looking statements are included in various sections of this report, including the section entitled Outlook appearing in Item 7 of this report. These statements are identified as forward-looking statements or by their use of terms (and variations thereof) such as will, may, can, anticipate, intend, continue, estimate, expect, plan, should, and similar terms (and variations thereof) and phrases.

When a forward-looking statement includes a statement of the assumptions or bases underlying the forward-looking statement, we caution that, while we believe such assumptions or bases to be reasonable and make them in good faith, assumed facts or bases almost always vary from actual results, and the differences between assumed facts or bases and actual results can be material, depending upon the circumstances. Where, in any forward-looking statement, we or our management expresses an expectation or belief as to future results, we express that expectation or belief in good faith and believe it has a reasonable basis, but we can give no assurance that the statement of expectation or belief will result or be achieved or accomplished.

Our actual results may differ significantly from the results discussed in the forward-looking statements. Factors that might cause such a difference include the matters described in the section entitled Risk Factors appearing in Item 1A of this report and the following:

general economic, business and market conditions;

potential legislation, regulatory changes and other governmental actions, including the ability to receive regulatory approvals and the timing of such approvals;

new technologies that reduce the demand for certain of our products or otherwise render them obsolete;

changes in distribution channels or competitive conditions in the markets and countries where we operate;

capital availability or costs, including changes in interest rates, market perceptions of the industries in which we operate or ratings of securities;

increases in the cost of compliance with regulations, including environmental regulations, and environmental liabilities in excess of the amount reserved;

changes by the Financial Accounting Standards Board or the Securities and Exchange Commission of authoritative accounting principles generally accepted in the United States of America;

acts of war or terrorism, including, but not limited to, the events taking place in the Middle East, the current military action in Iraq and the continuing war on terrorism, as well as actions taken or to be taken by the United States and other governments as a result of further acts or threats of terrorism, and the impact of these acts on economic, financial and social conditions in the countries where we operate; and

the timing and occurrence (or non-occurrence) of transactions and events which may be subject to circumstances beyond our control.

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PART I

ITEM 1. BUSINESS.

TENNECO INC.

General

Our company, Tenneco Inc., is one of the world's leading manufacturers of automotive emission control and ride control products and systems. Our company serves both original equipment vehicle manufacturers (OEMs) and the repair and replacement markets, or aftermarket, worldwide. As used herein, the term "Tenneco," "we," "us," "our," or the "Company" refers to Tenneco Inc. and its consolidated subsidiaries.

Tenneco was incorporated in Delaware in 1996 under the name New Tenneco Inc. ("New Tenneco") as a wholly owned subsidiary of the company then known as Tenneco Inc. ("Old Tenneco"). At that time, Old Tenneco's major businesses were shipbuilding, energy, automotive and packaging. On December 11, 1996, Old Tenneco completed the transfer of its automotive and packaging businesses to us, and spun off our company to its public stockholders. In connection with the 1996 spin-off, Old Tenneco also spun off its shipbuilding division to its public stockholders, the remaining energy company was acquired by El Paso Natural Gas Company and we changed our name from New Tenneco to Tenneco Inc. Unless the context otherwise requires, for periods prior to December 11, 1996, references to "Tenneco," "we," "us," "our" or the "Company" also refer to Old Tenneco. In a series of transactions commencing in January 1999 and culminating with the November 4, 1999 spin off to our shareholders of the common stock of Tenneco Packaging Inc., now known as Pactiv Corporation (the "1999 Spin-off"), we separated our packaging businesses from our automotive business and in connection therewith changed our name from Tenneco Inc. to Tenneco Automotive Inc.

In 2005, we changed our name from Tenneco Automotive Inc. back to Tenneco Inc. The name Tenneco better represents the expanding number of markets we serve through our commercial and specialty vehicle businesses. Building a stronger presence in these markets complements our core businesses of supplying ride control and emission control products and systems for light vehicles to automotive original equipment and aftermarket customers worldwide. Our common stock continues to trade on the New York Stock Exchange under the symbol "TEN".

Corporate Governance and Available Information

We have established a comprehensive corporate governance plan for the purpose of defining responsibilities, setting high standards of professional and personal conduct and assuring compliance with such responsibilities and standards. As part of its annual review process, the Board of Directors monitors developments in the area of corporate governance. Listed below are some of the key elements of our corporate governance plan.

For more information about these matters, see our definitive Proxy Statement for the Annual Meeting of Stockholders to be held May 8, 2007.

Independence of Directors

Nine of our eleven directors are independent under the New York Stock Exchange ("NYSE") listing standards.

Independent directors are scheduled to meet separately in executive session after every regularly scheduled Board of Directors meeting.

We have a lead independent director, Mr. Paul T. Stecko.

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Audit Committee

All members meet the independence standards for audit committee membership under the NYSE listing standards and applicable Securities and Exchange Commission (SEC) rules.

One member of the Audit Committee, Mr. Charles Cramb, qualifies as an audit committee financial expert, as defined in the SEC rules, and the remaining members of the Audit Committee satisfy the NYSE's financial literacy requirements.

The Audit Committee operates under a written charter which governs its duties and responsibilities, including its sole authority to appoint, review, evaluate and replace our independent auditors.

The Audit Committee has adopted policies and procedures governing the pre-approval of all audit, audit-related, tax and other services provided by our independent auditors.

Compensation/Nominating/Governance Committee

All members meet the independence standards for compensation and nominating committee membership under the NYSE listing standards.

The Compensation/Nominating/Governance Committee operates under a written charter that governs its duties and responsibilities, including the responsibility for executive compensation.

In December 2005, an Executive Compensation Subcommittee was formed which has the responsibility to consider and approve equity based compensation for our executive officers which is intended to qualify as performance based compensation under Section 162(m) of the Internal Revenue Code of 1986, as amended.

Corporate Governance Principles

We have adopted Corporate Governance Principles, including qualification and independence standards for directors.

Stock Ownership Guidelines

We have adopted Stock Ownership Guidelines to align the interests of our executives with the interests of stockholders and promote our commitment to sound corporate governance.

The Stock Ownership Guidelines apply to the independent directors, the Chairman and Chief Executive Officer, all Executive Vice Presidents and all Senior Vice Presidents. Ownership levels are determined as a multiple of the participant's base salary or, in the case of an independent director, his or her Board of Director's retainer fee and then converted to a fixed number of shares.

Communication with Directors

The Audit Committee has established a process for confidential and anonymous submission by our employees, as well as submissions by other interested parties, regarding questionable accounting or auditing matters.

Additionally, the Board of Directors has established a process for stockholders to communicate with the Board of Directors, as a whole, or any independent director.

Codes of Business Conduct and Ethics

We have adopted a Code of Ethical Conduct for Financial Managers, which applies to our Chief Executive Officer, Chief Financial Officer, Controller and other key financial managers. This code is filed as Exhibit 14 to this report.

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We also operate under an omnibus Statement of Business Principles that applies to all directors, officers and employees and includes provisions ranging from restrictions on gifts to conflicts of interests. All salaried employees are required to affirm in writing their acceptance of these principles.

Related Party Transactions Policy

We have adopted a Policy and Procedure for Transactions With Related Persons, under which our Audit Committee must generally pre-approve transactions involving more than \$120,000 with our directors, executive officers, five percent or greater stockholders and their immediate family members.

Equity Award Policy

We have adopted a written policy to be followed for all issuances by our company of compensatory awards in the form of our common stock or any derivative of the common stock.

Personal Loans to Executive Officers and Directors

We comply with and will operate in a manner consistent with the legislation outlawing extensions of credit in the form of a personal loan to or for our directors or executive officers.

Our Internet address is *www.tenneco.com*. We make our annual report on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K and amendments to those reports, as filed with or furnished to the SEC, available free of charge on our Internet website as soon as reasonably practicable after submission to the SEC. Securities ownership reports on Forms 3, 4 and 5 are also available free of charge on our website as soon as reasonably practicable after submission to the SEC. The contents of our website are not, however, a part of this report.

Our Audit Committee, Compensation/Nominating/Governance Committee and Executive Compensation Subcommittee Charters, Corporate Governance Principles, Stock Ownership Guidelines, Audit Committee policy regarding accounting complaints, Code of Ethical Conduct for Financial Managers, Statement of Business Principles, Policy and Procedures for Transactions with Related Persons, Equity Award Policy, policy for communicating with the Board of Directors and Audit Committee policy regarding the pre-approval of audit, non-audit, tax and other services are available free of charge on our website at *www.tenneco.com*. In addition, we will make a copy of any of these documents available to any person, without charge, upon written request to Tenneco Inc., 500 North Field Drive, Lake Forest, Illinois 60045, Attn: General Counsel. We intend to satisfy the disclosure requirements under Item 5.05 of Form 8-K and applicable NYSE rules regarding amendments to or waivers of our Code of Ethical Conduct for Financial Managers and Statement of Business Principles by posting this information on our website at *www.tenneco.com*.

CEO and CFO Certifications

In 2006 our chief executive officer provided to the NYSE, the Pacific Stock Exchange and the Chicago Stock Exchange the annual CEO certification regarding our compliance with the corporate governance listing standards of those exchanges. In addition, our chief executive officer (and during the applicable periods, our interim management committee known as the Office of the Chief Executive) and chief financial officer filed with the Securities and Exchange Commission all required certifications regarding the quality of our disclosures in our fiscal 2006 SEC reports, including the certifications required to be filed with this Annual Report on Form 10-K/A. There were no qualifications to these certifications.

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For information concerning our operating segments, geographic areas and major products or groups of products, see Note 12 to the consolidated financial statements of Tenneco Inc. and Consolidated Subsidiaries included in Item 8. The following tables summarize for each of our operating segments for the periods indicated: (i) net sales and operating revenues; (ii) earnings before interest expense, income taxes and minority interest (EBIT); and (iii) expenditures for plant, property and equipment. You should also read Management's Discussion and Analysis of Financial Condition and Results of Operations included in Item 7 for information about certain costs and charges included in our results. You should also read Note 4 to the consolidated financial statements included in Item 8 for a discussion of the changes in our results due to the restatement described in the Explanatory Note above and Note 5 for a discussion of the change effective January 1, 2005, in our method for valuing inventory.

Net Sales and Operating Revenues:

	2006		As Restated 2005		2004	
	(Dollar Amounts in Millions)					
North America	\$ 1,963	42%	\$ 2,033	46%	\$ 1,966	47%
Europe, South America and India	2,387	51	2,110	48	1,940	46
Asia Pacific	436	9	371	8	380	9
Intergroup sales	(104)	(2)	(74)	(2)	(73)	(2)
Total	\$ 4,682	100%	\$ 4,440	100%	\$ 4,213	100%

EBIT:

	2006		As Restated 2005		2004	
	(Dollar Amounts in Millions)					
North America	\$ 103	53%	\$ 148	69%	\$ 131	77%
Europe, South America and India	81	41	53	24	19	11
Asia Pacific	12	6	16	7	20	12
Total	\$ 196	100%	\$ 217	100%	\$ 170	100%

Expenditures for plant, property and equipment:

	2006	2005	2004
	(Dollar Amounts in Millions)		

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North America	\$ 100	59%	\$ 74	51%	\$ 55	43%
Europe, South America and India	51	30	54	38	59	45
Asia Pacific	19	11	16	11	16	12
Total	\$ 170	100%	\$ 144	100%	\$ 130	100%

Interest expense, income taxes, and minority interest that were not allocated to our operating segments are:

	2006	As Restated 2005 (Millions)	2004
Interest expense (net of interest capitalized)	\$ 136	\$ 133	\$ 178
Income tax expense (benefit)	5	26	(21)
Minority interest	6	2	4

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DESCRIPTION OF OUR BUSINESS

We design, engineer, manufacture, market and sell automotive emission control and ride control systems and products, with 2006 revenues of \$4.7 billion. We serve both original equipment manufacturers and replacement markets worldwide through leading brands, including Monroe[®], Rancho[®], Clevite[®] Elastomers, and Fric Rot[™] ride control products and Walker[®], Fonos[™], and Gillet[™] emission control products.

As an automotive parts supplier, we produce individual component parts for vehicles as well as groups of components that are combined as modules or systems within vehicles. These parts, modules and systems are sold globally to most leading OEMs and throughout all aftermarket distribution channels.

Overview of Automotive Parts Industry

The automotive parts industry is generally separated into two categories: (1) original equipment or OE sales, in which parts are sold in large quantities directly for use by OEMs; and (2) aftermarket sales, in which parts are sold as replacement parts in varying quantities to a wide range of wholesalers, retailers and installers. In the OE market, parts suppliers are generally divided into tiers Tier 1 suppliers, who provide their products directly to OEMs, and Tier 2 or Tier 3 suppliers, who sell their products principally to other suppliers for combination into the other suppliers own product offerings.

Demand for automotive parts in the OE market is generally a function of the number of new vehicles produced, which in turn is a function of prevailing economic conditions and consumer preferences. In 2006, the number of light vehicles (i.e. passenger cars and light trucks) produced was 15.3 million in North America, 27.6 million in Europe, South America and India and 23.4 million in Asia Pacific. Worldwide new light vehicle production is forecasted to increase to over 68.9 million units in 2007 from approximately 66.3 million units in 2006. Although OE demand is tied to planned vehicle production, parts suppliers also have the opportunity to grow through increasing their product content per vehicle, by further penetrating business with existing customers and by gaining new customers and markets. Companies with global presence and advanced technology, engineering, manufacturing and support capabilities, such as our company, are, we believe, well positioned to take advantage of these opportunities.

Demand for aftermarket products is driven by the quality of OE parts, the number of vehicles in operation, the average age of the vehicle fleet, vehicle usage and the average useful life of vehicle parts. Although more vehicles are on the road than ever before, the aftermarket has experienced longer replacement cycles due to improved quality of OE parts and increases in average useful lives of automotive parts as a result of technological innovation. Suppliers are increasingly being required to deliver innovative aftermarket products that upgrade the performance or safety of a vehicle s original components to drive aftermarket demand.

