FREEPORT MCMORAN COPPER & GOLD INC
Form 10-K/A
June 18, 2002

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-K/A

Amendment No. 1 to

(Mark One)

[x]	**ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934** **For the fiscal year ended December 31, 2001** **OR**
[ ]	**TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934** **For the transition period from .... to ....**

Commission file number 1-9916

Freeport-McMoRan Copper & Gold Inc.

(Exact name of registrant as specified in its charter)

Delaware *(State or other jurisdiction of incorporation or organization)*	**74-2480931** *(I.R.S. Employer Identification No.)*
1615 Poydras Street **New Orleans, Louisiana** *(Address of principal executive offices)*	**70112** *(Zip Code)*

Registrant's telephone number, including area code: (504) 582-4000

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

Title of each class	**Name of each exchange on which registered**

Class A Common Stock, par value $0.10 per share	New York Stock Exchange
Class B Common Stock, par value $0.10 per share	New York Stock Exchange
Depositary Shares representing 0.05 shares of Step-Up Convertible Preferred Stock, par value $0.10 per share	New York Stock Exchange
Depositary Shares representing 0.05 shares of Gold-Denominated Preferred Stock, par value $0.10 per share	New York Stock Exchange
Depositary Shares, Series II, representing 0.05 shares of Gold-Denominated Preferred Stock, Series II, par value $0.10 per share	New York Stock Exchange
Depositary Shares representing 0.015625 shares of Silver-Denominated Preferred Stock, par value $0.10 per share	New York Stock Exchange
8-1/4% Convertible Senior Notes due 2006 of the registrant and FCX Investment Ltd.	None

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

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 X No

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

The aggregate market value of classes of common stock held by non-affiliates of the registrant on February 26, 2002 was approximately $1,079,000,000.

On February 26, 2002, there were issued and outstanding 55,567,714 shares of Class A Common Stock and 88,584,099 shares of Class B Common Stock.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of our Proxy Statement for our 2002 Annual Meeting to be held on May 2, 2002 are incorporated by reference into Part III of this report.

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PART I

This Amendment No. 1 to the Annual Report on Form 10-K of Freeport-McMoRan Copper & Gold Inc. for the fiscal year ended December 31, 2001 reflects information as of March 8, 2002, the date of the original filing of the Form 10-K with the Securities and Exchange Commission. The only changes to the original filing are the inclusion of automatic links to the files containing maps and charts.

Items 1. and 2. Business and Properties.

General

We are one of the world's largest copper and gold mining companies in terms of reserves and production. We believe we are the lowest cost copper producer in the world, after taking into account customary credits for related gold and silver production.

Our principal operating subsidiary is PT Freeport Indonesia, a limited liability company organized under the laws of the Republic of Indonesia and domesticated in Delaware. PT Freeport Indonesia explores for, develops, mines and processes ore containing copper, gold and silver. Our operations are located in the remote rugged highlands of the Sudirman Mountain Range in the province of Papua (formerly Irian Jaya), Indonesia, which is located on the western half of the island of New Guinea. PT Freeport Indonesia markets its concentrates containing copper, gold and silver worldwide. As of December 31, 2001, we had an 85.86 percent ownership interest in this subsidiary and the Government of Indonesia had a 9.36 percent interest; PT Nusamba Mineral Industri (Nusamba), an Indonesian company, had most of the remaining ownership interest in PT Freeport Indonesia. See the discussion under "Nusamba Loan Guarantee" about our guarantee and repayment of certain Nusamba debt on February 27, 2002. After repayment of the Nusamba debt and the acquisition of Nusamba's interest in PT Indocopper Investama, we have an approximate 90.6 percent ownership interest in PT Freeport Indonesia.

PT Freeport Indonesia's operations are conducted pursuant to an agreement, called a Contract of Work, with the Government of Indonesia. The Contract of Work allows us to conduct exploration, mining and production activities in a 24,700-acre area that we call Block A. In 1988, we discovered our largest mine, Grasberg, in Block A. Grasberg contains the largest single gold reserve and one of the largest copper reserves of any mine in the world. The Contract of Work also allows us to explore for minerals in a 0.5 million-acre area that we call Block B. All of our current proven and probable reserves are located in Block A (see "Ore Reserves").

PT Freeport Indonesia's Contract of Work governs our rights and obligations relating to taxes, exchange controls, royalties, repatriation and other matters (see "Contracts of Work"). The Contract of Work provides a 35 percent corporate income tax rate for PT Freeport Indonesia and a withholding tax rate of 10 percent (based on the tax treaty between Indonesia and the United States) on dividends and interest paid to us by PT Freeport Indonesia. The Contract of Work also provides for royalties on the metals PT Freeport Indonesia sells.

Another of our operating subsidiaries, PT Irja Eastern Minerals, which we refer to as Eastern Minerals, holds an additional Contract of Work in Papua covering approximately 1.25 million acres and is conducting exploration activities under this Contract of Work. As of December 31, 2001, we had a 94.9 percent ownership interest in Eastern Minerals, but after acquiring Nusamba's interest in PT Indocopper Investama discussed in "Nusamba Loan Guarantee" we have a 100 percent ownership interest.

In 1996, we established joint ventures with Rio Tinto plc, an international mining company with headquarters in London, England. One joint venture covers PT Freeport Indonesia's mining operations in Block A. This joint venture gives Rio Tinto, through 2021, a 40 percent interest in certain assets and in production above specified levels from operations in Block A and, after 2021, a 40 percent interest in all production in Block A. Under our joint venture arrangements, Rio Tinto also has a 40 percent interest in PT Freeport Indonesia's Contract of Work and Eastern Minerals' Contract of Work. In addition, Rio Tinto has the option to participate in 40 percent of any of our other future exploration projects in Papua.

Under another joint venture agreement through PT Nabire Bakti Mining, we conduct exploration activities in an area covering approximately 0.5 million acres in five parcels contiguous to PT Freeport Indonesia's Block B and one of Eastern Minerals' blocks. Rio Tinto has elected to participate in 40 percent of our interest and cost in the venture.

Field exploration activities outside of our current mining operations in Block A have been temporarily suspended due to safety and security issues and uncertainty relating to a possible conflict between our mining and exploration rights in certain forest areas covered by our Contracts of Work and an Indonesian law enacted in 1999 prohibiting open-pit mining in forest preservation areas.

We also smelt and refine copper concentrates in Spain and market the refined copper products, through our wholly owned subsidiary, Atlantic Copper, S.A. In addition, PT Freeport Indonesia has a 25 percent interest in PT

Smelting, an Indonesian company that operates a copper smelter and refinery in Gresik, Indonesia.

The following maps indicate the location of the Papua province in which we operate; the location of our Contracts of Work areas within the Papua province; and the infrastructure of our Contracts of Work project area.

Nusamba Loan Guarantee

In 1997, we guaranteed a $253.4 million loan from a syndicate of commercial banks, including JPMorgan Chase Bank as agent, to PT Nusamba Mineral Industri. Nusamba, an Indonesian company, used the loan proceeds plus $61.6 million of cash, for a total of $315.0 million, to purchase stock in PT Indocopper Investama, a company whose only significant assets are its 9.36 percent of PT Freeport Indonesia's stock and its 10.0 percent of Eastern Minerals' stock. Nusamba owned approximately 51 percent of PT Indocopper Investama's stock and we owned approximately 49 percent. We guaranteed the Nusamba loan for the purpose of continuing minority Indonesian ownership in our principal operating subsidiary, PT Freeport Indonesia. Nusamba acquired the ownership interest from our previous Indonesian partner to whom we sold the interest in 1991 to satisfy the Indonesian ownership requirements in our Contract of Work. Those requirements were relaxed in 1997, but, at the time of the Nusamba transaction, we believed that it was prudent and in our best interests to facilitate the continuation of Indonesian ownership, although no longer legally required.

The loan was secured by a pledge of the PT Indocopper Investama stock owned by Nusamba and was to be due in March 2002. We had also agreed to lend Nusamba any amounts necessary to cover shortfalls between the interest payments on the loan and dividends received by Nusamba on the PT Indocopper Investama stock. This loan was also to be due in March 2002. Except for Nusamba's indirect ownership of PT Freeport Indonesia stock, our guarantee of Nusamba's bank loan and our loans to Nusamba, we had no ownership interest in, or contractual relationships with, Nusamba.

In discussions subsequent to December 31, 2001, Nusamba informed us that it did not expect to be able to repay the bank loan or our loan at maturity, which obligated us to pay the bank loan. On February 27, 2002, we repaid Nusamba's bank loan as provided for under the terms of our amended credit facilities and acquired Nusamba's ownership in PT Indocopper Investama. As a result of our payment of the Nusamba bank loan, on our year-end 2001 balance sheet we have:

- recorded an additional liability of $253.4 million to reflect the payment of the Nusamba bank loan;
- reduced our "other assets" by $61.6 million to reflect the nonpayment of our loan to Nusamba;
- increased deferred income taxes by $4.2 million to reflect tax liabilities relating to our increased equity ownership in PT Freeport Indonesia;
- reduced minority interests by $52.0 million to reflect our increased equity ownership in PT Freeport Indonesia; and
- increased property, plant and equipment by $267.3 million to reflect the cost of the acquisition in excess of the book value of the equity ownership in PT Freeport Indonesia we acquired.

Republic of Indonesia

The Republic of Indonesia consists of more than 17,000 islands stretching 3,000 miles along the equator from Malaysia to Australia and is the fourth most populous nation in the world with over 200 million people. Following many years of Dutch colonial rule, Indonesia gained independence in 1945 and now has a presidential republic system of government.

Maintaining a good working relationship with the Government of Indonesia is of particular importance to us because all of our mining operations are located in Indonesia. Our mining complex was Indonesia's first copper mining project and was the first major foreign investment in Indonesia following the economic development program instituted by the Government of Indonesia in 1967. We work closely with the central, provincial and local governments in development efforts in the area surrounding our operations.

In May 1998, President Suharto, Indonesia's political leader for more than 30 years, resigned in the wake of an economic crisis in Indonesia and other parts of Southeast Asia and in the face of growing social unrest. Vice President B.J. Habibie succeeded Suharto. In June 1999, Indonesia held a new parliamentary election on a generally peaceful basis as the first step in the process of electing a new president. In October 1999, in accordance with the Indonesian constitution, the country's highest political institution (the People's Consultative Assembly), composed of the newly elected national parliament along with additional provincial and other representatives, elected Abdurrahman Wahid as president and Megawati Sukarnoputri as vice president.

There were repeated challenges to the political leadership of President Wahid since his election in October 1999. In July 2001, the People's Consultative Assembly voted to immediately remove President Wahid, and elected Vice President Megawati Sukarnoputri as the new president. The international community, including the United States, expressed support for the newly elected president and cabinet.

Economic and political conditions remain challenging in Indonesia. The Indonesian economy grew by an estimated 3 percent in 2001 after growing by an estimated 5 percent in 2000 and remaining flat in 1999. Indonesia is Asia's second largest exporter of oil and has benefited from higher oil prices in recent years. Progress on reforming the nation's failed banking system and raising capital from the sale of bank-related assets has been slow. As a result, the country remains heavily reliant on foreign aid to balance its budget and the national currency, the rupiah, declined approximately 10 percent in value during 2001.

Despite gradual improvements on the economic front, Indonesia's recovery remains vulnerable to ongoing political and social tensions. Incidents of violence and separatist pressures continue to add to political instability within the country as the Sukarnoputri administration works to address the country's economic and social issues. Although incidents of violence continue to be reported in Papua, no incidents of separatist violence were reported in PT Freeport Indonesia's area of operations, where the local community leaders continue to support peaceful solutions to the complex issue of regional autonomy.

While the uncertainties of the autonomy process have created concern among foreign investors, the Indonesian government has repeatedly assured investors that existing contracts would be honored. The president of Indonesia and several cabinet members have publicly stated that the Government of Indonesia will honor previously existing contracts and that they have no intention of revoking or unilaterally amending such contracts, specifically including PT Freeport Indonesia's Contract of Work. Our belief that our Contracts of Work will continue to be honored is further supported by U.S. laws, which prohibit U.S. aid to countries that nationalize property owned by, or take steps to nullify a contract with, a U.S. citizen or company at least 50 percent owned by U.S. citizens if the foreign country does not within a reasonable time take appropriate steps to provide full value compensation or other relief under international law.

Pro-independence movements in certain areas continue to be prominent, especially in the province of Aceh, and to a lesser extent in Papua. The area surrounding our mining development is sparsely populated by local people and former residents of more populous areas of Indonesia, some of whom have resettled in Papua under the Government of Indonesia's transmigration program. A segment of the local population is opposing Indonesian rule over Papua, and several separatist groups have sought political independence for the province. In Papua, there have been sporadic attacks on civilians by separatists and sporadic but highly publicized conflicts between separatists and the Indonesian military.

We have a board-approved policy statement on social, employment and human rights, and have comprehensive and extensive social, cultural and community development programs, to which we have committed significant financial and managerial resources. These policies and programs are designed to address the impact of our operations on the local villages and people and to provide assistance for the development of the local people. While we believe these efforts should serve to avoid damage to and disruptions of our mining operations, our operations could be damaged or disrupted by social, economic and political forces beyond our control. For example, in March 1996, local people engaged in acts of vandalism that caused approximately $3 million in damages to our property and caused us to close the Grasberg mine and mill for three days as a precautionary measure, although our concentrate shipments were not interrupted. See "Risk Factors."

Contracts of Work

PT Freeport Indonesia and Eastern Minerals conduct their current exploration operations and PT Freeport Indonesia conducts its mining operations in Indonesia by virtue of their Contracts of Work. Both Contracts of Work govern our rights and obligations relating to taxes, exchange controls, royalties, repatriation and other matters. Both Contracts of Work were concluded pursuant to the 1967 Foreign Capital Investment Law, which expresses Indonesia's foreign investment policy and provides basic guarantees of remittance rights and protection against nationalization, a framework for economic incentives and basic rules regarding other rights and obligations of foreign investors. Any disputes regarding the provisions of the Contracts of Work are subject to international arbitration.

PT Freeport Indonesia's Contract of Work covers both Block A, which was first included in a 1967 Contract of Work that was replaced by a new Contract of Work in 1991, and Block B, to which we gained rights in 1991. The initial term of our Contract of Work expires in December 2021, but we can extend it for two 10-year periods subject to Indonesian government approval, which cannot be withheld or delayed unreasonably. We originally had the rights to explore 6.5 million acres in Block B, but pursuant to the Contract of Work we have only retained the rights to 0.5 million acres, which we believe, following significant geological assessment, contain the most promising exploration opportunities.

Eastern Minerals signed its Contract of Work in August 1994. The Contract of Work originally covered approximately 2.5 million acres. Eastern Minerals' Contract of Work provides for a four-to-seven year exploratory term and a 30-year term for mining operations, which we can extend for two 10-year periods subject to Indonesian government approval which cannot be withheld or delayed unreasonably. In 2001, because of safety and security issues and uncertainty relating to a possible conflict between our mining and exploration rights in certain forest areas covered by our Contracts of Work and an Indonesian law enacted in 1999 prohibiting open-pit mining in forest preservation areas, we requested and received from the Government of Indonesia formal temporary suspensions of our obligations under the Contracts of Work in all areas outside of Block A. These suspensions were granted for one-year periods ending February 26, 2002 for Block B, March 31, 2002 for PT Nabire Mining and November 15, 2002 for Eastern Minerals. We are currently seeking a renewal of the Block B suspension and expect to seek suspension renewals for the other areas in 2002 for one or more additional one-year periods by written request to the Government of Indonesia.

Like the PT Freeport Indonesia contract, the Eastern Minerals Contract of Work requires us to relinquish our rights to 25 percent of the original 2.5 million-acre Contract of Work area at the end of each of three specified periods. As of December 31, 2001, we had relinquished approximately 1.25 million acres, and within three months of resuming exploratory activity under the Contract of Work we must relinquish approximately 0.6 million additional acres.

PT Freeport Indonesia pays a copper royalty under its Contact of Work that varies from 1.5 percent of copper net revenue at a copper price of $0.90 or less per pound to 3.5 percent at a copper price of $1.10 or more per pound. The Contract of Work royalty rate for gold and silver sales is 1.0 percent.

A large part of the mineral royalties under Government of Indonesia regulations are designated to the provinces from which the minerals are extracted. In connection with our "fourth concentrator mill expansion," PT Freeport Indonesia agreed to pay the Government of Indonesia voluntary additional royalties, that is, royalties not required by our Contract of Work, to provide further support to the local governments and the people of Papua. The additional royalties are paid on metal from production above 200,000 metric tons of ore per day. The additional royalty for copper equals the Contract of Work royalty rate and for gold and silver equals twice the Contract of Work royalty rates. Therefore, our royalty rate on copper net revenues from production above 200,000 metric tons of ore per day is double the Contract of Work royalty rate, and our royalty rates on gold and silver sales from production above 200,000 metric tons of ore per day are triple the Contract of Work royalty rates.

