

TEXAS INSTRUMENTS INC  
Form 10-Q  
November 01, 2013

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

FORM 10-Q

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

For the quarterly period ended September 30, 2013

TRANSITION REPORT UNDER SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from \_\_\_\_\_ to \_\_\_\_\_  
Commission File Number 001-03761

TEXAS INSTRUMENTS INCORPORATED  
(Exact Name of Registrant as Specified in Its Charter)

Delaware  
(State of Incorporation) 75-0289970  
(I.R.S. Employer Identification No.)

12500 TI Boulevard, P.O. Box 660199, Dallas, Texas 75266-0199  
(Address of principal executive offices) (Zip Code)

Registrant's telephone number, including area code 214-479-3773

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes  No

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

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

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

1,094,563,114

Number of shares of Registrant's common stock outstanding as of  
September 30, 2013

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## PART I - FINANCIAL INFORMATION

## ITEM 1. Financial Statements.

## TEXAS INSTRUMENTS INCORPORATED AND SUBSIDIARIES

## Consolidated statements of income

[Millions of dollars, except share and per-share amounts]

|   | For Three Months Ended |         | For Nine Months Ended |         |
|---|------------------------|---------|-----------------------|---------|
|   | September 30,          |         | September 30,         |         |
|   | 2013                   | 2012    | 2013                  | 2012    |
| Revenue   | \$3,244                | \$3,390 | \$9,177               | \$9,846 |
| Cost of revenue (COR)                             | 1,465                  | 1,650   | 4,453                 | 4,924   |
| Gross profit                                      | 1,779                  | 1,740   | 4,724                 | 4,922   |
| Research and development (R&D)                    | 368                    | 463     | 1,176                 | 1,452   |
| Selling, general and administrative (SG&A)        | 465                    | 453     | 1,397                 | 1,372   |
| Acquisition charges                               | 86                     | 106     | 257                   | 363     |
| Restructuring charges/other                       | 16                     | (122)   | (251)                 | (99)    |
| Operating profit                                  | 844                    | 840     | 2,145                 | 1,834   |
| Other income (expense), net (OI&E)                | (4)                    | 24      | (2)                   | 8       |
| Interest and debt expense                         | 24                     | 21      | 71                    | 62      |
| Income before income taxes                        | 816                    | 843     | 2,072                 | 1,780   |
| Provision for income taxes                        | 187                    | 59      | 421                   | 285     |
| Net income  | \$629                  | \$784   | \$1,651               | \$1,495 |
| Earnings per common share:                        |                        |         |                       |         |
| Basic   | \$.56                  | \$.68   | \$1.47                | \$1.29  |
| Diluted   | \$.56                  | \$.67   | \$1.45                | \$1.27  |
| Average shares outstanding (millions):            |                        |         |                       |         |
| Basic   | 1,096                  | 1,130   | 1,102                 | 1,138   |
| Diluted   | 1,111                  | 1,141   | 1,117                 | 1,153   |
| Cash dividends declared per share of common stock | \$.28                  | \$.17   | \$.77                 | \$.51   |

See accompanying notes.

## TEXAS INSTRUMENTS INCORPORATED AND SUBSIDIARIES

## Consolidated statements of comprehensive income

[Millions of dollars]

|   | For Three Months Ended |       | For Nine Months Ended |         |
|---|------------------------|-------|-----------------------|---------|
|   | September 30,          |       | September 30,         |         |
|   | 2013                   | 2012  | 2013                  | 2012    |
| Net income  | \$629                  | \$784 | \$1,651               | \$1,495 |
| Other comprehensive income (loss):                        |                        |       |                       |         |
| Available-for-sale investments:                           |                        |       |                       |         |
| Unrealized gains (losses), net of taxes                   | —                      | 1     | —                     | 3       |
| Net actuarial gains (losses) of defined benefit plans:    |                        |       |                       |         |
| Adjustment, net of taxes                                  | 6                      | (3    | ) 86                  | 8       |
| Reclassification of recognized transactions, net of taxes | 13                     | 128   | 46                    | 151     |
| Prior service cost of defined benefit plans:              |                        |       |                       |         |
| Adjustment, net of taxes                                  | —                      | —     | (2                    | ) —     |
| Reclassification of recognized transactions, net of taxes | (1                     | ) —   | (3                    | ) —     |
| Derivative instrument:                                    |                        |       |                       |         |
| Change in fair value, net of taxes                        | —                      | (3    | ) (1                  | ) (3    |
| Reclassification of recognized transactions, net of taxes | —                      | —     | 1                     | —       |
| Other comprehensive income (loss), net of taxes           | 18                     | 123   | 127                   | 159     |
| Total comprehensive income                                | \$647                  | \$907 | \$1,778               | \$1,654 |

See accompanying notes.

## TEXAS INSTRUMENTS INCORPORATED AND SUBSIDIARIES

## Consolidated balance sheets

[Millions of dollars, except share amounts]

|   | September 30,<br>2013 | December 31,<br>2012 |
|---|-----------------------|----------------------|
| Assets  |                       |                      |
| Current assets:   |                       |                      |
| Cash and cash equivalents   | \$1,435               | \$1,416              |
| Short-term investments  | 2,158                 | 2,549                |
| Accounts receivable, net of allowances of (\$29) and (\$31)   | 1,524                 | 1,230                |
| Raw materials   | 107                   | 116                  |
| Work in process   | 954                   | 935                  |
| Finished goods  | 665                   | 706                  |
| Inventories   | 1,726                 | 1,757                |
| Deferred income taxes   | 1,039                 | 1,044                |
| Prepaid expenses and other current assets   | 219                   | 234                  |
| Total current assets  | 8,101                 | 8,230                |
| Property, plant and equipment at cost   | 6,539                 | 6,891                |
| Less accumulated depreciation   | (3,030)               | (2,979)              |
| Property, plant and equipment, net  | 3,509                 | 3,912                |
| Long-term investments   | 210                   | 215                  |
| Goodwill, net   | 4,362                 | 4,362                |
| Acquisition-related intangibles, net  | 2,305                 | 2,558                |
| Deferred income taxes   | 227                   | 280                  |
| Capitalized software licenses, net  | 139                   | 142                  |
| Overfunded retirement plans   | 119                   | 68                   |
| Other assets  | 272                   | 254                  |
| Total assets  | \$19,244              | \$20,021             |
| Liabilities and stockholders' equity  |                       |                      |
| Current liabilities:  |                       |                      |
| Current portion of long-term debt   | \$1,000               | \$1,500              |
| Accounts payable  | 426                   | 444                  |
| Accrued compensation  | 567                   | 524                  |
| Income taxes payable  | 37                    | 79                   |
| Deferred income taxes   | 2                     | 2                    |
| Accrued expenses and other liabilities  | 691                   | 881                  |
| Total current liabilities   | 2,723                 | 3,430                |
| Long-term debt  | 4,161                 | 4,186                |
| Underfunded retirement plans  | 253                   | 269                  |
| Deferred income taxes   | 564                   | 572                  |
| Deferred credits and other liabilities  | 492                   | 603                  |
| Total liabilities   | 8,193                 | 9,060                |
| Stockholders' equity:   |                       |                      |
| Preferred stock, \$25 par value. Authorized – 10,000,000 shares. Participating cumulative preferred. None issued. | —                     | —                    |
| Common stock, \$1 par value. Authorized – 2,400,000,000 shares. Shares issued – 1,740,815,939                     | 1,741                 | 1,741                |

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|  |          |           |   |
|--|----------|-----------|---|
| Paid-in capital  | 1,125    | 1,176     |   |
| Retained earnings  | 27,993   | 27,205    |   |
| Less treasury common stock at cost. Shares: September 30, 2013 – 646,252,825;<br>December 31, 2012 – 632,636,970 | (19,236  | ) (18,462 | ) |
| Accumulated other comprehensive income (loss), net of taxes  | (572     | ) (699    | ) |
| Total stockholders' equity   | 11,051   | 10,961    |   |
| Total liabilities and stockholders' equity   | \$19,244 | \$20,021  |   |

See accompanying notes.

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## TEXAS INSTRUMENTS INCORPORATED AND SUBSIDIARIES

## Consolidated statements of cash flows

[Millions of dollars]

|   | For Nine Months Ended<br>September 30, |          |   |
|---|--|----------|---|
|   | 2013                                   | 2012     |   |
| Cash flows from operating activities:             |  |          |   |
| Net income  | \$1,651                                | \$1,495  |   |
| Adjustments to net income:                        |  |          |   |
| Depreciation                                      | 666                                    | 725      |   |
| Amortization of acquisition-related intangibles   | 253                                    | 257      |   |
| Stock-based compensation                          | 221                                    | 199      |   |
| Gains on sales of assets                          | (6                                     | ) —      |   |
| Deferred income taxes                             | (9                                     | ) 136    |   |
| Gain on transfer of Japan substitutional pension  | —                                      | (144     | ) |
| Increase (decrease) from changes in:              |  |          |   |
| Accounts receivable                               | (302                                   | ) (70    | ) |
| Inventories                                       | 31                                     | (86      | ) |
| Prepaid expenses and other current assets         | (54                                    | ) 80     |   |
| Accounts payable and accrued expenses             | (297                                   | ) (123   | ) |
| Accrued compensation                              | 37                                     | (41      | ) |
| Income taxes payable                              | (29                                    | ) (177   | ) |
| Changes in funded status of retirement plans      | 82                                     | 59       |   |
| Other   | (59                                    | ) 19     |   |
| Cash flows from operating activities              | 2,185                                  | 2,329    |   |
| Cash flows from investing activities:             |  |          |   |
| Capital expenditures                              | (305                                   | ) (399   | ) |
| Proceeds from asset sales                         | 21                                     | —        |   |
| Purchases of short-term investments               | (3,177                                 | ) (2,141 | ) |
| Proceeds from short-term investments              | 3,564                                  | 1,639    |   |
| Purchases of long-term investments                | (1                                     | ) (1     | ) |
| Proceeds from long-term investments               | 18                                     | 52       |   |
| Cash flows from investing activities              | 120                                    | (850     | ) |
| Cash flows from financing activities:             |  |          |   |
| Proceeds from issuance of debt                    | 986                                    | 1,492    |   |
| Repayment of debt and commercial paper borrowings | (1,500                                 | ) (1,375 | ) |
| Dividends paid                                    | (849                                   | ) (584   | ) |
| Stock repurchases                                 | (2,134                                 | ) (1,200 | ) |
| Proceeds from common stock transactions           | 1,146                                  | 390      |   |
| Excess tax benefit from share-based payments      | 72                                     | 26       |   |
| Other   | (7                                     | ) (10    | ) |
| Cash flows from financing activities              | (2,286                                 | ) (1,261 | ) |
| Net change in cash and cash equivalents           | 19                                     | 218      |   |
| Cash and cash equivalents, beginning of period    | 1,416                                  | 992      |   |
| Cash and cash equivalents, end of period          | \$1,435                                | \$1,210  |   |

See accompanying notes.

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## TEXAS INSTRUMENTS INCORPORATED AND SUBSIDIARIES

### Notes to financial statements

#### 1. Description of business and significant accounting policies and practices

At Texas Instruments (TI), we design and make semiconductors that we sell to electronics designers and manufacturers all over the world. Effective January 1, 2013, we have two reportable segments, which are established along major categories of products as follows:

Analog - consists of the following major product lines: High Volume Analog & Logic (HVAL), Power Management (Power), High Performance Analog (HPA) and Silicon Valley Analog (SVA); and

Embedded Processing - consists of the following major product lines: Processors, Microcontrollers and Connectivity.

We report the results of our remaining business activities in Other. As previously announced, we restructured our Wireless business to focus our OMAP™ applications processors and connectivity products (formerly Wireless products) on embedded applications with long life cycles. Consistent with this restructuring, effective January 1, 2013, the Wireless segment was eliminated. Financial results for embedded OMAP applications processors and embedded connectivity products, both of which have many of the same characteristics as the products in our Embedded Processing segment, are now reported in that segment. Financial results for baseband products and Wireless products for the smartphone and consumer tablet markets, both of which are product lines that we have announced we are exiting, are included in Other and are collectively referred to as “legacy wireless products.” We also reclassified certain product lines, primarily radio frequency identification (RFID) products, from Other to Embedded Processing.