Industry Trends

Currently, we believe several significant existing and emerging trends are dramatically impacting the automotive industry. As the dynamics of the automotive industry change, so do the roles, responsibilities and relationships of its participants. Key trends that we believe are affecting automotive parts suppliers include:

Increasing Environmental Standards

Automotive parts suppliers and OE manufacturers are designing products and developing materials to respond to increasingly stringent environmental requirements, a growing diesel market, the demand for better fuel economy.

Government regulations adopted over the past decade require substantial reductions in automobile tailpipe emission, longer warranties on parts of an automobile's pollution control equipment and additional equipment to control fuel vapor emission. Some of these regulations also mandate more frequent emission inspections for the existing fleet of vehicles. Manufacturers have responded by focusing their efforts towards technological development to minimize pollution. As a leading supplier of emission control systems with strong technical capabilities, we believe we are well positioned to benefit from more rigorous environmental standards. For example, we developed the diesel particulate filter to meet stricter air quality

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regulations in Europe. We also have development contracts with North American light and medium-duty truck manufacturers for our particulate filter and De-NO_x converter which can reduce particulate emissions by up to 90 percent and nitrogen oxide emissions by up to 60 percent.

Increasing Technologically Sophisticated Content

As consumers continue to demand competitively priced vehicles with increased performance and functionality, the number of sophisticated components utilized in vehicles is increasing. By replacing mechanical functions with electronics and by integrating mechanical and electronic functions within a vehicle, OE manufacturers are achieving improved emission control, improved safety and more sophisticated features at lower costs.

Automotive parts customers are increasingly demanding technological innovation from suppliers to address more stringent emission and other regulatory standards and to improve vehicle performance. To develop innovative products, systems and modules, we have invested \$88 million for 2006, \$83 million for 2005 and \$76 million for 2004, net of customer reimbursements, into engineering, research and development and we continuously seek to take advantage of our technology investments and brand strength by extending our products into new markets and categories. For example, we were the first supplier to develop and commercialize a diesel particulate filter that can virtually eliminate carbon and hydrocarbon emissions with minimal impact on engine performance.

We have expanded our competence in diesel particulate filters in Europe and are winning business in North America on these same applications. In addition, we supply Volvo and Audi with a computerized electronic suspension system that we co-developed with Öhlins Racing AB. As another example, in 2002 we extended our stability improvement valve technology to Europe which is similar to our acceleration sensitive damping technology used on our Monroe Reflex[®] premium aftermarket shock originally launched in North America in 1999.

Our customers reimburse us for engineering, research, and development costs on some platforms when we prepare prototypes and incur costs before platform awards. Our engineering, research and development expense for 2006, 2005, and 2004 has been reduced by \$61 million, \$51 million, and \$46 million, respectively, for these reimbursements.

Safety

Vehicle safety continues to gain increased industry attention and play a critical role in consumer purchasing decisions. As such, OEMs are seeking out suppliers with new technologies, capabilities and products that have the ability to advance vehicle safety. Continued research and development by select automotive suppliers in rollover protection systems, smart airbag systems, braking electronics and safer, more durable materials has dramatically advanced the market for safety products and its evolving functional demands. Those suppliers are able to enhance vehicle safety through innovative products and technologies and have a distinct competitive advantage with the consumer, and thus their OEM customers.

Outsourcing and Demand for Systems and Modules

OE manufacturers are increasingly moving towards outsourcing automotive parts and systems to simplify the vehicle assembly process, lower costs and reduce vehicle development time. Outsourcing allows OE manufacturers to take advantage of the lower cost structure of the automotive parts suppliers and to benefit from multiple suppliers engaging in simultaneous development efforts. Furthermore, development of advanced electronics has enabled formerly independent vehicle components to become interactive, leading to a shift in demand from individual parts to fully integrated systems. As a result, automotive parts suppliers offer OE

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manufacturers component products individually, as well as in a variety of integrated forms such as modules and systems:

Modules are groups of component parts arranged in close physical proximity to each other within a vehicle. Modules are often assembled by the supplier and shipped to the OEM for installation in a vehicle as a unit. Seats, instrument panels, axles and door panels are examples.

Systems are groups of component parts located throughout a vehicle which operate together to provide a specific vehicle function. Anti-lock braking systems, safety restraint systems, roll control systems, emission control systems and powertrain systems are examples.

This shift in demand towards fully integrated systems has created the role of the Tier 1 systems integrator. These systems integrators increasingly have the responsibility to execute a number of activities, such as design, product development, engineering, testing of component systems and purchasing from Tier 2 suppliers. We are an established Tier 1 supplier with more than ten years of product integration experience. We have modules or systems for various vehicle platforms in production worldwide and modules or systems for additional platforms under development. For example, we supply ride control modules for the DaimlerChrysler Caravan, the Nissan Pathfinder, the VW Transporter and the Peugeot 1007 and the emission control system for the Porsche Boxster, Nissan Xterra, Ford Focus/Mazda 3, DaimlerChrysler DR Ram, Jaguar XJ Type, GM Lamda, and Ford Super-Duty truck.

Global Consolidation of OE Customers

Given the trend in business combinations among vehicle manufacturers such as the DaimlerChrysler merger and General Motors acquisition of Daewoo as well as the global OE expansion over the last decade, OEMs are increasingly requesting suppliers to provide parts on a global basis. As the customer base of OEMs has consolidated and emerging markets have become more important to achieving growth, suppliers must be prepared to provide products any place in the world.

Growing Importance of Emerging Markets: Because the North American and Western European automotive markets are relatively mature, OE manufacturers are increasingly focusing on emerging markets for growth opportunities, particularly China, Eastern Europe, India and Latin America. This increased OE focus has, in turn, increased the growth opportunities in the aftermarkets in these regions.

Governmental Tariffs and Local Parts Requirements: Many governments around the world require that vehicles sold within their country contain specified percentages of locally produced parts. Additionally, some governments place high tariffs on imported parts.

Location of Production Closer to End Markets: OE manufacturers and parts suppliers have relocated production globally on an onsite basis that is closer to end markets. This international expansion allows suppliers to pursue sales in developing markets and take advantage of relatively lower labor costs.

With facilities around the world, including the key regions of North America, South America, Europe and Asia, we can supply our customers on a global basis.

Global Rationalization of OE Vehicle Platforms

OE manufacturers are increasingly designing global platforms. A global platform is a basic mechanical structure of a vehicle that can accommodate different features and is in production and/or development in more than one region. Thus, OE manufacturers can design one platform for a number of similar vehicle models. This allows manufacturers

to realize significant economies of scale through limiting variations across items such as steering columns, brake systems, transmissions, axles, exhaust systems, support structures and power window and door lock mechanisms. We believe that this shift towards standardization will have a large impact on automotive parts suppliers, who should experience a reduction in production costs as OE manufacturers reduce variations in components. We also expect parts suppliers to experience higher production volumes per unit and greater economies of scale, as well as reduced total investment costs for molds, dies and

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prototype development. Light vehicle platforms of over one million units are expected to grow from 30 percent to 43 percent of global OE production from 2006 to 2011.

Extended Product Life of Automotive Parts

The average useful life of automotive parts both OE and replacement has been steadily increasing in recent years due to innovations in products and technologies. The longer product lives allow vehicle owners to replace parts of their vehicles less often. As a result, although more vehicles are on the road than ever before, the global aftermarket has not grown as fast as the number of vehicles on the road. Accordingly, a supplier's future viability in the aftermarket will depend, in part, on its ability to reduce costs and leverage its advanced technology and recognized brand names to maintain or achieve additional sales. As a Tier 1 OE supplier, we believe we are well positioned to leverage our products and technology into the aftermarket.

Changing Aftermarket Distribution Channels

From 1996 to 2006, the number of retail automotive parts stores increased 50 percent while the number of jobber stores declined more than 17 percent in North America. Major automotive aftermarket retailers, such as AutoZone and Advance Auto Parts, are attempting to increase their commercial sales by selling directly to automotive parts installers in addition to individual consumers. These installers have historically purchased from their local warehouse distributors and jobbers, who are our more traditional customers. This enables the retailers to offer the option of a premium brand, which is often preferred by their commercial customers, or a standard product, which is often preferred by their retail customers. We believe we are well positioned to respond to this trend in the aftermarket because of our focus on cost reduction and high-quality, premium brands.

Contracting Supplier Base

Over the past few years, automotive suppliers have been consolidating in an effort to become more global, have a broader, more integrated product offering and gain economies of scale in order to remain competitive amidst growing pricing pressures and increased outsourcing demands from the OEMs. Industry forecasters estimate that the number of U.S. based automotive parts suppliers will decrease from 3,000 in 2004 to 1,320 by 2008. In addition, the forecasters estimate that 65 percent of the companies disappearing will be liquidated, not acquired. A supplier's viability in this market will depend, in part, on its ability to maintain and increase operating efficiencies and provide value-added services.

Table of Contents**Analysis of Revenues**

The table below provides, for each of the years 2006 through 2004, information relating to our net sales and operating revenues, by primary product lines and customer categories. You should read Note 4 to the consolidated financial statements included in Item 8 for a discussion of the changes in our results due to the restatement described in the Explanatory Note above.

	As Restated Net Sales and Operating Revenues Years Ended December 31, 2006 2005 2004 (Millions)		
Emission Control Systems & Products			
Aftermarket	\$ 384	\$ 368	\$ 365
OE market	2,592	2,390	2,287
	2,976	2,758	2,652
Ride Control Systems & Products			
Aftermarket	690	653	630
OE market	1,016	1,029	931
	1,706	1,682	1,561
Total	\$ 4,682	\$ 4,440	\$ 4,213

Brands

In each of our operating segments, we manufacture and market leading brand names. Monroe[®] ride control products and Walker[®] exhaust products are two of the most recognized brand names in the automotive parts industry. We emphasize product value differentiation with these and other key brands such as Monroe Sensa-Trac[®] and Reflex[®] (shock absorbers and struts), Quiet-Flow[®] (mufflers), DynoMax[®] (performance exhaust products), Rancho[®] (ride control products for the high performance light truck market) and Clevite[®] Elastomers (elastomeric vibration control components), and Lukey (performance exhaust and filters). In Europe, our Gillet[™] brand is recognized as a leader in developing highly engineered exhaust systems for OE customers.

Customers

We have developed long-standing business relationships with our customers around the world. In each of our operating segments, we work together with our customers in all stages of production, including design, development, component sourcing, quality assurance, manufacturing and delivery. With a balanced mix of OE and aftermarket products and facilities in major markets worldwide, we believe we are well-positioned to meet customer needs. We believe we have a strong, established reputation with customers for providing high-quality products at competitive prices, as well as for timely delivery and customer service.

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Worldwide we serve more than 35 different OE manufacturers, and our products or systems are included on 9 of the top 10 passenger car models produced for sale in Europe and 9 of the top 10 SUV and light truck models produced for sale in North America for 2006. During 2006, our OE customers included:

North America

AM General
 CAMI Automotive
 Caterpillar
 Club Car
 Daimler Chrysler/Freightliner
 E-Z Go Golf Car
 Ford
 General Motors
 Harley-Davidson
 Honda
 Mazda (Auto Alliance)
 Motor Coach Industries
 Navistar
 Nissan
 Paccar
 Toyota
 Volkswagen
 Volvo Truck

South America

Daimler Chrysler
 Fiat
 Ford
 General Motors
 PSA Peugeot Citroen
 Renault
 Scania
 Toyota
 Volkswagen

Europe

BMW
 Daimler Chrysler
 Fiat
 Ford
 General Motors
 Nissan
 Paccar
 Porsche
 PSA Peugeot Citroen
 Renault
 Scania
 Suzuki
 Toyota
 Volkswagen
 Volvo Truck

Australia

Club Car
 Ford
 General Motors
 Mazda
 Mitsubishi
 Nissan
 Toyota

Asia

BMW
 Chang an Automobile
 Daimler Chrysler
 Dongfeng Motor Co.
 First Auto Works
 Ford
 General Motors
 Jinbei Automobile Co.
 Isuzu
 Mitsubishi
 PSA Peugeot Citroen
 Renault
 Shanghai Automotive (SAIC)
 Volkswagen

India

General Motors
 Mahindra & Mahindra
 Suzuki
 TATA Motors
 Toyota
 TVS Motors

During 2006, our aftermarket customers were comprised of full-line and specialty warehouse distributors, retailers, jobbers, installer chains and car dealers. These customers included such wholesalers and retailers as

National Auto Parts Association (NAPA), Advance Auto Parts, Uni-Select and O'Reilly Automotive in North America and Temot, Group Auto Union, Kwik-Fit Europe and Auto Distribution International in Europe. We believe we have a balanced mix of aftermarket customers, with our top 10 aftermarket customers accounting for 37 percent of our total net aftermarket sales and only 23 percent of our total net sales for 2006.

General Motors accounted for approximately 14 percent, 17 percent, and 18 percent of our net sales in 2006, 2005 and 2004, respectively; Ford accounted for approximately 11 percent, 12 percent and 12 percent of our net sales in 2006, 2005 and 2004, respectively; Volkswagen accounted for approximately 11 percent, 9 percent and 11 percent of our net sales in 2006, 2005 and 2004, respectively; and Daimler Chrysler accounted for approximately 11 percent, 9 percent

and 8 percent of our net sales in 2006, 2005 and 2004, respectively. No other customer accounted for more than 9 percent of our net sales for any of those years.

Competition

We operate in highly competitive markets. Customer loyalty is a key element of competition in these markets and is developed through long-standing relationships, customer service, high quality value-added products and timely delivery. Product pricing and services provided are other important competitive factors.

In both the OE market and aftermarket, we compete with the vehicle manufacturers, some of which are also customers of ours, and numerous independent suppliers. In the OE market, we believe that we are among

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the top two suppliers in the world for both emission control and ride control products and systems for light vehicles. In the aftermarket, we believe that we are the market share leader in the supply of both emission control and ride control products for light vehicles in the markets we serve throughout the world.