The combined royalties, including the voluntary additional royalties which became effective January 1, 1999, totaled $24.3 million in 2001, $20.2 million in 2000 and $23.0 million in 1999.

Ore Reserves

During 2001, additions to the aggregate proven and probable reserves at the Grasberg mining complex totaled approximately 156 million metric tons of ore representing increases of 3.2 billion recoverable pounds of copper and 4.3 million recoverable ounces of gold. Year-end aggregate proven and probable recoverable reserves, net of 2001 production, were 2.6 billion metric tons of ore averaging 1.13 percent copper, 1.05 grams of gold per metric ton and 3.72 grams of silver per metric ton representing 52.5 billion pounds of copper, 64.5 million ounces of gold and 151.6 million ounces of silver. Additions were made to the Dom open pit, the Grasberg block cave, the Deep Ore Zone block cave and at Kucing Liar. Improvements to gold recovery at the Grasberg open pit offset reductions to gold recovery expectations at Kucing Liar.

Pursuant to joint venture arrangements between PT Freeport Indonesia and Rio Tinto, Rio Tinto has a 40 percent interest in production from reserves above those reported at December 31, 1994. Net of Rio Tinto's share, PT Freeport Indonesia's share of proven and probable recoverable copper, gold and silver reserves was 39.4 billion pounds of copper, 50.2 million ounces of gold and 114.5 million ounces of silver as of December 31, 2001. FCX's equity interest in proven and probable recoverable reserves as of December 31, 2001, including Nusamba's interest that we acquired subsequent to year end, was 35.7 billion pounds of copper, 45.5 million ounces of gold and 103.8 million ounces of silver. We estimated recoverable reserves using an average copper price of $0.87 per pound and an average gold price of $285 per ounce. Using a copper price of $0.75 per pound and a gold price of $270 per ounce would have resulted in less than a one percent reduction in our estimated recoverable copper and gold reserves.

All of our proven and probable reserves lie within Block A. The Grasberg deposit contains the largest single gold reserve and is one of the largest copper reserves of any mine in the world. Aggregate Grasberg open pit and underground proven and probable ore reserves as of December 31, 2001, are shown below along with those of our other deposits. Reserve calculations were prepared by our employees under the supervision of George MacDonald, Vice President of Exploration for Freeport-McMoRan Copper & Gold Inc. (FCX), and were verified by Independent Mining Consultants, Inc., experts in mining, geology and reserve determination. See "Risk Factors." Our current mine plan has been developed and our operations are based on completing the mining of all of our currently designated recoverable reserves before 2041, which would be the expiration of our Contract of Work including two 10-year extensions. Prior to the expiration of the initial term of our Contract of Work in December 2021, under our current mine plan we expect to mine approximately 63 percent of aggregate proven and probable ore, representing approximately 71 percent of PT Freeport Indonesia's share of recoverable copper reserves and approximately 77 percent of PT Freeport Indonesia's share of recoverable gold reserves.

	Proven				Probable				
		Average Ore Grade				Average Ore Grade			Total
	Metric Tons of Ore (000s)[a]	Copper	Gold	Silver	Metric Tons of Ore (000s)[a]	Copper	Gold	Silver	Metric Tons of Ore (000s)[a]

		(%)	(g/t)	(g/t)		(%)	(g/t)	(g/t)	
Developed and producing:									
Grasberg open pit	242,954	1.14	1.59	2.67	703,925	0.99	1.11	2.38	946,879
Deep Ore Zone	72,196	1.03	0.75	5.65	96,684	0.93	0.68	5.00	168,880
Intermediate Ore Zone	2,597	1.27	0.25	8.93	1,052	1.18	0.25	6.80	3,649
Undeveloped:									
Grasberg block cave	119,605	1.24	1.23	2.92	662,850	1.13	0.85	2.90	782,455
Kucing Liar	161,170	1.32	1.05	5.25	261,786	1.34	1.32	6.53	422,956
Mill Level Zone	23,826	1.53	1.07	6.90	26,507	1.28	1.01	3.06	50,333
Big Gossan	-	-	-	-	37,349	2.69	1.02	16.42	37,349
Ertsberg Stockwork Zone	21,469	0.58	0.84	1.84	79,262	0.55	0.80	1.73	100,731
Dom block cave	11,894	1.18	0.31	6.40	31,757	1.07	0.31	5.76	43,651
Dom open pit	6,882	1.87	0.46	9.88	20,118	1.78	0.42	9.50	27,000
Total	662,593	1.19	1.22	3.96	1,921,290	1.11	0.99	3.65	2,583,883

	Mill Recoveries (%)			Proven and Probable Recoverable Reserves[b]		
	Copper	Gold	Silver	Copper	Gold	Silver
				(Billions of Lbs.)	(Millions of Ozs.)	(Millions of Ozs.)
Developed and producing:						
Grasberg open pit	85.0	83.7	63.8	17.6	30.7	37.3
Deep Ore Zone	85.0	79.1	63.8	3.0	3.0	14.3
Intermediate Ore Zone	85.0	79.1	63.8	0.1	-	0.5
Undeveloped:						
Grasberg block cave	85.0	79.1	63.8	16.3	17.6	36.5
Kucing Liar	82.8	53.1	59.5	9.9	8.5	38.4
Mill Level Zone	85.0	79.1	63.8	1.3	1.3	3.9
Big Gossan	85.0	79.1	63.8	1.8	0.9	9.9
Ertsberg Stockwork Zone	85.0	79.1	63.8	1.0	2.0	2.8
Dom block cave	82.6	75.2	62.0	0.8	0.3	4.1

Dom open pit	69.0	68.0	59.0	0.7	0.2	3.9
Total				52.5	64.5	151.6
PT Freeport Indonesia's share				39.4	50.2	114.5
FCX's equity share[c]				35.7	45.5	103.8

a. Ore reserve tonnage estimates are after application of applicable mining recovery factors.
b. Recoverable reserves represent estimated payable metal after application of estimated mill recovery rates and smelter recovery rates of 96.5 percent for copper, 97.0 percent for gold and 78.5 percent for silver. The term "recoverable reserve" means that part of a mineral deposit which we estimate can be economically and legally extracted or produced at the time of the reserve determination.
c. Reflects our 90.6 percent ownership interest after repayment of the Nusamba debt and acquisition of Nusamba's interest in PT Freeport Indonesia in February 2002. See "Nusamba Loan Guarantee."

The following table sets forth the average drill hole spacing for each of our ore bodies. The average drill hole spacing within each ore body has been calculated using the distance from the center of each block in the resource model to the nearest drill hole composite. The averages of these values were calculated within the volume of each ore body and are reported under the column entitled "Average Distance: To Nearest Sample." This value represents at least one-half of the average drill hole spacing within each deposit. The value under the column entitled "Average Distance: Between Drill Holes" was calculated by multiplying the average minimum distance value by two, and represents the maximum average drill hole spacing.

		Spacing (in meters)			Average Distance (in meters)	
Deposit	Mining Unit	Surface Drilling Grids	Underground (& Surface) Drill Fans	Drilling Method	To Nearest Sample	Between Drill Holes (less than)
Grasberg	Open Pit	50	75	core	45	89
Grasberg	Block Cave	-	100	core	46	92
Deep Ore Zone	Block Cave	-	50	core	13	25
Intermediate Ore Zone	Block Cave	-	50	core	13	25
Ertsberg Stockwork Zone	Block Cave	100	50	core	26	52
Mill Level Zone	Sublevel Cave	-	50	core	20	40
Kucing Liar	Block Cave	-	75	core	36	72
Big Gossan	Open Stope	100	50	core	22	45

Dom	Open Pit	-	50	core	25	50
Dom	Block Cave	-	50	core	26	52

Mining Operations

We and our predecessors have conducted exploration and mining operations in Block A since 1967 and have been the only operator of those operations. Following are descriptions of ore mines in production, ore mines in development and our ore bodies.

Mines in Production

. We currently have three mines in operation: the Grasberg open pit, the Intermediate Ore Zone and the Deep Ore Zone. As of December 31, 2001, our capital expenditures incurred to date for our mining operations in Indonesia totaled $4.6 billion. Our mine development, expansion and infrastructure capital expenditures totaled $83.7 million in 2001, $61.0 million in 2000 and $56.8 million in 1999. These expenditures primarily related to development of the Deep Ore Zone ore body. We began open-pit mining of the Grasberg ore body in January 1990. Production is at the 3,520- to 4,250-meter elevation level and totaled 78.2 million metric tons of ore in 2001, which provided 89 percent of our mill feed. The underground Grasberg reserves will be mined near the end of open-pit mining, which is expected to continue until approximately 2015.

The Intermediate Ore Zone is an underground block-cave operation that began production in the first half of 1994. Production is at the 3,475-meter elevation level and totaled 7.6 million metric tons of ore in 2001. We expect to fully deplete the Intermediate Ore Zone by 2003.

The Deep Ore Zone ore body lies vertically below the Intermediate Ore Zone. We began production from the Deep Ore Zone ore body in 1989, but we suspended production in 1991 in favor of production from the Grasberg deposit. Production using the block-cave method at the Deep Ore Zone officially restarted in September 2000. Production is at the 3,150-meter elevation level and totaled 2.0 million metric tons of ore in 2001. The Deep Ore Zone is expected to ramp up from its approximately 14,000 metric tons of ore per day rate at December 31, 2001, to a full production rate of 25,000 metric tons of ore per day by mid-2002, well ahead of original projections. We are conducting a feasibility study to assess increasing the Deep Ore Zone mine production rate to 35,000 metric tons of ore per day.

Our principal source of power for all our operations is a coal-fired power plant that was built in conjunction with our fourth concentrator expansion (see "Infrastructure Improvements"). Peaking and backup power is supplied by medium-speed diesel generators. Water for our operations is provided by a combination of naturally occurring mountain streams and water derived from our underground operations. The average annual rainfall in the project area is 180 inches.

Mines in Development

. Four other significant ore bodies, referred to as the Dom, Big Gossan, Kucing Liar and the newly discovered Ertsberg Stockwork Zone are located in Block A. These ore bodies are at various stages of development, and are included in our proven and probable reserves. We incurred $8.4 million for mine development, expansion and infrastructure capital expenditures related to these ore bodies during the last three years. See "Risk Factors."

The Dom ore body lies approximately 1,500 meters southeast of the depleted Ertsberg open-pit deposit. We completed pre-production development at the Dom including all maintenance, warehouse and service facilities just as Grasberg began open-pit production in 1990. We have deferred production at the Dom ore body and may not begin until after completion of open-pit mining.

The Big Gossan ore body is located approximately 1,000 meters southwest of the original Ertsberg open-pit deposit. We began the initial underground development of the ore body in 1993 when we drove tunnels from the mill area into the ore zone at the 3,000-meter elevation level. We expect to use a variety of stoping methods to mine the deposit, and plan to complete a detailed feasibility study in 2002 to determine when to begin production.

The Kucing Liar ore body lies on the southern flank of and underneath the southern portion of the Grasberg open pit at the 2,500- to 3,100-meter elevation level. We are reviewing development plans for Kucing Liar.

The Ertsberg Stockwork Zone ore body extends off the southwest side of the Deep Ore Zone ore body at the 3,150- to 3,750-meter elevation level. Drilling efforts continue to determine the extent of this ore body, which we expect to mine using a block-cave method after we complete mining at the Deep Ore Zone ore body.

The projected aggregate capital expenditures required to reach full production capacity for each of our undeveloped ore bodies based on our current mine plans and our proven and probable reserves as of December 31, 2001, are shown below (in millions). Actual costs could differ materially from these estimates as most of the expenditures will not be incurred for several years. In addition, these costs will be shared with Rio Tinto in accordance with our joint venture agreement.

Grasberg block cave	$950
Kucing Liar block cave	700
Dom block cave	200
Big Gossan	150
Ertsberg Stockwork Zone block cave	100
Dom open pit	40
Mill Level Zone sublevel cave	30
Total	$2,170

Description of Ore Bodies

. Our ore bodies cluster within and around two main igneous intrusions, the Grasberg Monzo diorite and the Ertsberg diorite. The host rocks of these ore bodies include both carbonate and clastic rocks that form the ridge crests and upper flanks of the Sudirman Range, and the igneous rocks of monzonitic to dioritic composition that intrude them. The igneous-hosted ore bodies (the Grasberg pit and block cave and the Ertsberg Stockwork Zone block cave) occur as vein stockworks and disseminations of copper sulphides, dominated by chalcopyrite and, to a much lesser extent, bornite. The sedimentary-rock hosted ore bodies occur as 'magnetite-rich, calcium/magnesian skarn' replacements, whose location and orientation are strongly influenced by major faults and by the chemistry of the carbonate rocks along the margins of the intrusions.

The copper mineralization in these skarn deposits is also dominated by chalcopyrite, but higher bornite concentrations are common. Moreover, gold occurs in significant concentrations in all of the district's ore bodies, though rarely visible to the naked eye. These gold concentrations usually occur as inclusions within the copper sulphide minerals, though, in some deposits, can also be strongly associated with pyrite.

The following map, which encompasses an area of approximately 42 square kilometers (approximately 16 square miles), indicates the relative positions and sizes of our reported reserve ore bodies and their locations.

The following diagram indicates the relative elevations (in meters) of our reported reserve ore bodies.

The following chart illustrates our current plans for sequencing and producing each of our ore bodies and the years in which we currently expect that production of each ore body will begin and end. Our mine plan is subject to change based on a number of factors including the results of our exploration efforts.

During 2001, we mined an average of 684,800 metric tons of material per day, including ore and overburden. We expect to mine approximately 786,000 metric tons of material per day in 2002 and do not require any additional approvals for higher rates. The following chart illustrates our current aggregate mill capacity; our aggregate permitted mill capacity; and our projected milling rates. The decline in milling rates in 2015 reflects the expected completion date of open-pit mining at the Grasberg ore body. We are continuing to develop mine plans to optimize production levels and to offset the anticipated decline in 2015.

Exploration

As a result of our joint venture arrangements, Rio Tinto pays for 40 percent of our exploration and drilling costs in Papua. The joint ventures incurred total exploration costs of $14.4 million in 2001 and the joint ventures' exploration budget for 2002 totals approximately $4 million. As a result of continuing low commodity prices, we have reduced our exploration program for 2002 to focus largely on available exploration data. Limited drilling during 2002 will be directed towards delineation of reserves adjacent to our Deep Ore Zone.

In June 1998, we entered into a joint venture agreement to conduct exploration activities in PT Nabire Bakti Mining's Contract of Work area covering approximately 1.0 million acres in several blocks contiguous to PT Freeport Indonesia's Block B and one of Eastern Minerals' blocks in Papua. Rio Tinto shares in 40 percent of our interest and costs in this exploration joint venture. We and Rio Tinto can earn up to a 62 percent interest in the PT Nabirie Bakti Mining Contract of Work by spending up to $21 million on exploration and other activities in the joint venture areas. We have spent $15.7 million through December 31, 2001.

Field exploration activities in Block B, which includes the Wabu Ridge gold prospect, as well as in the other Contract of Work areas of Eastern Minerals and PT Nabire Bakti Mining have been temporarily suspended. The suspensions are due to safety and security issues and uncertainty relating to a possible conflict between our mining and exploration rights in certain forest areas covered by the Contracts of Work and an Indonesian law enacted in 1999 prohibiting open-pit mining in forest preservation areas. All of these areas are outside of our current mining operations area.

Milling and Production

The ore from our mines moves by a conveyor system to a series of ore passes through which it drops to our milling and concentrating complex located approximately 2,900 meters above sea level. At the mill, the ore is crushed and ground and mixed in tanks with water and small amounts of flotation reagents where it is continuously agitated with air. During this physical separation process, copper-, gold- and silver-bearing particles rise to the top of the tanks and are collected and thickened into a concentrate. The concentrate leaves the mill complex as a slurry, consisting of approximately 65 percent solids by weight, and is pumped through three parallel 115 kilometer pipelines to our coastal port site facility at Amamapare where it is filtered, dried and stored for shipping. Ships are loaded at dock facilities at the port until they draw their maximum water, then move to deeper water, where loading is completed from shuttling barges.

In early 1998, PT Freeport Indonesia completed construction on the fourth concentrator mill expansion. Pursuant to the expansion joint venture agreement, in addition to funding its 40 percent share of all expansion costs including the fourth concentrator mill expansion, Rio Tinto provided a $450 million nonrecourse loan to PT Freeport Indonesia for PT Freeport Indonesia's share of the cost of the expansion. In less than two and one-half years beginning in 1998, PT Freeport Indonesia repaid the $450 million loan, plus interest, from its share of incremental cash flow attributable to the expansion. Operating, nonexpansion capital and administrative costs are shared proportionately between PT Freeport Indonesia and Rio Tinto based on the ratio of (a) the incremental revenues from production from the expansion and (b) total revenues from production from Block A, including production from PT Freeport Indonesia's previously existing reserves. PT Freeport Indonesia receives 100 percent of the cash flow from specified annual amounts of copper, gold and silver production through 2021 and will receive 60 percent of all remaining cash flow thereafter.