See Note 11 for the results of our business segments. On May 3, 2013, we filed a Form 8-K to update our Form 10-K for the year ended December 31, 2012, to reflect these changes. Prior period segment presentations have been recast to conform to this new reporting structure.

#### Basis of presentation

The consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the U.S. (U.S. GAAP) and on the same basis as the audited financial statements included in our annual report on Form 10-K for the year ended December 31, 2012, and as updated by the Form 8-K. The consolidated statements of income, statements of comprehensive income and statements of cash flows for the periods ended September 30, 2013 and 2012, and the balance sheet as of September 30, 2013, are not audited but reflect all adjustments that are of a normal recurring nature and are necessary for a fair statement of the results of the periods shown. Certain amounts in the prior periods' financial statements have been reclassified to conform to the current period presentation. Certain information and note disclosures normally included in annual consolidated financial statements have been omitted pursuant to the rules and regulations of the U.S. Securities and Exchange Commission. Because the consolidated interim financial statements do not include all of the information and notes required by U.S. GAAP for a complete set of financial statements, they should be read in conjunction with the audited consolidated financial statements and notes included in our annual report on Form 10-K for the year ended December 31, 2012, as updated by the Form 8-K. The results for the three- and nine-month periods are not necessarily indicative of a full year's results.

The consolidated financial statements include the accounts of all subsidiaries. All intercompany balances and transactions have been eliminated in consolidation. All dollar amounts in the financial statements and tables in these notes, except per-share amounts, are stated in millions of U.S. dollars unless otherwise indicated.

#### Earnings per share (EPS)

Unvested awards of share-based payments with rights to receive dividends or dividend equivalents, such as our restricted stock units (RSUs), are considered to be participating securities and the two-class method is used for purposes of calculating EPS. Under the two-class method, a portion of net income is allocated to these participating securities and, therefore, is excluded from the calculation of EPS allocated to common stock, as shown in the table below.



Computation and reconciliation of earnings per common share are as follows (shares in millions):

|  | For Three Months Ended<br>September 30, 2013 |        |        | For Three Months Ended<br>September 30, 2012 |        |        |
|--|--|--------|--------|--|--------|--------|
|  | Net Income                                   | Shares | EPS    | Net Income                                   | Shares | EPS    |
| Basic EPS:   |  |        |        |  |        |        |
| Net income   | \$629  |        |        | \$784  |        |        |
| Less income allocated to RSUs                                | (11  | )      |        | (15  | )      |        |
| Income allocated to common stock for basic EPS calculation   | \$618  | 1,096  | \$.56  | \$769  | 1,130  | \$.68  |
| Adjustment for dilutive shares:                              |  |        |        |  |        |        |
| Stock-based compensation plans                               |  | 15     |        |  | 11     |        |
| Diluted EPS:   |  |        |        |  |        |        |
| Net income   | \$629  |        |        | \$784  |        |        |
| Less income allocated to RSUs                                | (11  | )      |        | (14  | )      |        |
| Income allocated to common stock for diluted EPS calculation | \$618  | 1,111  | \$.56  | \$770  | 1,141  | \$.67  |
|  | For Nine Months Ended<br>September 30, 2013  |        |        | For Nine Months Ended<br>September 30, 2012  |        |        |
|  | Net Income                                   | Shares | EPS    | Net Income                                   | Shares | EPS    |
| Basic EPS:   |  |        |        |  |        |        |
| Net income   | \$1,651                                      |        |        | \$1,495                                      |        |        |
| Less income allocated to RSUs                                | (29  | )      |        | (27  | )      |        |
| Income allocated to common stock for basic EPS calculation   | \$1,622                                      | 1,102  | \$1.47 | \$1,468                                      | 1,138  | \$1.29 |
| Adjustment for dilutive shares:                              |  |        |        |  |        |        |
| Stock-based compensation plans                               |  | 15     |        |  | 15     |        |
| Diluted EPS:   |  |        |        |  |        |        |
| Net income   | \$1,651                                      |        |        | \$1,495                                      |        |        |
| Less income allocated to RSUs                                | (28  | )      |        | (27  | )      |        |
| Income allocated to common stock for diluted EPS calculation | \$1,623                                      | 1,117  | \$1.45 | \$1,468                                      | 1,153  | \$1.27 |

There were no potentially dilutive securities excluded from the computation of diluted earnings per common share during the third quarter and the first nine months of 2013. Potentially dilutive securities representing 65 million shares of common stock that were outstanding during both the third quarter and the first nine months of 2012 were excluded from the computation of diluted earnings per common share for these periods because their effect would have been anti-dilutive.

#### Derivatives and hedging

In connection with the issuance of variable-rate long-term debt in May 2011, we entered into an interest rate swap designated as a hedge of the variability of cash flows related to interest payments. Gains and losses from changes in the fair value of the interest rate swap were credited or charged to Accumulated other comprehensive income (loss), net of taxes (AOCI). In connection with the repayment of this long-term debt in the second quarter of 2013, this interest rate swap was settled for no gain or loss. In association with the issuance of long-term debt, we use financial

derivatives such as treasury rate lock agreements, the results of which have not been material.

We also use derivative financial instruments to manage exposure to foreign exchange risk. These instruments are primarily forward foreign currency exchange contracts that are used as economic hedges to reduce the earnings impact exchange rate fluctuations may have on our non-U.S. dollar net balance sheet exposures. Gains and losses from changes in the fair value of these forward foreign currency exchange contracts are credited or charged to OI&E. We do not apply hedge accounting to our foreign currency derivative instruments.

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We do not use derivatives for speculative or trading purposes.

#### Fair values of financial instruments

The fair values of our derivative financial instruments were not significant at September 30, 2013. Our investments in cash equivalents, short-term investments and certain long-term investments, as well as our deferred compensation liabilities, are carried at fair value and are discussed in Note 5. The carrying values for other current financial assets and liabilities, such as accounts receivable and accounts payable, approximate fair value due to the short maturity of such instruments. The carrying value of our long-term debt approximates the fair value as measured using broker-dealer quotes, which are based on Level 2 inputs. See Note 5 for the definition of Level 2 inputs.

#### Changes in Accounting Standards

In January 2013, the FASB issued Accounting Standards Update (ASU) No. 2013-01, Balance Sheet (Topic 210): Clarifying the Scope of Disclosures about Offsetting Assets and Liabilities. This standard clarifies that a previously issued standard on disclosure requirements of offsetting (or netting) financial instruments applies only to derivatives, repurchase agreements and certain securities lending transactions. The required disclosures are both gross and net information about instruments and transactions eligible for offset in the statement of financial position and instruments and transactions subject to an agreement similar to a master netting arrangement. This standard is effective as of the first quarter of 2013 and did not have a material impact on our financial disclosures because the derivatives to which it applies are not significant.

In February 2013, the FASB issued ASU No. 2013-02, Comprehensive Income (Topic 220): Reporting of Amounts Reclassified Out of Accumulated Other Comprehensive Income. This standard requires an entity to disclose information about amounts reclassified out of AOCI by component and by statement of income line item. This standard is effective as of the first quarter of 2013 and is applied prospectively. See Note 10 for the required disclosure.

#### 2. Acquisition-related charges

We completed the acquisition of National Semiconductor Corporation (National) in September 2011. Various costs incurred as a result of that acquisition are included in Other, consistent with how management measures the performance of its segments. These total acquisition-related charges are as follows:

|  | For Three Months Ended<br>September 30, |       | For Nine Months Ended<br>September 30, |       |
|--|---|-------|--|-------|
|  | 2013                                    | 2012  | 2013                                   | 2012  |
| Acquisition charges:                             |   |       |  |       |
| Amortization of intangible assets                | \$81                                    | \$81  | \$244                                  | \$244 |
| Retention bonuses                                | 2                                       | 5     | 5                                      | 53    |
| Severance and other benefits                     | —                                       | 3     | —                                      | 17    |
| Stock-based compensation                         | 3                                       | 4     | 8                                      | 14    |
| Transaction and other costs                      | —                                       | 13    | —                                      | 35    |
| As recorded in Acquisition charges               | 86                                      | 106   | 257                                    | 363   |
| Distributor contract termination recorded in COR | —                                       | —     | —                                      | 21    |
| Total acquisition-related costs                  | \$86                                    | \$106 | \$257                                  | \$384 |

The amount of recognized amortization of acquired intangible assets resulting from the National acquisition is based on estimated useful lives varying between two and ten years. See Note 6 for additional information.

Retention bonuses reflect amounts already or expected to be paid to former National employees who fulfill agreed-upon service period obligations and are recognized ratably over the required service period.

Severance and other benefits costs were for former National employees who were terminated after the closing date. About 350 jobs were eliminated by the end of 2012 as a result of redundancies and cost efficiency measures. As of September 30, 2013, a total of \$86 million in cumulative charges have been recognized, of which \$82 million has been paid.

Stock-based compensation was recognized for the accelerated vesting of equity awards upon the termination of employees, with additional compensation being recognized over the applicable vesting period for the remaining grantees.

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Transaction and other costs include various expenses incurred in connection with the National acquisition.

In 2011, we discontinued using one of National's distributors. We acquired the distributor's inventory at fair value, resulting in an incremental charge of \$21 million to COR upon sale of the inventory in 2012.

### 3. Restructuring charges/other

Restructuring charges/other is included in Other and is comprised of the following components:

|   | For Three Months Ended<br>September 30, |        | For Nine Months Ended<br>September 30, |         | Cumulative<br>Since Actions<br>Initiated |
|---|---|--------|--|---------|--|
|   | 2013                                    | 2012   | 2013                                   | 2012    |  |
| Restructuring charges:                              |   |        |  |         |  |
| 2012 Wireless action                                |   |        |  |         |  |
| Severance and benefits cost                         | \$—                                     | \$—    | \$30                                   | \$—     | \$275                                    |
| Accelerated depreciation                            | —                                       | —      | 6                                      | —       | 9  |
| Other exit costs                                    | —                                       | —      | 2                                      | —       | 105                                      |
|   | —                                       | —      | 38                                     | —       | 389                                      |
| 2011 actions  |   |        |  |         |  |
| Severance and benefits cost                         | 2                                       | 1      | 3                                      | 3       | 116                                      |
| Accelerated depreciation                            | —                                       | 4      | 5                                      | 13      | 28                                       |
| Other exit costs                                    | 14                                      | 9      | 18                                     | 21      | 43                                       |
|   | 16                                      | 14     | 26                                     | 37      | 187                                      |
| Total restructuring charges                         | 16                                      | 14     | 64                                     | 37      | \$576                                    |
| Other:  |   |        |  |         |  |
| Gain on technology transfer                         | —                                       | —      | (315                                   | ) —     |  |
| Gain on transfer of Japan<br>substitutional pension | —                                       | (144   | ) —                                    | (144    | )  |
| Other   | —                                       | 8      | —                                      | 8       |  |
| Total Restructuring charges/other                   | \$16                                    | \$(122 | ) \$(251                               | ) \$(99 | )  |

Restructuring actions related to the acquisition of National are discussed in Note 2 and are reflected on the Acquisition charges line of our Consolidated statements of income.

#### 2012 Wireless action

In November 2012, we announced an action concerning our former Wireless segment that, when complete, is expected to reduce annualized expenses by about \$450 million and will focus our investments on embedded markets with greater potential for sustainable growth. This action will be substantially complete by the end of 2013, eliminating about 1,700 jobs worldwide. As of September 30, 2013, \$124 million has been paid to terminated employees for severance and benefits related to this action.

#### 2011 actions

Beginning in the fourth quarter of 2011, we recognized restructuring charges associated with the closure of two older semiconductor manufacturing facilities in Houston, Texas, and Hiji, Japan, in 2013. This action will be substantially complete by the end of 2013. As of September 30, 2013, about \$90 million has been paid to terminated employees for severance and benefits related to this action.