Seasonality

Our business is somewhat seasonal. OE manufacturers' production requirements have historically been higher in the first two quarters of the year as compared to the last two quarters. Production requirements tend to decrease in the third quarter due to plant shutdowns for model changeovers. In addition, we believe this seasonality is due, in part, to consumer demand for new vehicles softening during the holiday season and as a result of the winter months in North America and Europe. Also, the major North American OE manufacturers generally close their production facilities for the last two weeks of the year. Our aftermarket business also experiences seasonality. Demand for aftermarket products increases during the spring as drivers prepare for the summer driving season. Although seasonality does impact our business, actual results may vary from the above trends due to timing of platform launches and other production related events.

Emission Control Systems

Vehicle emission control products and systems play a critical role in safely conveying noxious exhaust gases away from the passenger compartment and reducing the level of pollutants and engine exhaust noise to an acceptable level. Precise engineering of the exhaust system – from the manifold that connects an engine's exhaust ports to an exhaust pipe, to the catalytic converter that eliminates pollutants from the exhaust, to the muffler – leads to a pleasant, tuned engine sound, reduced pollutants and optimized engine performance.

We design, manufacture and distribute a variety of products and systems designed to optimize engine performance, acoustic tuning and weight, including the following:

Mufflers and resonators – Devices to provide noise elimination and acoustic tuning;

Catalytic converters – Devices – consisting of a substrate coated with precious metals enclosed in a steel casing used to convert harmful gaseous emission, such as carbon monoxide, from a vehicle's exhaust system into harmless components such as water vapor and carbon dioxide;

Exhaust manifolds – Components that collect gases from individual cylinders of a vehicle's engine and direct them into a single exhaust pipe;

Pipes – Utilized to connect various parts of both the hot and cold ends of an exhaust system;

Hydroformed tubing – Forms into various geometric shapes, such as Y-pipes or T-pipes, which provides optimization in both design and installation as compared to conventional pipes;

Hangers and isolators – Used for system installation and noise and vibration elimination;

Diesel Particulate Filters – Devices to eliminate particulate matter emitted from diesel engines; and

Selective Catalytic Reduction (SCR) systems – Devices which reduce Nitrogen Oxide (NOx) emissions from diesel powertrains.

We entered this product line in 1967 with the acquisition of Walker Manufacturing Company, which was founded in 1888. With the acquisition of Heinrich Gillet GmbH & Co. in 1994, we also became one of Europe's leading OE emission control systems suppliers. When the term "Walker" is used in this document, it refers to our subsidiaries and affiliates that produce emission control products and systems.

We supply our emission control offerings to over 32 vehicle-makers for use on over 140 vehicle models, including 7 of the top 10 passenger cars produced for sale in Europe and 6 of the top 10 SUVs and light trucks produced for sale in North America in 2006.

With respect to catalytic converters, we buy the substrate coated with precious metals, or sometimes the completed catalytic converter, from third parties, use them in our manufacturing process and sell them as part of the completed system. This often occurs at the direction of the OE customers. See Item 7, "Management's

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Discussion and Analysis of Financial Condition and Results of Operations for more information on our sales of these products.

In the aftermarket, we manufacture, market and distribute replacement mufflers for virtually all North American, European, and Asian makes of light vehicles under brand names including Quiet-Flow®, TruFit® and Aluminox Pro™, in addition to offering a variety of other related products such as pipes and catalytic converters (Walker Perfection®). We also serve the specialty exhaust aftermarket, where our key offerings include Mega-Flow™ exhaust products for heavy-duty vehicle applications and DynoMax® high performance exhaust products. We continue to emphasize product value differentiation with other aftermarket brands such as Thrush® and Fonos™.

The following table provides, for each of the years 2006 through 2004, information relating to our sales of emission control products and systems for certain geographic areas:

	Percentage of Net Sales		
	Years Ended December 31,		
	2006	2005	2004
United States			
Aftermarket	19%	18%	18%
OE market	81	82	82
	100%	100%	100%
Foreign Sales			
Aftermarket	10%	11%	11%
OE market	90	89	89
	100%	100%	100%
Total Sales by Geographic Area(a)			
United States	29%	33%	33%
European Union	49	46	45
Canada	5	7	8
Other areas	17	14	14
	100%	100%	100%

- (a) See Note 12 to the consolidated financial statements included under Item 8 for information about our foreign and domestic operations. See Item 1A, Risk Factors We are subject to risks related to our international operations and Exchange rate fluctuations could cause a decline in our financial conditions and results of operations for information about the risks associated with foreign operations.

Ride Control Systems

Superior ride control is governed by a vehicle's suspension system, including its shock absorbers and struts. Shock absorbers and struts help maintain vertical loads placed on a vehicle's tires to help keep the tires in contact with the

road. A vehicle's ability to steer, brake and accelerate depends on the contact between the vehicle's tires and the road. Worn shocks and struts can allow excess weight transfer from side to side, which is called roll, from front to rear, which is called pitch, and up and down, which is called bounce. Variations in tire-to-road contact can affect a vehicle's handling and braking performance and the safe operation of a vehicle. Shock absorbers are designed to control vertical loads placed on tires by providing resistance to vehicle roll, pitch and bounce. Thus, by maintaining the tire to road contact, ride control products are designed to function as safety components of a vehicle, in addition to providing a comfortable ride.

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We design, manufacture and distribute a variety of ride control products and systems. Our ride control offerings include:

Shock absorbers A broad range of mechanical shock absorbers and related components for light- and heavy-duty vehicles. We supply both twin-tube and monotube shock absorbers to vehicle manufacturers and the aftermarket;

Struts A complete line of struts and strut assemblies for light vehicles;

Vibration control components (Clevite® Elastomers) Generally rubber-to-metal bushings and mountings to reduce vibration between metal parts of a vehicle. Our offerings include a broad range of suspension arms, rods and links for light- and heavy-duty vehicles;

Kinetic® Suspension Technology A suite of roll control, near equal wheel loading systems ranging from simple mechanical systems to complex hydraulic systems featuring proprietary and patented technology. The Kinetic® Suspension Technology was incorporated on the Citroen World Rally Car that was featured in the World Rally Championship 2003, 2004 and 2005. Additionally, the Kinetic® Suspension Technology was incorporated on the Lexus GX 470 sport utility vehicle which resulted in winning the PACE Award;

Advanced suspension systems Electronically adjustable shock absorbers and suspension systems that change performance based on vehicle inputs such as steering and braking; and

Other We also offer other ride control products such as load assist products, springs, steering stabilizers, adjustable suspension systems, suspension kits and modular assemblies.

We supply our ride control offerings to over 35 vehicle-makers for use on over 160 vehicle models, including 8 of the top 10 SUV and light truck models produced for sale in North America for 2006. We also supply OE ride control products and systems to a range of heavy-duty and specialty vehicle manufacturers including Volvo Truck, Scania, International Truck and Engine (Navistar), PACCAR.

In the ride control aftermarket, we manufacture, market and distribute replacement shock absorbers for virtually all North American, European and Asian makes of light vehicles under several brand names including Gas Matic®, Sensa-Trac®, Monroe Reflex® and Monroe Adventure®, as well as Clevite® Elastomers for elastomeric vibration control components. We also sell ride control offerings for the heavy duty, off-road and specialty aftermarket, such as our Gas-Magnum® shock absorbers for the North American heavy-duty category.

We entered the ride control product line in 1977 with the acquisition of Monroe Auto Equipment Company, which was founded in 1916 and introduced the world's first modern tubular shock absorber in 1930. When the term Monroe is used in this document it refers to our subsidiaries and affiliates that produce ride control products and systems.

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The following table provides, for each of the years 2006 through 2004, information relating to our sales of ride control equipment for certain geographic areas:

	Percentage of Net Sales		
	Years Ended December 31,		
	2006	2005	2004
United States			
Aftermarket	53%	46%	47%
OE market	47	54	53
	100%	100%	100%
Foreign Sales			
Aftermarket	33%	33%	35%
OE market	67	67	65
	100%	100%	100%
Total Sales by Geographic Area(a)			
United States	38%	42%	43%
European Union	33	32	34
Canada	6	4	4
Other areas	23	22	19
	100%	100%	100%

- (a) See Note 12 to the consolidated financial statements included under Item 8 for information about our foreign and domestic operations. See Item 1A, Risk Factors We are subject to risks related to our international operations and Exchange rate fluctuations could cause a decline in our financial conditions and results of operations for information about the risks associated with foreign operations.

Sales, Marketing and Distribution

We have separate and distinct sales and marketing efforts for our OE and aftermarket businesses.

For OE sales, our sales and marketing team is an integrated group of professionals, including skilled engineers and program managers that are organized by customer and product type (e.g., ride control and emission control). Our sales and marketing team provides the appropriate mix of operational and technical expertise needed to interface successfully with the OEMs. Our new business capture process involves working closely with the OEM platform engineering and purchasing team. Bidding on OE automotive platforms typically encompasses many months of engineering and business development activity. Throughout the process, our sales team, program managers and product engineers assist the OE customer in defining the project's technical and business requirements. A normal part of the process includes our engineering and sales personnel working on customers' integrated product teams, and assisting with the development of component/system specifications and test procedures. Given that the OE business

involves long-term production contracts awarded on a platform-by-platform basis, our strategy is to leverage our engineering expertise and strong customer relationships to obtain platform awards and increase operating margins.

For aftermarket sales and marketing, our sales force is generally organized by customer and region and covers multiple product lines. We sell aftermarket products through five primary channels of distribution: (1) the traditional three-step distribution system: full line warehouse distributors, jobbers and installers; (2) the specialty two-step distribution system: specialty warehouse distributors that carry only specified automotive product groups and installers; (3) direct sales to retailers; (4) direct sales to installer chains; and (5) direct sales to car dealers. Our aftermarket sales and marketing representatives cover all levels of the distribution channel, stimulating interest in our products and helping our products move through the distribution system. Also, to generate demand for our products from end-users, we run print and television advertisements and

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offer pricing promotions. We were one of the first parts manufacturers to offer business-to-business services to customers with TA-Direct, an on-line order entry and customer service tool. In addition, we maintain detailed web sites for each of the Walker[®], Monroe[®], Rancho[®] and DynoMax[®] brands and our heavy duty products.

Manufacturing and Engineering

We focus on achieving superior product quality at the lowest operating costs possible and generally use state-of-the-art manufacturing processes to achieve that goal. Our manufacturing strategy centers on a lean production system designed to reduce overall costs especially indirect costs while maintaining quality standards and reducing manufacturing cycle time. In addition, we have implemented Six Sigma in our processes to minimize product defects and improve operational efficiencies. We deploy new technology where it makes sense to differentiate our processes from our competitors or to achieve balance in one-piece flow through production lines.

Emission Control

Our consolidated businesses operate 14 emission control manufacturing facilities in the U.S. and 39 emission control manufacturing facilities outside of the U.S. We operate ten of these international facilities through joint ventures in which we own a controlling interest. We also operate four additional manufacturing facilities outside of the U.S. through four joint ventures in which we hold a noncontrolling interest. We operate five emission control engineering and technical facilities worldwide and two other such facilities with our ride control operations.

Within each of our emission control manufacturing facilities, operations are organized by component (muffler, catalytic converter, pipe, resonator and manifold). Our manufacturing systems incorporate cell-based designs, allowing work-in-process to move through the operation with greater speed and flexibility. We continue to invest in plant and equipment to stay on top of the industry. For instance, in our Harrisonburg, Virginia, aftermarket manufacturing facility, we have developed a completely automated production process that handles all facets of pipe production from tube milling to pipe bending.

In an effort to further improve our OE customer service and position ourselves as a Tier-1 OE systems supplier, we have been developing some of our emission control manufacturing operations into just-in-time or JIT systems. In this system, a JIT facility located close to our OE customer's manufacturing plant receives product components from both our manufacturing operations and independent suppliers, assembles and then ships products to the OEMs on an as-needed basis. To manage the JIT functions and material flow, we have advanced computerized material requirements planning systems linked with our customers' and supplier partners' resource management systems. We have five emission control JIT assembly facilities in the United States and 20 in the rest of the world, including three that are operated through non-controlled joint ventures.

During the 1990's, we expanded our converter and emission system design, development, test and manufacturing capabilities. Our engineering capabilities now include advanced predictive design tools, advanced prototyping processes and state-of-the-art testing equipment. This expanded technological capability makes us a full system integrator, supplying complete emission control systems from the manifold to the tailpipe, to provide full emission and noise control. It also allows us to provide JIT delivery and, when feasible, sequence delivery of emission control systems to meet customer production requirements. For 2003, we introduced our new Tubular Integrated (catalytic) Converter (TIC) to major vehicle manufacturers in North America. The TIC shortens production time, reduces manufacturing cost by up to 25 percent and reduces weight by up to 20 percent using a new cold-formed, weld-free production process.

Ride Control

Our consolidated businesses operate eight ride control manufacturing facilities in the U.S. and 22 ride control manufacturing facilities outside the U.S. We operate two of these international facilities through joint ventures in which we own a controlling interest. We operate seven engineering and technical facilities worldwide and share two other such facilities with our emission control operations.

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Within each of our ride control manufacturing facilities, operations are organized by product (shocks, struts and vibration control products) and include computer numerically controlled and conventional machine centers; tube milling and drawn-over-mandrel manufacturing equipment; metal inert gas and resistance welding; powdered metal pressing and sintering; chrome plating; stamping; and assembly/test capabilities. Our manufacturing systems incorporate cell-based designs, allowing work-in-process to move through the operation with greater speed and flexibility.

As in the emission control business, in an effort to further improve our OE customer service and position us as a Tier 1 OE module supplier, we have been developing some of our manufacturing operations into JIT systems. We have one JIT ride control assembly facility in the United States and four additional JIT ride control facilities in the rest of the world.

In designing our shock absorbers and struts, we use advanced engineering and test capabilities to provide product reliability, endurance and performance. Our engineering capabilities feature advanced computer aided design equipment and testing facilities. Our dedication to innovative solutions has led to such technological advances as:

Adaptive damping systems adapts to the vehicle's motion to better control undesirable vehicle motions;

Electronically adjustable suspensions changes suspension performance based on a variety of inputs such as steering, braking, vehicle height, and velocity; and

Air leveling systems manually or automatically adjust the height of the vehicle.