Our production results for the last three years are as follows:

	Years Ended December 31,			Percentage Change	
	2001	2000	1999	2000 to 2001	1999 to 2000
Mill throughput (metric tons of ore per day)	237,800	223,500	220,700	6%	1%
Copper production, net to PT Freeport Indonesia (000 pounds)	1,393,400	1,388,100	1,428,100	-	(3)%
Gold production, net to PT Freeport Indonesia (ounces)	2,634,900	1,899,500	2,379,100	39%	(20)%
Average net cash production costs per pound of copper[a]	$0.07	$0.23	$0.09	(70)%	156%

a. Includes site production and delivery costs, smelting and refining costs, and royalties, less credits for gold and silver sales.

Mill throughput averaged a record 237,800 metric tons of ore per day during 2001. In May 2000, PT Freeport Indonesia, in consultation with the Government of Indonesia, voluntarily agreed to temporarily limit Grasberg open-pit production because of an incident at its Wanagon overburden stockpile. Normal overburden placement at the Wanagon overburden stockpile resumed and the restriction on production from the Grasberg open pit was lifted at the end of 2000 (see "Wanagon Overburden Stockpile Slippage").

Copper production remained relatively unchanged over the past three years as the record throughput rates were offset by lower ore grades. Gold production has fluctuated primarily because of variances in ore grades, and is expected to decline in 2002 because of lower projected ore grades than those mined in 2001. Average net cash production costs per pound of copper were a record-low $0.07 per pound in 2001 primarily because of higher credits from gold sales and because of lower site production costs. For more information regarding our operating and financial results, see "Item 6. Selected Financial Data" and "Items 7. and 7A. Management's Discussion and Analysis of Financial Condition and Results of Operations and Quantitative and Qualitative Disclosures About Market Risk."

Infrastructure Improvements

The location of our mining operations in a remote area requires that our operations be virtually self-sufficient. In addition to the mining facilities described above, in the course of the development of our project we have constructed ourselves or participated with others in the construction of an airport, a port, a 119 kilometer road, an aerial tramway, a hospital and related medical facilities, and two town sites with housing, schools and other facilities sufficient to support more than 17,000 persons.

In 1996, we completed a significant infrastructure program, which includes various residential, community and commercial facilities. We designed the program to provide the infrastructure needed for our operations, to enhance the living conditions of our employees, and to develop and promote the growth of local and other third party activities and enterprises in Papua. We have developed the facilities through joint ventures or direct ownership involving local Indonesian interests and other investors.

From December 1993 to March 1997, PT Freeport Indonesia sold $270.0 million of infrastructure assets to joint ventures owned one-third by PT Freeport Indonesia and two-thirds by PT ALatieF Nusakarya Corporation (ALatieF), an Indonesian investor. Funding for the purchases consisted of $90.0 million in equity contributions by the joint venture partners, a $60.0 million bank loan and FCX's 93/4% senior notes, which were repaid in 2001. PT Freeport Indonesia subsequently sold its one-third interest in the joint ventures to ALatieF in March 1997. In September 1998, PT Freeport Indonesia reacquired for $30 million an aggregate one-third interest in the joint ventures. During 2000, PT Freeport Indonesia purchased the remaining interest in the joint ventures for $25.9 million cash and the assumption of $34.1 million of bank debt.

In December 1997, we sold the new coal-fired power plant facilities associated with the fourth concentrator mill expansion for $366.4 million to the joint venture that owns the power plants that already provided electricity to us. The purchase price included $123.2 million for Rio Tinto's share of the new power plant facilities. Asset sales to the power joint venture totaled $581.4 million through 1997, including $458.2 million of assets we owned. We subsequently sold our 30 percent interest in the joint venture to the other partners and we purchase power under infrastructure asset financing arrangements pursuant to a power sales agreement.

Marketing

PT Freeport Indonesia sells its copper concentrates, which contain significant quantities of gold and silver, under United States dollar-denominated sales agreements, mostly to companies in Asia and Europe and to international trading companies. We sell substantially all of our budgeted production of copper concentrates under long-term contracts with the selling price based on world metals prices (generally the London Metal Exchange settlement prices for Grade A copper). Under these contracts, initial billing occurs at the time of shipment and final settlement on the copper portion is generally based on average prices for a specified future period. Gold generally is sold at the average London Bullion Market Association price for a specified month near the month of shipment.

Revenues from concentrate sales are recorded net of royalties (see "Contracts of Work"), treatment and all refining charges (including participation charges, if applicable, based on the market prices of metals), and the impact of derivative financial instruments, if any, used to hedge against risks from metals price fluctuations. Moreover, because a portion of the metals contained in copper concentrates is unrecoverable as a result of the smelting process, our revenues from concentrate sales are also recorded net of allowances based on the quantity and value of these unrecoverable metals. These allowances are a negotiated term of our contracts and vary by customer. Treatment and refining charges represent payments to smelters and refiners and are either fixed or in certain cases vary with the price of copper. We sell some copper concentrates in the spot market. See "Risk Factors."

We have commitments, including commitments from Atlantic Copper and PT Smelting, for essentially all of our estimated 2002 production at market prices. We expect our share of sales for 2002 to approximate 1.5 billion pounds of copper and 2.1 million ounces of gold. Projected 2002 copper and gold sales reflect the expectation of higher average mill throughput rates than in 2001 and lower gold grades. See "Risk Factors."

PT Freeport Indonesia has a long-term contract through 2007 to provide Atlantic Copper with approximately 60 percent of its copper concentrate requirements at market prices. PT Freeport Indonesia's agreement with PT Smelting provides for the supply of 100 percent of the copper concentrate requirements necessary to reach the Gresik smelter's design capacity and substantially all of any incremental copper concentrate requirements that may be needed in excess of that amount. For the first 15 years of PT Smelting's operations beginning in December 1998, the treatment and refining charges on the majority of the concentrate PT Freeport Indonesia supplies will not fall below a specified minimum rate, currently $0.23 per pound, which has been the rate since commencement of operations in 1998 and is the expected rate for 2002. We anticipate that PT Freeport Indonesia will sell approximately 50 percent of its annual concentrate production to Atlantic Copper and PT Smelting. A recap of PT Freeport Indonesia's aggregate percentage concentrate sales to its affiliates and to other parties for the last three years follows:

	2001	2000	1999
PT Smelting	28%	25%	17%
Atlantic Copper	23%	22%	23%
Other parties	49%	53%	60%
	100%	100%	100%

Investment in Smelters

Our investment in smelters (Atlantic Copper and PT Smelting) serves an important role in our concentrate marketing strategy. Approximately one-half of PT Freeport Indonesia's concentrate production is sold to its affiliated smelters, Atlantic Copper and PT Smelting, and the remainder is sold to other customers.

Treatment charges for smelting and refining copper concentrates represent a cost to PT Freeport Indonesia and income to Atlantic Copper and PT Smelting. However, because we have integrated our upstream (mining and milling) and downstream (smelting and refining) operations, we are able to achieve operating hedges which substantially offset the effect of changes in treatment charges for smelting and refining PT Freeport Indonesia's copper concentrates. For example, while low smelting and refining charges will adversely affect the operating results of Atlantic Copper and PT Smelting, low charges will benefit the operating results to PT Freeport Indonesia's mining operations.

As a result, changes in smelting and refining charges do not have a significant impact on our consolidated operating results. Taking into account taxes and minority ownership interests, an equivalent change in the charges PT Freeport Indonesia pays and the charges Atlantic Copper and PT Smelting receive would essentially offset in our consolidated operating results.

Atlantic Copper, S.A.

We own 100 percent of Atlantic Copper. Atlantic Copper completed the last expansion of its production capacity in 1997 and its smelter currently has a design capacity of 290,000 metric tons of copper per year. During 2001, Atlantic Copper treated 891,100 metric tons of concentrate and produced 280,000 metric tons of new copper anodes. Production for 2001 was negatively impacted by a scheduled 27-day major maintenance turnaround in April 2001. The next scheduled major maintenance turnaround is not anticipated for three years. Atlantic Copper purchased approximately 63 percent of its 2001 concentrate requirements from PT Freeport Indonesia at market prices. We have no present plans to expand Atlantic Copper's production capacity. Atlantic Copper has experienced no material operating problems, and we are not aware of any potential material environmental liabilities at Atlantic Copper.

We contributed $7.6 million to Atlantic Copper during 2001, $32.4 million in 2000 and $40.0 million in 1999. The funds are intended to strengthen Atlantic Copper's financial structure during this period of extremely low treatment and refining charge rates. Our total investment in Atlantic Copper through December 31, 2001, totaled $219.9 million.

PT Smelting

PT Freeport Indonesia owns 25 percent of PT Smelting. During 2001, PT Smelting treated 702,900 metric tons of concentrate and produced 217,500 metric tons of new copper anodes. PT Smelting has no present plans to expand its treatment capacity and has experienced no material operating problems. We are not aware of any potential material environmental liabilities at PT Smelting.

PT Smelting is a joint venture among PT Freeport Indonesia, Mitsubishi Materials Corporation, Mitsubishi Corporation and Nippon Mining & Metals Co., Ltd., which own 25 percent, 60.5 percent, 9.5 percent and 5 percent, respectively, of the outstanding PT Smelting common stock. PT Freeport Indonesia is providing nearly all of PT Smelting's copper concentrate requirements. PT Freeport Indonesia agreed to assign its earnings in PT Smelting to support a 13 percent cumulative annual return to the other owners for the first 20 years of operations. PT Freeport Indonesia's total investment in PT Smelting through December 31, 2001, totaled $96.4 million.

Competition

We compete with other mining companies in the sale of our mineral concentrates and the recruitment and retention of qualified personnel. Some competing companies possess financial resources equal to or greater than ours and possess multiple mining assets less geographically concentrated in a single area than ours. We believe, however, that we are the lowest cost copper producer in the world, taking into account customary credits for related gold and silver production, which we believe gives us a significant competitive advantage.

Social Development, Employment and Human Rights

We have a social, employment and human rights policy to ensure that we operate in compliance with the laws in the areas of our operations, and in a manner that respects basic human rights and the culture of the people who are indigenous to the area. We continue to incur significant costs on social and cultural activities, primarily in Papua. These activities include:

- comprehensive job training programs

- basic education programs
- several public health programs, including extensive malaria control
- agricultural assistance programs
- a business incubator program to encourage the local people to establish their own small scale businesses
- cultural preservation programs
- charitable donations

In 1996, PT Freeport Indonesia agreed to commit at least one percent of its revenues for the following 10 years to the Freeport Fund for Irian Jaya Development to support village-based health, education, economic and social development programs in its area of operations. This commitment replaced our community development programs in which we spent a similar amount of money each year. We contributed $14.1 million in 2001, $14.1 million in 2000 and $14.7 million in 1999 to the Freeport Fund for Irian Jaya Development.

Lembaga Pengembangan Masyarakat-Irian Jaya, or the People's Development Foundation-Irian Jaya, oversees disbursement of the funds we contribute to the Freeport Fund for Irian Jaya Development. The foundation's board of directors is made up of the head of the local government, currently a Kamoro; a leader of the Amungme people; a leader of the Kamoro people and leaders of the three local churches.

We believe that our social and economic development programs are responsive to the issues raised by the local villages and people and should help us to avoid disruptions of mining operations. Nevertheless, social and political instability in the area may adversely impact our mining operations. See "Risk Factors."

In December 2000, we endorsed the joint U.S. State Department-British Foreign Office Voluntary Principles on Human Rights and Security. Several major natural resources companies and important human rights organizations also endorsed the Voluntary Principles. We participated in drafting these principles with all of the parties involved and incorporated them into our social and human rights policy.

Environmental Matters

We have an environmental policy that commits us not only to compliance with applicable federal, state and local environmental statutes and regulations, but also to continuous improvement of our environmental performance at every operational site. We believe that we conduct our Indonesian operations pursuant to all necessary permits and are in compliance in all material respects with applicable Indonesian environmental laws, rules and regulations.

Mining operations on the scale of our operations in Papua involve significant environmental challenges, primarily related to the disposition of tailings, which are the crushed and ground rock material resulting from the physical separation of commercially valuable minerals from the ore. We have comprehensive, ongoing environmental monitoring and management plans for the disposal of tailings resulting from our milling operations, which have been approved by the Government of Indonesia. Pursuant to these plans, we manage and monitor the impact of our tailings disposal on the ecosystem of the Ajkwa River and the ecosystems of adjoining water bodies and the surrounding coastal areas. In 1997, we completed an engineered levee system to minimize the impact of the tailings through a controlled deposition area located on a portion of the flood plain on the Ajkwa River. We will revegetate and reclaim the deposition area when our mining operations are completed.

In furtherance of our commitments to the Indonesian government pursuant to our tailings plan, we monitor the acid-neutralizing capacity of tailings on a daily basis to ensure the discharge of non-acid generating tailings into our tailings deposition area. The net acid-neutralizing capacity of our tailings discharge is maintained through a managed program of blending underground ore with ore from the open pit, the addition of supplemental limestone (or lime) to the ore blend, and the addition of lime for control of the pH levels in the flotation system. Daily samples are collected and tested and this data is communicated to our mill operations so that adjustments in ore blending and lime/limestone addition can be made as appropriate.

With respect to waste rock, acid rock drainage is our primary environmental issue. Our approaches to this issue include the mitigation of acid rock drainage generation, the control of acid rock drainage migration, and the capture and treatment of acid rock drainage emanating from the stockpile. In addition, tests have shown the feasibility of revegetating the stockpile and, as a result, we have engaged in stockpile reclamation as an additional means of mitigating acid rock drainage.

We have made significant capital expenditures with respect to the capture and treatment of acid rock drainage and additional capital expenditures are currently in progress. In addition, we are in the process of developing and implementing technology for the treatment of captured acid rock drainage. In the interim, acid rock drainage collected by boreholes near the base of the stockpile is neutralized.

We have committed to independent external environmental audits of our Papua operations by qualified experts every three years, with the results to be made public. The second such audit was completed in 1999. The second audit reported that we continue to be in material compliance with Indonesian environmental laws and regulations and that we had fulfilled the recommendations in the 1996 audit report. The 1999 external audit report made some additional environmental management recommendations that are being implemented. The report concluded that our environmental management systems achieve the standard of practice for world-class mines. The auditors also found our environmental management systems to be exemplary and a showcase for the mining industry. We also are continuing our annual internal audits, through the life of our mining operations, so that our environmental management and monitoring programs will remain sound and our operations will remain in material compliance with local laws.

We have environmental approvals from the Government of Indonesia to expand our milling rate up to a maximum of 300,000 metric tons of ore per day. In 2001, we averaged 237,800 metric tons of ore per day and we expect to average 245,000 metric tons of ore per day in 2002.

The costs of complying with environmental laws is a fundamental cost of our business. We incurred aggregate environmental capital expenditures and other environmental costs totaling $78.2 million in 2001, $106.1 million in 2000 and $73.3 million in 1999, including tailings management levee maintenance and mine reclamation. In 2002, we expect to incur approximately $11 million of environmental capital expenditures and $40 million of other environmental costs. These environmental capital expenditures are part of our $170 million overall 2002 capital expenditure budget.

Upon the completion of our mining operations, we will fulfill the remaining commitments we made to the Indonesian government in connection with our tailings management plan. Our options for revegetation of affected areas of the deposition area will include forage crops and grasses, fruits, grains and vegetables, and other traditional food and medicinal crops. Decisions on these options will be made after consultation with local and regional government and local residents. In addition to the revegetation and reclamation of the deposition area, we will continue to operate our wastewater treatment plants as long as necessary. We will also monitor and test the water discharged from our mine and the pH, sulfate and electrical conductivity levels of ground water in the deposition area. In addition, we will provide flood protection to surrounding areas by diverting the Ajkwa and Otomona Rivers and enhancing levee embankments. The stability of our levees will be ensured through periodic visual inspection, revegetation of the levee embankments, and the transfer of our levee roads for public use. Moreover, we will submit an annual written report to the Indonesian government regarding our reclamation activities.

Our ultimate reclamation and closure activities will be determined after consultation with the Indonesian government, affected local residents and other affected parties. Thus, we cannot currently project with precision the ultimate amount of reclamation and closure costs we will incur. Our best estimate at this time is that PT Freeport Indonesia's total reclamation and closure costs may require in excess of $100 million but are not expected to exceed $150 million. Estimates of reclamation and closure costs involve complex issues requiring integrated assessments over a period of many years and are subject to revision over time as we perform more complete studies. Some reclamation costs will be incurred during mining activities, while most closure costs and the remaining reclamation costs will be incurred at the end of mining activities, which are currently estimated to continue for more than 30 years.