The table below reflects the changes in accrued restructuring balances associated with these actions:

|   | 2012 Wireless Action   |               | 2011 Actions           |               | Prior Actions          |               | Total  |
|---|------------------------|---------------|------------------------|---------------|------------------------|---------------|--------|
|   | Severance and Benefits | Other Charges | Severance and Benefits | Other Charges | Severance and Benefits | Other Charges |        |
| Remaining accrual at December 31, 2012  | \$241                  | \$—           | \$94                   | \$3           | \$5                    | \$6           | \$349  |
| Restructuring charges                   | 30                     | 8             | 3                      | 23            | —                      | —             | 64     |
| Non-cash items (a)                      | —                      | (6 )          | (1 )                   | (11 )         | —                      | —             | (18 )  |
| Payments                                | (119 )                 | (2 )          | (79 )                  | (13 )         | (4 )                   | —             | (217 ) |
| Remaining accrual at September 30, 2013 | \$152                  | \$—           | \$17                   | \$2           | \$1                    | \$6           | \$178  |

(a) Reflects charges for stock-based compensation, impacts of postretirement benefit plans and accelerated depreciation.

The accrual balances above are primarily a component of Accrued expenses and other liabilities or Deferred credits and other liabilities on our Consolidated balance sheets, depending on the expected timing of payment.

#### Other

##### Gain on technology transfer

During the second quarter of 2013, we entered into an agreement to transfer wireless connectivity technology to a customer. This technology was associated with the former Wireless business that we have previously announced we are exiting. As a result, we recognized a gain of \$315 million.

##### Gain on transfer of Japan substitutional pension

During the third quarter of 2012, we transferred the obligations and assets of the substitutional portion of our Japan pension plan to the government of Japan, resulting in a net gain of \$144 million. See Note 7 for additional details.

#### 4. Income taxes

Federal income taxes for the interim periods presented have been included in the accompanying financial statements on the basis of an estimated annual effective tax rate. As of September 30, 2013, the estimated annual effective tax rate for 2013 is about 24 percent, which differs from the 35 percent statutory corporate tax rate due to lower statutory tax rates applicable to our operations in many of the jurisdictions in which we operate and from U.S. tax benefits. These lower tax rates are generally statutory in nature, without expiration and available to companies that operate in those taxing jurisdictions. The tax provision for the nine months ended September 30, 2013 includes a \$65 million discrete tax benefit from the reinstatement in the first quarter of 2013 of the federal research tax credit retroactive to the beginning of 2012.

#### 5. Valuation of debt and equity investments and certain liabilities

##### Debt and equity investments

We classify our investments as available for sale, trading, equity method or cost method. Most of our investments are classified as available for sale.

Available-for-sale and trading securities are stated at fair value, which is generally based on market prices, broker quotes or, when necessary, financial models (see fair-value discussion below). Unrealized gains and losses on available-for-sale securities are recorded as an increase or decrease, net of taxes, in AOCI on our Consolidated balance sheets. We record other-than-temporary impairments on available-for-sale securities in OI&E in our Consolidated statements of income.

We classify certain mutual funds as trading securities. These mutual funds hold a variety of debt and equity investments intended to generate returns that offset changes in certain deferred compensation liabilities. We record changes in the fair value of these mutual funds and the related deferred compensation liabilities in SG&A.

Our other investments are not measured at fair value but are accounted for using either the equity method or cost method. These investments consist of interests in venture capital funds and other non-marketable equity securities. Gains and losses from equity-method investments are reflected in OI&E based on our ownership share of the investee's financial results. Gains and losses on cost-method investments are recorded in OI&E when realized or when an impairment of the investment's value is warranted based on our assessment of the recoverability of each investment.

Details of our investments are as follows:

|   | September 30, 2013              |                           |                          | December 31, 2012               |                           |                          |
|---|---------------------------------|---------------------------|--------------------------|---------------------------------|---------------------------|--------------------------|
|   | Cash and<br>Cash<br>Equivalents | Short-term<br>Investments | Long-term<br>Investments | Cash and<br>Cash<br>Equivalents | Short-term<br>Investments | Long-term<br>Investments |
| Measured at fair value:                           |                                 |                           |                          |                                 |                           |                          |
| Available-for-sale securities                     |                                 |                           |                          |                                 |                           |                          |
| Money market funds                                | \$582                           | \$—                       | \$—                      | \$211                           | \$—                       | \$—                      |
| Corporate obligations                             | 75                              | 317                       | —                        | 188                             | 325                       | —                        |
| U.S. Government agency and<br>Treasury securities | 680                             | 1,841                     | —                        | 795                             | 2,224                     | —                        |
| Trading securities                                |                                 |                           |                          |                                 |                           |                          |
| Mutual funds                                      | —                               | —                         | 168                      | —                               | —                         | 159                      |
| Total   | \$1,337                         | \$2,158                   | \$168                    | \$1,194                         | \$2,549                   | \$159                    |
| Other measurement basis:                          |                                 |                           |                          |                                 |                           |                          |
| Equity-method investments                         | \$—                             | \$—                       | \$24                     | \$—                             | \$—                       | \$34                     |
| Cost-method investments                           | —                               | —                         | 18                       | —                               | —                         | 22                       |
| Cash on hand                                      | 98                              | —                         | —                        | 222                             | —                         | —                        |
| Total   | \$1,435                         | \$2,158                   | \$210                    | \$1,416                         | \$2,549                   | \$215                    |

As of September 30, 2013, and December 31, 2012, we had no significant unrealized gains or losses associated with our available-for-sale investments. For the three months and nine months ended September 30, 2013 and 2012, we did not recognize in earnings any credit losses related to these investments.

For the nine months ended September 30, 2013 and 2012, the proceeds from sales, redemptions and maturities of short-term available-for-sale investments were \$3.56 billion and \$1.64 billion, respectively. Gross realized gains and losses from these sales were not significant.

The following table presents the aggregate maturities of investments in debt securities classified as available for sale at September 30, 2013:

| Due                | Fair Value |
|--------------------|------------|
| One year or less   | \$3,230    |
| One to three years | 265        |

#### Fair-value considerations

We measure and report certain financial assets and liabilities at fair value on a recurring basis. Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date.

The three-level hierarchy discussed below indicates the extent and level of judgment used to estimate fair-value measurements.

Level 1 — Uses unadjusted quoted prices that are available in active markets for identical assets or liabilities as of the reporting date.

Level 2 — Uses inputs other than Level 1 that are either directly or indirectly observable as of the reporting date through correlation with market data, including quoted prices for similar assets and liabilities in active markets and quoted prices in markets that are not active. Level 2 also includes assets and liabilities that are valued using models or other pricing methodologies that do not require significant judgment since the input assumptions used in the models, such as interest rates and volatility factors, are corroborated by readily observable data. Our Level 2 assets consist of corporate obligations and some U.S. government agency and Treasury securities. We utilize a third-party data service to provide Level 2

valuations, verifying these valuations for reasonableness relative to unadjusted quotes obtained from brokers or dealers based on observable prices for similar assets in active markets.

Level 3 — Uses inputs that are unobservable, supported by little or no market activity and reflect the use of significant management judgment. These values are generally determined using pricing models that utilize management estimates of market participant assumptions.

The following are our assets and liabilities that were accounted for at fair value on a recurring basis as of September 30, 2013, and December 31, 2012. For these periods, we had no Level 3 assets or liabilities. These tables do not include cash on hand, assets held by our postretirement plans, or assets and liabilities that are measured at historical cost or any basis other than fair value.

|  | Fair Value<br>September 30,<br>2013 | Level 1 | Level 2 |
|--|-------------------------------------|---------|---------|
| Assets:  |                                     |         |         |
| Money market funds                             | \$582                               | \$582   | \$—     |
| Corporate obligations                          | 392                                 | —       | 392     |
| U.S. Government agency and Treasury securities | 2,521                               | 1,667   | 854     |
| Mutual funds                                   | 168                                 | 168     | —       |
| Total assets                                   | \$3,663                             | \$2,417 | \$1,246 |

|                       |       |       |     |
|-----------------------|-------|-------|-----|
| Liabilities:          |       |       |     |
| Deferred compensation | \$186 | \$186 | \$— |
| Total liabilities     | \$186 | \$186 | \$— |

|  | Fair Value<br>December 31,<br>2012 | Level 1 | Level 2 |
|--|------------------------------------|---------|---------|
| Assets:  |                                    |         |         |
| Money market funds                             | \$211                              | \$211   | \$—     |
| Corporate obligations                          | 513                                | —       | 513     |
| U.S. Government agency and Treasury securities | 3,019                              | 1,145   | 1,874   |
| Mutual funds                                   | 159                                | 159     | —       |
| Total assets                                   | \$3,902                            | \$1,515 | \$2,387 |

|                       |       |       |     |
|-----------------------|-------|-------|-----|
| Liabilities:          |       |       |     |
| Deferred compensation | \$174 | \$174 | \$— |
| Total liabilities     | \$174 | \$174 | \$— |

The following table summarizes the change in the fair values for Level 3 assets:

|  |                                       |   |
|--|---------------------------------------|---|
| Changes in fair value during the period (pre-tax): | Level 3<br>Auction-rate<br>Securities |   |
| Balance, December 31, 2011                         | \$134                                 |   |
| Change in unrealized loss – included in AOCI       | 13                                    |   |
| Redemptions  | (84                                   | ) |
| Sales  | (63                                   | ) |

Balance, September 30, 2012

\$—

We had no Level 3 assets as of either September 30, 2013, or December 31, 2012.

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## 6. Goodwill and acquisition-related intangibles

Goodwill was \$4.362 billion net of accumulated impairment of \$90 million as of September 30, 2013, and December 31, 2012. There was no impairment of goodwill during the three months and nine months ended September 30, 2013. The following table shows the components of acquisition-related intangible assets as of September 30, 2013, and December 31, 2012:

| Acquisition-related Intangibles | Amortization Period (Years) | September 30, 2013    |                          |         | December 31, 2012     |                          |         |
|---------------------------------|-----------------------------|-----------------------|--------------------------|---------|-----------------------|--------------------------|---------|
|                                 |                             | Gross Carrying Amount | Accumulated Amortization | Net     | Gross Carrying Amount | Accumulated Amortization | Net     |
| Developed technology            | 5 - 10                      | \$2,153               | \$469                    | \$1,684 | \$2,145               | \$312                    | \$1,833 |
| Customer relationships          | 5 - 8                       | 820                   | 213                      | 607     | 821                   | 137                      | 684     |
| Other intangibles               | 5                           | 5                     | 3                        | 2       | 46                    | 36                       | 10      |
| In-process R&D                  | (a)                         | 12                    | n/a                      | 12      | 31                    | n/a                      | 31      |
| Total                           |                             | \$2,990               | \$685                    | \$2,305 | \$3,043               | \$485                    | \$2,558 |

(a) In-process R&D is not amortized until the associated project has been successfully completed, at which point it would be reclassified to developed technology. Alternatively, if the associated project is determined not to be viable, it will be expensed.

Amortization of acquisition-related intangibles was \$83 million and \$86 million for the three months (\$253 million and \$257 million for the nine months) ended September 30, 2013 and 2012.