Conventional shock absorbers and struts generally compromise either ride comfort or vehicle control. Our innovative grooved-tube, gas-charged shock absorbers and struts provide both ride comfort and vehicle control, resulting in improved handling, reduced vibration and a wider range of vehicle control. This technology can be found in our premium quality Sensa-Trac® shock absorbers. In late 1997, we further enhanced this technology by adding the SafeTech™ fluon banded piston, which improves shock absorber performance and durability. In 1999, we introduced the Monroe Reflex® shock absorber, which incorporates our Impact Sensor™ device. This technology permits the shock absorber to automatically switch in milliseconds between firm and soft compression damping when the vehicle encounters rough road conditions, thus maintaining better tire-to-road contact and improving handling and safety. We supply Volvo with an innovative computerized electronic suspension system, which features dampers developed by Tenneco and electronic valves designed by Öhlins Racing AB.

The continuously controlled electronic suspension (CES) ride control system is featured on Volvo's S60R, V70R, and S80R (4C-2WD) passenger cars. CES is also available as an option on the Volvo S60, V70, S80 and XC70. In 2005, Audi began offering CES as an option on the Audi A6 and the A6 Avant.

Quality Control

Quality control is an important part of our production process. Our quality engineers establish performance and reliability standards in the product's design stage, and use prototypes to confirm the component/system can be manufactured to specifications. Quality control is also integrated into the manufacturing process, with shop operators being responsible for quality control of their specific work product. In addition, our inspectors test work-in-progress at various stages to ensure components are being fabricated to meet customers' requirements.

We believe our commitment to quality control and sound management practices and policies is demonstrated by our successful participation in the International Standards Organization/Quality Management Systems certification

process (ISO/TS). ISO/TS certifications are semi-annual or annual audits that certify that a company's facilities meet stringent quality and business systems requirements. Without ISO or TS certification, we would not be able to supply our products for the aftermarket or the OE market, respectively, either locally or globally. Of those manufacturing facilities where we have determined that TS certification is required to service our customers or would provide us with an advantage in securing additional business,

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88 percent have achieved TS 16949:2002 certification. We plan to complete the certification of the remaining plants by year end 2008. Of those manufacturing facilities where we have determined that ISO 9000 certification is required or would provide us with an advantage in securing additional business, 100 percent have achieved ISO 9000 certification.

Business Strategy

Our objective is to enhance profitability by leveraging our global position in the manufacture of emission control and ride control products and systems. We intend to apply our competitive strengths and balanced mix of products, markets, customers and distribution channels to capitalize on many of the significant existing and emerging trends in the automotive and specialty industries. The key components of our business strategy are described below.

Leverage Global Engineering and Advanced System Capabilities

We continue to focus on the development of highly engineered systems and complex assemblies and modules, which are designed to provide value-added solutions to customers and generally increase vehicle content and carry higher profit margins than individualized components. We have developed integrated, electronically linked global engineering and manufacturing facilities, which we believe help us to maintain our presence on top-selling vehicles. We have more than 10 years of experience in integrating systems and modules. In addition, our JIT and in-line sequencing manufacturing and distribution capabilities have enabled us to better respond to our customers needs. We operate 30 JIT facilities worldwide.

Own the Product Life Cycle

We seek to leverage our aftermarket expertise, which provides us with valuable consumer demand information, to strengthen our competitive position with OEMs. Our market knowledge, coupled with our leading aftermarket presence, strengthens our ties with our OE customer base and drives OE acceptance of our aftermarket products and technologies for use in original equipment vehicle manufacturing.

Commercialize Innovative, Value-Added Products

To differentiate our offerings from those of our competitors, we focus on commercializing innovative, value-added products, both on our own and through strategic alliances, with emphasis on highly engineered systems and complex assemblies and modules. We seek to continually identify and target new, fast-growing niche markets and commercialize our new technologies for these markets, as well as our existing markets. For example, our exclusive Kinetic[®] Dynamic Suspension System, a version of the Kinetic[®] Reversible Function Stabilizer Technology, is featured as an option on the Lexus GX470 sports utility vehicle through a licensing arrangement between us and Lexus.

Expand Our Aftermarket Business

We manufacture and market leading brand name products. Monroe[®] ride control products and Walker[®] emission control products, which have been offered to consumers for approximately 75 years, are two of the most recognized brand name products in the automotive parts industry. We continue to emphasize product value differentiation with these brands and our other primary brands, including:

The Monroe Reflex[®] shock absorber which features an Acceleration Sensitive Damping Technology (ASD) to maintain better tire-to-road contact and improve handling and safety for high center of gravity vehicles (SUVs and light trucks) requiring more control;

The Monroe Sensa-Trac® line of shock absorbers, that has been enhanced by the PSD (Position Sensitive Damping) technology which offers both comfort and control when you need it;

Walker's Quiet-Flow® muffler, which features an open flow design that increases exhaust flow, improves sound quality and significantly reduces exhaust back pressure when compared to other replacement mufflers;

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Rancho® ride control products provides on and off road performance for both stock or raised light truck vehicles;

DynoMax®, which offers a complete line of mufflers, cat-back performance exhaust systems, headers and pipes engineered to increase the efficiency, horsepower, torque and sound of virtually any car, truck, or light vehicle;

Walker Ultra™ catalytic converters, which offer a higher loading of precision metals to help problematic vehicles pass emissions testing;

Monroe® Dynamics and Ceramics brakes offer the Complete Solution, combining wire wear sensors, hardware and lube allowing installers to do the job right the first time; and

In European markets, Walker™ and Aluminox Pro™ mufflers.

We are capitalizing on our brand strength by incorporating newly acquired product lines within existing product families. We believe brand equity is a key asset in a time of customer consolidation and merging channels of distribution.

Our plans to expand our aftermarket business are focused on four key marketing initiatives: new product introductions; building customer and industry awareness of the maintenance, performance and other benefits of ensuring that a vehicle's ride control systems are in good working condition; adding coverage to current brands; and extending our brands and aftermarket penetration to new product segments. For example, in North America we introduced a ride control line extension with the Quick Strut. This strut is a completed module that incorporates the spring and upper mount, resulting in a much easier installation. This allows installers quicker turn over of vehicles in their bay and the opportunity for do it yourself consumers to perform a task that previously required special tools and skills. In addition, Monroe® Dynamics and Ceramic Disc brake pads were introduced in the United States in 2006. We also created the Monroe® 50,000 mile replacement campaign to help increase customer and industry awareness. The campaign is being advertised via radio and outdoor billboards throughout the United States and Canada stating *Monroe® Recommends Replacing Your Shocks and Struts at 50,000 Miles.* We will continue to carry that message to consumers and the trade in 2007, again utilizing billboards, radio spots and ads in both trade and consumer magazines. We are exploring a number of opportunities to extend our existing well-known brands, such as Monroe®, and our product line generally, to aftermarket product segments not previously served. We believe that, when combined with our expansive customer service network, these initiatives will yield incremental aftermarket revenues.

Achieve Greater Content per Vehicle

As a result of increasing emissions standards we believe that available emission control content per light vehicle will rise over the next several years. We believe that consumers' greater emphasis on automotive safety could also allow available ride control content per light vehicle to rise. In addition, advanced technologies and modular assemblies represent an opportunity to increase vehicle content. For example, our innovative CES system, which we supply on several Volvo and Audi passenger cars, increases our content revenues seven-fold compared to a standard shock offering. We plan to take advantage of these trends by leveraging our existing position on many top-selling vehicle platforms and by continuing to enhance our modular/systems capabilities.

Execute Focused Transactions

In the past, we have been successful in identifying and capitalizing on strategic acquisitions and alliances to achieve growth. Through these acquisitions and alliances, we have (1) expanded our product portfolio; (2) realized incremental business with existing customers; (3) gained access to new customers; and (4) achieved leadership positions in new geographic markets.

We have developed a strategic alliance with Futaba, a leading exhaust manufacturer in Japan that also includes a joint venture operation in Burnley, England. We also have an alliance with Hitachi (as successor to Tokico Ltd. following its acquisition of Tokico), a leading Japanese ride control manufacturer. These alliances help us grow our business with Japan-based OEMs by leveraging the geographical presence of each partner to

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serve Japan-based global platforms. We have established a presence in Thailand through a joint venture that supplies exhaust components for GMIsuzu. Our joint venture operations in Dalian and Shanghai, China have established us as one of the leading exhaust suppliers in the rapidly growing Chinese automotive market. We also operate joint ventures with Eberspächer International GmbH to supply emission control products and systems for luxury cars produced by BMW and Audi in China, and with Chengdu Lingchuan Mechanical Plant to supply emission control products and systems for various Ford platforms produced in China.

We recently announced that we are expanding our operations in China with investment in both manufacturing and engineering facilities. We opened our first solely-owned operation in China, an elastomer manufacturing facility in Suzhou. In addition, we are extending our joint venture with Shanghai Tractor and Engine Company, a subsidiary of Shanghai Automotive Industry Corp., by establishing an engineering center to develop automotive exhaust products. The engineering center opened during the fourth quarter of 2006. Finally, we increased our ownership stake in the Beijing Monroe Shock Absorber Co. Ltd. (a joint venture with Beijing Automotive Industry Corp.) from 51 percent to 65 percent.

In February 2005, we acquired substantially all the exhaust assets, and assumed certain related liabilities of, Gabilan Manufacturing Inc., a manufacturer of exhaust systems for Harley-Davidson Motorcycles. The acquisition represents an example of our strategy to grow through niche opportunities.

Where appropriate, we intend to continue to pursue strategic alliances, joint ventures, acquisitions and other transactions that complement or enhance our existing products, technology, systems development efforts, customer base and/or domestic or international presence. We strive to align with strong local partners to help us further develop our leadership in systems integration and to penetrate international markets. In addition, we align with companies that have proven products, proprietary technology, research capabilities and/or market penetration to help us achieve further leadership in product offerings, customer relationships, and systems integration and overall presence.

Growth in Adjacent Markets

One of our goals is to apply our existing design, engineering and manufacturing capabilities to penetrate a variety of adjacent markets and to achieve growth in higher-margin businesses. For example, we are aggressively leveraging our technology and engineering leadership in emission and ride control into adjacent markets, such as the heavy-duty market for trucks, buses, agricultural equipment, construction machinery and other commercial vehicles. As an established leading supplier of heavy-duty ride control and elastomer products, we are already serving customers like Volvo Truck, Mack, Navistar International, Freightliner and Scania. We also see tremendous opportunity to expand our presence in the heavy-duty market with our emission control products and systems, having recently entered this market in both North America and Europe with diesel technologies that will help customers meet environmental requirements.

Improve Efficiency and Reduce Costs

We are a process-oriented company and have implemented and are continuing to implement several programs designed to improve efficiency and reduce costs, including:

In February 2006, we announced a workforce reduction at certain of our global locations as part of our ongoing effort to reduce our cost structure. We recorded a pre-tax charge of approximately \$8 million during 2006 for severance and other benefits related to this reduction in force, substantially all of which have been paid in cash.

We are successfully completing the workforce reduction announced in October 2004 which eliminated 250 salaried positions worldwide. The majority of the eliminated positions are at the middle and senior

management levels. As of December 31, 2006, we have incurred \$23 million in severance costs. Of the total \$23 million in severance costs incurred to date, \$21 million represents cash payments with the remainder accrued in other short-term liabilities.

We have successfully completed Project Genesis, our primary initiative for improving global manufacturing and distribution efficiency. Since launching Project Genesis in December 2001, we have reduced

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excess manufacturing capacity and costs. We have closed eight facilities and improved workflow at 20 plants worldwide.

We anticipate long-term savings through our Six Sigma program, a methodology and approach designed to minimize product defects and improve operational efficiencies.

We have implemented a Lean manufacturing program to reduce costs, inventories and customer lead times while improving delivery.

We have adopted the Business Operating System (BOS), a disciplined system to promote and manage continuous improvement. BOS focuses on the assembly and analysis of data for quick and effective problem resolution to create more efficient and profitable operations.

We are using Economic Value Added (EVA¹), a financial tool that more effectively measures how efficiently we employ our capital resources, and have linked the successful application of this management discipline to our incentive compensation program.

In addition, we continue to work to reduce costs by standardizing products and processes throughout our operations; further developing our global supply chain management capabilities; improving our information technology; increasing efficiency through employee training; investing in more efficient machinery; and enhancing the global coordination of costing and quoting procedures, along with other steps to reduce administrative and operational costs and improve cost management.

Reduce Borrowings and Improve Cash Flow

We are focused on a core set of goals designed to reduce borrowings and improve cash flow: (i) continuing to reduce selling, general and administrative expenses plus engineering, research and development costs (SGA&E) as a percentage of sales, while continuing to invest in sales and engineering; (ii) extracting significant cash flow from working capital initiatives; (iii) offsetting to the greatest extent possible pressures on overall gross margins in a challenging economic environment; and (iv) strengthening existing customer relationships and winning new long-term OE business.

Environmental Matters

We estimate that we and our subsidiaries will make expenditures for plant, property and equipment for environmental matters of approximately \$7 million in 2007 and approximately \$4 million in 2008.

For additional information regarding environmental matters, see Item 3, Legal Proceedings, Item 7, Management s Discussion and Analysis of Financial Condition and Results of Operations Environmental and Other Matters, and Note 13 to the financial statements of Tenneco Inc. and Consolidated Subsidiaries included under Item 8.

Employees

As of December 31, 2006, we had approximately 19,000 employees of which approximately 50 percent are covered by collective bargaining agreements. Approximately 23 percent of our employees that are covered by collective bargaining agreements are also governed by European works councils. Several of our existing labor agreements in the United States and Mexico are scheduled for renegotiation in 2007, in addition to five agreements expiring in Europe covering plants in Spain, France, Belgium, Portugal and the United Kingdom. We regard our employee relations as generally satisfactory.