Moreover, we cannot predict with any certainty the ultimate future uses of the deposition area once our mining operations are completed. In addition to forage crop and grass planting and food and medicinal crop production, possible future uses of the deposition area include rainforest production, production of timber, fuel woods, fruits and nuts and other economic forestry, and the cultivation of fish, shellfish and other aquaculture. The ultimate future uses of the deposition area will be determined after consultation with local and regional government and local residents.

In 1996, we began contributing approximately $0.6 million annually to a cash fund ($3.3 million balance at December 31, 2001) designed to accumulate at least $100 million by the end of our Indonesian mining activities. We plan to use this fund, including accrued interest, to pay for mine closure and reclamation costs. Any incremental costs in excess of the $100 million fund are expected to be incurred throughout the life of the mine and would be funded by operational cash flow or the sale of assets, as needed. An increasing emphasis on environmental issues and future changes in regulations could require us to incur additional costs that would be charged against future operations. Estimates involving environmental matters are by their nature imprecise and changes in government regulations, operations, technology and inflation could require us to revise them over time.

In 1998, a court in Huelva, Spain found an employee of Atlantic Copper guilty of a criminal offense against the environment in connection with Atlantic Copper's transportation and use of weak acid and spent electrolyte at a facility owned and operated by Minas de Rio Tinto, S.A.L. The court fined the employee approximately $48,000. The Huelva court ruling, which is currently on appeal, did not prohibit Atlantic Copper's Huelva complex from continuing to engage in these operations. Moreover, Atlantic Copper's weak acid and spent electrolyte transport and use operations have been authorized by Spanish environmental regulators. In response to the Huelva court decision, Atlantic Copper has voluntarily constructed an on-site plant for the treatment of weak acid and recycling of spent electrolyte. Since June 2001, no weak acid or spent electrolyte has been sent to the Minas de Rio Tinto facilities.

We believe that Atlantic Copper's facilities and operations are in compliance in all material respects with all applicable Spanish environmental laws, rules and regulations. During 1999, Atlantic Copper achieved ISO 14001 certification for its two remaining uncertified facilities. In addition, environmental management systems at all of Atlantic Copper's facilities have been validated as being in compliance with the European Union Regulation on Environmental Eco-Management and Eco-Auditing.

The Indonesian and Spanish governments may periodically revise their environmental laws and regulations or adopt new ones, and we cannot predict the effects on our operations of new or revised regulations. We have expended significant resources, both financial and managerial, to comply with environmental regulations and permitting and approval requirements, and we anticipate that we will continue to do so in the future. There can be no assurance that we will not incur additional significant costs and liabilities to comply with such current and future regulations or that such regulations will not have a material effect on our operations. See "Risk Factors."

Wanagon Overburden Stockpile Slippage

In May 2000, a slippage occurred in the overburden waste stockpile at the Wanagon basin following a period of excessive rainfall, causing a wave of water and material to overflow from the basin. Four employees of a contractor to PT Freeport Indonesia were working in the area and perished. Contained within the mud were the treatment solids from the lime precipitation of acid rock drainage, which then entered the tailings river system near the village of Banti. PT Freeport Indonesia charged $2.9 million to its 2000 production costs, primarily for assets lost as a result of the incident. In addition, we incurred environmental costs for overburden disposition, stockpile stabilization, laboratory testing and consulting studies relating to the Wanagon overburden waste stockpile.

Sampling and monitoring were initiated at a number of stations covering the entire tailings system between the mine and estuary. A specific risk analysis was conducted as a result of this event and was based on the monitoring program. No long-term environmental effects were found from the direct monitoring nor predicted by the risk assessment. The slippage caused a flow of sediments containing elevated levels of precipitated copper. As a result, water quality in the river was temporarily diminished due to higher levels of total suspended solids. According to water quality tests, the pre-slippage water quality in the river was substantially reestablished by the following day and was fully reestablished within 22 days after the incident.

PT Freeport Indonesia engaged international experts and outside consultants led by a team from the Institute of Technology of Bandung (Indonesia) to conduct a comprehensive study of the cause of the slippage and to recommend a future course of action. Working with the close cooperation of the Indonesian Department of Energy and Natural Resources and also BAPEDAL (the Indonesian environmental protection agency), the company initiated a stockpile stabilization program and voluntarily agreed to a temporary limitation on average production from the Grasberg open pit of 200,000 tons per day. Underground ore production was not affected. A safe-zone based on engineering calculations was subsequently identified along the Wanagon River and within the village of Banti. The residents within this zone were temporarily moved to Tembagapura, our original mining town site, and the houses were removed. These families were relocated to new housing designed according to their wishes and located on higher ground in Banti.

After successful completion of the stabilization program and consultation with affected local residents, and with the approval of the Indonesian government, normal overburden placement at the Wanagon stockpile resumed and the restriction on production from the Grasberg open pit was lifted at the end of 2000.

Employees and Relationship with FM Services Company

As of December 31, 2001, PT Freeport Indonesia had 7,488 employees (approximately 98 percent Indonesian). In addition, as of December 31, 2001, PT Freeport Indonesia had 1,672 contract workers, the vast majority of whom were Indonesian. Approximately 46 percent of our Indonesian employees are members of the All Indonesia Workers' Union, which operates under Government of Indonesia supervision. PT Freeport Indonesia has a labor agreement covering its hourly-paid Indonesian employees, the key provisions of which are renegotiated biannually. PT Freeport Indonesia's labor agreement was scheduled to expire on September 30, 2001. In June 2001, PT Freeport Indonesia and its workers agreed to terms for a new labor agreement that expires September 30, 2003. PT Freeport Indonesia's relations with the workers' union have generally been positive.

As of December 31, 2001, Atlantic Copper had 731 employees, of which approximately 76 percent are covered by a union contract that expires December 31, 2002. Atlantic Copper experienced no work stoppages in 2001 and relations with these unions have also generally been good.

FM Services Company, a Delaware corporation 50 percent owned by us as of December 31, 2001, has furnished executive, administrative, financial, accounting, legal, tax and similar services to us. We reimburse FM Services at its cost, including allocated overhead, for these services on a monthly basis. As of December 31, 2001, FCX had 16 employees and FM Services had 142 employees. FM Services employees also provide services to two other publicly traded companies.

Risk Factors

This report contains "forward-looking statements" within the meaning of the federal securities laws. Forward-looking statements are all statements other than statements of historical facts, such as statements regarding anticipated production volumes, sales volumes, ore grades, commodity prices, development and capital expenditures, mine production and development plans, environmental reclamation and closure cost and plans, reserve estimates, political, economic and social conditions in our areas of operations, and exploration efforts and results. Except for our ongoing obligations under the federal securities laws, we do not intend, and we undertake no obligation, to update or revise any forward-looking statements. Readers are cautioned that forward-looking statements are not guarantees of future performance and actual results may differ materially from those projected, anticipated or assumed in the forward-looking statements. Important factors that could cause our actual results to differ materially from those anticipated in the forward-looking statements include the following:

The terrorist attacks in the United States on September 11, 2001, as well as the United States-led response and the potential for additional future terrorist acts, have created economic and political uncertainties that could have a material adverse effect on our business and the prices of our securities.

The terrorist attacks that took place in the United States on September 11, 2001, as well as the United States-led response to such attacks and the potential for additional future terrorist acts, have caused uncertainty in the world's financial and insurance markets and may significantly increase political, economic and social instability in the geographic areas in which we operate, including the Republic of Indonesia where our primary operating assets are located. Moreover, there have been anti-American demonstrations in certain sections of Indonesia reportedly led by radical Islamic activists. Radical activists have also threatened to attack foreign assets and have called for the expulsion of United States and British citizens and companies from Indonesia.

It is possible that further acts of terrorism may be directed against the United States domestically or abroad, and such acts of terrorism could be directed against properties and personnel of companies such as ours. The attacks and the resulting economic and political uncertainties, including the potential for further terrorist acts, may cause the premiums charged for our insurance coverages to increase dramatically and may cause some coverages to be unavailable altogether. These developments may materially and adversely affect our business and profitability and the prices of our securities in ways we cannot predict at this time.

Because our primary operating assets are located in the Republic of Indonesia, our business may be adversely affected by Indonesian political, economic and social uncertainties beyond our control, in addition to the usual risks associated with conducting business in a foreign country.

Maintaining a good working relationship with the Indonesian government is important to us because all of our mining operations are located in Indonesia and are conducted pursuant to Contracts of Work with the Indonesian government. For a discussion of the risks relating to our Contracts of Work, see the risk factor below.

Indonesia continues to face political and economic uncertainties, including separatist movements and civil and religious strife in a number of provinces. In particular, social, economic and political instability in the province of Papua, where our mining operations are located, could have a material adverse impact on us if this instability results in damage to our property or interruption of our activities.

With the approval of the Indonesian government, we have temporarily suspended our field exploration activities outside of Block A due to safety and security issues and uncertainty relating to a possible conflict between our mining and exploration rights in certain forest areas covered by the Contracts of Work and an Indonesian law enacted in 1999 prohibiting open-pit mining in forest preservation areas.

In August 1998, we suspended operations for three days at our Grasberg mine in response to a wildcat work stoppage (not authorized by the workers' union) by a group of workers, a majority of whom were employees of our contractors. The workers cited employment issues as the reasons for their work stoppage. In March 1996, local people engaged in acts of vandalism that caused approximately $3 million of damages to our property and caused us to close the Grasberg mine and mill for three days as a precautionary measure.

Several separatist groups are opposing Indonesian rule over Papua and have sought political independence for the province. In response to the demands for political independence from Indonesia, new regional autonomy laws became effective January 1, 2001. However, the manner in which these new autonomy laws will be implemented and the degree of political and economic autonomy that is being provided to individual provinces, including Papua, is uncertain and is a current issue in Indonesian politics.

In Papua, there have been sporadic attacks on civilians by separatists and sporadic but highly publicized conflicts between separatists and the Indonesian military. For example, on September 29, 2001, a group of separatists set fire to facilities and took over an airfield in Ilaga, Papua, which is approximately 50 miles northeast of our mining operations and separated by a rugged, 14,000-foot mountain range through which there are no roads. The separatists occupied the airfield for three days, after which Indonesian security forces successfully reclaimed the airfield.

We are also subject to the usual risks associated with conducting business in a foreign country, including the risk of forced modification of existing contracts, changes in the country's laws or policies, including laws or policies relating to taxation, royalties, imports, exports and currency, and the risk of having to submit to the jurisdiction of a foreign court or having to enforce the judgment of a foreign court or arbitration panel against a sovereign nation within its own territory. In addition, we are subject to the risk of expropriation and our insurance policies do not provide coverage for losses caused by expropriation.

Our Contracts of Work are subject to termination if we do not comply with our contractual obligations and, if a dispute arises, we may have to submit to the jurisdiction of a foreign court or panel. In addition, unless the Indonesian government permits us to suspend activities under our Contracts of Work, we are required to continue those activities or potentially be declared in default.

PT Freeport Indonesia's and Eastern Minerals' Contracts of Work were entered into under Indonesia's 1967 Foreign Capital Investment Law, which provides guarantees of remittance rights and protection against nationalization. Our Contracts of Work can be terminated by the Government of Indonesia if we do not satisfy our contractual obligations, which include the payment of royalties and taxes to the government and the satisfaction of certain mining, environmental, safety and health requirements. Indonesian government officials have periodically raised questions regarding our compliance with Indonesian environmental laws and regulations and the terms of the Contracts of Work. In order to address these questions, the Government of Indonesia formed a fact-finding team in 2000 that reviewed our compliance with all aspects of PT Freeport Indonesia's Contract of Work. It is uncertain if or when the Indonesian government will release its report on its investigation. In addition, we cannot assure you that the Indonesian government's report, if and when released, will conclude that we are in compliance with all of the provisions of PT Freeport Indonesia's Contract of Work.

Moreover, in recent years, certain government officials and others in Indonesia have called into question the validity of contracts entered into by the Government of Indonesia prior to October 1999, including PT Freeport Indonesia's Contract of Work, which was signed in December 1991. We cannot assure you that the validity of, or our compliance with the terms of, the Contracts of Work will not be challenged for political or other reasons. PT Freeport Indonesia's and Eastern Minerals' Contracts of Work require that disputes with the Indonesian government be submitted to international arbitration. Notwithstanding the international arbitration provision, if a dispute arises under the Contracts of Work, we face the risk of having to submit to the jurisdiction of a foreign court or having to enforce the judgment of a foreign court or arbitration panel against Indonesia within its own territory.

In addition, our Contracts of Work permit us to suspend activities under the contracts for a period of one year by making a written request to the Indonesian government. These suspension requests are subject to the approval of the Indonesian government and are renewable annually. If we do not request a suspension or are denied a suspension, then we are required to continue our activities under the Contract of Work or potentially be declared in default. Moreover, if a suspension continues for more than one year for reasons other than force majeure and the Indonesian government has not approved such continuation, then the Indonesian government would be entitled to declare a default under the Contract of Work.

Servicing our debt will require a significant amount of cash, and our ability to generate sufficient cash depends on many factors, some of which are beyond our control.

Our ability to make payments on and to refinance our debt depends on our ability to generate sufficient cash flow. This, to a significant extent, is subject to commodity prices and general economic, financial, regulatory, political and other factors that are beyond our control. In addition, our ability to borrow funds in the future to service our debt will depend on our meeting the financial covenants in our amended bank credit facilities and other debt agreements we may have in the future. Future borrowings may not be available to us under our amended bank credit facilities or otherwise in amounts sufficient to enable us to pay our debt or to fund other liquidity needs. As a result, we may need to refinance all or a portion of our debt on or before maturity. Any inability to generate sufficient cash flow or refinance our debt on favorable terms could have a material adverse effect on our financial condition.

Political and economic conditions in Indonesia have had a negative effect on our credit ratings. The major credit rating agencies have generally had a policy of limiting the credit ratings of companies with operations limited to a particular country to the credit rating for the sovereign debt of that country. The current sovereign credit ratings of Indonesia are B3 by Moody's Investors Service and CCC by Standard & Poor's and our credit ratings on our senior unsecured debt are currently B3 by Moody's Investors Service and CCC by Standard & Poor's.

Our current credit ratings have an impact on the availability and cost of capital to us. As a result, in connection with our amended bank credit facilities, we have agreed to apply our future cash flows, after servicing scheduled payments of other debt, funding permitted capital expenditures and paying operating and other costs, to reducing amounts owed to the banks.

Although our amended credit facilities do not restrict our ability to use funds for exploration and will not preclude us from funding our anticipated exploration budget, the amended facilities do impose annual limitations on PT Freeport Indonesia's capital expenditures that limit the amount of funds we can use to develop new projects. These annual limitations are approximately $171 million for 2002, $188 million for 2003, $128 million for 2004 and $136 million 2005. If our capital expenditures in any year are less than 80% of the annual limitation for the year, then the unused amount for the year below 80% may be carried forward to the next two succeeding years, provided that the unused amount may only be used for deferred mining projects. While PT Freeport Indonesia's currently anticipated capital requirements do not exceed those limitations, funding significant new projects would require us to seek alternate sources of capital. The availability and cost of capital for projects in Indonesia is uncertain because of global financial markets' assessment of Indonesia's political and economic conditions.

Covenants in our amended credit facilities impose restrictions on us.

Our amended bank credit facilities:

- prohibit the repurchase of, and payment of dividends on, our common stock;
- limit, among other things, our ability to:
    - redeem and pay dividends on our preferred stock in certain circumstances;
    - make investments;
    - engage in transactions with affiliates; and
    - create liens on our assets;

    and
- require us to maintain specified financial ratios and satisfy financial condition tests.

Events beyond our control, including changes in general economic and business conditions, may affect our ability to satisfy these covenants, which could result in a default under our amended bank credit facilities. If an event of default under our amended credit facilities occurs, the banks could elect to declare all amounts outstanding thereunder, together with accrued interest, to be immediately due and payable. An event of default under our amended bank credit facilities may also give rise to an event of default under our existing and future debt agreements.

We have pledged substantially all of our assets to secure the repayment of our amended credit facilities and other obligations.

The repayment of our amended credit facilities is secured by a lien on over 80% of PT Freeport Indonesia's assets and by our pledge of 50.1% and 100% of the outstanding capital stock of PT Freeport Indonesia and PT Indocopper Investama, respectively. PT Freeport Indonesia's remaining assets secure other of our obligations. In addition, PT Freeport Indonesia has pledged it rights under its Contract of Work to secure its obligations under the amended credit facilities.

If we are unable to generate sufficient cash flow to satisfy our repayment obligations, our lenders could elect to foreclose on our pledged assets, which would have a material adverse effect on our business and profitability.