## 7. Postretirement benefit plans

Components of net periodic employee benefit cost are as follows:

|  | U.S. Defined Benefit |      | U.S. Retiree Health Care |      | Non-U.S. Defined Benefit |         |
|--|----------------------|------|--------------------------|------|--------------------------|---------|
|  | 2013                 | 2012 | 2013                     | 2012 | 2013                     | 2012    |
| For Three Months Ended September 30                  |                      |      |                          |      |                          |         |
| Service cost   | \$6                  | \$6  | \$1                      | \$1  | \$9                      | \$10    |
| Interest cost  | 12                   | 11   | 5                        | 6    | 15                       | 19      |
| Expected return on plan assets                       | (11)                 | (12) | (6)                      | (6)  | (17)                     | (20)    |
| Amortization of prior service cost (credit)          | —                    | —    | 1                        | 1    | (1)                      | (1)     |
| Recognized net actuarial loss                        | 5                    | 4    | 3                        | 4    | 7                        | 10      |
| Net periodic benefit cost                            | 12                   | 9    | 4                        | 6    | 13                       | 18      |
| Settlement loss                                      | 5                    | —    | —                        | —    | 4                        | 193     |
| Curtailment gain                                     | —                    | —    | —                        | —    | (2)                      | —       |
| Special termination benefit gain                     | —                    | —    | —                        | —    | —                        | (337)   |
| Total, including other postretirement losses (gains) | \$17                 | \$9  | \$4                      | \$6  | \$15                     | \$(126) |
|  |                      |      |                          |      |                          |         |
| For Nine Months Ended September 30                   |                      |      |                          |      |                          |         |
| Service cost   | \$20                 | \$18 | \$4                      | \$4  | \$29                     | \$29    |
| Interest cost  | 33                   | 33   | 15                       | 18   | 46                       | 58      |
| Expected return on plan assets                       | (36)                 | (37) | (18)                     | (18) | (50)                     | (59)    |
| Amortization of prior service cost (credit)          | —                    | 1    | 3                        | 3    | (3)                      | (3)     |
| Recognized net actuarial loss                        | 16                   | 12   | 9                        | 10   | 24                       | 34      |
| Net periodic benefit cost                            | 33                   | 27   | 13                       | 17   | 46                       | 59      |

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|  |      |      |      |      |      |       |   |
|--|------|------|------|------|------|-------|---|
| Settlement loss                                      | 18   | —    | —    | —    | 4    | 193   |   |
| Curtailement gain                                    | —    | —    | —    | (1   | ) (5 | ) —   |   |
| Special termination benefit gain                     | —    | (2   | ) —  | —    | —    | (337  | ) |
| Total, including other postretirement losses (gains) | \$51 | \$25 | \$13 | \$16 | \$45 | \$(85 | ) |

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In the nine months ended September 30, 2013, we remeasured our U.S. and Japan defined benefit plans, as a result of increased retirement activities. These remeasurements resulted in net actuarial gains on a pre-tax basis in Other comprehensive income of \$14 million and \$79 million for the three and nine months ended September 30, 2013, respectively. Of these gains, \$7 million related to the U.S. plans and \$7 million was for the Japan plan in the three-month period; \$24 million related to the U.S. plans and \$55 million was for the Japan plan in the nine-month period. From these remeasurements, we recognized settlement losses on the U.S. and Japan plans, as well as curtailment gains on the Japan plan. These are detailed in the above table. The effects of these remeasurements, and the effects of foreign currency exchange rate fluctuations, are reflected in Overfunded retirement plans and Underfunded retirement plans on our Consolidated balance sheets.

#### Transfer of Japan substitutional pension

In Japan, we maintained employee pension fund plans (EPFs) pursuant to the Japanese Welfare Pension Insurance Law (JWPIL). An EPF consists of two portions: a substitutional portion based on JWPIL-determined minimum old-age pension benefits similar to Social Security benefits in the United States; and a corporate portion established at the discretion of each employer. Employers and employees are exempt from contributing to the Japanese Pension Insurance (JPI) if the substitutional portion is funded by an EPF.

The JWPIL was amended to permit each EPF to separate the substitutional portion and transfer those obligations and related assets to the government of Japan. After such a transfer, the employer is required to contribute periodically to JPI, and the government of Japan is responsible for future benefit payments relating to the substitutional portion.

During the third quarter of 2012, our EPF received final approval for such a separation and transferred the obligations and assets of its substitutional portion to the government of Japan. On a pre-tax basis, this resulted in a net gain of \$144 million recorded in Restructuring charges/other on our Consolidated statements of income and included in Other. This net gain of \$144 million consisted of two parts - a gain of \$337 million, representing the difference between the fair values of the obligations settled (\$533 million) and the assets transferred from the pension trust to the government of Japan (\$196 million), offset by a settlement loss of \$193 million related to the recognition of previously unrecognized actuarial losses included in AOCI.

#### 8. Debt and lines of credit

##### Short-term borrowings

We maintain a line of credit to support commercial paper borrowings, if any, and to provide additional liquidity through bank loans. As of September 30, 2013, we have a variable-rate revolving credit facility from a consortium of investment-grade banks that allows us to borrow up to \$2 billion through March 2018. The interest rate on borrowings under this credit facility, if drawn, is indexed to the applicable London Interbank Offered Rate (LIBOR). As of September 30, 2013, our credit facility was undrawn and we had no commercial paper outstanding.

##### Long-term debt

In May 2013, we issued an aggregate principal amount of \$1.0 billion of fixed-rate long-term debt, with \$500 million due in 2018 and \$500 million due in 2023. The proceeds of the offering were \$986 million net of the original issuance discount and were used toward the repayment of \$1.5 billion of maturing debt, including floating-rate notes. In connection with this repayment, we settled the associated interest rate swap. We also incurred \$6 million of issuance and other related costs that are being amortized to Interest and debt expense over the term of the debt.

In August 2012, we issued an aggregate principal amount of \$1.5 billion of fixed-rate long-term debt, with \$750 million due in 2015 and \$750 million due in 2019. The proceeds of the offering were \$1.492 billion, net of the original issuance discount. We also incurred \$7 million of issuance costs that are being amortized to Interest and debt expense over the term of the debt.



The following table summarizes the total long-term debt outstanding as of September 30, 2013 and December 31, 2012:

|   | September 30,<br>2013 | December 31,<br>2012 |
|---|-----------------------|----------------------|
| Floating-rate notes due 2013 (swapped to a 0.922% fixed rate) | \$—                   | \$1,000              |
| Notes due 2013 at 0.875%                                      | —                     | 500                  |
| Notes due 2014 at 1.375%                                      | 1,000                 | 1,000                |
| Notes due 2015 at 3.95% (assumed with National acquisition)   | 250                   | 250                  |
| Notes due 2015 at 0.45%                                       | 750                   | 750                  |
| Notes due 2016 at 2.375%                                      | 1,000                 | 1,000                |
| Notes due 2017 at 6.60% (assumed with National acquisition)   | 375                   | 375                  |
| Notes due 2018 at 1.00%                                       | 500                   | —                    |
| Notes due 2019 at 1.65%                                       | 750                   | 750                  |
| Notes due 2023 at 2.25%                                       | 500                   | —                    |
|   | 5,125                 | 5,625                |
| Add net unamortized premium                                   | 36                    | 61                   |
| Less current portion of long-term debt                        | (1,000                | ) (1,500             |
| Total long-term debt  | \$4,161               | \$4,186              |

Interest incurred on debt, net of the amortization of the debt premium and other debt issuance costs, was \$24 million and \$21 million for the three months (\$71 million and \$62 million for the nine months) ended September 30, 2013 and 2012, respectively. Capitalized interest was not material.

#### 9. Contingencies

##### Indemnification guarantees

We routinely sell products with an intellectual property indemnification included in the terms of sale. Historically, we have had only minimal, infrequent losses associated with these indemnities. Consequently, we cannot reasonably estimate or accrue for any future liabilities that may result.

##### Warranty costs/product liabilities

We accrue for known product-related claims if a loss is probable and can be reasonably estimated. During the periods presented, there have been no material accruals or payments regarding product warranty or product liability. Historically, we have experienced a low rate of payments on product claims. Although we cannot predict the likelihood or amount of any future claims, we do not believe they will have a material adverse effect on our financial condition, results of operations or liquidity. Consistent with general industry practice, we enter into formal contracts with certain customers that include negotiated warranty remedies. Typically, under these agreements our warranty for semiconductor products includes: three years of coverage; an obligation to repair, replace or refund; and a maximum payment obligation tied to the price paid for our products. In some cases, product claims may exceed the price of our products.

##### General

We are subject to various legal and administrative proceedings. Although it is not possible to predict the outcome of these matters, we believe that the results of these proceedings will not have a material adverse effect on our financial condition, results of operations or liquidity. From time to time, we also negotiate contingent consideration payment arrangements associated with certain acquisitions, which are recorded at fair value.

##### Discontinued operations indemnity

In connection with the 2006 sale of the former Sensors & Controls (S&C) business, we have agreed to indemnify Sensata Technologies, Inc., for specified litigation matters and certain liabilities, including environmental liabilities.

In a settlement with a third party, we have agreed to indemnify that party for certain events relating to S&C products, which events we consider remote. We believe our total remaining potential exposure from both of these indemnities will not exceed \$200 million. As of September 30, 2013, we believe future payments related to these indemnity obligations will not have a material effect on our financial condition, results of operations or liquidity.

## 10. Supplemental financial information

In conformance with ASU No. 2013-02, Comprehensive Income (Topic 220): Reporting of Amounts Reclassified Out of Accumulated Other Comprehensive Income, the table below details where reclassifications of recognized transactions out of AOCI are recorded on the Consolidated statements of income.

| Details About AOCI Components                             | For Three Months Ended<br>September 30, |       | For Nine Months Ended<br>September 30, |       | Related Statement of<br>Income Line |
|---|---|-------|--|-------|-------------------------------------|
|   | 2013                                    | 2012  | 2013                                   | 2012  |                                     |
| Net actuarial gains (losses) of defined benefit plans (a) | \$24                                    | \$211 | \$71                                   | \$249 | Pension expense (b)                 |
| Taxes   | (11                                     | ) (83 | ) (25                                  | ) (98 | ) Provision for income taxes        |
| Reclassification of recognized transactions, net of taxes | \$13                                    | \$128 | \$46                                   | \$151 | Net income                          |
| Prior service cost of defined benefit plans (c)           | \$(2                                    | ) \$— | \$(5                                   | ) \$— | Pension expense (b)                 |
| Taxes   | 1                                       | —     | 2                                      | —     | Provision for income taxes          |
| Reclassification of recognized transactions, net of taxes | \$(1                                    | ) \$— | \$(3                                   | ) \$— | Net income                          |
| Derivative instruments                                    | \$—                                     | \$—   | \$2                                    | \$—   | Interest and debt expense           |
| Taxes   | —                                       | —     | (1                                     | ) —   | Provision for income taxes          |
| Reclassification of recognized transactions, net of taxes | \$—                                     | \$—   | \$1                                    | \$—   | Net income                          |

(a) Net actuarial gains (losses) of defined benefit plans is equal to the sum of Recognized net actuarial loss and Settlement loss as detailed in Note 7. This also includes the settlement loss of \$193 million associated with the transfer of the Japan substitutional pension in 2012.

(b) This AOCI component is included in the computation of total employee benefit cost which is allocated to COR, R&D, SG&A and Restructuring charges/other in the Consolidated statements of income.

(c) Prior service cost of defined benefit plans is equal to the sum of Amortization of prior service cost (credit) and Curtailment gain as detailed in Note 7.

## 11. Segment data

See Note 1 for a detailed description of our reportable segments. Prior period segment presentations have been revised to conform to our new reporting structure.

| Segment Revenue:    | For Three Months Ended<br>September 30, |         | For Nine Months Ended<br>September 30, |         |
|---------------------|---|---------|--|---------|
|                     | 2013                                    | 2012    | 2013                                   | 2012    |
| Analog              | \$1,931                                 | \$1,843 | \$5,325                                | \$5,329 |
| Embedded Processing | 668                                     | 591     | 1,846                                  | 1,711   |
| Other               | 645                                     | 956     | 2,006                                  | 2,806   |
| Total revenue       | \$3,244                                 | \$3,390 | \$9,177                                | \$9,846 |

  

|  | For Three Months Ended<br>September 30, |      | For Nine Months Ended<br>September 30, |      |
|--|---|------|--|------|
|  | 2013                                    | 2012 | 2013                                   | 2012 |
|  |   |      |  |      |

Segment Operating Profit:

|                        |       |       |         |         |
|------------------------|-------|-------|---------|---------|
| Analog                 | \$583 | \$460 | \$1,298 | \$1,231 |
| Embedded Processing    | 83    | 60    | 144     | 147     |
| Other                  | 178   | 320   | 703     | 456     |
| Total operating profit | \$844 | \$840 | \$2,145 | \$1,834 |

We use centralized manufacturing and facilities organizations to provide products and support to our operating segments.

Costs incurred by these organizations, including depreciation, are charged to the segments on a per-unit basis. Consequently, depreciation expense is not an independently identifiable component within the segments' results and therefore is not provided.

12. Dividends

In September 2013, we announced a 7 percent increase in our quarterly cash dividend rate, which increased from \$0.28 to \$0.30 per share. This dividend will be payable November 18, 2013, to stockholders of record on October 31, 2013.