Other

The principal raw material utilized by us is steel. We obtain steel from a number of sources pursuant to various contractual and other arrangements. We believe that an adequate supply of steel can presently be

¹ EVA is a registered trademark of Stern Stewart & Co

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obtained from a number of different domestic and foreign suppliers. However, we are actively addressing higher steels costs which are expected to continue through 2007. See Outlook in Item 7, Management's Discussion and Analysis of Financial Condition and Results of Operations.

We hold a number of domestic and foreign patents and trademarks relating to our products and businesses. We manufacture and distribute our products primarily under the Walker® and Monroe® brand names, which are well-recognized in the marketplace and are registered trademarks. The patents, trademarks and other intellectual property owned by or licensed to us are important in the manufacturing, marketing and distribution of our products.

ITEM 1A. RISK FACTORS.

Changes in consumer demand and prices could materially and adversely impact our financial condition and results of operations.

Demand for and pricing of our products are subject to economic conditions and other factors present in the various domestic and international markets where the products are sold. Demand for our OE products is subject to the level of consumer demand for new vehicles that are equipped with our parts. The level of new light vehicle purchases is cyclical, affected by such factors as interest rates, consumer confidence, patterns of consumer spending, fuel cost and the automobile replacement cycle. For example, sales of North American light trucks and SUVs decreased by 14 percent in 2006 as compared to 2005, as consumers shifted their preferences from light trucks and SUVs to other vehicles in light of higher fuel costs. Because the percentage of our North American OE revenues related to light trucks and SUVs is greater than the percentage of the total North American light vehicle build rate represented by light trucks and SUVs, our North American OE business is sensitive to this change in consumer preferences. Demand for our aftermarket, or replacement, products varies based upon such factors as the level of new vehicle purchases, which initially displaces demand for aftermarket products, the severity of winter weather, which increases the demand for certain aftermarket products, and other factors, including the average useful life of parts and number of miles driven. Further decreases in demand for automobiles and automotive products generally, or in the demand for our products in particular, could materially and adversely impact our financial condition and results of operations.

We may be unable to realize sales represented by our awarded business, which could materially and adversely impact our financial condition and results of operations.

The realization of future sales from awarded business is inherently subject to a number of important risks and uncertainties, including the number of vehicles that our OE customers will actually produce, the timing of that production and the mix of options that our OE customers and consumers may choose. Substantially all of our North American vehicle manufacturing customers have slowed or maintained at flat levels new vehicle production for the past several years. For example, production rates for SUVs and light trucks decreased 1.8 percent in 2005 compared to 2004 and 8.0 percent in 2006 compared to 2005 while production rates for passenger cars increased 2.7 percent in 2005 compared to 2004 and 5.0 percent in 2006 compared to 2005. We remain cautious regarding production volumes for 2007 due to rising oil and steel prices, current OE manufacturers' inventory levels and uncertainty regarding the willingness of OE manufacturers to continue support to vehicle sales. Production rates for SUVs and light trucks in North America are expected to increase by 3.9 percent while passenger car production rates are expected to decrease by 5.0 percent in 2007. We expect the light vehicle build for Asia to significantly increase in 2007 and production rates in Eastern Europe and South America to increase slightly. All other regions are expected to remain flat. In addition, our customers generally have the right to replace us with another supplier at any time for a variety of reasons and have increasingly demanded price decreases over the life of awarded business. Accordingly, we cannot assure you that we will in fact realize any or all of the future sales represented by our awarded business. Any failure to realize these sales could have a material adverse effect on our financial condition and results of operations.

In many cases, we must commit substantial resources in preparation for production under awarded OE business well in advance of the customer's production start date. In certain instances, the terms of our OE customer arrangements permit us to recover these pre-production costs if the customer cancels the business

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through no fault of our company. Although we have been successful in recovering these costs under appropriate circumstances in the past, we can give no assurance that our results of operations will not be materially impacted in the future if we are unable to recover these types of pre-production costs related to OE cancellation of awarded business.

We are dependent on large customers for future revenue. The loss of any of these customers or the loss of market share by these customers could have a material adverse impact on us.

We depend on major vehicle manufacturers for a substantial portion of our net sales. For example, during 2006, General Motors, Ford, Volkswagen, and DaimlerChrysler accounted for 14 percent, 11 percent, 11 percent, and 11 percent of our net sales, respectively. The loss of all or a substantial portion of our sales to any of our large-volume customers could have a material adverse effect on our financial condition and results of operations by reducing cash flows and our ability to spread costs over a larger revenue base. We may make fewer sales to these customers for a variety of reasons, including: (1) loss of awarded business; (2) reduced or delayed customer requirements; or (3) strikes or other work stoppages affecting production by the customers. In 2006, Ford announced a plan to significantly reduce the number of its global suppliers. While we currently believe that our relationship with Ford will not be impacted by this plan, any significant reduction in sales to Ford could have a material adverse effect on us.

During the past several years, General Motors, Ford and Daimler Chrysler have lost market share in the United States, primarily to Asian competitors. While revenue from Japanese automakers represented approximately 20 percent of our North American OE sales in 2006 and we are actively targeting Korean automakers, any further market share loss by these North American- and European-based automakers could, if we are unable to achieve increased sales to the Asian OE manufacturers, have a material adverse effect on our business.

Financial difficulties facing other automotive companies may have an adverse impact on us.

A number of companies in the automotive industry are, and over the last several years have been, facing severe financial difficulties. As a result, there have been numerous recent bankruptcies of companies in the automotive industry, including the 2005 bankruptcy of Delphi Corporation, one of the world's largest automotive parts suppliers. In addition, Dana Corporation filed for bankruptcy protection in March 2006. Severe financial difficulties at any major automotive manufacturer or automotive supplier could have a significantly disruptive effect on the automotive industry in general, including by leading to labor unrest, supply chain disruptions and weakness in demand. In particular, severe financial difficulties at any of our major suppliers could have a material adverse effect on us if we are unable to obtain on a timely basis the quantity and quality of components we require to produce our products. In addition, such financial difficulties at any of our major customers could have a material adverse impact on us if such customer was unable to pay for the products we provide or we experienced a loss of, or material reduction in, business from such customer.

The hourly workforce in the automotive industry is highly unionized and our business could be adversely affected by labor disruptions.

Although we consider our current relations with our employees to be satisfactory, if major work disruptions were to occur, our business could be adversely affected by, for instance, a loss of revenues, increased costs or reduced profitability. We have not experienced a material labor disruption in our workforce in the last ten years, but there can be no assurance that we will not experience a material labor disruption at one of our facilities in the future in the course of renegotiation of our labor arrangements or otherwise. In addition, substantially all of the hourly employees of North American vehicle manufacturers and many of their other suppliers are represented by the United Automobile, Aerospace and Agricultural Implement Workers of America under collective bargaining agreements. Vehicle manufacturers and such suppliers and their employees in other countries are also subject to labor agreements. A work

stoppage or strike at our production facilities, at those of a significant customer, or at a significant supplier of ours or any of our customers could

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have an adverse impact on us by disrupting demand for our products and/or our ability to manufacture our products.

We have experienced significant increases in raw materials pricing, and further changes in the prices of raw materials could have a material adverse impact on us.

Significant increases in the cost of certain raw materials used in our products, to the extent they are not timely reflected in the price we charge our customers or otherwise mitigated, could materially and adversely impact our results. For example, since 2004, we have experienced significant increases in processed metal and steel prices. High steel prices are expected to continue into the foreseeable future. We expect that the pricing environment for steel will increase our costs by up to \$100 million in 2007. We worked hard in 2005 and 2006 and continue to work hard to address this issue by evaluating alternative materials and processes, reviewing material substitution opportunities, increasing component and assembly outsourcing to low cost countries and aggressively negotiating with our customers to allow us to recover these higher costs from them. In addition to these actions, we continue to pursue productivity initiatives and review opportunities to reduce costs through restructuring activities. The situation remains fluid as we continue to pursue these actions and, at this point, we cannot assure you that these actions and recent increases in new business awards will be effective in containing margin pressures from these significant raw materials price increases. See Management's Discussion and Analysis of Financial Conditions and Results of Operations Outlook included in Item 7 for more information.

The cyclical nature of automotive production and sales could cause a decline in our financial condition and results.

A decline in automotive sales and production would likely cause a decline in our sales to vehicle manufacturers, and could result in a decline in our results of operations and financial condition. The automotive industry has been characterized historically by periodic fluctuations in overall demand for vehicles due to, among other things, changes in general economic conditions and consumer preferences. These fluctuations generally result in corresponding fluctuations in demand for our products. The highly cyclical nature of the automotive industry presents a risk that is outside our control and that cannot be accurately predicted. See Management's Discussion and Analysis of Financial Conditions and Results of Operations Outlook included in Item 7 for more information.

We may be unable to realize our business strategy of improving operating performance and generating savings and improvements to help offset pricing pressures from our suppliers and customers.

We have either implemented or plan to implement strategic initiatives designed to improve our operating performance. The failure to achieve the goals of these strategic initiatives could have a material adverse effect on our business, particularly since we rely on these initiatives to offset pricing pressures from our suppliers and our customers, as described above. We cannot assure you that we will be able to successfully implement or realize the expected benefits of any of these initiatives or that we will be able to sustain improvements made to date.

We may incur material costs related to product warranties, environmental and regulatory matters and other claims, which could have a material adverse impact on our financial condition and results of operations.

From time to time, we receive product warranty claims from our customers, pursuant to which we may be required to bear costs of repair or replacement of certain of our products. Vehicle manufacturers are increasingly requiring their outside suppliers to guarantee or warrant their products and to be responsible for the operation of these component products in new vehicles sold to consumers. Warranty claims may range from individual customer claims to full recalls of all products in the field. We cannot assure you that costs associated with providing product warranties will not be material, or that those costs will not exceed any amounts reserved for them in our financial statements. For a description of our accounting policies regarding

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warranty reserves, see Management's Discussion and Analysis of Financial Condition and Results of Operations Critical Accounting Policies included in Item 7.

Additionally, we are subject to a variety of environmental and pollution control laws and regulations in all jurisdictions in which we operate. Soil and groundwater remediation activities are being conducted at certain of our current and former real properties. We record liabilities for these activities when environmental assessments indicate that the remedial efforts are probable and the costs can be reasonably estimated. On this basis, we have established reserves that we believe are adequate for the remediation activities at our current and former real properties for which we could be held responsible. Although we believe our estimates of remediation costs are reasonable and are based on the latest available information, the cleanup costs are estimates and are subject to revision as more information becomes available about the extent of remediation required. In future periods, we could be subject to cash or non-cash charges to earnings if we are required to undertake material additional remediation efforts based on the results of our ongoing analyses of the environmental status of our properties, as more information becomes available to us.

We also from time to time are involved in legal proceedings, claims or investigations that are incidental to the conduct of our business. Some of these proceedings allege damages against us relating to environmental liabilities, intellectual property matters, personal injury claims, taxes, employment matters or commercial or contractual disputes. For example, we are subject to a number of lawsuits initiated by a significant number of claimants alleging health problems as a result of exposure to asbestos. Many of these cases involve significant numbers of individual claimants. Many of these cases also involve numerous defendants, with the number of defendants in some cases exceeding 200 defendants from a variety of industries. As major asbestos manufacturers or other companies that used asbestos in their manufacturing processes continue to go out of business, we may experience an increased number of these claims.

We vigorously defend ourselves in connection with all of the matters described above. We cannot, however, assure you that the costs, charges and liabilities associated with these matters will not be material, or that those costs, charges and liabilities will not exceed any amounts reserved for them in our financial statements. In future periods, we could be subject to cash costs or non-cash charges to earnings if any of these matters is resolved unfavorably to us. See Management's Discussion and Analysis of Financial Condition and Results of Operations Environmental and Other Matters, included in Item 7 for further description.

We may have difficulty competing favorably in the highly competitive automotive parts industry.

The automotive parts industry is highly competitive. Although the overall number of competitors has decreased due to ongoing industry consolidation, we face significant competition within each of our major product areas. The principal competitive factors include price, quality, service, product performance, design and engineering capabilities, new product innovation, global presence and timely delivery. As a result, many suppliers have established or are establishing themselves in emerging, low-cost markets to reduce their costs of production and be more conveniently located for customers. Although we are also pursuing a low-cost country production strategy and otherwise continue to seek process improvements to reduce costs, we cannot assure you that we will be able to continue to compete favorably in this competitive market or that increased competition will not have a material adverse effect on our business by reducing our ability to increase or maintain sales or profit margins.

The decreasing number of automotive parts customers and suppliers could make it more difficult for us to compete favorably.

Our financial condition and results of operations could be adversely affected because the customer base for automotive parts is decreasing in both the original equipment market and aftermarket. As a result, we are competing for business from fewer customers. Due to the cost focus of these major customers, we have been, and expect to continue to be, requested to reduce prices as part of our initial business quotations and over the life of vehicle

platforms we have been awarded. We cannot be certain that we will be able to generate cost savings and operational improvements in the future that are sufficient to offset price reductions requested by existing customers and necessary to win additional business.

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Furthermore, the trend toward consolidation and bankruptcies among automotive parts suppliers is resulting in fewer, larger suppliers who benefit from purchasing and distribution economies of scale. If we cannot achieve cost savings and operational improvements sufficient to allow us to compete favorably in the future with these larger companies, our financial condition and results of operations could be adversely affected due to a reduction of, or inability to increase, sales.

We may not be able to successfully respond to the changing distribution channels for aftermarket products.

Major automotive aftermarket retailers, such as AutoZone and Advance Auto Parts, are attempting to increase their commercial sales by selling directly to automotive parts installers in addition to individual consumers. These installers have historically purchased from their local warehouse distributors and jobbers, who are our more traditional customers. We cannot assure you that we will be able to maintain or increase aftermarket sales through increasing our sales to retailers. Furthermore, because of the cost focus of major retailers, we have occasionally been requested to offer price concessions to them. Our failure to maintain or increase aftermarket sales, or to offset the impact of any reduced sales or pricing through cost improvements, could have an adverse impact on our business and operating results.