Our mining operations create difficult and costly environmental challenges, and future changes in environmental laws, or unanticipated environmental impacts from our operations, could require us to incur increased costs.

Mining operations on the scale of our operations in Papua involve significant environmental challenges. Our primary challenge is to dispose of the large amount of crushed and ground rock material, called tailings, that results from the process by which we physically separate the copper, gold and silver from the ore that we mine. Under our tailings management plan, the river system near our mine transports the tailings to the lowlands where deposits of the tailings and natural sediments are controlled through a levee system for future revegetation and reclamation. We incurred costs of $9.7 million in 2001, $8.2 million in 2000 and $11.7 million in 1999 for our tailings management plan.

Another of our major environmental challenges is managing overburden, which is the rock that must be moved aside in order to reach the ore in the mining process. In the presence of air, water and naturally occurring bacteria, some overburden can cause acid rock drainage, or acidic water containing dissolved metals which, if not properly managed, can have a negative impact on the environment.

Certain Indonesian governmental officials have from time to time raised issues with respect to our tailings management plan and overburden management plan, including a suggestion that a pipeline system rather than our current system be implemented for tailings disposal. Our ongoing assessment of tailings management has identified significant unresolved technical, environmental and economic issues associated with a pipeline system. Because our mining operations are remotely located in steep mountainous terrain and in an active seismic area, a pipeline system would be costly, difficult to construct and maintain, and more prone to catastrophic failure. For these reasons, we do not believe that a pipeline system is practical.

We anticipate that we will continue to spend significant financial and managerial resources on environmental compliance. In addition, changes in Indonesian environmental laws or unanticipated environmental impacts from our operations could require us to incur significant additional costs.

The volume and grade of the reserves we recover and our rates of production may be more or less than anticipated. In addition, we do not anticipate the mining of all of our reserves prior to the expiration of the initial term of our Contract of Work.

Our reserve amounts are determined in accordance with established mining industry practices and standards, but are only estimates of the mineral deposits that can be economically and legally recovered. In addition, our mines may not conform to standard geological expectations. Because ore bodies do not contain uniform grades of minerals, our metal recovery rates will vary from time to time, which will result in variations in the volumes of minerals that we can sell from period to period. Some of our reserves may become unprofitable to develop if there are unfavorable long-term market price fluctuations in copper and gold, or if there are significant increases in our operating and capital costs. In addition, our exploration programs may not result in the discovery of additional mineral deposits that we can mine profitably.

All of our current proven and probable reserves, including the Grasberg deposit, are located in Block A. The initial term of our Contract of Work covering Block A expires at the end of 2021. We can extend this term for two successive 10-year periods, subject to the approval of the Indonesian government, which cannot be withheld or delayed unreasonably. Our reserve amounts reflect our estimates of the reserves that can be recovered before 2041 (i.e. before the expiration of the two 10-year extensions) and our current mine plan has been developed and our operations are based on our receiving the two 10-year extensions. As a result, we do not anticipate the mining of all of our reserves prior to the end of 2021 based on our current mine plan, and there can be no assurance that the Indonesian government will approve the extensions. Prior to the end of 2021, we expect to mine approximately 63 percent of aggregate proven and probable ore, representing approximately 71 percent of PT Freeport Indonesia's share of recoverable copper reserves and approximately 77 percent of PT Freeport Indonesia's share of recoverable gold reserves.

Our net income can vary significantly with fluctuations in the market prices of copper and gold.

Our revenues are derived primarily from the sale of copper concentrates, which also contain significant amounts of gold, and from the sale of copper cathodes, copper wire rod and copper wire. Most of our copper concentrates are sold under long-term contracts, but the selling price is based on world metal prices at or near the time of shipment and delivery.

Copper and gold prices fluctuated widely in 2001, primarily due to the slowdown in global economic activity and the economic and political uncertainties created by the terrorist attacks in the United States on September 11, 2001. During 2001, the daily closing price for copper on the London spot market ranged from 60 cents per pound to 83 cents per pound and the daily closing price for gold on the London spot market ranged from $256 per ounce to $293 per ounce.

World metal prices for copper have historically fluctuated widely and are affected by numerous factors beyond our control, including:

- the strength of the United States economy and the economies of other industrialized and developing nations;
- available supplies of copper from mine production and inventories;
- sales by holders and producers of copper;
- demand for industrial products containing copper; and
- speculation.

World gold prices have also historically fluctuated widely and are affected by numerous factors beyond our control, including:

- the strength of the United States economy and the economies of other industrialized and developing nations;
- global or regional political or economic crises;
- the relative strength of the United States dollar and other currencies;
- expectations with respect to the rate of inflation;
- interest rates;
- sales of gold by central banks and other holders;
- demand for jewelry containing gold; and
- speculation.

Any material decrease in market prices of copper or gold would have a material adverse impact on our results of operations and financial condition.

In addition to the usual risks encountered in the mining industry, we face additional risks because our operations are located on difficult terrain in a very remote area of the world.

Our mining operations are located in steeply mountainous terrain in a very remote area in Indonesia. These conditions have required us to overcome special engineering difficulties and to develop extensive infrastructure facilities. In addition, the area receives considerable rainfall, which has led to periodic floods and mud slides. The mine site is also in an active seismic area and has experienced earth tremors from time to time. In addition to these special risks, we are also subject to the usual risks associated with the mining industry, such as the risk of encountering unexpected geological conditions that may result in cave-ins and flooding of mine areas. Our insurance coverages may not be sufficient to cover an unexpected natural or operating disaster. Our insurance policies do not provide coverage for damages and losses caused by war. Moreover, while our property and business interruption insurance policy currently provides coverage for damages to insured property directly caused by terrorism, this policy in the future may, in view of the events of September 11, 2001, exclude such coverage.

Movements in foreign currency exchange rates or interest rates could have a negative effect on our operating results.

All of our revenues are denominated in U.S. dollars. However, some of our costs and some of our assets and liabilities are denominated in Indonesian rupiah, Australian dollars or euros. As a result, our profitability is generally adversely affected when the U.S. dollar weakens against these foreign currencies.

The Indonesian rupiah/U.S. dollar exchange rate was volatile during 2001. The rupiah/U.S. dollar daily closing exchange rate ranged from 8,470 rupiahs per U.S. dollar to 11,980 rupiahs per U.S. dollar during 2001, and on December 31, 2001, the closing exchange rate was 10,160 rupiahs per U.S. dollar. The Australian dollar/U.S. dollar and euro/U.S. dollar exchange rates also fluctuated substantially in 2001. During 2001, the Australian dollar/U.S. dollar daily closing exchange rate ranged from $0.48 per Australian dollar to $0.57 per Australian dollar and the euro/U.S. dollar daily closing exchange rate ranged from $0.84 per euro to $0.96 per euro. On December 31, 2001, the closing exchange rates were $0.51 per Australian dollar and $0.88 per euro.

From time to time we have in the past and may in the future implement currency hedges intended to reduce our exposure to changes in foreign currency exchange rates. However, our hedging strategies may not be successful, and any of our unhedged foreign exchange payment requirements will continue to be subject to market fluctuations. In addition, our amended bank credit facilities are based on fluctuating interest rates. Accordingly, an increase in interest rates could have an adverse impact on our results of operations and financial condition.

Because we are primarily a holding company, our ability to pay our debts depends upon the ability of our subsidiaries to pay us dividends and to advance us funds. In addition, our ability to participate in any distribution of our subsidiaries' assets is generally subject to the prior claims of the subsidiaries' creditors.

Because we conduct business primarily through PT Freeport Indonesia, our major subsidiary, and other subsidiaries, our ability to pay our debts depends upon the earnings and cash flow of PT Freeport Indonesia and our other subsidiaries and their ability to pay us dividends and to advance us funds. Contractual and legal restrictions applicable to our subsidiaries could also limit our ability to obtain cash from them. Our rights to participate in any distribution of our subsidiaries' assets upon their liquidation, reorganization or insolvency would generally be subject to the prior claims of the subsidiaries' creditors, including trade creditors and preferred stockholders, if any.

Item 3. Legal Proceedings.

Yosefa Alomang v. Freeport-McMoRan Inc. and Freeport-McMoRan Copper & Gold Inc., Civ. No. 96-9962 (Orleans Civ. Dist. Ct. La. filed June 19, 1996). The plaintiff alleges environmental, human rights and social/cultural violations in Indonesia and seeks unspecified monetary damages and other equitable relief. In March 2000, the Civil District Court for the Parish of Orleans, State of Louisiana, granted our exception of no cause of action and dismissed the entire case with prejudice. The plaintiff appealed to the Louisiana Fourth Circuit Court of Appeal and, in February 2002, the Louisiana Fourth Circuit Court of Appeal affirmed the lower court's dismissal of the case with prejudice.

In addition to the foregoing proceeding, we are involved from time to time in various legal proceedings of a character normally incident to the ordinary course of our business. We believe that potential liability in such proceedings would not have a material adverse effect on our financial condition or results of operations. We maintain liability insurance to cover some, but not all, potential liabilities normally incident to the ordinary course of our business as well as other insurance coverage customary in our business, with coverage limits that we deem prudent.

Item 4. Submission of Matters to a Vote of Security Holders.

Not applicable.

Executive Officers of the Registrant.

Certain information as of February 26, 2002 about our executive officers, including their position or office with FCX, PT Freeport Indonesia and Atlantic Copper, is set forth in the following table and accompanying text:

Name	Age	Position or Office
Richard C. Adkerson	55	President and Chief Financial Officer of FCX. Director and Executive Vice President of PT Freeport Indonesia. Chairman of the Board of Directors of Atlantic Copper.
Adrianto Machribie	60	President Director of PT Freeport Indonesia.
James R. Moffett	63	Director, Chairman of the Board and Chief Executive Officer of FCX. President Commissioner of PT Freeport Indonesia.

Richard C. Adkerson

has served as FCX's President since April 1997 and Chief Financial Officer since October 2000. Mr. Adkerson is also Executive Vice President and a director of PT Freeport Indonesia, Chairman of the Board of Directors of Atlantic Copper, and Co-Chairman of the Board, President and Chief Executive Officer of McMoRan Exploration Co. (McMoRan). From April 1994 to November 1998 he was Co-Chairman of the Board and Chief Executive Officer of McMoRan Oil & Gas Co. (McMoRan Oil & Gas), and from November 1997 to November 1998 he was Vice Chairman of the Board of Freeport-McMoRan Sulphur Inc. (Freeport Sulphur). Mr. Adkerson served as Executive Vice President of FCX from July 1995 to April 1997, and as Chief Financial Officer from July 1995 to November 1998. He also served as Chairman of the Board of Stratus Properties Inc., a real estate development company, from March 1992 to August 1998, and as Chief Executive Officer from August 1995 to May 1998. Mr. Adkerson served as Vice Chairman of the Board of Freeport-McMoRan Inc. from August 1995 until December 1997 and as Senior Vice President.

Adrianto Machribie

has served as President Director of PT Freeport Indonesia since March 1996. From September 1992 to March 1996, Mr. Machribie was a director and Executive Vice President of PT Freeport Indonesia.

James R. Moffett

has served as Chairman of the Board and Chief Executive Officer of FCX since July 1995 and has served as Chairman of the Board of FCX since May 1992. He is also President Commissioner of PT Freeport Indonesia and Co-Chairman of the Board of McMoRan. From April 1994 to November 1998 he was Co-Chairman of the Board of McMoRan Oil & Gas and from November 1997 to November 1998 he was Co-Chairman of the Board of Freeport Sulphur. Mr. Moffett served as Chairman of the Board of Freeport-McMoRan Inc. from September 1984 to December 1997.

PART II

Item 5. Market for Registrant's Common Equity and Related Stockholder Matters.

Class A Common Shares

Our Class A common shares trade on the New York Stock Exchange (NYSE) under the symbol "FCX.A." The FCX.A share price is reported daily in the financial press under "FMCGA" in most listings of NYSE securities. At year-end 2001, the number of holders of record of Class A common shares was 5,802. NYSE composite tape Class A common share price ranges during 2001 and 2000:

	2001		2000	
	High	Low	High	Low
First Quarter	$ 13.200	$ 8.000	$ 18.625	$ 11.000
Second Quarter	15.400	10.030	11.750	8.438
Third Quarter	11.530	9.060	9.875	8.000
Fourth Quarter	13.500	8.750	8.813	6.750

Class B Common Shares

Our Class B common shares trade on the NYSE under the symbol "FCX." The FCX share price is reported daily in the financial press under "FMCG" in most listings of NYSE securities. At year-end 2001, the number of holders of record of our Class B common shares was 9,803. NYSE composite tape Class B common share price ranges during 2001 and 2000:

	2001		2000	
	High	Low	High	Low
First Quarter	$ 14.690	$ 8.313	$ 21.438	$ 12.063
Second Quarter	17.150	11,050	12.750	8.813
Third Quarter	12.980	10.230	10.625	8.188
Fourth Quarter	14.240	9.400	9.375	6.750

As of February 26, 2002, there were 5,734 and 9,681 holders of record of our Class A and Class B common stock, respectively.

Common Share Dividends

There were no cash dividends paid on our common stock during 2000 and 2001.

Reclassification of Class A and Class B Common Shares

On February 28, 2002, FCX's Board of Directors authorized and recommended to its stockholders a proposal to reclassify its Class A and Class B common stock into a single class of common stock on a one share-for-one share basis. The reclassification proposal will require the affirmative vote of the holders of a majority of each class of common stock, voting as separate classes, and will be presented at the upcoming annual meeting of stockholders on

May 2, 2002. The reclassification is intended to simplify the company's capital structure, enhance the company's ability to structure and execute equity-based transactions, increase the trading liquidity of the company's common stock, and generate administrative cost savings.

Item 6. Selected Financial Data.

FREEPORT-McMoRan COPPER & GOLD INC.
SELECTED FINANCIAL AND OPERATING DATA

	2001		2000
			(Financial Data in Thousands, Except Per Share Amounts)
FCX CONSOLIDATED FINANCIAL DATA			
Years Ended December 31:			
Revenues	$ 1,838,866		$ 1,868,61
Operating Income	542,926	a	492,29
Net income applicable to common stock	76,496	a	39,50
Basic net income per common share	.53	a	.2
Diluted net income per common share	.53	a	.2
Dividends paid per common share	-		-
Basic average shares outstanding	143,952		153,99
Diluted average shares	144,938		154,51

outstanding		
At December 31:		
Property, plant and equipment, net	3,457,277	3,248,710
Total assets	4,211,929	3,950,741
Long-term debt, including current portion and short-term borrowings	2,338,600	2,190,025
Redeemable preferred stock	462,504	475,005
Stockholders' equity	104,444	December 31, 2013

. The results for the three-month 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 share-based payment awards that contain non-forfeitable 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.

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TEXAS INSTRUMENTS INCORPORATED AND SUBSIDIARIES

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

	For Three Months Ended September 30, 2014			For Three Months Ended September 30, 2013		
	Net Income	Shares	EPS	Net Income	Shares	EPS
Basic EPS:						
Net income	$826			$629		
Income allocated to RSUs	(13)			(11)		
Income allocated to common stock for basic EPS calculation	$813	1,060	$.77	$618	1,096	$.56
Adjustment for dilutive shares:						
Stock-based compensation plans		14			15	
Diluted EPS:						
Net income	$826			$629		
Income allocated to RSUs	(13)			(11)		
Income allocated to common stock for diluted EPS calculation	$813	1,074	$.76	$618	1,111	$.56

	For Nine Months Ended September 30, 2014			For Nine Months Ended September 30, 2013		
	Net Income	Shares	EPS	Net Income	Shares	EPS
Basic EPS:						
Net income	$1,996			$1,651		
Income allocated to RSUs	(31)			(29)		
Income allocated to common stock for basic EPS calculation	$1,965	1,070	$1.84	$1,622	1,102	$1.47
Adjustment for dilutive shares:						
Stock-based compensation plans		15			15	
Diluted EPS:						
Net income	$1,996			$1,651		
Income allocated to RSUs	(31)			(28)		
Income allocated to common stock for diluted EPS calculation	$1,965	1,085	$1.81	$1,623	1,117	$1.45

Potentially dilutive securities representing 11 million shares of common stock that were outstanding during both the third quarter and first nine months of 2014 were excluded from the computation of diluted earnings per common share for these periods because their effect would have been anti-dilutive. 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.

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TEXAS INSTRUMENTS INCORPORATED AND SUBSIDIARIES

Derivatives and hedging

In association with the issuance of certain long-term debt, we use financial derivatives such as treasury rate lock agreements that are recognized in AOCI and amortized over the life of the related debt. The results of these derivative transactions 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, which are used as economic hedges to reduce the earnings impact that 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.