## ITEM 2. Management's discussion and analysis of financial condition and results of operations

The following should be read in conjunction with the financial statements and the related notes that appear elsewhere in this document. All dollar amounts in the tables in this discussion are stated in millions of U.S. dollars, except per-share amounts.

### Overview

We design and make semiconductors that we sell to electronics designers and manufacturers all over the world. We began operations in 1930. We are incorporated in Delaware, headquartered in Dallas, Texas, and have design, manufacturing or sales operations in more than 35 countries. We have three segments: Analog, Embedded Processing and Other. We expect Analog and Embedded Processing to be our primary growth engines in the years ahead, and we therefore focus our resources on these segments.

We were the world's fourth largest semiconductor company in 2012 as measured by revenue, according to industry data from an external source.

### Product information

Semiconductors are electronic components that serve as the building blocks inside modern electronic systems and equipment. Semiconductors come in two basic forms: individual transistors and integrated circuits (generally known as "chips") that combine multiple transistors on a single piece of material to form a complete electronic circuit. Our products, more than 100,000 orderable parts, are integrated circuits that are used to accomplish many different things, such as converting and amplifying signals, interfacing with other devices, managing and distributing power, processing data, canceling noise and improving signal resolution. This broad portfolio includes products that are integral to almost all electronic equipment.

We sell catalog and, to a lesser extent, custom semiconductor products. Catalog products are designed for use by many customers and/or many applications and are sold through both distribution and direct channels. The majority of our catalog products are proprietary, but some are commodity products. The life cycles of catalog products generally span multiple years, with some products continuing to sell for decades after their initial release. Custom products are designed for a specific customer for a specific application, are sold only to that customer and are typically sold directly to the customer. The life cycles of custom products are generally determined by end-equipment upgrade cycles and can be as short as 12 to 24 months.

Our segments represent groups of similar products that are combined on the basis of similar design and development requirements, product characteristics, manufacturing processes and distribution channels, and how management allocates resources and measures results. Additional information regarding each segment's products follows.

#### Analog

Analog semiconductors change real-world signals - such as sound, temperature, pressure or images - by conditioning them, amplifying them and often converting them to a stream of digital data that can be processed by other semiconductors, such as digital signal processors (DSPs). Analog semiconductors are also used to manage power in every electronic device, whether plugged into a wall or running off a battery. We estimate that we sell our Analog products to more than 100,000 customers. These sales generated about 55 percent of our revenue in 2012. According to external sources, the worldwide market for analog semiconductors was about \$39 billion in 2012. Our Analog segment's revenue in 2012 was about \$7.0 billion, or about 18 percent of this fragmented market, the leading position. We believe that we are well positioned to increase our market share over time.

Our Analog segment includes the following major product lines: High Volume Analog & Logic (HVAL), Power Management (Power), High Performance Analog (HPA) and Silicon Valley Analog (SVA).

**HVAL products:** These include both high-volume analog and logic products. High-volume analog includes integrated analog products for specific applications, including custom products. End markets for high-volume analog products include communications, automotive, computing and many consumer electronics products. Logic includes some



commodity products marketed to many different customers for many different applications.

Power products: These include both catalog and application-specific products that help customers manage power in any type of electronic system. We design and manufacture power management semiconductors for both portable devices (battery-powered

devices, such as handheld consumer electronics, laptop computers and cordless power tools) and line-powered systems (products that require an external electrical source, such as computers, digital TVs, wireless basestations and high-voltage industrial equipment).

HPA products: These include catalog analog products, such as amplifiers, data converters and interface semiconductors, that we market to many different customers who use them in manufacturing a wide range of products sold in many end markets, including the industrial, communications, computing and consumer electronics markets.

HPA products generally have long life cycles, often more than 10 years.

SVA products: These include power management, data converter, interface and operational amplifier catalog analog products. This portfolio of thousands of products is marketed to many different customers who use them in manufacturing a wide range of products sold in many end markets. SVA products generally have long life cycles, often more than 10 years.

#### Embedded Processing

Embedded Processing products are the “brains” of many electronic devices. Compared with general purpose microprocessors that perform many different tasks, embedded processors are designed to handle specific tasks and can be optimized for various combinations of performance, power and cost, depending on the application. The devices vary from simple, low-cost products used in electric toothbrushes to highly specialized, complex devices used in wireless basestation communications infrastructure equipment. Our Embedded Processing products are used in many end markets, particularly industrial, automotive and communications infrastructure.

An important characteristic of our Embedded Processing products is that our customers often invest their own research and development (R&D) to write software that operates on our products. This investment tends to increase the length of our customer relationships because many customers prefer to re-use software from one product generation to the next.

Sales of Embedded Processing products generated about 18 percent of our revenue in 2012. According to external sources, the worldwide market for embedded processors was about \$17 billion in 2012. Our Embedded Processing segment's revenue in 2012 was about \$2.3 billion. This was the number two position and represented about 13 percent of this fragmented market. We believe we are well positioned to increase our market share over time.

Our Embedded Processing segment includes the following major product lines: Processors, Microcontrollers and Connectivity.

Processor products: These include DSPs and applications processors. DSPs perform mathematical computations almost instantaneously to process or improve digital data. Applications processors like our embedded OMAP™ and Sitara™ products run an industry-standard operating system and perform multiple complex tasks, often communicating with other systems.

Microcontroller products: Microcontrollers are self-contained systems with a processor core, memory and peripherals that are designed to control a set of specific tasks for electronic equipment. Microcontrollers tend to have minimal requirements for memory and program length, with no operating system and low software complexity. Analog components that control or interface with sensors and other systems are often integrated into microcontrollers.

Microcontroller products also include radio frequency identification (RFID) products, which are frequently used in automotive applications and sold along with our microcontroller products.

Connectivity products: Connectivity products enable electronic devices to seamlessly connect and transfer data, and the requirements for speed, data capability, distance and power vary depending on the application. Our Connectivity products support many wireless technologies to meet these requirements, including low-power wireless network standards like Zigbee® and other technologies like Bluetooth®, WiFi, GPS and Near Field Communications. Our Connectivity products are usually designed into customer devices alongside our processor and microcontroller products, enabling data to be collected, transmitted and acted upon.

#### Other

Other includes revenue from our smaller product lines, such as DLP® (primarily used in projectors to create high-definition images), custom semiconductors known as application-specific integrated circuits (ASICs) and calculators. It includes royalties received for our patented technology that we license to other electronics companies and revenue from transitional supply agreements related to acquisitions and divestitures. We also include revenue, about \$1.2 billion in 2012, from our baseband products and from our OMAP applications processors and connectivity

products sold into smartphone and consumer tablet applications, all of which are product lines that we have previously announced we are exiting and are collectively

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referred to as “legacy wireless products.” We expect this revenue to substantially cease by the end of 2013. Other generated about \$3.6 billion of revenue in 2012.

We also include in Other restructuring charges and certain acquisition-related charges that are not used in evaluating results of and allocating resources to our Analog and Embedded Processing segments. These acquisition-related charges include certain fair-value adjustments, restructuring charges, transaction expenses, acquisition-related retention bonuses and amortization of intangible assets. Other also includes certain non-recurring and corporate-level items, such as litigation and environmental costs, insurance proceeds, and assets and liabilities associated with our centralized operations, such as our worldwide manufacturing, facilities and procurement operations.

#### Inventory

Our inventory practices differ by product, but we generally maintain inventory levels that are consistent with our expectations of customer demand. Because of the longer product life cycles of catalog products and their inherently lower risk of obsolescence, we generally carry more inventory of those products than custom products. Additionally, we sometimes maintain catalog-product inventory in unfinished wafer form, as well as higher finished-goods inventory of low-volume products, allowing greater flexibility in periods of high demand. We also have consignment inventory programs in place for our largest customers and some distributors.

#### Manufacturing

Semiconductor manufacturing begins with a sequence of photo-lithographic and chemical processing steps that fabricate a number of semiconductor devices on a thin silicon wafer. Each device on the wafer is tested, the wafer is cut into individual units and each unit is assembled into a package that then is usually retested. The entire process takes place in highly specialized facilities and requires an average of 12 weeks, with most products completing within 8 to 16 weeks.

The cost and lifespan of the equipment and processes we use to manufacture semiconductors vary by technology. Our Analog products and most of our Embedded Processing products can be manufactured using mature and stable, and therefore less expensive, equipment than is needed for manufacturing advanced CMOS logic products, such as our OMAP products.

We own and operate semiconductor manufacturing facilities in North America, Asia, Japan and Europe. These include both wafer fabrication and assembly/test facilities. Our facilities require substantial investment to construct and are largely fixed-cost assets once in operation. Because we own much of our manufacturing capacity, a significant portion of our operating cost is fixed. In general, these fixed costs do not decline with reductions in customer demand or utilization of capacity, potentially hurting our profit margins. Conversely, as product demand rises and factory utilization increases, the fixed costs are spread over increased output, potentially benefiting our profit margins. We expect to maintain sufficient internal wafer fabrication capacity to meet the vast majority of our production needs. To supplement our internal wafer fabrication capacity and maximize our responsiveness to customer demand and return on capital, our wafer manufacturing strategy utilizes the capacity of outside suppliers, commonly known as foundries, and subcontractors. In 2012, we sourced about 20 percent of our total wafers and about 75 percent of our advanced CMOS logic needs from external foundries.

In 2011, we initiated closure of an older wafer fabrication facility in Hiji, Japan, and another in Houston, Texas. We expect to complete these plant closures in 2013.

#### Product cycle

The global semiconductor market is characterized by constant, though generally incremental, advances in product designs and manufacturing processes. Semiconductor prices and manufacturing costs tend to decline over time as manufacturing processes and product life cycles mature.

#### Market cycle

The “semiconductor cycle” is an important concept that refers to the ebb and flow of supply and demand. The semiconductor market historically has been characterized by periods of tight supply caused by strengthening demand and/or insufficient manufacturing capacity, followed by periods of surplus inventory caused by weakening demand and/or excess manufacturing capacity. These are typically referred to as upturns and downturns in the semiconductor cycle. The semiconductor cycle is affected by the significant time and money required to build and maintain semiconductor manufacturing facilities.



### Seasonality

Our revenue is subject to some seasonal variation. Our semiconductor revenue tends to be weaker in the first and fourth quarters when compared to the second and third quarters. Calculator revenue is tied to the U.S. back-to-school season and is therefore at its highest in the second and third quarters.

### Tax considerations

We operate in a number of tax jurisdictions and are subject to several types of taxes including those that are based on income, capital, property and payroll, as well as sales and other transactional taxes. The timing of the final determination of our tax liabilities varies by jurisdiction and taxing authority. As a result, during any particular reporting period we may reflect in our financial statements one or more tax refunds or assessments, or changes to tax liabilities, involving one or more taxing authorities.

### Third-Quarter 2013 results

Our third-quarter revenue was \$3.24 billion, net income was \$629 million and earnings per share (EPS) were \$0.56.

Our third-quarter performance reflects the positive structural changes we have made over the past few years as we have focused on Analog and Embedded Processing. Our revenue in the quarter was up 6 percent sequentially. Excluding the legacy wireless products, revenue grew 10 percent sequentially. Our book-to-bill ratio was 0.97, consistent with an expected seasonal revenue decline in the fourth quarter.

Analog and Embedded Processing are now 80 percent of TI's revenue, eight points higher than a year ago. The combined revenue from these two businesses grew 10 percent sequentially and 7 percent from a year ago. Our legacy wireless products declined to less than 2 percent of revenue.

Earnings per share were higher than expected due to better revenue and gross profit, tight expense control and discrete tax items. Gross margin of 54.8 percent was an all-time high for TI, exceeding the prior record set in the third quarter of 2010, even though both revenue and factory utilization were lower. We believe this reflects the increased quality of revenue that comes from our focus on Analog and Embedded Processing and the efficiency of our manufacturing strategy.

Our business model continues to generate strong cash flow from operations. Free cash flow for the trailing 12 months was almost \$3 billion, up 4 percent compared with a year ago. Free cash flow was 24 percent of revenue, consistent with our target of 20-25 percent.