Longer product lives of automotive parts are adversely affecting aftermarket demand for some of our products.

The average useful life of automotive parts has steadily increased in recent years due to innovations in products and technologies. The longer product lives allow vehicle owners to replace parts of their vehicles less often. As a result, a portion of sales in the aftermarket has been displaced. This has adversely impacted, and could continue to adversely impact, our aftermarket sales. Also, any additional increases in the average useful lives of automotive parts would further adversely affect the demand for our aftermarket products. Recently, we have experienced relative stabilization in our aftermarket business due to our ability to win new customers and recover steel price increases. However, there can be no assurance that we will be able to maintain this stabilization. Aftermarket sales represented approximately 23 percent of our net sales for both 2006 and 2005.

Any acquisitions we make could disrupt our business and seriously harm our financial condition.

We may, from time to time, consider acquisitions of complementary companies, products or technologies. Acquisitions involve numerous risks, including difficulties in the assimilation of the acquired businesses, the diversion of our management's attention from other business concerns and potential adverse effects on existing business relationships with current customers and suppliers. In addition, any acquisitions could involve the incurrence of substantial additional indebtedness. We cannot assure you that we will be able to successfully integrate any acquisitions that we pursue or that such acquisitions will perform as planned or prove to be beneficial to our operations and cash flow. Any such failure could seriously harm our business, financial condition and results of operations.

We are subject to risks related to our international operations.

We have manufacturing and distribution facilities in many regions and countries, including Australia, China, India, North America, Europe and South America, and sell our products worldwide. For 2006, approximately 58 percent of our net sales were derived from operations outside North America. International operations are subject to various risks which could have a material adverse effect on those operations or our business as a whole, including:

exposure to local economic conditions;

exposure to local political conditions, including the risk of seizure of assets by a foreign government;

exposure to local social unrest, including any resultant acts of war, terrorism or similar events;

exposure to local public health issues and the resultant impact on economic and political conditions;

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currency exchange rate fluctuations;

hyperinflation in certain foreign countries;

controls on the repatriation of cash, including imposition or increase of withholding and other taxes on remittances and other payments by foreign subsidiaries; and

export and import restrictions.

Exchange rate fluctuations could cause a decline in our financial condition and results of operations.

As a result of our international operations, we generate a significant portion of our net sales and incur a significant portion of our expenses in currencies other than the U.S. dollar. To the extent we are unable to match revenues received in foreign currencies with costs paid in the same currency, exchange rate fluctuations in that currency could have a material adverse effect on our business. For example, where we have significantly more costs than revenues generated in a foreign currency, we are subject to risk if the foreign currency in which our costs are paid appreciates against the currency in which we generate revenue because the appreciation effectively increases our cost in that country.

The financial condition and results of operations of some of our operating entities are reported in foreign currencies and then translated into U.S. dollars at the applicable exchange rate for inclusion in our consolidated financial statements. As a result, appreciation of the U.S. dollar against these foreign currencies generally will have a negative impact on our reported revenues and operating profit while depreciation of the U.S. dollar against these foreign currencies will generally have a positive effect on reported revenues and operating profit. For example, our European operations were positively impacted in 2004 and 2006 due to the strengthening of the Euro against the U.S. dollar. However, in 2005, the dollar strengthened against the Euro which had a negative effect on our results of operations. Our South American operations were negatively impacted by the devaluation in 2000 of the Brazilian currency as well as by the devaluation of the Argentine currency in 2002. We do not generally seek to mitigate this translation effect through the use of derivative financial instruments.

Further significant changes in our stockholder composition may jeopardize our ability to use some or all of our net operating loss carryforwards.

As of December 31, 2006, we had U.S. Federal tax net operating loss (NOL) carryforwards of \$597 million available to reduce taxable income in future years, and these NOL carryforwards expire in various years through 2026. The federal tax effect of these NOLs is \$209 million and is recorded as a deferred tax asset on our balance sheet as of December 31, 2006. We also have state NOL carryforwards at December 31, 2006 of \$585 million, which will expire in various years through 2026. The tax effect of the state NOL, net of a valuation allowance, is \$29 million and is recorded as a deferred tax asset on our balance sheet at December 31, 2006. Our ability to utilize our NOL carryforwards could become subject to significant limitations under Section 382 of the Internal Revenue Code (Section 382) if we undergo a majority ownership change. We would undergo a majority ownership change if, among other things, the stockholders who own or have owned, directly or indirectly, five percent or more of our common stock or are otherwise treated as five percent stockholders under Section 382 and the regulations promulgated thereunder, increase their aggregate percentage ownership of our stock by more than 50 percentage points over the lowest percentage of stock owned by these stockholders at any time during the testing period, which is generally the three-year period preceding the potential ownership change. In the event of a majority ownership change, Section 382 imposes an annual limitation on the amount of taxable income a corporation may offset with the NOL carryforwards. Any unused annual limitation may be carried over to later years until the applicable expiration of the respective NOL

carryforwards. If we were to undergo a majority ownership change, we would be required to record a reserve for some or all of the asset currently recorded on our balance sheet. As of December 31, 2006, we believe that there has not been a significant change in our ownership during the prior three years. We cannot, however, assure you that we will not undergo a majority ownership change in the future. Further, because an ownership change for federal tax purposes can occur based on trades among our existing stockholders, whether we undergo a majority ownership change may be a matter beyond our control.

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We have disclosed a material weakness in our internal control over financial reporting relating to our accounting for income taxes which could adversely affect our ability to report our financial condition and results of operations accurately and on a timely basis.

In connection with our assessment of internal control over financial reporting under Section 404 of the Sarbanes-Oxley Act of 2002, we identified a material weakness in our internal control over financial reporting relating to our accounting for income taxes as of December 31, 2006. For a discussion of our internal control over financial reporting and a description of the identified material weakness, see Management's Report on Internal Control over Financial Reporting under Item 8, Financial Statements and Supplementary Data.

A material weakness in our internal control over financial reporting could adversely impact our ability to provide timely and accurate financial information. While we have taken measures to strengthen our internal controls in response to the identified material weakness related to accounting for income taxes, and engaged outside professionals to assist us in our efforts, additional work remains to be done to address the identified material weakness. If we are unsuccessful in implementing or following our remediation plan, we may not be able to timely or accurately report our financial condition, results of operations or cash flows or maintain effective disclosure controls and procedures. If we are unable to report financial information timely and accurately or to maintain effective disclosure controls and procedures, we could be subject to, among other things, regulatory or enforcement actions by the SEC and the NYSE, including a delisting from the NYSE, securities litigation, debt rating agency downgrades or rating withdrawals, and a general loss of investor confidence, any one of which could adversely affect our business prospects and the valuation of our common stock.

ITEM 1B. UNRESOLVED STAFF COMMENTS.

None.

ITEM 2. PROPERTIES.

We lease our principal executive offices, which are located at 500 North Field Drive, Lake Forest, Illinois, 60045.

Walker's consolidated businesses operate 14 manufacturing facilities in the U.S. and 39 manufacturing facilities outside of the U.S., operate five engineering and technical facilities worldwide and share two other such facilities with Monroe. Twenty-two of these manufacturing plants are JIT facilities. Walker operates four additional manufacturing facilities outside of the U.S. through four non-controlled joint ventures three of which are JIT facilities.

Monroe's consolidated businesses operate eight manufacturing facilities in the U.S. and 22 manufacturing facilities outside the U.S., operate 7 engineering and technical facilities worldwide and share two other such facilities with Walker. Five of these manufacturing plants are JIT facilities.

The above-described manufacturing locations outside of the U.S. are located in Argentina, Australia, Belgium, Brazil, Canada, China, the Czech Republic, Denmark, France, Germany, India, Mexico, New Zealand, Poland, Portugal, Russia, Spain, South Africa, Sweden, Thailand and the United Kingdom, We also have sales offices located in Australia, Argentina, China, Croatia, Egypt, Greece, Hungary, Italy, Japan, Korea, Lithuania, Singapore, Turkey and the Ukraine.

We own approximately one half of the properties described above and lease the other half. We hold twelve of the above-described international manufacturing facilities through seven joint ventures in which we own a controlling interest. In addition, we hold four others through four joint ventures in which we own a non-controlling interest. We also have distribution facilities at our manufacturing sites and at a few offsite locations, substantially all of which we

lease.

We believe that substantially all of our plants and equipment are, in general, well maintained and in good operating condition. They are considered adequate for present needs and, as supplemented by planned construction, are expected to remain adequate for the near future.

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We also believe that we have generally satisfactory title to the properties owned and used in our respective businesses.

ITEM 3. LEGAL PROCEEDINGS.

As of December 31, 2006, we are designated as a potentially responsible party in one Superfund site. Including the Superfund site, we may have the obligation to remediate current or former facilities, and we estimate our share of environmental remediation costs at these facilities to be approximately \$8 million. For the Superfund site and the current and former facilities, we have established reserves that we believe are adequate for these costs. Although we believe our estimates of remediation costs are reasonable and are based on the latest available information, the cleanup costs are estimates and are subject to revision as more information becomes available about the extent of remediation required. At some sites, we expect that other parties will contribute to the remediation costs. In addition, at the Superfund site, the Comprehensive Environmental Response, Compensation and Liability Act provides that our liability could be joint and several, meaning that we could be required to pay in excess of our share of remediation costs. Our understanding of the financial strength of other potentially responsible parties at the Superfund site, and of other liable parties at our current and former facilities, has been considered, where appropriate, in our determination of our estimated liability.

We believe that any potential costs associated with our current status as a potentially responsible party in the Superfund site, or as a liable party at our current or former facilities, will not be material to our results of operations or consolidated financial position.

From time to time we are subject to product warranty claims whereby we are required to bear costs of repair or replacement of certain of our products. Warranty claims may range from individual customer claims to full recalls of all products in the field. We believe that our warranty reserve is appropriate; however, actual claims incurred could differ from the original estimates requiring adjustments to the reserve. The reserve is included in current liabilities on the balance sheet. See Note 13 to our consolidated financial statements included under Item 8 for information regarding our warranty reserves.

We also from time to time are involved in legal proceedings, claims or investigations that are incidental to the conduct of our business. Some of these proceedings allege damages against us relating to environmental liabilities (including toxic tort, property damage and remediation), intellectual property matters (including patent, trademark and copyright infringement, and licensing disputes), personal injury claims (including injuries due to product failure, design or warnings issues, and other product liability related matters), taxes, employment matters, and commercial or contractual disputes, sometimes related to acquisitions or divestitures. For example, one of our Chinese joint ventures is currently defending a legal proceeding by Chinese government officials related to whether the joint venture applied the proper tariff code to certain of its imports. We vigorously defend ourselves against all of these claims. In future periods, we could be subjected to cash costs or non-cash charges to earnings if any of these matters is resolved on unfavorable terms. However, although the ultimate outcome of any legal matter cannot be predicted with certainty, based on present information, including our assessment of the merits of the particular claim, we do not expect that these legal proceedings or claims will have any material adverse impact on our future consolidated financial position or results of operations.

In addition, we are subject to a number of lawsuits initiated by a significant number of claimants alleging health problems as a result of exposure to asbestos. A small percentage of claims have been asserted by railroad workers alleging exposure to asbestos products in railroad cars manufactured by The Pullman Company, one of our subsidiaries. Nearly all of the claims are related to alleged exposure to asbestos in our automotive emission control products. Only a small percentage of these claimants allege that they were automobile mechanics and a significant number appear to involve workers in other industries or otherwise do not include sufficient information to determine

whether there is any basis for a claim against us. We believe, based on scientific and other evidence, it is unlikely that mechanics were exposed to asbestos by our former muffler products and that, in any event, they would not be at increased risk of asbestos-related disease based on their work with these products. Further, many of these cases involve numerous defendants, with the number

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of each in some cases exceeding 200 defendants from a variety of industries. Additionally, the plaintiffs either do not specify any, or specify the jurisdictional minimum, dollar amount for damages. As major asbestos manufacturers continue to go out of business or file for bankruptcy, we may experience an increased number of these claims. We vigorously defend ourselves against these claims as part of our ordinary course of business. In future periods, we could be subject to cash costs or non-cash charges to earnings if any of these matters is resolved unfavorably to us. To date, with respect to claims that have proceeded sufficiently through the judicial process, we have regularly achieved favorable resolution. Accordingly, we presently believe that these asbestos-related claims will not have a material adverse impact on our future financial condition or results of operations.

ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS.

No matters were submitted to the vote of security holders during the fourth quarter of 2006.

ITEM 4.1. EXECUTIVE OFFICERS OF THE REGISTRANT.

The following provides information concerning the persons who serve as our executive officers as of March 1, 2007. For periods prior to November 4, 1999, the date of the 1999 Pactiv spin-off, references to service to us or our company reflect services to Old Tenneco's automotive operations.

Name (and Age at December 31, 2006)	Offices Held
Gregg Sherrill (53)	Chairman of the Board of Directors and Chief Executive Officer
Timothy R. Donovan (51)	Executive Vice President, Strategy and Business Development, General Counsel
Hari N. Nair (46)	Executive Vice President and Managing Director Europe, South America and India
Kenneth R. Trammell (46)	Executive Vice President and Chief Financial Officer
Brent J. Bauer (51)	Senior Vice President and General Manager North American Original Equipment Emission Control
Neal Yanos (44)	Senior Vice President and General Manager North American Original Equipment Ride Control and North American Aftermarket
Timothy E. Jackson (49)	Senior Vice President Global Technology and Managing Director, Asia Pacific
Richard P. Schneider (59)	Senior Vice President Global Administration
Paul Schultz (56)	Senior Vice President Global Manufacturing and Supply Chain Management
Paul D. Novas (48)	Vice President and Controller
J. Jeffrey Zimmerman (47)	Vice President Law and Corporate Secretary

Gregg Sherrill Mr. Sherrill was named the Chairman and Chief Executive Officer of Tenneco in January 2007. Mr. Sherrill joined us from Johnson Controls Inc., where he served since 1998, most recently as President, Power Solutions. From 2002 to 2003, Mr. Sherrill served as the Vice President and Managing Director of Europe, South Africa and South America for Johnson Controls Automotive Systems Group. Prior to joining Johnson Controls, Mr. Sherrill held various engineering and manufacturing assignments over a 22-year span at Ford Motor Company, including Plant Manager of Ford's Dearborn, Michigan engine plant and Director of Supplier Technical Assistance. Mr. Sherrill became a director of our company in January 2007.