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, 2014. 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 its 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 April 2014, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) No. 2014-08, Presentation of Financial Statements (Topic 205) and Property, Plant, and Equipment (Topic 360): Reporting Discontinued Operations and Disclosures of Disposals of Components of an Entity. This standard raises the threshold for a disposal to qualify as a discontinued operation. Under the new guidance, only a disposal representing a strategic shift in operations that has or will have a major effect on an entity's operations and financial results, such as a disposal of a major geographic area or a major line of business, should be presented as discontinued operations. In addition, the new standard requires additional disclosures of both discontinued operations and certain other disposals that do not meet the revised definition of a discontinued operation. This standard is effective for annual and interim reporting periods beginning as of January 1, 2015. In the event that a future disposition meets the revised criteria, we expect that this standard will have an impact on the presentation of our financial statements and we will note the appropriate disclosures at that time.

In May 2014, the FASB issued ASU No. 2014-09, Revenue from Contracts with Customers (Topic 606). This standard provides a single set of guidelines for revenue recognition to be used across all industries and requires additional disclosures. This standard is effective for annual and interim reporting periods beginning as of January 1, 2017. We are currently evaluating the potential impact of this standard on our financial position and results of operations.

In August 2014, the FASB issued ASU No. 2014-15, Presentation of Financial Statements-Going Concern (Subtopic 205-40), Disclosure of Uncertainties about an Entity's Ability to Continue as a Going Concern. This standard sets forth management's responsibility to evaluate, each reporting period, whether there is substantial doubt about our ability to continue as a going concern, and if so, to provide related footnote disclosures. The standard is effective for annual and interim reporting periods ending after December 15, 2016. We are currently evaluating this new standard and expect it to have no impact on our financial position and results of operations.

2. Acquisition charges

We incurred various costs as a result of the 2011 acquisition of National that are included in Other for segment reporting purposes, consistent with how management measures the performance of our segments. These acquisition charges are as follows:

	For Three Months Ended September 30,		For Nine Months Ended September 30,	
	2014	2013	2014	2013
Amortization of intangible assets	$80	$81	$239	$244
Stock-based compensation	3	3	9	8
Retention bonuses	—	2	—	5
Acquisition charges	$83	$86	$248	$257

Amortization of intangible assets resulting from the National acquisition is based on estimated useful lives. See Note 6 for additional information. Stock-based compensation reflects awards to former National employees and is recognized over the applicable vesting period for the remaining grantees. Retention bonuses reflect amounts paid to former National employees who fulfilled agreed-upon service period obligations and were recognized ratably over the required service period.

TEXAS INSTRUMENTS INCORPORATED AND SUBSIDIARIES

3. Restructuring charges/other

Restructuring charges/other is comprised of the following components, all of which are recognized in Other for segment reporting purposes:

	For Three Months Ended September 30,		For Nine Months Ended September 30,		
	2014	2013	2014	2013	Cumulative Since January 1, 2011
Restructuring charges by action:					
2013 actions					
Severance and benefits cost (a)	$(3)	$—	$18	$—	$67
Other exit costs	—	—	7	—	7
	(3)	—	25	—	74
2012 Wireless action					
Severance and benefits cost (a)	—	—	(6)	30	269
Accelerated depreciation	—	—	—	6	9
Other exit costs	—	—	—	2	105
	—	—	(6)	38	383
Prior actions					
Severance and benefits cost	—	2	—	3	119
Accelerated depreciation	—	—	1	5	29
Other exit costs (a)	—	14	(1)	18	52
	—	16	—	26	200
Total restructuring charges	(3)	16	19	64	$657
Other:					
Gains on sales of assets	(8)	—	(47)	—	
Gain on technology transfer	—	—	—	(315)	
Other	2	—	4	—	
Restructuring charges/other	$(9)	$16	$(24)	$(251)	

(a) Includes changes in estimates for the three and nine months ended September 30, 2014.

2013 actions

In January 2014, we announced cost-saving actions in Embedded Processing and in Japan to reduce expenses and focus our investments on markets with greater potential for sustainable growth and strong long-term returns. We expect the actions to be completed by mid-2015. Cost reductions include the elimination of about 1,100 jobs worldwide. Through September 30, 2014, we have recognized $74 million in cumulative restructuring charges, with no further material charges expected. As of September 30, 2014, $36 million has been paid to terminated employees for severance and benefits.

2012 Wireless action

In 2012, we announced a restructuring of our Wireless business to reduce expenses and focus our investments on markets with greater potential for sustainable growth and strong long-term returns. This action is now complete. We recognized $383 million in cumulative restructuring charges, including a $90 million impairment of goodwill. As of September 30, 2014, $241 million has been paid to terminated employees for severance and benefits.

Prior actions

In 2012, we announced closure of two older semiconductor manufacturing facilities in Houston, Texas, and Hiji, Japan. We recognized $200 million in cumulative restructuring charges related to these closures, completing both by the end of 2013. As of September 30, 2014, $102 million has been paid to terminated employees for severance and benefits.

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As of September 30, 2014, and December 31, 2013, we carried immaterial liabilities related to actions commenced in 2008 and 2009.

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

	2013 Actions		2012 Wireless Action	Prior Actions		
	Severance and Benefits	Other Charges	Severance and Benefits	Severance and Benefits	Other Charges	Total
Remaining accrual at December 31, 2013	$49	$—	$95	$10	$7	$161
Restructuring charges	18	7	(6)	—	—	19
Payments	(36)	—	(61)	(6)	(7)	(110)
Remaining accrual at September 30, 2014	$31	$7	$28	$4	$—	$70

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

Gains on sales of assets

During the first quarter of 2014, we completed the sale of our site in Nice, France. The planned shut-down of this site was part of our 2012 Wireless restructuring action. As a result of the sale, we recognized a gain of $30 million in the first quarter of 2014. We also recognized gains of $17 million on a year-to-date basis tied to the sales of other assets associated primarily with our Houston and Hiji manufacturing facilities, with $8 million recognized in the third quarter of 2014.

Gain on technology transfer

During the second quarter of 2013, we recognized a gain of $315 million on a transfer of wireless connectivity technology to a customer.

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. The rate is based on current tax law and for 2014 does not assume reinstatement of the federal research tax credit, which expired at the end of 2013. As of September 30, 2014, the estimated annual effective tax rate for 2014 is about 28 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. The first-quarter 2013 tax provision included a $65 million discrete tax benefit from the reinstatement 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.

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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, 2014			December 31, 2013		
	Cash and Cash Equivalents	Short-term Investments	Long-term Investments	Cash and Cash Equivalents	Short-term Investments	Long-term Investments
Measured at fair value:						
Available-for-sale securities						
Money market funds	$364	$ —	$ —	$500	$ —	$ —
Corporate obligations	90	345	—	123	217	—
U.S. Government agency and Treasury securities	625	1,535	—	787	1,985	—
Trading securities						
Mutual funds	—	—	180	—	—	179
Total	1,079	1,880	180	1,410	2,202	179
Other measurement basis:						
Equity-method investments	—	—	27	—	—	24
Cost-method investments	—	—	12	—	—	13
Cash on hand	227	—	—	217	—	—
Total	$1,306	$ 1,880	$ 219	$1,627	$ 2,202	$ 216

At September 30, 2014, and December 31, 2013, we had no significant unrealized gains or losses associated with our available-for-sale investments. We did not recognize any credit losses related to available-for-sale investments for the nine months ended September 30, 2014, and 2013.

For the nine months ended September 30, 2014, and 2013, the proceeds from sales, redemptions and maturities of short-term available-for-sale investments were $2.49 billion and $3.56 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, 2014:

Due	Fair Value
One year or less	$2,759
One to two years	200

Gross realized gains and losses from sales of long-term investments were not significant for the nine months ended September 30, 2014, and 2013. Other-than-temporary declines and impairments in the values of these investments recognized in OI&E were also not significant for the nine months ended September 30, 2014, and 2013.

Fair-value considerations

TEXAS INSTRUMENTS INCORPORATED AND SUBSIDIARIES

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 a 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. We verify 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, 2014, and December 31, 2013. 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 September 30, 2014	Level 1	Level 2
Assets:			
Money market funds	$364	$364	$—
Corporate obligations	435	—	435
U.S. Government agency and Treasury securities	2,160	1,595	565
Mutual funds	180	180	—
Total assets	$3,139	$2,139	$1,000
Liabilities:			
Deferred compensation	$196	$196	$—
Total liabilities	$196	$196	$—

	Fair Value December 31, 2013	Level 1	Level 2

Assets:			
Money market funds	$500	$500	$—
Corporate obligations	340	—	340
U.S. Government agency and Treasury securities	2,772	2,107	665
Mutual funds	179	179	—
Total assets	$3,791	$2,786	$1,005
Liabilities:			
Deferred compensation	$197	$197	$—
Total liabilities	$197	$197	$—

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6. Goodwill and acquisition-related intangibles

Goodwill was $4.36 billion net of accumulated impairment of $90 million as of September 30, 2014, and December 31, 2013. There was no impairment of goodwill during the nine months ended September 30, 2014 and 2013.

Components of acquisition-related intangible assets are as follows:

		September 30, 2014			December 31, 2013		
Acquisition-related Intangibles	Amortization Period (Years)	Gross Carrying Amount	Accumulated Amortization	Net	Gross Carrying Amount	Accumulated Amortization	Net
Developed technology	5 - 10	$2,128	$ 659	$1,469	$2,157	$ 526	$1,631
Customer relationships	8	810	305	505	821	239	582
Other intangibles	5	3	2	1	5	3	2
In-process R&D	(a)	7	n/a	7	8	n/a	8
Total		$2,948	$ 966	$1,982	$2,991	$ 768	$2,223

(a) In-process R&D is not amortized until the associated project has been completed. Alternatively, if the associated project is determined not to be viable, it is expensed.

Amortization of acquisition-related intangibles was $80 million and $83 million for the three months ended and $241 million and $253 million for the nine months ended September 30, 2014, and 2013, respectively, primarily related to developed technology. Fully amortized assets are written off against accumulated amortization.

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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	
For Three Months Ended September 30,	2014	2013	2014	2013	2014	2013
Service cost	$6	$6	$1	$1	$9	$9
Interest cost	11	12	6	5	17	15
Expected return on plan assets	(10)	(11)	(5)	(6)	(21)	(17)
Amortization of prior service cost (credit)	—	—	1	1	—	(1)
Recognized net actuarial loss	6	5	1	3	6	7
Net periodic benefit costs	13	12	4	4	11	13
Settlement losses (a)	11	5	—	—	1	4
Curtailment gain	—	—	—	—	(2)	(2)
Total, including other postretirement (gains) losses	$24	$17	$4	$4	$10	$15

	U.S. Defined Benefit		U.S. Retiree Health Care		Non-U.S. Defined Benefit	
For Nine Months Ended September 30,	2014	2013	2014	2013	2014	2013
Service cost	$16	$20	$3	$4	$29	$29
Interest cost	33	33	17	15	52	46
Expected return on plan assets	(31)	(36)	(15)	(18)	(62)	(50)
Amortization of prior service cost (credit)	—	—	3	3	(1)	(3)
Recognized net actuarial loss	19	16	5	9	19	24
Net periodic benefit costs	37	33	13	13	37	46
Settlement losses (a)	14	18	—	—	1	4
Curtailment gain	—	—	—	—	(2)	(5)
Total, including other postretirement (gains) losses	$51	$51	$13	$13	$36	$45

(a) Includes non-restructuring and restructuring-related settlement losses.

In the first nine months of 2014, as a result of increased retirement activities, we remeasured our U.S. and Japan defined benefit plans. These remeasurements resulted in a net actuarial gain on a pre-tax basis of $12 million in Other comprehensive income. A gain of $17 million related to Japan was partially offset by a loss of $5 million related to the U.S. plans. For the nine months ended September 30, 2014, we also recognized settlement losses of $15 million related to our U.S. and Japan defined benefit plans, with a $2 million curtailment gain also related to Japan.

In the first nine months of 2013, as a result of increased retirement activities, we remeasured our U.S. and Japan defined benefit plans. These remeasurements resulted in a net actuarial gain on a pre-tax basis of $79 million in Other comprehensive income. Of this gain, $24 million related to the U.S. plans and $55 million was for Japan. For the nine months ended September 30, 2013, we also recognized settlement losses of $22 million on our U.S. and Japan defined benefit plans, with a $5 million curtailment gain also related to Japan.

The effects of these remeasurements and the effects of foreign currency exchange rate fluctuations are reflected in AOCI and in our Overfunded retirement plans and Underfunded retirement plans on our Consolidated Balance Sheets.

TEXAS INSTRUMENTS INCORPORATED AND SUBSIDIARIES

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, 2014, we had a variable-rate revolving credit facility from a consortium of investment-grade banks that allows us to borrow up to $2 billion through March 2019. The interest rate on borrowings under this credi facility, if drawn, is indexed to the applicable London Interbank Offered Rate (LIBOR). As o September 30, 2014, our credit facility was undrawn and we had no commercial paper outstanding.

Long-term debt

In March 2014, we issued an aggregate principal amount of $500 million of fixed-rate long-term debt, with $250 million due in 2017 and $250 million due in 2021. The proceeds o the offering were $498 million, net of the original issuance discount and were used toward the repayment of the $1.0 billion of debt that matured in May 2014. We incurred $3 million of issuance and other related costs, which are being amortized to Interest and debt expense over the term of the 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. We incurred $6 million of issuance and other related costs, which are being amortized to Interest and debt expense over the term of the debt. 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 a floating-to-fixec interest rate swap associated with the maturing debt.

Long-term debt outstanding as of September 30, 2014, and December 31, 2013, is as follows:

	September 30, 2014	December 31 2013
Notes due 2014 at 1.375%	$ —	$ 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 2017 at 0.875%	250	—
Notes due 2018 at 1.00%	500	500
Notes due 2019 at 1.65%	750	750
Notes due 2021 at 2.75%	250	—
Notes due 2023 at 2.25%	500	500
	4,625	5,125
Net unamortized premium	20	33
Current portion of long-term debt	(1,002)	(1,000)
Long-term debt	$ 3,643	$ 4,158

Interest and debt expense was $23 million and $24 million for the three months ended and $72 million and $71 million for the nine months ended September 30, 2014, and 2013, respectively. This was net of the amortization of the debt premium and other debt issuance costs. 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.

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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, 2014, 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

Prepaid expenses and other current assets

	September 30, 2014	December 31, 2013
Prepaid taxes on intercompany inventory profits	$743	$667
Assets held for sale (a)	77	—
Other prepaid expenses and current assets	144	196
Prepaid expenses and other current assets	$964	$863

(a) As of September 30, 2014, we had excess assets in various locations, with an aggregate carrying value of $77 million, which met the criteria to be considered held for sale and were included in Prepaid expenses and other current assets in our Consolidated Balance Sheets. Prior to the reclassification in the first quarter of 2014, the comparable carrying amount of these assets as of December 31, 2013, of $81 million, was in Property, plant anc equipment, net. Assets considered held for sale are no longer being depreciated. We expec the sales transactions applicable to these assets to be completed within the next year and any resulting gain on such sales will be recognized on the Restructuring charges/other line of our Consolidated Statements of Income in Other.

TEXAS INSTRUMENTS INCORPORATED AND SUBSIDIARIES

Details on amounts reclassified out of Accumulated other comprehensive income (loss), net of taxes, recognized within Net income

Our Consolidated Statements of Comprehensive Income include items which have been recognized within Net income during the periods ended September 30, 2014 and 2013. The table below details where these transactions are recorded on the Consolidated Statements of Income.

	For Three Months Ended September 30,		For Nine Months Ended September 30,		Impact to Related Statement of
Details About AOCI Components	2014	2013	2014	2013	Income Line
Net actuarial gains (losses) of defined benefit plans:					
Recognized net actuarial loss and Settlement losses (a)	$25	$24	$58	$71	Increase to Pension expense (b)
Tax effect	(8)	(11)	(20)	(25)	Decrease to Provision for income taxes
Recognized within Net income, net of taxes	$17	$13	$38	$46	Decrease to Net income
Prior service cost of defined benefit plans:					
Amortization of prior service cost (credit) and Curtailment gain (a)	$(1)	$(2)	$—	$(5)	Decrease to Pension expense (b
Tax effect	—	1	—	2	Increase to Provision for income taxes
Recognized within Net income, net of taxes	$(1)	$(1)	$—	$(3)	Increase to Net income
Derivative instruments:					
Amortization of treasury rate locks	$—	$—	$1	$2	Increase to Interest and debt expense
Tax effect	—	—	—	(1)	Decrease to Provision for income taxes
Recognized within Net income, net of taxes	$—	$—	$1	$1	Decrease to Net income

(a) Detailed in Note 7.

(b) Pension expense 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.

TEXAS INSTRUMENTS INCORPORATED AND SUBSIDIARIES

11. Segment data

See Note 1 for a detailed description of our reportable segments.