We returned \$1.0 billion to shareholders through dividends and stock repurchases in the quarter. For the trailing 12 months, the return to shareholders totaled \$3.8 billion or 133 percent of free cash flow. In the quarter, we announced a dividend increase, our second in 2013. In total, we have increased our dividend by 43 percent this year, resulting in an annualized rate of \$1.20 per share. Our strategy to return to shareholders all of our free cash flow not needed for debt repayment reflects our confidence in the long-term sustainability of our Analog and Embedded Processing business model.

Our balance sheet remains strong, with \$3.6 billion of cash and short-term investments at the end of the quarter, 82 percent owned by the company's U.S. entities. Inventory days were 106, up from 101 a year ago, and consistent with our model of 105-115 days.

Free cash flow and revenue excluding legacy wireless are non-GAAP financial measures. For reconciliation to GAAP and an explanation for the purpose of providing these non-GAAP measures, see the Non-GAAP financial information section after the Liquidity and Capital Resources section.



## Consolidated Statements of Income

(Millions of dollars, except share and per-share amounts)

|   | For Three Months Ended |                |               |   |
|---|------------------------|----------------|---------------|---|
|   | Sept. 30, 2013         | Sept. 30, 2012 | June 30, 2013 |   |
| Revenue   | \$ 3,244               | \$ 3,390       | \$ 3,047      |   |
| Cost of revenue                                   | 1,465                  | 1,650          | 1,477         |   |
| Gross profit                                      | 1,779                  | 1,740          | 1,570         |   |
| Research and development (R&D)                    | 368                    | 463            | 389           |   |
| Selling, general and administrative (SG&A)        | 465                    | 453            | 471           |   |
| Acquisition charges                               | 86                     | 106            | 86            |   |
| Restructuring charges/other                       | 16                     | (122)          | (282)         |   |
| Operating profit                                  | 844                    | 840            | 906           |   |
| Other income (expense), net (OI&E)                | (4)                    | 24             | —             |   |
| Interest and debt expense                         | 24                     | 21             | 24            |   |
| Income before income taxes                        | 816                    | 843            | 882           |   |
| Provision for income taxes                        | 187                    | 59             | 222           |   |
| Net income  | \$ 629                 | \$ 784         | \$ 660        |   |
| Earnings per common share:                        |                        |                |               |   |
| Basic   | \$ .56                 | \$ .68         | \$ .59        |   |
| Diluted   | \$ .56                 | \$ .67         | \$ .58        |   |
| Average shares outstanding (millions):            |                        |                |               |   |
| Basic   | 1,096                  | 1,130          | 1,103         |   |
| Diluted   | 1,111                  | 1,141          | 1,117         |   |
| Cash dividends declared per share of common stock | \$ .28                 | \$ .17         | \$ .28        |   |
| Percentage of revenue:                            |                        |                |               |   |
| Gross profit                                      | 54.8                   | % 51.3         | % 51.5        | % |
| R&D   | 11.3                   | % 13.6         | % 12.8        | % |
| SG&A  | 14.4                   | % 13.4         | % 15.5        | % |
| Operating profit                                  | 26.0                   | % 24.8         | % 29.7        | % |

As required by accounting rule ASC 260, net income allocated to unvested restricted stock units (RSUs), on which we pay dividend equivalents, is excluded from the calculation of EPS. The amount excluded is \$11 million, \$14 million and \$11 million for the quarters ending September 30, 2013, September 30, 2012, and June 30, 2013, respectively.

The information presented in this Management's discussion and analysis of financial condition and results of operations (MD&A) is based on our segment structure as revised as of January 1, 2013. Segment-level information for the periods presented has been recast to reflect the changes in our reportable segments.

Our exit from legacy wireless products and the elimination of the Wireless segment resulted in changes to our corporate-level expense allocations, which negatively affected segment-level profitability in the third quarter and the nine months ended September 30, 2013. We expect a similar effect through the end of 2013. We allocate our corporate-level expenses, which are largely fixed, among our product lines in proportion to the operating expenses directly generated by them. Legacy wireless products generated lower operating expenses in the third quarter and the nine-month period than they did in the year-ago periods because we are no longer investing in them. The corporate-level expenses allocated to those products were, therefore, proportionately lower, and the corporate-level



expenses allocated to the remaining product lines were proportionately higher. This allocation change affects the profitability of each of our segments, but does not impact operating expense or profitability trends at the consolidated level.

Throughout the following discussion of our results of operations, unless otherwise noted, changes in our revenue are attributable to changes in customer demand, which are evidenced by fluctuations in shipment volumes. New products tend not to have a significant impact because our revenue is derived from such a large number of products. From time to time, our revenue and gross profit are affected by changes in demand for higher-priced or lower-priced products, which we refer to as changes in the “mix” of products shipped.

#### Details of financial results

Revenue for the third quarter of 2013 was \$3.24 billion, a decrease of \$146 million, or 4 percent, from the year-ago quarter primarily due to lower revenue from our legacy wireless products, which more than offset higher revenue from Analog and Embedded Processing. Compared with the prior quarter, revenue increased \$197 million, or 6 percent, primarily due to higher revenue from Analog and Embedded Processing, partially offset by lower revenue from our legacy wireless products.

Gross profit for the third quarter of 2013 was \$1.78 billion, or 54.8 percent of revenue, an increase of \$39 million, or 2 percent, from the year-ago quarter. The increase was due to a more favorable mix of products shipped and, to a lesser extent, lower expense resulting from improved utilization of our manufacturing facilities, partially offset by lower revenue. Underutilization expense in the third quarter of 2013 was about \$70 million compared with about \$150 million in the year-ago quarter. Compared with the prior quarter, gross profit increased \$209 million, or 13 percent, primarily due to higher revenue.

Operating expenses for the third quarter of 2013 were \$368 million for R&D and \$465 million for SG&A. R&D expense decreased \$95 million, or 21 percent, from the year-ago quarter, and \$21 million, or 5 percent, from the prior quarter, primarily reflecting the wind-down of our legacy wireless products. SG&A expense increased \$12 million, or 3 percent, compared with the year-ago quarter due to higher variable compensation and other support costs, partially offset by reductions from the wind-down of our legacy wireless products. Compared with the prior quarter, SG&A expense was about even.

In the third quarter of 2013, we incurred \$86 million of Acquisition charges associated with our acquisition of National Semiconductor Corporation, compared with \$106 million in the year-ago quarter and \$86 million in the prior quarter. The quarterly Acquisition charges are primarily from the ongoing amortization of intangible assets. The year-ago quarter also included integration-related expenses. See Note 2 to the financial statements for detailed information.

Restructuring charges/other for the third quarter of 2013 was \$16 million, representing \$2 million of severance and benefit costs and \$14 million of other exit costs associated with the 2011 actions to close certain manufacturing facilities in Houston, Texas, and Hiji, Japan. This compares with a net credit of \$122 million for the year-ago quarter and a net credit of \$282 million in the prior quarter. The year-ago quarter included a net benefit of \$144 million associated with our transfer of the obligations and assets of a portion of our Japan pension program to the government of Japan (the Japan pension program change), partially offset by \$22 million in charges related to facilities closings. The prior quarter included a gain of \$315 million from the transfer of wireless connectivity technology to a customer, partially offset by restructuring charges of \$33 million (of which \$29 million was associated with the 2012 action to restructure our former Wireless business). All of these restructuring charges and the net credit are included in Other. We expect all of these restructuring actions to be completed in 2013. See Note 3 to the financial statements for additional information.

For the third quarter of 2013, our operating profit was \$844 million, or 26.0 percent of revenue, compared with \$840 million or 24.8 percent of revenue for the year-ago quarter. Compared with the prior quarter, operating profit decreased \$62 million, or 7 percent.

OI&E for the third quarter was an expense of \$4 million compared with income of \$24 million for the year-ago quarter, and essentially unchanged from the prior quarter. The decrease from the year-ago quarter was primarily due to lower income from equity investments.

Interest and debt expense was \$24 million compared with \$21 million for the year-ago quarter and was unchanged from the prior quarter. The increase from the year-ago quarter was due to higher average interest rates. See Note 8 to the financial statements for details regarding debt outstanding.

Quarterly income taxes are calculated using the estimated annual effective tax rate. As of September 30, 2013, our estimated annual effective tax rate is about 24 percent. Our annual effective tax rate benefits from the lower tax rates applicable to our operations in many of the jurisdictions in which we operate and from U.S. tax benefits. These lower tax rates are generally statutory in nature, without expiration and available to companies that operate in those taxing jurisdictions. See Note 4 to the financial statements for additional information.

For the third quarter of 2013, our tax provision was \$187 million compared with \$59 million in the year-ago quarter and \$222 million in the prior quarter. The year-ago quarter included a \$90 million discrete tax benefit and a \$67 million benefit from lowering our estimated effective tax rate for 2012. The decrease in our tax provision from the prior quarter was due to lower income before income taxes and, to a lesser extent, a net benefit of \$14 million from discrete tax items.

In the third quarter of 2013, our net income was \$629 million compared with \$784 million for the year-ago quarter and \$660 million for the prior quarter. EPS was \$0.56 compared with \$0.67 for the year-ago quarter and \$0.58 for the prior quarter.

#### Segment results

##### Analog

|                               | 3Q13     | 3Q12     | Change |   | 2Q13     | Change |   |
|-------------------------------|----------|----------|--------|---|----------|--------|---|
| Revenue                       | \$ 1,931 | \$ 1,843 | 5      | % | \$ 1,745 | 11     | % |
| Operating profit              | 583      | 460      | 27     | % | 416      | 40     | % |
| Operating profit % of revenue | 30.2     | 25.0     |        | % | 23.8     |        | % |

Analog revenue increased 5 percent from the year-ago quarter primarily due to higher revenue from SVA. Also contributing to the increase was higher revenue from HPA and, to a lesser extent, Power. HVAL revenue was about even. Compared with the prior quarter, revenue increased 11 percent due to higher revenue from, in decreasing order, Power, HVAL, HPA and SVA. Operating profit increased from the year-ago quarter due to higher gross profit. Compared with the prior quarter, operating profit increased due to higher revenue and associated gross profit.

##### Embedded Processing

|                               | 3Q13   | 3Q12   | Change |   | 2Q13   | Change |   |
|-------------------------------|--------|--------|--------|---|--------|--------|---|
| Revenue                       | \$ 668 | \$ 591 | 13     | % | \$ 618 | 8      | % |
| Operating profit              | 83     | 60     | 38     | % | 54     | 54     | % |
| Operating profit % of revenue | 12.4   | 10.1   |        | % | 8.8    |        | % |

Embedded Processing revenue increased 13 percent compared with the year-ago quarter due to higher revenue from, in decreasing order, Microcontrollers, Processors and Connectivity. Compared with the prior quarter, Embedded Processing revenue increased 8 percent primarily due to higher revenue from Processors. Also contributing to the increase was higher revenue from Microcontrollers and, to a lesser extent, Connectivity. Operating profit increased from the year-ago quarter due to higher revenue and associated gross profit, partially offset by higher operating expenses. Operating profit increased from the prior quarter due to higher revenue and associated gross profit.

##### Other

|                               | 3Q13   | 3Q12   | Change |   | 2Q13   | Change |   |
|-------------------------------|--------|--------|--------|---|--------|--------|---|
| Revenue                       | \$ 645 | \$ 956 | -33    | % | \$ 684 | -6     | % |
| Operating profit              | 178    | 320    | -44    | % | 436    | -59    | % |
| Operating profit % of revenue | 27.6   | 33.4   |        | % | 63.7   |        | % |
| Acquisition charges*          | 86     | 106    |        |   | 86     |        |   |
| Restructuring charges/other*  | 16     | (122)  |        |   | (282)  |        |   |

\*Included in operating profit

Other revenue decreased 33 percent from the year-ago quarter primarily due to lower revenue from legacy wireless products, and to a lesser extent, the nonrecurrence of business interruption insurance proceeds from the Japan earthquake. Revenue from DLP and custom ASIC products also declined, while revenue from calculators and

royalties increased. Compared with the prior

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quarter, Other revenue decreased 6 percent due to lower revenue from legacy wireless products. Revenue from calculators, custom ASIC products and royalties increased. Revenue from custom ASIC products increased as a result of a more favorable mix of products shipped. Revenue from DLP products was about even. Operating profit decreased from the year-ago quarter due to lower revenue and associated gross profit and higher Restructuring charges/other, which in the year-ago quarter included a gain from the Japan pension program change. These decreases were partially offset by lower operating expenses resulting from the wind-down of legacy wireless products. Operating profit decreased from the prior quarter due to higher Restructuring charges/other, which in the prior quarter included the gain from the technology transfer to a customer.