Timothy R. Donovan Mr. Donovan resigned as a director of our company, effective February 28, 2007. He has agreed to remain as an executive officer of our company through mid-March 2007. Mr. Donovan was named Executive Vice President, Strategy and Business Development in July 2005. He was promoted to Executive Vice President in December 2001 and was named Senior Vice President and General Counsel in August 1999. Mr. Donovan also is in charge of our worldwide Environmental, Health and Safety Program.

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From October 2004 through July 2005, Mr. Donovan served as Managing Director-Asia Pacific, with responsibility for Australia, New Zealand, Asia and the Japanese original equipment business worldwide. From May 2001 through October 2004, he served as Managing Director of our International Group with responsibility for all of our operations in Asia and South America, as well as the Japanese original equipment business worldwide. From July 2006 until January 2007 during our search for our new Chief Executive Officer, he served as a member of our interim management committee known as the Office of the Chief Executive. Mr. Donovan was a partner in the law firm of Jenner & Block from 1989 until his resignation in September 1999, and from approximately 1997 through 1999 served as the Chairman of Jenner & Block's Corporate and Securities Department and as a member of its Executive Committee. He is also a director of John B. Sanfilippo & Son, Inc., where he is a member of its Compensation Committee and is the Chairman of its Audit Committee. Mr. Donovan became a director of our company in March 2004.

Hari N. Nair Mr. Nair was named our Executive Vice President and Managing Director Europe effective June 2001. His responsibilities were expanded to include Tenneco's South American and Indian operations during 2005. Previously he was Senior Vice President and Managing Director International. Prior to December 2000, Mr. Nair was the Vice President and Managing Director Emerging Markets. Previously, Mr. Nair was the Managing Director for Tenneco Automotive Asia, based in Singapore and responsible for all operations and development projects in Asia. He began his career with the former Tenneco Inc. in 1987, holding various positions in strategic planning, marketing, business development, quality and finance. From July 2006 until January 2007 during our search for our new Chief Executive Officer, he served as a member of our interim management committee known as the Office of the Chief Executive. Prior to joining Tenneco, Mr. Nair was a senior financial analyst at General Motors Corp. focusing on European operations.

Kenneth R. Trammell Mr. Trammell was promoted to Executive Vice President and Chief Financial Officer in January 2006. Mr. Trammell was named our Senior Vice President and Chief Financial Officer in September 2003, having served as our Vice President and Controller from September 1999. From April 1997 to November 1999 he served as Corporate Controller of Tenneco Inc. He joined Tenneco Inc. in May 1996 as Assistant Controller. From July 2006 until January 2007 during our search for our new Chief Executive Officer, he served as a member of our interim management committee known as the Office of the Chief Executive. Before joining Tenneco Inc., Mr. Trammell spent 12 years with the international public accounting firm of Arthur Andersen LLP, last serving as a senior manager.

Brent J. Bauer Mr. Bauer joined Tenneco Automotive in August 1996 as a Plant Manager and was named Vice President and General Manager European Original Equipment Emission Control in September 1999. Mr. Bauer was named Vice President and General Manager European and North American Original Equipment Emission Control in July 2001. Currently, Mr. Bauer serves as the Senior Vice President and General Manager North American Original Equipment Emission Control. Prior to joining Tenneco, he was employed at AeroquipVickers Corporation for 20 years in positions of increasing responsibility serving most recently as Director of Operations.

Neal Yanos Mr. Yanos was named our Senior Vice President and General Manager North American Original Equipment Ride Control and North American Aftermarket in May 2003. He joined our Monroe ride control division as a process engineer in 1988 and since that time has served in a broad range of assignments including product engineering, strategic planning, business development, finance, program management and marketing, including Director of our North American original equipment GM/VW business unit and most recently as our Vice President and General Manager North American Original Equipment Ride Control from December 2000. From July 2006 until January 2007 during our search for our new Chief Executive Officer, he served as a member of our interim management committee known as the Office of the Chief Executive. Before joining our company, Mr. Yanos was employed in various engineering positions by Sheller Globe Inc. from 1985 to 1988.

Timothy E. Jackson Mr. Jackson joined us as Senior Vice President and General Manager North American Original Equipment and Worldwide Program Management in June 1999. He served in this position until August 2000, at which time he was named Senior Vice President Global Technology. From 2002 to 2005, Mr. Jackson served as Senior Vice President Manufacturing, Engineering, and Global Technology. In

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July 2005, Mr. Jackson was named Senior Vice President Global Technology and General Manager, Asia Pacific. Mr. Jackson joined us from ITT Industries where he was President of that company's Fluid Handling Systems Division. With over 20 years of management experience, 14 within the automotive industry, he was also Chief Executive Officer for HiSAN, a joint venture between ITT Industries and Sanoh Industrial Company. Mr. Jackson has also served in senior management positions at BF Goodrich Aerospace and General Motors Corporation.

Richard P. Schneider Mr. Schneider was named as our Senior Vice President Global Administration in connection with the 1999 Spin-Off and is responsible for the development and implementation of human resources programs and policies and employee communications activities for our worldwide operations. Prior to the 1999 Spin-Off, Mr. Schneider served as our Vice President Human Resources. He joined us in 1994 from International Paper Company where, during his 20 year tenure, he held key positions in labor relations, management development, personnel administration and equal employment opportunity.

Paul Schultz Mr. Schultz was named our Senior Vice President Global Supply Chain Management in April 2002. In July 2005, Mr. Schultz was also named Senior Vice President of Global Manufacturing. Prior to joining the company, Mr. Schultz was the Vice President, Supply Chain Management at Ingersoll-Rand Company. Mr. Schultz joined Ingersoll-Rand in 1998 as Vice President, Strategic Sourcing for their joint venture company, Ingersoll Dresser Pump. He was later promoted to Vice President, Manufacturing Operations, where he successfully introduced and led the Six Sigma initiative. Prior to joining Ingersoll-Rand, Mr. Schultz was with AlliedSignal (now Honeywell International) where he served for 25 years in staff and management positions. Most recently, he was Corporate Director, Global Commodity Management.

Paul D. Novas Mr. Novas was named our Vice President and Controller in July 2006. Mr. Novas served as Vice President, Finance and Administration for Tenneco Europe from January 2004 until July 2006 and as Vice President and Treasurer of Tenneco from November 1999 until January 2004. Mr. Novas joined Tenneco in 1996 as assistant treasurer responsible for corporate finance and North American treasury operations. Prior to joining Tenneco, Mr. Novas worked in the treasurer's office of General Motors Corporation for ten years.

J. Jeffrey Zimmerman Mr. Zimmerman has served as Vice President Law and Corporate Secretary of Tenneco since May 2006. Mr. Zimmerman joined Tenneco in January, 2000 as Corporate Counsel. He was promoted to Assistant General Counsel in April, 2001 and to Vice President Law in July 2004. Prior to joining Tenneco, Mr. Zimmerman was a partner in the law firm of Jenner & Block from 1993 to 1999.

Table of Contents**PART II****ITEM 5. MARKET FOR REGISTRANT'S COMMON EQUITY, RELATED STOCKHOLDER MATTERS, AND ISSUER REPURCHASES OF EQUITY SECURITIES.**

Our outstanding shares of common stock, par value \$.01 per share, are listed on the New York, Chicago and London Stock Exchanges. The following table sets forth, for the periods indicated, the high and low sales prices of our common stock on the New York Stock Exchange Composite Transactions Tape.

Quarter	Sales Prices	
	High	Low
2006		
1st	\$ 23.33	\$ 19.61
2nd	27.55	20.64
3rd	26.39	20.03
4th	25.34	21.41
2005		
1st	\$ 17.36	\$ 12.07
2nd	17.22	11.55
3rd	20.06	16.30
4th	19.95	15.70

As of February 20, 2007, there were approximately 22,631 holders of record of our common stock, including brokers and other nominees.

The declaration of dividends on our common stock is at the discretion of our Board of Directors. The Board has not adopted a dividend policy as such; subject to legal and contractual restrictions, its decisions regarding dividends are based on all considerations that in its business judgment are relevant at the time. These considerations may include past and projected earnings, cash flows, economic, business and securities market conditions and anticipated developments concerning our business and operations.

We are highly leveraged and restricted with respect to the payment of dividends under the terms of our financing arrangements. On January 10, 2001, we announced that our Board of Directors eliminated the regular quarterly dividend on the Company's common stock. The Board took this action in response to then-current industry conditions, primarily greater than anticipated production volume reductions by original equipment manufacturers in North America and continued softness in the global aftermarket. We have not paid dividends on our common stock since the fourth quarter of 2000. There are no current plans to reinstate a dividend on our common stock, as the Board of Directors intends to retain any earnings for use in our business for the foreseeable future. For additional information concerning our payment of dividends, see Item 7, Management's Discussion and Analysis of Financial Condition and Results of Operations.

See Item 12, Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters for information regarding securities authorized for issuance under our equity compensation plans.

Purchase of equity securities by the issuer and affiliated purchasers

The following table provides information relating to our purchase of shares of our common stock in the fourth quarter of 2006. All of these purchases reflect shares withheld upon vesting of restricted stock to satisfy minimum tax withholding obligations.

Period	Total Number of Shares Purchased	Average Price Paid
October 2006	345	\$ 23.59
November 2006		
December 2006		
Total	345	\$ 23.59

We presently have no publicly announced repurchase plan or program, but intend to continue to satisfy statutory minimum tax withholding obligations in connection with the vesting of outstanding restricted stock through the withholding of shares.

Table of Contents**ITEM 6. SELECTED FINANCIAL DATA.****TENNECO INC. AND CONSOLIDATED SUBSIDIARIES
SELECTED CONSOLIDATED FINANCIAL DATA**

	As Restated				
	Years Ended December 31,				
	2006(a)	2005(a)	2004(a)(c)	2003(b)(c)	2002(b)(c)
	(Millions Except Share and Per Share Amounts)				
Statements of Income					
(Loss) Data:					
Net sales and operating revenues					
North America	\$ 1,963	\$ 2,033	\$ 1,966	\$ 1,889	\$ 1,907
Europe, South America and India	2,387	2,110	1,940	1,611	1,367
Asia Pacific	436	371	380	322	236
Intergroup sales	(104)	(74)	(73)	(54)	(50)
	\$ 4,682	\$ 4,440	\$ 4,213	\$ 3,768	\$ 3,460
Income before interest expense, income taxes, and minority interest					
North America	\$ 103	\$ 148	\$ 131	\$ 128	\$ 128
Europe, South America and India	81	53	19	20	22
Asia Pacific	12	16	20	23	17
Total	196	217	170	171	167
Interest expense (net of interest capitalized)	136	133	178	146	140
Income tax expense (benefit)	5	26	(21)	(6)	(6)
Minority interest	6	2	4	6	4
Income before cumulative effect of change in accounting principle	49	56	9	25	29
Cumulative effect of change in accounting principle, net of income tax(d)					(218)
Net income (loss)	\$ 49	\$ 56	\$ 9	\$ 25	\$ (189)

Average number of shares of common stock outstanding								
Basic	44,625,220	43,088,558	41,534,810	40,426,136	39,795,481			
Diluted	46,755,573	45,321,225	44,180,460	41,767,959	41,667,815			
Earnings (loss) per average share of common stock								
Basic:								
Before cumulative effect of change in accounting principle	\$ 1.11	\$ 1.30	\$ 0.22	\$ 0.60	\$ 0.73			
Cumulative effect of change in accounting principle(d)								(5.48)
	\$ 1.11	\$ 1.30	\$ 0.22	\$ 0.60	\$ (4.75)			
Diluted:								
Before cumulative effect of change in accounting principle	\$ 1.05	\$ 1.24	\$ 0.21	\$ 0.58	\$ 0.69			
Cumulative effect of change in accounting principle(d)								(5.48)
	\$ 1.05	\$ 1.24	\$ 0.21	\$ 0.58	\$ (4.79)			
Cash dividends per common share	\$	\$	\$	\$	\$			

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As Restated
Years Ended December 31,
2006(a) 2005(a) 2004(a)(c) 2003(b)(c) 2002(b)(c)
(Millions Except Ratio and Percent Amounts)

Balance Sheet Data:

Total assets	\$ 3,274	\$ 2,945	\$ 3,134	\$ 2,883	\$ 2,587
Short-term debt	28	22	19	20	228
Long-term debt	1,357	1,361	1,402	1,410	1,217
Minority interest	28	24	24	23	19
Shareholders' equity	226	137	170	81	(70)

Statement of Cash Flows Data:

Net cash provided by operating activities	\$ 203	\$ 123	\$ 218	\$ 290	\$ 196
Net cash used by investing activities	(172)	(164)	(131)	(134)	(114)
Net cash provided (used) by financing activities	12	(28)	(15)	(51)	(74)
Cash Payments for plant, property and equipment	177	140	132	130	138

Other Data:

EBITDA(e)	\$ 380	\$ 394	\$ 347	\$ 334	\$ 311
Ratio of EBITDA to interest expense	2.79	2.96	1.95	2.29	2.22
Ratio of total debt to EBITDA	3.64	3.51	4.10	4.28	4.65
Ratio of earnings to fixed charges(f)	1.35	1.55	0.95	1.15	1.17
Working capital as a percent of sales(g)	2.6%	2.4%	1.2%	2.4%	4.0%

NOTE: Our financial statements for the three years ended December 31, 2006, which are discussed in the following notes, are included in this Form 10-K/A under Item 8.

- (a) These amounts reflect the restatement discussed in Note 4 to the consolidated financial statements included in Item 8 – Financial Statements and Supplementary Data.