	For Three Months Ended September 30,		For Nine Months Ended September 30,	
	2014	2013	2014	2013
Segment Revenue:				
Analog	$2,149	$1,931	$5,981	$5,325
Embedded Processing	711	668	2,070	1,846
Other	641	645	1,725	2,006
Total revenue	$3,501	$3,244	$9,776	$9,177

	For Three Months Ended September 30,		For Nine Months Ended September 30,	
	2014	2013	2014	2013
Segment Operating Profit:				
Analog	$802	$583	$1,964	$1,298
Embedded Processing	114	83	270	144
Other	259	178	613	703
Total operating profit	$1,175	$844	$2,847	$2,145

We use centralized manufacturing and support organizations, such as facilities, procurement and logistics, 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.

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 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.

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 application-specific standard semiconductor products, both of which we market to multiple customers. Catalog products are designed for use by many customers and/or many applications and are sold through both distribution and direct channels. The vast majority of our catalog products are differentiated. We also sell catalog commodity products, but they account for a small percentage of our revenue. The life cycles of catalog products generally span multiple years, with some products continuing to sell for decades after their initial release. Application-specific standard products (ASSPs) are designed for use by a smaller number of customers and are targeted to a specific application. The life cycles of ASSPs are generally determined by end-equipment upgrade cycles and can be as short as 12 to 24 months, although some can be used across multiple generations of customers’ products.

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 embedded processors. 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. Our Analog products are used in many markets, particularly personal electronics and industrial.

Sales of our Analog products generated about 60 percent of our revenue in 2013. According to external sources, the worldwide market for analog semiconductors was about $40 billion ir 2013. Our Analog segment's revenue in 2013 was $7.2 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 high-volume integrated analog products for specific applications and high-volume catalog products. HVAL products support applications like automotive safety devices, touch screen controllers, low voltage motor drivers and integrated motor controllers.

Power products: These include both catalog products and ASSPs that help customers manage power in electronic systems. Our broad portfolio of Power products is designed to enhance the efficiency of powered devices using battery management solutions, portable power conversion devices, power supply controls and point-of-load products.

HPA products: These include catalog analog products that we market to many different customers who use them in manufacturing a wide range of products. HPA products include high-speed data converters, amplifiers, sensors, high reliability products, interface products and precision analog products that are typically used in systems that require high performance. HPA products generally have long life cycles, often more than 10 years.

SVA products: These include a broad portfolio of power management, data converter, interface and operational amplifier catalog analog products used in manufacturing a wide range of products. SVA products support applications like video and data interface products, electrical fault/arc detection systems and mobile lighting and display systems. SVA products generally have long life cycles, often more than 10 years. SVA consists primarily of products that we acquired through our purchase of National Semiconductor Corporation (National) in 2011.

Embedded Processing

Embedded Processing products are the “brains” of many electronic devices. 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 communications infrastructure equipment. Our Embedded Processing products are used in many markets, particularly industrial and automotive.

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 20 percent of our revenue in 2013. According to external sources, the worldwide market for embedded processors was about $17 billion in 2013. Our Embedded Processing segment’s revenue in 2013 was $2.4 billion. This was the number two position and represented about 14 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 digital signal processors (DSPs) and applications processors. DSPs perform mathematical computations almost instantaneously to process or improve digital data. Applications processors are typically tailored for a specific class of applications such as communications infrastructure, automotive (infotainment and advanced driver assistance systems) and broad industrial applications.

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.

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 and GPS. 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), certain 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 from our baseband products and from our OMAP™ applications processors and connectivity products sold into smartphones and consumer tablets, all of which are product lines that we previously announced we are exiting and are collectively referred to as "legacy wireless products." Revenue from legacy wireless products declined throughout 2013, and ou exit from these products is complete. Other generated $2.6 billion of revenue in 2013.

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We also include in Other restructuring charges and certain acquisition-related charges, as these charges are not used in evaluating the results of or in allocating resources to our segments. 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 corporate-level items, such as litigation expenses, environmental costs, insurance proceeds, and assets and liabilities associated with our centralized operations, such as our worldwide manufacturing, facilities and procurement operations.

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 a 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.

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 logic products, such as some of our processor 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 a decrease in factory loadings, potentially lowering our profit margins. Conversely, as factory loadings increase, the fixed costs are spread over increased output, potentially benefiting our profit margins.

We expect to maintain sufficient internal manufacturing capacity to meet the vast majority of our production needs. To supplement our manufacturing capacity and maximize our responsiveness to customer demand and return on capital, we utilize the capacity of outside suppliers, commonly known as foundries, and subcontractors. In 2013, we sourced about 20 percent of our total wafers from external foundries and about 35 percent of our assembly/test services from subcontractors.

In 2013, we closed older wafer fabrication facilities in Hiji, Japan, and Houston, Texas. In December 2013, we acquired an assembly/test facility in the Hi-Tech Zone of Chengdu, China, adjacent to our existing fabrication facility in Chengdu.

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 application-specific products. Additionally, we sometimes maintain product inventory in unfinished wafer form, as well as higher finished-goods inventory of low-volume catalog products, allowing greater flexibility in periods of high demand. We also have consignment inventory programs in place for our largest customers and some distributors.

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.

Results of operations

Our third-quarter revenue was $3.50 billion, net income was $826 million and earnings per share (EPS) were $0.76 cents.

Revenue for the quarter was solidly in the upper half of our expected range and earnings were at the top of the range, marking another quarter of strong progress and execution. We delivered 8 percent year-over-year revenue growth. Analog and Embedded Processing comprised 82 percent of third-quarter revenue.

Gross margin of 58.4 percent, a new record, reflects the quality of our portfolio of Analog and Embedded Processing products as well as the efficiency of our manufacturing strategy.

Our cash flow from operations once again reflects the strength of our business model. Free cash flow for the trailing twelve-month period was up 20 percent from a year ago to $3.5 billion or 27 percent of revenue. This represents an improvement of 3 percentage points from a year ago and is consistent with our targeted range of 20-30 percent of revenue.

We returned $4.2 billion to shareholders in the past twelve months through stock repurchases and dividends paid. In the quarter, we announced a dividend increase of 13 percent, resulting in an annualized rate of $1.36 per share. Our strategy to return to shareholders all free cash flow not needed for net debt retirement, and to return proceeds from exercises of equity compensation, reflects our confidence in the long-term sustainability of our business model.

Our balance sheet remains strong, with $3.2 billion of cash and short-term investments at the end of the quarter, 81 percent of which was owned by the company’s U.S. entities. Inventory days were 108, consistent with our model of 105-115 days.

Free cash flow is a non-GAAP financial measure. For a reconciliation to GAAP and an explanation of the purpose for providing this non-GAAP measure, see the Non-GAAP financial information section in this MD&A.

Summary of Selected Financial Data

	Three Months Ended		Nine Months Ended	
	September 30, 2014	September 30, 2013	September 30, 2014	September 30, 2013
Revenue	$ 3,501	$ 3,244	$ 9,776	$ 9,177
Gross profit	2,044	1,779	5,532	4,724
Research and development (R&D)	332	368	1,047	1,176
Selling, general and administrative (SG&A)	463	465	1,414	1,397
Acquisition charges	83	86	248	257
Restructuring charges/other	(9)	16	(24)	(251)
Operating profit	1,175	844	2,847	2,145
Net income	$ 826	$ 629	$ 1,996	$ 1,651
Diluted earnings per common share	$ .76	$ .56	$ 1.81	$ 1.45
Percentage of revenue:				
Gross Profit	58.4%	54.8%	56.6%	51.5%
R&D	9.5%	11.3%	10.7%	12.8%
SG&A	13.2%	14.4%	14.5%	15.2%
Operating profit	33.6%	26.0%	29.1%	23.4%

Our exit from legacy wireless products and the elimination (effective January 1, 2013) of the Wireless segment resulted in changes to our corporate-level expense allocations, which negatively affected Analog and Embedded Processing profitability in the year ended December 31, 2013. We expect a similar, although less significant, effect through the end of 2014. We allocate our corporate-level expenses, which are largely fixed, among our product lines in proportion to the operating expenses directly generated by them. Because we stopped investing in legacy wireless products, the corporate-level expenses allocated to them were 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 on our results in any given period 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.

Third-quarter 2014 compared with third-quarter 2013

For the third quarter of 2014, we report the following:

Revenue was $3.50 billion, an increase of $257 million, or 8 percent, from the year-ago quarter due to higher revenue from Analog and Embedded Processing. Analog and Embedded Processing comprised 82 percent of revenue compared with 80 percent in the year-ago quarter.

Gross profit was $2.04 billion, or 58.4 percent of revenue, an increase of $265 million from the year-ago quarter primarily due to higher revenue and, to a lesser extent, a more favorable mix of products shipped.

Operating expenses were $332 million for R&D and $463 million for SG&A. R&D expense decreased $36 million, or 10 percent, from the year-ago quarter due about equally to cost savings from previously-announced restructuring actions and other efforts across the company to align costs with growth opportunities. SG&A expense was about even compared with the year-ago quarter as higher variable compensation costs were offset by savings from previously-announced restructuring actions and other cost alignment efforts.

Acquisition charges associated with our 2011 acquisition of National are recorded in Other and were $83 million in the current quarter compared with $86 million in the year-ago quarter. These Acquisition charges were from the ongoing amortization of intangible assets. See Note 2 to the financial statements for detailed information.

Restructuring charges/other was a net credit of $9 million compared with charges of $16 million in the year-ago quarter. The net credit in the third quarter of 2014 included gains fron sales of assets. These items are included in Other for segment reporting purposes. For details on the types of costs incurred and the amounts associated with each restructuring action, see Note 3 to the financial statements.

Operating profit was $1.18 billion, or 33.6 percent of revenue, compared with $844 million, or 26.0 percent of revenue, in the year-ago quarter.

Quarterly income taxes are calculated using the estimated annual effective tax rate. At the enc of the third quarter, our estimated annual effective tax rate for 2014 is about 28 percent. The tax rate is based on current tax law and does not include the effect of the federal research tax credit, which expired at the end of 2013. Our annual effective tax rate benefits from lower tax rates (compared to the U.S. statutory rate) applicable to our operations in many of the jurisdictions in which we operate and from U.S. tax benefits. These lower non-U.S. 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 detailed information.

Our tax provision was $329 million compared with $187 million in the year-ago quarter. The increase was primarily due to an increase in income before income taxes, and to a lesser extent, the expiration of the federal research tax credit at the end of 2013.

Net income was $826 million compared with $629 million in the year-ago quarter. EPS was $0.76 compared with $0.56 in the year-ago quarter.

Third-quarter 2014 segment results
Our segment results compared with the year-ago quarter are as follows:

Analog

	3Q14	3Q13	Change
Revenue	$ 2,149	$ 1,931	11%
Operating profit	802	583	38%
Operating profit % of revenue	37.3%	30.2%	

Analog revenue increased in all product lines. Revenue from Power grew the most, followed by revenue from HVAL, HPA and SVA. Operating profit increased primarily due to higher revenue and associated gross profit.

Embedded Processing

	3Q14	3Q13	Change
Revenue	$ 711	$ 668	6%
Operating profit	114	83	37%
Operating profit % of revenue	16.0%	12.4%	

Embedded Processing revenue increased due to higher revenue from Microcontrollers, Connectivity and Processors, each of which grew by about the same amount. Revenue increased due to increased shipments, except Processors revenue, which increased due to a more favorable mix of products shipped. Operating profit increased due to higher gross profit and, to a lesser extent, lower operating expenses.

Other

	3Q14	3Q13	Change
Revenue	$ 641	$ 645	-1%
Operating profit*	259	178	46%
Operating profit % of revenue	40.4%	27.6%	

*Includes Acquisition charges and Restructuring charges/other

Other revenue was about even as lower revenue from legacy wireless products was mostly offset by higher revenue from DLP products. Operating profit increased due to, in decreasing order, higher gross profit resulting from a more favorable mix of products shipped, lower Restructuring charges/other and lower operating expenses.

First nine months of 2014 compared with first nine months of 2013
For the first nine months of 2014, we report the following:

Revenue was $9.78 billion, an increase of $599 million, or 7 percent, primarily due to higher revenue from Analog and Embedded Processing, which more than offset lower revenue from legacy wireless products. Analog and Embedded Processing comprised 82 percent of revenue compared with 78 percent in the year-ago period.

Gross profit was $5.53 billion, an increase of $808 million, or 17 percent, primarily due to higher revenue and, to a lesser extent, a more favorable mix of products shipped.

R&D expense of $1.05 billion decreased $129 million, or 11 percent, due to savings from ongoing efforts across the company to align costs with growth opportunities, including previously-announced actions such as the wind-down of our legacy wireless products and the restructuring actions in Embedded Processing and Japan. SG&A expense of $1.41 billion was about even, as higher variable compensation costs were offset by savings from our cost alignment efforts.

Acquisition charges were $248 million compared with $257 million in the year-ago period. These charges were from the ongoing amortization of intangible assets. See Note 2 to the financial statements for detailed information.

Restructuring charges/other was a net credit of $24 million compared with a net credit of $251 million in the year-ago period. The 2014 net credit included $44 million of gains on sales of assets partially offset by restructuring charges. The net credit in 2013 included a $315 million gain from the transfer of wireless connectivity technology to a customer in the second quarter partially offset by restructuring charges. See Note 3 to the financial statements for detailed information.

Operating profit was $2.85 billion, or 29.1 percent of revenue, compared with $2.14 billion, or 23.4 percent of revenue, in the year-ago period.

The tax provision was $791 million compared with $421 million in the year-ago period. The increase was primarily due to higher income before income taxes, and to a lesser extent, the impact of the federal research tax credit, which included a $65 million discrete tax benefit in the first quarter of 2013. The federal research tax credit expired at the end of 2013. See Note 4 to the financial statements for detailed information.

Net income was $2.00 billion compared with $1.65 billion in the year-ago period. EPS was $1.81 compared with $1.45 in the year-ago period.

Year-to-date segment results

Our segment results compared with the year-ago period are as follows:

Analog

	YTD 2014	YTD 2013	Change
Revenue	$ 5,981	$ 5,325	12%
Operating profit	1,964	1,298	51%
Operating profit % of revenue	32.8%	24.4%	

Analog revenue increased due to higher revenue from, in decreasing order, Power, HPA, HVAL and SVA. Operating profit increased primarily due to higher revenue and associated gross profit.

Embedded Processing

	YTD 2014	YTD 2013	Change
Revenue	$ 2,070	$ 1,846	12%
Operating profit	270	144	88%
Operating profit % of revenue	13.0%	7.8%	

Embedded Processing revenue increased due to higher revenue from, in decreasing order, Microcontrollers, Processors, and Connectivity. Revenue increased due to increased shipments, except Processors revenue, which increased due to a more favorable mix of products shipped. Operating profit increased due to higher revenue and associated gross profit.

Other

	YTD 2014	YTD 2013	Change
Revenue	$ 1,725	$ 2,006	-14%
Operating profit*	613	703	-13%
Operating profit % of revenue	35.5%	35.0%	

*Includes Acquisition and Restructuring charges/other.

Other revenue decreased due to lower revenue from legacy wireless products. Operating profit decreased primarily due to the non-recurrence of the gain on the technology transfer partially offset by lower operating expenses resulting from the legacy wireless wind-down.

Financial condition

At the end of the third quarter of 2014, total cash (Cash and cash equivalents plus Short-term investments) was $3.19 billion, with 81 percent owned by our U.S. entities.

Accounts receivable were $1.48 billion at the end of the third quarter. This was an increase of $274 million from the end of 2013 as a result of higher revenue at the end of the third quarter compared with the end of the year. Days sales outstanding were 38 at the end of the third quarter compared with 36 at the end of 2013.

Inventory was $1.75 billion at the end of the third quarter, an increase of $20 million from the end of 2013. Days of inventory at the end of the third quarter were 108 compared with 112 at the end of 2013, consistent with our target range of 105 to 115 days.

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 a revolving credit facility. Cash flows from operating activities for the first nine months of 2014 was $2.62 billion, an increase of $435 million from the year-ago period, primarily due to higher net income.

We had $1.31 billion of Cash and cash equivalents and $1.88 billion of Short-term investments as of September 30, 2014.

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 2019. This credit facility also serves as support for the issuance of commercial paper. As of September 30, 2014, our credit facility was undrawn and we had no commercial paper outstanding.

For the first nine months of 2014, investing activities provided cash of $114 million compared with $120 million in the year-ago period. Proceeds from sales of short-term investments, net of purchases, provided cash of $321 million compared with $387 million in the year-ago period. Capital expenditures in the first nine months of 2014 totaled $260 million compared with $305 million in the year-ago period. These expenditures were primarily for semiconductor manufacturing equipment. We also received $46 million of cash proceeds from sales of assets in the first nine months of 2014 compared with $21 million in the year-ago period.