#### First nine months of 2013 results

For the first nine months of 2013, we report the following:

Revenue was \$9.18 billion, a decrease of \$669 million, or 7 percent, compared with the year-ago period primarily due to lower revenue from legacy wireless products.

Gross profit was \$4.72 billion, a decrease of \$198 million, or 4 percent, from the year-ago period due to lower revenue, partially offset by a more favorable mix of products shipped. Gross profit margin was 51.5 percent of revenue compared with 50.0 percent in the year-ago period.

R&D expense of \$1.18 billion decreased \$276 million, or 19 percent, from the year-ago period primarily reflecting the wind-down of our legacy wireless products. R&D expense as a percent of revenue was 12.8 percent compared with 14.7 percent in the year-ago period. SG&A expense was \$1.40 billion, an increase of 2 percent from the year-ago period due to higher variable compensation and other support costs, partially offset by reductions from the wind-down of our legacy wireless products. SG&A expense as a percent of revenue was 15.2 percent compared with 13.9 percent in the year-ago period.

Acquisition charges for the first nine months of 2013 were \$257 million compared with \$363 million in the year-ago period. The charges were primarily from the ongoing amortization of intangible assets. The decrease from the year-ago period is primarily due to the nonrecurrence of integration-related expenses. See Note 2 to the financial statements for detailed information.

Restructuring charges/other for the first nine months of 2013 was a net credit of \$251 million, reflecting the \$315 million gain from the technology transfer in the second quarter, partially offset by restructuring charges of \$64 million. This compares with a net credit of \$99 million for the year-ago period, which included a \$144 million gain from the Japan pension program change, partially offset by restructuring and other charges of \$45 million. See Note 3 to the financial statements for more information.

Operating profit was \$2.14 billion, or 23.4 percent of revenue, compared with \$1.83 billion, or 18.6 percent of revenue, in the year-ago period.

Interest and debt expense was \$71 million compared with \$62 million in the year-ago period. The increase was primarily due to higher average interest rates.

The tax provision was \$421 million compared with \$285 million in the year-ago period. The increase was primarily due to higher income before income taxes.

Net income was \$1.65 billion compared with \$1.49 billion in the year-ago period. EPS was \$1.45 compared with \$1.27 in the year-ago period.

Segment results

Analog

|                               | YTD<br>2013 |   | YTD 2012 |   | Change |
|-------------------------------|-------------|---|----------|---|--------|
| Revenue                       | \$ 5,325    |   | \$ 5,329 |   | 0 %    |
| Operating profit              | 1,298       |   | 1,231    |   | 5 %    |
| Operating profit % of revenue | 24.4        | % | 23.1     | % |        |

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Revenue from each of the four product lines was about even with the year-ago period. For the first nine months of 2013, operating profit increased 5 percent from the year-ago period due to higher gross profit that benefitted from lower manufacturing costs. This increase was partially offset by higher operating expenses.

#### Embedded Processing

|                               | YTD<br>2013 |   | YTD 2012 |   | Change |
|-------------------------------|-------------|---|----------|---|--------|
| Revenue                       | \$ 1,846    |   | \$ 1,711 |   | 8 %    |
| Operating profit              | 144         |   | 147      |   | -2 %   |
| Operating profit % of revenue | 7.8         | % | 8.6      | % |        |

Embedded Processing revenue increased 8 percent from the year-ago period due to higher revenue from Microcontrollers and, to a lesser extent, Processors and Connectivity. Operating profit decreased as higher gross profit was more than offset by higher operating expenses.

#### Other

|                               | YTD<br>2013 |   | YTD 2012 |   | Change |
|-------------------------------|-------------|---|----------|---|--------|
| Revenue                       | \$ 2,006    |   | \$ 2,806 |   | -29 %  |
| Operating profit              | 703         |   | 456      |   | 54 %   |
| Operating profit % of revenue | 35.0        | % | 16.2     | % |        |
| Acquisition charges*          | 257         |   | 363      |   |        |
| Restructuring charges/other*  | (251        | ) | (99      | ) |        |

\* Included in operating profit

Other revenue decreased 29 percent from the year-ago period primarily due to lower revenue from legacy wireless products. Also contributing were, in decreasing order, the nonrecurrence of business interruption insurance proceeds related to the Japan earthquake and lower revenue from custom ASIC products, DLP products and calculators. Royalties increased. Operating profit increased from the year-ago period primarily due to lower operating expenses, reflecting the wind-down of our legacy wireless products, and to a lesser extent, lower Restructuring charges/other and Acquisition charges. These increases were partially offset by lower revenue and associated gross profit.

#### Financial Condition

At the end of the third quarter of 2013, total cash (Cash and cash equivalents plus Short-term investments) was \$3.59 billion, with 82 percent owned by our U.S. entities.

Accounts receivable were \$1.52 billion at the end of the third quarter. This was an increase of \$294 million from the end of 2012 as a result of higher revenue at the end of the third quarter compared with the end of the year. Days sales outstanding were 42 at the end of the third quarter compared with 37 at the end of 2012.

Inventory was \$1.73 billion at the end of the third quarter. This was a decrease of \$31 million from the end of 2012. Days of inventory at the end of the third quarter were 106 compared with 103 at the end of 2012.

#### Liquidity and Capital Resources

Our primary source of liquidity is cash flow from operations. Additional sources of liquidity are our cash and cash equivalents, short-term investments and revolving credit facilities. Cash flow from operations for the first nine months of 2013 was \$2.19 billion, a decrease of \$144 million from the year-ago period, as higher net income was more than



offset by changes in working capital.

We had \$1.43 billion of Cash and cash equivalents and \$2.16 billion of Short-term investments as of September 30, 2013. We have a variable-rate revolving credit facility with a consortium of investment-grade banks that allows us to borrow up to \$2 billion through March 2018. This credit facility also serves as support for the issuance of commercial paper. As of September 30, 2013, our credit facility was undrawn and we had no commercial paper outstanding.

For the first nine months of 2013, investing activities provided cash of \$120 million compared with using cash of \$850 million in the year-ago period. Proceeds from sales of short-term investments, net of purchases, provided cash of \$387 million compared with \$502 million used in the year-ago period to purchase short-term investments, net of proceeds from sales. Net proceeds from long-term investments provided \$17 million in the current period compared with \$51 million in the year-ago period. Capital expenditures in the first nine months of 2013 totaled \$305 million compared with \$399 million in the year-ago period. These expenditures were primarily for semiconductor manufacturing equipment. We also received \$21 million of cash proceeds from the sale of two sites.

Net cash used in financing activities was \$2.29 billion for the first nine months of 2013 compared with \$1.26 billion in the year-ago period. During the first nine months of 2013, we used \$1.5 billion to repay maturing debt compared with \$1.38 billion used to repay debt and commercial paper borrowings in the year-ago period. In May 2013, we issued \$1.0 billion principal amount of fixed-rate long-term debt consisting of \$500 million of 1.00% notes maturing in 2018 and \$500 million of 2.25% notes maturing in 2023. The \$986 million of net proceeds from this issuance were used for repayment of a portion of our maturing debt. In August 2012, we received proceeds of \$1.49 billion from the issuance of fixed-rate long-term debt, net of original issuance discount. In the first nine months of 2013, we paid dividends of \$849 million compared with \$584 million in the year-ago period, due to increases in the dividend rate. We also used \$2.13 billion in the first nine months of 2013 to repurchase shares of our common stock. In the same period last year we used \$1.20 billion to repurchase shares of our common stock. Employee exercises of stock options are also reflected in cash from financing activities. In the first nine months of 2013, these exercises provided cash proceeds of \$1.15 billion compared with \$390 million for the year-ago period.

In September 2013, we announced a 7 percent increase in our quarterly cash dividend, which increased from \$0.28 to \$0.30 per share. This dividend will be payable November 18, 2013, to stockholders of record on October 31, 2013.

We believe we have the necessary financial resources and operating plans to fund our working capital needs, capital expenditures, dividend and debt-related payments, and other business requirements for at least the next 12 months.

#### Non-GAAP financial information

##### Revenue excluding legacy wireless

This MD&A includes a reference to TI's revenue excluding revenue from legacy wireless products. This measure, which was not prepared in accordance with generally accepted accounting principles (GAAP) in the United States, provides investors with insight into TI's underlying business results and is supplemental to the comparable GAAP measure.

#### TEXAS INSTRUMENTS INCORPORATED

(Millions of dollars)

|  | For Three Months Ended |               |        |   |
|--|------------------------|---------------|--------|---|
|  | Sept. 30, 2013         | June 30, 2013 | Change |   |
| Revenue (GAAP)                                     | \$3,244                | \$3,047       | 6      | % |
| Less legacy wireless revenue                       | 57                     | 148           |        |   |
| TI Revenue less legacy wireless revenue (non-GAAP) | \$3,187                | \$2,899       | 10     | % |

Free cash flow

This MD&A also includes references to free cash flow and various ratios based on that measure. These are financial measures that were not prepared in accordance with GAAP. Free cash flow was calculated by subtracting Capital expenditures from the most directly comparable GAAP measure of Cash flows from operating activities (also referred to as Cash flow from operations).

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The free cash flow measures were compared to the following GAAP items to determine the various non-GAAP ratios presented below and referred to in the MD&A: Revenue, Dividends paid and Stock repurchases. Reconciliation to the most directly comparable GAAP-based ratios is provided in the tables below.

We believe these non-GAAP measures provide insight into our liquidity, our cash-generating capability and the amount of cash available to return to investors, as well as insight into our financial performance. These non-GAAP measures are supplemental to the comparable GAAP measures.

TEXAS INSTRUMENTS INCORPORATED

(Millions of dollars)

|                                  | For Twelve Months Ended |                | Change |   |
|----------------------------------|-------------------------|----------------|--------|---|
|                                  | Sept. 30, 2013          | Sept. 30, 2012 |        |   |
| Cash flow from operations (GAAP) | \$ 3,270                | \$ 3,298       | -1     | % |
| Less Capital expenditures        | 402                     | 551            | -27    | % |
| Free cash flow (non-GAAP)        | \$ 2,868                | \$ 2,747       | 4      | % |

|                                  | For Twelve Months Ended |                | Percentage of Revenue |                |
|----------------------------------|-------------------------|----------------|-----------------------|----------------|
|                                  | Sept. 30, 2013          | Sept. 30, 2012 | Sept. 30, 2013        | Sept. 30, 2012 |
| Revenue                          | \$12,155                |                |                       |                |
| Cash flow from operations (GAAP) | \$3,270                 | \$3,298        | 27                    | 27             |
| Less Capital expenditures        | 402                     | 551            | 3                     | 3              |
| Free cash flow (non-GAAP)        | \$2,868                 | \$2,747        | 24                    | 24             |

|                                     | For Twelve Months Ended Sept. 30, 2013 | Percentage of Cash Flow from Operations (GAAP) |          | Percentage of Free Cash Flow (Non-GAAP) |          |
|-------------------------------------|--|--|----------|---|----------|
|                                     |  | GAAP   | Non-GAAP | GAAP                                    | Non-GAAP |
| Dividends paid                      | \$1,084                                | 33   | 38       | 38                                      | 38       |
| Stock repurchases                   | 2,734                                  | 84   | 95       | 95                                      | 95       |
| Total cash returned to shareholders | \$3,818                                | 117  | 133      | 133                                     | 133      |

Long-term contractual obligations

In addition to the long-term debt obligations described in the long-term contractual obligations chart on pages 51-52 of Exhibit 13 to our Form 10-K for the year ended December 31, 2012, in May 2013, we issued \$500 million of 1.00% notes maturing in 2018 and \$500 million of 2.25% notes maturing in 2023.

Changes in accounting standards

See Note 1 to the financial statements for detailed information regarding the status of new accounting and reporting standards.