For a discussion of the significant items affecting comparability of the financial information for the years ended 2006, 2005 and 2004, see Item 7, Management's Discussion and Analysis of Financial Condition and Results of Operations.

- (b) Similar correcting entries have been made to the 2003 and 2002 amounts for the restatement discussed in Note 4 to the consolidated financial statements included in Item 8 – Financial Statements and Supplementary Data.
- (c) Prior to the first quarter of 2005, inventories in the U.S. based operations (17 percent and 19 percent of our total consolidated inventories at December 31, 2004 and 2003, respectively) were valued using the last-in, first-out (LIFO) method and all other inventories were valued using the first-in, first-out (FIFO) or average cost methods at the lower of cost or market value. Effective January 1, 2005, we changed our accounting method for valuing inventory for our U.S. based operations from the LIFO method to the FIFO method. As a result, all U.S. inventories are now stated at the lower of cost, determined on a FIFO basis, or market. We elected to change to the FIFO method as we believe it is preferable for the following reasons: 1) the change will provide

better matching of revenue and expenditures and 2) the change will achieve greater consistency in valuing our global inventory. Additionally, we initially adopted LIFO as it provided certain U.S. tax benefits which we no longer realize due to our U.S. net operating losses (when applied for tax purposes, tax laws require that LIFO be applied for accounting principles generally accepted in the United States of America (GAAP) as well). As a result of the change, we also expect to realize administrative efficiencies. In accordance with GAAP, the change in inventory accounting has been applied by restating prior year s financial statements. The effect of the change on our financial position and results of operations are presented below.

	As of December 31,		
	2004	2003	2002
	(Millions)		
	Increase (Decrease)		
Inventories	\$ 14	\$ 11	\$ 13
Deferred income tax assets (noncurrent)	\$ (5)	\$ (4)	\$ (5)
Shareholders' equity	\$ 9	\$ 7	\$ 8

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	Increase (Decrease)		
	Years Ended December 31,		
	2004	2003	2002
	(Millions except per share amounts)		
Income (loss) before interest expense, income taxes and minority interest	\$ 3	\$ (2)	\$
Income tax expense (benefit)	1	(1)	
Income (loss) before cumulative effect of change in accounting principle and net income (loss)	\$ 2	\$ (1)	\$
Basic earnings (loss) per share of common stock	\$ 0.04	\$ (0.03)	\$
Diluted earnings (loss) per share of common stock	\$ 0.04	\$ (0.03)	\$

You should also read Note 5 to the consolidated financial statements included in Item 8 for a discussion of the changes in our results due to the change in our method for valuing inventory.

In October 2004 and July 2005, we announced a change in the structure of our organization which changed the components of our reportable segments. The European segment now includes our South American and Indian operations. While this has no impact on our consolidated results, it changes our segment results.

- (d) In 2002, we adopted SFAS No. 142 which changed the accounting for purchased goodwill from an amortization method to an impairment-only approach. You should also read the notes to the financial statements of Tenneco Inc. and Consolidated Subsidiaries, appearing in Item 8, for additional information.
- (e) EBITDA represents income before extraordinary item, cumulative effect of change in accounting principle, interest expense, income taxes, minority interest and depreciation and amortization. EBITDA is not a calculation based upon generally accepted accounting principles. The amounts included in the EBITDA calculation, however, are derived from amounts included in the historical statements of income data. In addition, EBITDA should not be considered as an alternative to net income or operating income as an indicator of our operating performance, or as an alternative to operating cash flows as a measure of liquidity. We have reported EBITDA because we regularly review EBITDA as a measure of our company's performance. In addition, we believe our debt holders utilize and analyze our EBITDA for similar purposes. We also believe EBITDA assists investors in comparing a company's performance on a consistent basis without regard to depreciation and amortization, which can vary significantly depending upon many factors. However, the EBITDA measure presented in this document may not always be comparable to similarly titled measures reported by other companies due to differences in the components of the calculation. EBITDA is derived from the statements of income (loss) as follows:

As Restated				
Year Ended December 31,				
2006(a)	2005(a)	2004(a)(c)	2003(b)(c)	2002(b)(c)
(Millions)				

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Net income (loss)	\$ 49	\$ 56	\$ 9	\$ 25	\$ (189)
Cumulative effect of change in accounting principle, net of income tax					218
Minority interest	6	2	4	6	4
Income tax expense (benefit)	5	26	(21)	(6)	(6)
Interest expense, net of interest capitalized	136	133	178	146	140
Depreciation and amortization of other intangibles	184	177	177	163	144
Total EBITDA	\$ 380	\$ 394	\$ 347	\$ 334	\$ 311

(f) For purposes of computing this ratio, earnings generally consist of income before income taxes and fixed charges excluding capitalized interest. Fixed charges consist of interest expense, the portion of rental expense considered representative of the interest factor and capitalized interest. For the year ended December 31, 2004, earnings were insufficient by \$9 million to cover fixed charges. See Exhibit 12 to this Form 10-K/A for the calculation of this ratio.

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(g) For purposes of computing working capital as a percentage of sales, we exclude cash and the current portion of long term debt from the calculation. We exclude these items because we manage our working capital activity through cash and short term debt. To include these items in the calculation would distort actual working capital changes. Our calculation of working capital as a percentage of sales is as follows:

	As Restated				
	Years Ended December 31,				
	2006(a)	2005(a)	2004(a)(c)	2003(b)(c)	2002(b)(c)
	(Dollar amount in Millions				
	Except Percentage Amounts)				
Current Assets:					
Receivables Customer notes and accounts, net	\$ 578	\$ 518	\$ 460	\$ 427	\$ 394
Receivables Other	17	21	23	19	15
Inventories	441	361	396	354	365
Deferred income taxes	51	43	70	63	56
Prepayments and other	126	99	122	107	95
	\$ 1,213	\$ 1,042	\$ 1,071	\$ 970	\$ 925
Current Liabilities:					
Trade payables	\$ 781	\$ 652	\$ 699	\$ 621	\$ 505
Accrued taxes	49	31	24	23	40
Accrued interest	33	31	28	42	23
Accrued liabilities	194	193	224	162	172
Other accruals	34	29	45	30	45
	\$ 1,091	\$ 936	\$ 1,020	\$ 878	\$ 785
Working Capital (Current assets less current liabilities)	\$ 122	\$ 106	\$ 51	\$ 92	\$ 140
Net sales and operating revenues	\$ 4,682	\$ 4,440	\$ 4,213	\$ 3,768	\$ 3,460
Working capital as a percent of sales	2.6%	2.4%	1.2%	2.4%	4.0%

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

As you read the following review of our financial condition and results of operations, you should also read our financial statements and related notes beginning on page 69. As discussed on Note 4 to the consolidated financial statements, we have restated our financial statements as of December 31, 2006 and 2005 and for the three year period ended December 31, 2006. This management's discussion and analysis reflects that restatement.

Executive Summary

We are one of the world's leading manufacturers of automotive emission control and ride control products and systems. We serve both original equipment (OE) vehicle designers and manufacturers and the repair and replacement markets, or aftermarket, globally through leading brands, including Monroe®, Rancho®, Clevite®, Elastomers and Fric Rot™ ride control products and Walker®, Fonos™, and Gillet™ emission control products. Worldwide we serve more than 35 different original equipment manufacturers, and our products or systems are included on nine of the top 10 passenger car models produced for sale in Europe and nine of the top 10 light truck and SUV models produced for sale in North America for 2006. Our aftermarket customers are comprised of full-line and specialty warehouse distributors, retailers, jobbers, installer chains and car dealers. We operate more than 80 manufacturing facilities worldwide and employ approximately 19,000 people to service our customers' demands.

Factors that are critical to our success include winning new business awards, managing our overall global manufacturing footprint to ensure proper placement and workforce levels in line with business needs, maintaining competitive wages and benefits, maximizing efficiencies in manufacturing processes, fixing or eliminating unprofitable businesses and reducing overall costs. In addition, our ability to adapt to key industry trends, such as the consolidation of OE customers, a shift in consumer preferences to other vehicles in response to higher fuel costs and other economic and social factors, increasing technologically sophisticated content, changing aftermarket distribution channels, increasing environmental standards and extended product life of automotive parts, also play a critical role in our success. Other factors that are critical to our success include adjusting to environmental and economic challenges such as increases in the cost of raw materials and our ability to successfully reduce the impact of any such cost increases through material substitutions, cost reduction initiatives and other methods.

We have a substantial amount of indebtedness. As such, our ability to generate cash both to fund operations and service our debt is also a significant area of focus for our company. See "Liquidity and Capital Resources" below for further discussion of cash flows.

Total revenues for 2006 were \$4.7 billion, a five percent increase over 2005. Excluding the impact of currency and substrate sales, revenue was down \$60 million, or two percent, driven primarily by lower OE production volumes in North America, particularly light trucks and SUVs, partially offset by higher aftermarket sales. In addition, our geographic balance and diverse customer base helped partially offset the North American production decline. Gross margin for 2006 was 18.1 percent, down 1.3 percent from 19.4 percent in 2005. Higher substrate sales, driven by more diesel aftertreatment and hot-end exhaust business, which typically carry lower margins, diluted gross margin. Also impacting gross margin were increased steel and other material costs, reduced North American production volumes, and higher restructuring charges, all of which more than offset savings and improved efficiencies from Lean manufacturing, Six Sigma programs, cost recoveries and other cost reduction initiatives. We reported selling, general, administrative and engineering expenses for 2006 of 9.8 percent of revenues, as compared to 10.5 percent of revenues for 2005. The improvement was driven by the aggressive effort to reduce costs globally, including tight discretionary spending controls and the benefit from our 2006 decision to freeze future accruals under our defined benefit pension

plans for substantially all U.S. salaried and non-union hourly employees effective December 31, 2006. Earnings before interest expense, taxes and minority interest (EBIT) was \$196 million for 2006, down \$21 million from the \$217 million reported in 2005. Higher material costs, reduced North American production volumes and increased restructuring charges more than offset increased global aftermarket

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revenues, lower selling, general, administrative and engineering costs, benefits from the company's ongoing manufacturing efficiency programs and reduced costs through tight controls on discretionary spending.

In October 2004 and July 2005, we announced changes in the structure of our organization which changed the components of our reportable segments. The European segment now includes our Indian (as well as South American) operations. The Asia Pacific segment includes our other Asian and Australian operations. While this had no impact on our consolidated results, it changed our segment results. These changes in segment reporting have been reflected in this Management's Discussion and Analysis, and the accompanying consolidated financial statements, for all periods presented.

In February 2005, we acquired substantially all the exhaust assets, and assumed certain related liabilities, of Gabilan Manufacturing, Inc., a privately held company that had developed and manufactured motorcycle exhaust systems for Harley-Davidson motorcycles since 1978. The company also produced aftermarket muffler kits for Harley-Davidson. We purchased Gabilan's assets, including working capital adjustments, for \$11 million in cash.

In December 2005, we completed the acquisition of the minority interest of the joint venture partner for our Indian ride control operations. We purchased the minority owned interest for approximately \$5 million in cash and property.

Years 2006 and 2005

Net Sales and Operating Revenues

The following tables reflect our revenues for the years of 2006 and 2005. We present these reconciliations of revenues in order to reflect the trend in our sales in various product lines and geographic regions separately from the effects of doing business in currencies other than the U.S. dollar. We have not reflected any currency impact in the 2005 table since this is the base period for measuring the effects of currency during 2006 on our operations.

Additionally, we show the component of our revenue represented by substrate sales (previously referred to as pass-through catalytic converter sales) in the following table. While we generally have primary design, engineering and manufacturing responsibility for OE emission control systems, we do not manufacture substrates. Substrates are porous ceramic filters coated with a catalyst—precious metals such as platinum, palladium and rhodium. These are supplied to us by Tier 2 suppliers and directed by our OE customers. We generally earn a small margin on these components of the system. As the need for more sophisticated emission control solutions increases to meet more stringent environmental regulations, and as we capture more diesel aftertreatment business, these substrate components have been increasing as a percentage of our revenue. While these substrates dilute our gross margin, they are a necessary component of an emission control system. We view the growth of substrates as a key indicator that our value add content in an emission control system is moving toward the higher technology hot-end gas and diesel business.

Our value-add content in an emission control system includes designing the system to meet environmental regulations through integration of the substrates into the system, maximizing use of thermal energy to heat up the catalyst quickly, efficiently managing airflow to reduce back pressure as the exhaust stream moves past the catalyst, managing the expansion and contraction of the emission control system components due to temperature extremes experienced by an emission control system, using advanced acoustic engineering tools to design the desired exhaust sound, minimizing the opportunity for the fragile components of the substrate to be damaged when we integrate it into the emission control system and reducing unwanted noise, vibration and harshness transmitted through the emission control system. We present these substrate sales separately in the following table because we believe investors utilize this information to understand the impact of this portion of our revenues on our overall business and because it removes the impact of potentially volatile precious metals pricing from our revenues.

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	As Restated Year Ended December 31, 2006				
	Revenues	Currency Impact	Revenues Excluding Currency (Millions)	Substrate Sales Excluding Currency	Revenues Excluding Currency and Substrate Sales
North America Original Equipment					
Ride Control	\$ 483	\$	\$ 483	\$	\$ 483
Emission Control	928	6	922	272	650
Total North America Original Equipment	1,411	6	1,405	272	1,133
North America Aftermarket					
Ride Control	383		383		383
Emission Control	162		162		162
Total North America Aftermarket	545		545		545
Total North America	1,956	6	1,950	272	1,678
Europe Original Equipment					
Ride Control	380	10	370		370
Emission Control	1,264	34	1,230	504	726
Total Europe Original Equipment	1,644	44	1,600	504	1,096
Europe Aftermarket					
Ride Control	178	3	175		175
Emission Control	211	5	206		206
Total Europe Aftermarket	389	8	381		381
South America & India	272	14	258	32	226
Total Europe, South America & India	2,305	66	2,239	536	1,703
Asia	246		246	85	161
Australia	175	(1)	176	19	157
Total Asia Pacific	421	(1)	422	104	318
Total Tenneco	\$				