ITEM 4. Controls and Procedures.

An evaluation as of the end of the period covered by this report was carried out under the supervision and with the participation of management, including our Chief Executive Officer and Chief Financial Officer, of the effectiveness of the design and operation of our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange

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Act of 1934). Based upon that evaluation, the Chief Executive Officer and Chief Financial Officer concluded that those disclosure controls and procedures were effective. In addition, there has been no change in our internal control over financial reporting (as defined in Rule 13a-15(f) and 15d-15(f) under the Securities Exchange Act of 1934) that occurred during the period covered by this report that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

## PART II – OTHER INFORMATION

## ITEM 1A. Risk Factors.

Information concerning our risk factors is contained on pages 10-14 of our Form 10-K for the year ended December 31, 2012, and is incorporated by reference herein.

## ITEM 2. Unregistered Sales of Equity Securities and Use of Proceeds.

The following table contains information regarding our purchases of our common stock during the quarter.

## ISSUER PURCHASES OF EQUITY SECURITIES

| Period                                       | Total Number of Shares Purchased | Average Price Paid per Share | Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs <sup>(1)</sup> | Approximate Dollar Value of Shares that May Yet Be Purchased Under the Plans or Programs <sup>(1)</sup> |
|--|----------------------------------|------------------------------|---|---|
| July 1, 2013 through July 31, 2013           | 10,670,100                       | \$ 37.30                     | 10,670,100  | \$7.07 billion  |
| August 1, 2013 through August 31, 2013       | 8,571,433                        | 39.20                        | 8,571,433   | \$6.74 billion  |
| September 1, 2013 through September 30, 2013 | —                                | —                            | —   | \$6.74 billion  |
| Total  | 19,241,533                       | <sup>(2)</sup> \$38.15       | 19,241,533  | <sup>(2)</sup> \$6.74 billion <sup>(3)</sup>  |

All purchases during the quarter were made under the authorization from our board of directors to purchase up to \$7.5 billion of additional shares of TI common stock announced on September 16, 2010. On February 21, 2013, our Board of Directors authorized the purchase of an additional \$5.0 billion of our common stock. No expiration date has been specified for these authorizations.

<sup>(2)</sup> All purchases during the quarter were open-market purchases.

<sup>(3)</sup> As of September 30, 2013, this amount consisted of the remaining portion of the \$7.5 billion authorized in September 2010 and the \$5.0 billion authorized in February 2013.

ITEM 6. Exhibits.

| Designation of Exhibits in This Report | Description of Exhibit  |
|--|---|
| 3(a)                                   | Restated Certificate of Incorporation of the Registrant, dated April 18, 1985 (incorporated by reference to Exhibit 3(a) of the Registrant's Annual Report on Form 10-K for the year ended December 31, 2011).  |
| 3(b)                                   | Certificate of Amendment to Restated Certificate of Incorporation of the Registrant, dated April 16, 1987 (incorporated by reference to Exhibit 3(b) of the Registrant's Annual Report on Form 10-K for the year ended December 31, 2011).                  |
| 3(c)                                   | Certificate of Amendment to Restated Certificate of Incorporation of the Registrant, dated April 21, 1988 (incorporated by reference to Exhibit 3(c) of the Registrant's Annual Report on Form 10-K for the year ended December 31, 2011).                  |
| 3(d)                                   | Certificate of Amendment to Restated Certificate of Incorporation of the Registrant, dated April 18, 1996 (incorporated by reference to Exhibit 3(d) of the Registrant's Annual Report on Form 10-K for the year ended December 31, 2011).                  |
| 3(e)                                   | Certificate of Ownership merging Texas Instruments Automation Controls, Inc. into the Registrant, dated March 28, 1988 (incorporated by reference to Exhibit 3(e) of the Registrant's Annual Report on Form 10-K for the year ended December 31, 2011).     |
| 3(f)                                   | Certificate of Elimination of Designations of Preferred Stock of the Registrant, dated March 18, 1994 (incorporated by reference to Exhibit 3(f) of the Registrant's Annual Report on Form 10-K for the year ended December 31, 2011).                      |
| 3(g)                                   | Certificate of Ownership and Merger merging Tiburon Systems, Inc. into the Registrant, dated November 2, 1995 (incorporated by reference to Exhibit 3(g) of the Registrant's Annual Report on Form 10-K for the year ended December 31, 2011).              |
| 3(h)                                   | Certificate of Ownership and Merger merging Tartan, Inc. into the Registrant, dated June 21, 1995 (incorporated by reference to Exhibit 3(h) of the Registrant's Annual Report on Form 10-K for the year ended December 31, 2011).                          |
| 3(i)                                   | Certificate of Designation relating to the Registrant's Participating Cumulative Preferred Stock, dated June 23, 1998 (incorporated by reference to Exhibit 3(i) of the Registrant's Annual Report on Form 10-K for the year ended December 31, 2011).      |
| 3(j)                                   | Certificate of Elimination of Designation of Preferred Stock of the Registrant, dated June 18, 1998 (incorporated by reference to Exhibit 3(j) of the Registrant's Annual Report on Form 10-K for the year ended December 31, 2011).                        |
| 3(k)                                   | Certificate of Ownership and Merger merging Intersect Technologies, Inc. with and into the Registrant, dated July 15, 1999 (incorporated by reference to Exhibit 3(k) of the Registrant's Annual Report on Form 10-K for the year ended December 31, 2011). |
| 3(l)                                   | Certificate of Ownership and Merger merging Soft Warehouse, Inc. with and into the Registrant, dated September 23, 1999 (incorporated by reference to Exhibit 3(l) of the Registrant's Annual Report on Form 10-K for the year ended December 31, 2011).    |
| 3(m)                                   | Certificate of Ownership and Merger merging Silicon Systems, Inc. with and into the Registrant, dated December 17, 1999 (incorporated by reference to Exhibit 3(m) of the Registrant's Annual Report on Form 10-K for the year ended December 31, 2011).    |
| 3(n)                                   | Certificate of Amendment to Restated Certificate of Incorporation, dated April 20, 2000 (incorporated by reference to Exhibit 3(n) of the Registrant's Annual Report on Form 10-K for the year ended December 31, 2011).                                    |
| 3(o)                                   | Certificate of Ownership and Merger merging Power Trends, Inc. with and into the Registrant, dated May 31, 2001 (incorporated by reference to Exhibit 3(o) of the Registrant's Annual Report on Form 10-K for the year ended December 31, 2011).            |



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- 3(p) Certificate of Ownership and Merger merging Amati Communications Corporation with and into the Registrant, dated September 28, 2001 (incorporated by reference to Exhibit 3(p) of the Registrant's Annual Report on Form 10-K for the year ended December 31, 2011).
- 3(q) Certificate of Ownership and Merger merging Texas Instruments San Diego Incorporated with and into the Registrant, dated August 27, 2002 (incorporated by reference to Exhibit 3(q) of the Registrant's Annual Report on Form 10-K for the year ended December 31, 2011).
- 3(r) Certificate of Ownership and Merger merging Texas Instruments Burlington Incorporated with and into the Registrant, dated December 31, 2003 (incorporated by reference to Exhibit 3(r) of the Registrant's Annual Report on Form 10-K for the year ended December 31, 2011).

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- 3(s) Certificate of Ownership and Merger merging Texas Instruments Automotive Sensors and Controls San Jose Inc. with and into the Registrant, dated October 31, 2004 (incorporated by reference to Exhibit 3(s) of the Registrant's Annual Report on Form 10-K for the year ended December 31, 2011).
- 3(t) Certificate of Elimination of Series B Participating Cumulative Preferred Stock (incorporated by reference to Exhibit 3 to the Registrant's Current Report on Form 8-K filed June 23, 2008).
- 3(u) By-Laws of the Registrant (incorporated by reference to Exhibit 3 to the Registrant's Current Report on Form 8-K filed July 18, 2008).
- 31.1 Certification of Chief Executive Officer of Periodic Report Pursuant to Rule 13a-15(e) or Rule 15d-15(e).
- 31.2 Certification of Chief Financial Officer of Periodic Report Pursuant to Rule 13a-15(e) or Rule 15d-15(e).
- 32.1 Certification by Chief Executive Officer of Periodic Report Pursuant to 18 U.S.C. Section 1350.
- 32.2 Certification by Chief Financial Officer of Periodic Report Pursuant to 18 U.S.C. Section 1350.
- 101.ins XBRL Instance Document
- 101.def XBRL Taxonomy Extension Definition Linkbase Document
- 101.sch XBRL Taxonomy Extension Schema Document
- 101.cal XBRL Taxonomy Extension Calculation Linkbase Document
- 101.lab XBRL Taxonomy Extension Label Linkbase Document
- 101.pre XBRL Taxonomy Extension Presentation Linkbase Document

“Safe Harbor” Statement under the Private Securities Litigation Reform Act of 1995:

This report includes forward-looking statements intended to qualify for the safe harbor from liability established by the Private Securities Litigation Reform Act of 1995. These forward-looking statements generally can be identified by phrases such as TI or its management “believes,” “expects,” “anticipates,” “foresees,” “forecasts,” “estimates” or other words or phrases of similar import. Similarly, statements herein that describe TI’s business strategy, outlook, objectives, plans, intentions or goals also are forward-looking statements. All such forward-looking statements are subject to certain risks and uncertainties that could cause actual results to differ materially from those in forward-looking statements.

We urge you to carefully consider the following important factors that could cause actual results to differ materially from the expectations of TI or its management:

• Market demand for semiconductors, particularly in key markets such as communications, computing, industrial, consumer electronics and automotive;

• TI’s ability to maintain or improve profit margins, including its ability to utilize its manufacturing facilities at sufficient levels to cover its fixed operating costs, in an intensely competitive and cyclical industry;

• TI’s ability to develop, manufacture and market innovative products in a rapidly changing technological environment;

• TI’s ability to compete in products and prices in an intensely competitive industry;

• TI’s ability to maintain and enforce a strong intellectual property portfolio and obtain needed licenses from third parties;

• Expiration of license agreements between TI and its patent licensees, and market conditions reducing royalty payments to TI;

• Economic, social and political conditions in the countries in which TI, its customers or its suppliers operate, including security risks, health conditions, possible disruptions in transportation, communications and information technology networks and fluctuations in foreign currency exchange rates;

• Natural events such as severe weather and earthquakes in the locations in which TI, its customers or its suppliers operate;

• Availability and cost of raw materials, utilities, manufacturing equipment, third-party manufacturing services and manufacturing technology;

• Changes in the tax rate applicable to TI as the result of changes in tax law, the jurisdictions in which profits are determined to be earned and taxed, the outcome of tax audits and the ability to realize deferred tax assets;

• Changes in laws and regulations to which TI or its suppliers are or may become subject, such as those imposing fees or reporting or substitution costs relating to the discharge of emissions into the environment or the use of certain raw materials in our manufacturing processes;

• Losses or curtailments of purchases from key customers and the timing and amount of distributor and other customer inventory adjustments;

Customer demand that differs from our forecasts;

The financial impact of inadequate or excess TI inventory that results from demand that differs from projections;

Impairments of our non-financial assets;

Product liability or warranty claims, claims based on epidemic or delivery failure or recalls by TI customers for a product containing a TI part;

TI's ability to recruit and retain skilled personnel;

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• Timely implementation of new manufacturing technologies and installation of manufacturing equipment, and the ability to obtain needed third-party foundry and assembly/test subcontract services;

• TI's obligation to make principal and interest payments on its debt;

• TI's ability to successfully integrate and realize opportunities for growth from acquisitions, and our ability to realize our expectations regarding the amount and timing of restructuring charges and associated cost savings; and

• Breaches of our information technology systems.

For a more detailed discussion of these factors see the Risk Factors discussion in Item 1A of our most recent Form 10-K. The forward-looking statements included in this report are made only as of the date of this report and we undertake no obligation to update the forward-looking statements to reflect subsequent events or circumstances.

SIGNATURE

Pursuant to the requirements of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

TEXAS INSTRUMENTS INCORPORATED

BY /s/ Kevin P. March  
Kevin P. March  
Senior Vice President and  
Chief Financial Officer

Date: November 1, 2013