Net cash used in financing activities was $3.06 billion for the first nine months of 2014 compared with $2.29 billion in the year-ago period. In March 2014, we issued $500 million principal amount of debt, receiving net proceeds of $498 million. This compares with May 2013, when we issued $1.0 billion principal amount of debt, receiving net proceeds of $986 million. We used the net proceeds from these issuances to repay maturing debt of $1.0 billion in the first nine months of 2014 and $1.5 billion in the year-ago period. In the first nine months of 2014, we paid dividends of $967 million compared with $849 million in the year-ago period, a result of a higher dividend rate. We also used $2.13 billion in the first nine months of 2014 to repurchase 46.8 million shares of our common stock. In the same period last year, we used $2.13 billion to repurchase 59.8 million shares of our common stock. Employee exercises of stock options are also reflected in cash from financing activities. In the first nine months of 2014, these exercises provided cash proceeds of $476 million compared with $1.15 billion in the year-ago period. See Note 8 for detailed information on debt outstanding.

In September 2014, we announced a 13 percent increase in our quarterly cash dividend, which increased from $0.30 to $0.34 per share. This dividend will be payable November 17, 2014, to stockholders of record on October 31, 2014.

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

Free cash flow and associated ratios

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

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

Reconciliation to the most directly comparable GAAP-based measures is provided in the table below.

	For Twelve Months Ended September 30,		
	2014	2013	Change
Cash flow from operations (GAAP)	$ 3,819	$ 3,270	17%
Capital expenditures	(367)	(402)	
Free cash flow (non-GAAP)	$ 3,452	$ 2,868	20%
Revenue	$ 12,804	$ 12,155	
Cash flow from operations as a percent of revenue (GAAP)	30%	27%	
Free cash flow as a percent of revenue (non-GAAP)	27%	24%	

Long-term contractual obligations
In addition to the long-term debt obligations described in the long-term contractual obligations chart on page 47 of Exhibit 13 to our Form 10-K for the year ended December 31 2013: in March 2014 we issued $250 million principal amount of 0.875% notes maturing in 2017 and $250 million principal amount of 2.750% notes maturing in 2021, and in May 2014 we repaid $1.0 billion of debt that was maturing.

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 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.

You should read the following Risk Factors in conjunction with the factors discussed elsewhere in this and other of our filings with the Securities and Exchange Commission (SEC) and in materials incorporated by reference in these filings. These Risk Factors are intended to highlight certain factors that may affect our financial condition and results of operations and are not meant to be an exhaustive discussion of risks that apply to companies like TI with broad international operations. Like other companies, we are susceptible to macroeconomic downturns in the United States or abroad that may affect the general economic climate and our performance and the performance of our customers. Similarly, the price of our securities is subject to volatility due to fluctuations in general market conditions, actual financial results that do not meet our and/or the investment community's expectations, changes in our and/or the investment community's expectations for our future results and other factors, many of which are beyond our control.

Cyclicality in the Semiconductor Market May Affect Our Performance.

Semiconductor products are the principal source of our revenue. The semiconductor market historically has been cyclical and subject to significant and often rapid increases and decreases in product demand. These changes could have adverse effects on our results of operations, and on the market price of our securities. The results of our operations may be adversely affected in the future if demand for our semiconductors decreases or if this market or key end-equipment markets grow at a significantly slower pace than management expects.

Our Margins May Vary over Time.

Our profit margins may be adversely affected in the future by a number of factors, including decreases in our shipment volume, reductions in, or obsolescence of our inventory and shifts in our product mix. In addition, the highly competitive market environment in which we operate might adversely affect pricing for our products. Because we own much of our manufacturing capacity, a significant portion of our operating costs is fixed. In general, these fixed costs do not decline with reductions in customer demand or utilization of manufacturing capacity, and can adversely affect profit margins as a result.

The Technology Industry Is Characterized by Rapid Technological Change That Requires Us to Develop New Technologies and Products.

Our results of operations depend in part upon our ability to successfully develop, manufacture and market innovative products in a rapidly changing technological environment. We require significant capital to develop new technologies and products to meet changing customer demands that, in turn, may result in shortened product life cycles. Moreover, expenditures for technology and product development are generally made before the commercial viability for such developments can be assured. As a result, there can be no assurance that we will successfully develop and market these new products. There also is no assurance that the products we do develop and market will be well-received by customers, nor that we will realize a return on the capital expended to develop such products.

We Face Substantial Competition That Requires Us to Respond Rapidly to Product Development and Pricing Pressures.

We face intense technological and pricing competition in the markets in which we operate. We expect this competition will continue to increase from large competitors and from smaller competitors serving niche markets, and also from emerging companies, particularly in Asia, that sell products into the same markets in which we operate. Certain of our competitors possess sufficient financial, technical and management resources to develop and market products that may compete favorably against our products. The price and product development pressures that result from competition may lead to reduced profit margins and lost business opportunities in the event that we are unable to match the price declines or cost efficiencies, or meet the technological, product, support, software or manufacturing advancements of our competitors.

Our Performance Depends in Part on Our Ability to Enforce Our Intellectual Property Rights and to Develop and License New Intellectual Property.

Access to worldwide markets depends in part on the continued strength of our intellectual property portfolio. There can be no assurance that, as our business expands into new areas, we will be able to independently develop the technology, software or know-how necessary to conduct our business or that we can do so without infringing the intellectual property rights o others. To the extent that we have to rely on licensed technology from others, there can be no assurance that we will be able to obtain licenses at all or on terms we consider reasonable. The lack of a necessary license could expose us to claims for damages and/or injunction from third parties, as well as claims for indemnification by our customers in instances where we have a contractual or other legal obligation to indemnify them against damages resulting fron infringement claims.

With regard to our own intellectual property, we actively enforce and protect our rights. However, there can be no assurance that our efforts will be adequate to prevent the misappropriation or improper use of our protected technology.

We benefit from royalty revenue generated from various patent license agreements. The amount of such revenue depends in part on negotiations with new licensees, and with existin licensees in connection with renewals of their licenses. There is no guarantee that such negotiations will be successful. Future royalty revenue also depends on the strength and enforceability of our patent portfolio and our enforcement efforts, and on the sales and financial stability of our licensees. Additionally, consolidation of our licensees may negatively affect our royalty revenue. Royalty revenue from licensees is not always uniform or predictable, in part due to the performance of our licensees and in part due to the timing of new license agreements or the expiration and renewal of existing agreements.

A Decline in Demand in Certain Markets Could Have a Material Adverse Effect on the Demand for Our Products and Results of Operations.

Our customer base includes companies in a wide range of markets, but we generate a significant amount of revenue from sales to customers in the personal electronics market, particularly the mobile phone sector, and from sales to industrial customers. Decline in one o these markets could have a material adverse effect on the demand for our products and our results of operations and financial condition.

Our Global Operations Subject Us to Complex Laws, Regulations and Policies and Risks Associated with International Political, Economic or Other Conditions.

We have facilities in 35 countries worldwide. About 85 percent of our revenue comes from shipments to locations outside the United States; in particular, shipments of products into China typically represent a large portion of our revenue. Our global operations subject us to complex U.S. and foreign laws, regulations and policies relating to, for example, trade and export controls, anti-bribery, antitrust and privacy. Violations of or changes in these laws, regulations and policies could result in fines, penalties, and sanctions that could adversely affect our results of operations. Operating internationally also exposes us to political and economic conditions, security risks, health conditions and possible disruptions in transportation, communications and information technology networks of the various countrie in which we operate. Any of these could result in an adverse effect on our business operation and our financial results. Additionally, in periods when the U.S. dollar significantly fluctuate in relation to the non-U.S. currencies in which we transact business, the remeasurement of non-U.S. dollar transactions can have an adverse effect on our results of operations and financial condition.

Our Results of Operations Could be Affected by Natural Events in the Locations in Which We or Our Customers or Suppliers Operate.

We have manufacturing, data and design facilities and other operations in locations subject to natural occurrences such as health epidemics, severe weather and geological events that could disrupt operations. In addition, our suppliers and customers have similar facilities and operations in such locations. A natural disaster that results in a prolonged disruption to our operations, or the operations of our customers or suppliers, may adversely affect our results and financial condition.

The Loss of or Significant Curtailment of Purchases by Any of Our Largest Customers Could Adversely Affect Our Results of Operations.

We generate revenue from thousands of customers worldwide. The loss of or significant curtailment of purchases by one or more of our top customers (including curtailments due to a change in the design or manufacturing sourcing policies or practices of these customers, or the timing of customer or distributor inventory adjustments) may adversely affect our results of operations and financial condition.

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Our Results of Operations Could be Adversely Affected by Our Distributors' Promotion of Competing Product Lines or Our Distributors' Financial Performance.

In 2013, about 55 percent of our revenue was generated from sales of our products to distributors. Our distributors carry competing product lines, and our sales could be affected if our distributors promote competing products over our products. Moreover, our results of operations could be affected if our distributors suffer financial difficulties that result in their inability to pay amounts owed to us.

Our Results of Operations and Financial Condition Could be Adversely Affected if a Customer or a Distributor Suffers a Loss with Respect to Our Inventory.

We have consignment inventory programs in place for some of our largest customers and for some distributors. If a customer or distributor were to experience a loss with respect to TI-consigned inventory, our results of operations and financial condition may be adversely affected if we do not recover the full value of the lost inventory from the customer, distributo or insurer, or if our recovery is delayed.

Incorrect Forecasts of Customer Demand Could Adversely Affect Our Results of Operations.

Our ability to match inventory and production with the product mix needed to fill orders may affect our ability to meet a quarter's revenue forecast. In addition, when responding to customers' requests for shorter shipment lead times, we manufacture products based on forecasts of customers' demands. These forecasts are based on multiple assumptions. If we inaccurately forecast customer demand, we may hold inadequate, excess or obsolete inventory that would reduce our profit margins and adversely affect our results of operations and financial condition.

Our Performance Depends on the Availability and Cost of Raw Materials, Utilities, Critical Manufacturing Equipment, Manufacturing Processes and Third-Party Manufacturing Services.

Our manufacturing processes and critical manufacturing equipment, and those of some of our customers and suppliers, require that certain key raw materials, natural resources and utilities be available. Limited or delayed access to and high costs of these items could adversely affec our results of operations. Our products contain materials that are subject to conflict minerals reporting requirements. Our relationships with customers and suppliers may be adversely affected if we are unable to describe our products as conflict-free. Additionally, our costs may increase if customers demand that we change the sourcing of materials we cannot identify as conflict-free.

Our inability to timely implement new manufacturing technologies or install manufacturing equipment could adversely affect our results of operations. We subcontract a portion of our wafer fabrication and assembly and testing of our integrated circuits. We also depend on thir parties to provide advanced logic manufacturing process technology development. A limited number of third parties perform these functions, and we do not have long-term contracts with all of them. Reliance on these third parties involves risks, including possible shortages of capacity in periods of high demand, the third parties' inability to develop and deliver advance logic manufacturing process technology in a timely, cost effective and appropriate manner and the possibility of third parties imposing increased costs on us.

Our Results of Operations Could be Affected by Changes in Tax-Related Matters.

We have facilities in 35 countries worldwide and as a result are subject to taxation and audit by a number of taxing authorities. Tax rates vary among the jurisdictions in which we operate. Our results of operations could be affected by market opportunities or decisions we make that cause us to increase or decrease operations in one or more countries, or by changes in applicable tax rates or audits by the taxing authorities in countries in which we operate.

In addition, we are subject to laws and regulations in various jurisdictions that determine how much profit has been earned and when it is subject to taxation in that jurisdiction. Changes in these laws and regulations could affect the locations where we are deemed to earn income, which could in turn affect our results of operations. We have deferred tax assets on our balance sheet. Changes in applicable tax laws and regulations or in our business performance could affect our ability to realize those deferred tax assets, which could also affect our results of operations. Each quarter we forecast our tax liability based on our forecast of our performance for the year. If that performance forecast changes, our forecasted tax liability will change.

Our Operations Could be Affected by Changes in Environmental, Safety and Health Laws and Regulations.

We are subject to environmental, safety and health laws and regulations in the jurisdictions in which we operate our business, particularly those in which we manufacture our products. If we fail to comply with these laws and regulations, we could be subject to fines, penalties or other legal liability. Furthermore, should these laws and regulations be amended or expanded or new ones enacted, we could incur materially greater compliance costs or restrictions on ou ability to manufacture our products and operate our business, particularly if such laws and regulations: require the use of abatement equipment beyond what we currently employ; require the addition or elimination of a raw material or process to or from our current manufacturing processes; or impose costs, fees or reporting requirements on the direct or indirect use of energy, or of materials or gases used or emitted into the environment, in connection with the manufacture of our products. There can be no assurance that in all instances a substitute for a prohibited raw material or process would be available, or be available at reasonable cost.

Our Results of Operations Could be Affected by Changes in the Financial Markets.

We maintain bank accounts, one or more multi-year revolving credit agreements, and a portfolio of investments to support the financing needs of the company. Our ability to fund our daily operations, invest in our business, make strategic acquisitions and service our debt obligations requires continuous access to our bank and investment accounts, as well as access to our bank credit lines that support commercial paper borrowings and provide additional liquidity through short-term bank loans. If we are unable to access these accounts and credit lines (for example, due to instability in the financial markets), our results of operations and financial condition could be adversely affected. Similarly, such circumstances could also restrict our ability to access the capital markets or redeem our investments. If our customers or suppliers are unable to access credit markets and other sources of needed liquidity, we may receive fewer customer orders or be unable to obtain needed supplies, collect accounts receivable or access needed technology.

Material Impairments of Our Goodwill or Intangible Assets Could Adversely Affect Our Results of Operations.

Charges associated with impairments of our goodwill or intangible assets could adversely affect our financial condition and results of operations. Goodwill is reviewed for impairment annually or more frequently if certain impairment indicators arise or upon the disposition of a significant portion of a reporting unit. The review compares the fair value for each reporting unit to its associated book value including goodwill. A decrease in the fair value associated with a reporting unit resulting from, among other things, unfavorable changes in the estimated future discounted cash flow of the reporting unit, may require us to recognize impairments of goodwill. Most of our intangible assets are amortized over their estimated useful lives, but they are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of the asset may not be recoverable. If the sum of the future undiscounted cash flows expected to result from the use of the intangible asset and its eventual disposition is less than the carrying amount of the asset, we would recognize an impairment loss to the extent the carrying amount of the asset exceeds its fair value.

Our Results of Operations Could be Affected by Warranty Claims, Product Recalls or Product Liability.

We could be subject to warranty or product liability claims or claims based on epidemic or delivery failures that could lead to significant expenses as we defend such claims or pay damage awards or settlements. In the event of a warranty claim, we may also incur costs if we decide to compensate the affected customer or end consumer. We maintain product liability insurance, but there is no guarantee that such insurance will be available or adequate to protect against all such claims. In addition, it is possible for one of our customers to recall a product containing a TI part. In such instances, we may incur costs and expenses relating to the recall. Costs or payments we may make in connection with warranty, epidemic failure and delivery claims or product recalls may adversely affect our results of operations and financial condition.

Our Continued Success Depends in Part on Our Ability to Retain and Recruit a Sufficient Number of Qualified Employees in a Competitive Environment.

Our continued success depends in part on the retention and recruitment of skilled personnel, including technical, marketing, management and staff personnel. There can be no assurance that we will be able to successfully retain and recruit the key personnel that we require.

Our Debt Could Affect Our Operations and Financial Condition.
From time to time, we issue debt securities with various interest rates and maturities. While we believe we will have the ability to service this debt, our ability to make principal and interest payments when due depends upon our future performance, which will be subject to general economic conditions, industry cycles, and business and other factors affecting our operations, including the other risk factors described under Item 1A, many of which are beyond our control. In addition, our obligation to make principal and interest payments could divert funds that otherwise would be invested in our operations, or cause us to raise funds through such means as the issuance of new debt or equity, or the disposition of assets.
Our Ability to Successfully Implement Business and Organizational Changes Could Affect Our Business Plans and Results of Operations.
From time to time, we undertake business and organizational changes, including acquisitions, divestitures and restructuring actions, to support or carry out our strategic objectives. Our failure to successfully implement these changes could adversely affect our business plans and operating results. For example, we may not realize the expected benefits of an acquisition if we are unable to timely and successfully integrate acquired operations, product lines and technology, and our pre-acquisition due diligence may not identify all possible issues and risks that might arise with respect to an acquisition. Further, we may not achieve or sustain the expected growth or cost savings benefits of business and organizational changes, and restructuring charges could differ materially in amount and timing from our expectations.
Our Operating Results and Our Reputation Could be Adversely Affected by Breaches of Our Information Technology Systems.
Breaches of our information technology systems caused by computer viruses, unauthorized access, sabotage, vandalism or terrorism could compromise our information technology networks and result in unauthorized release of our, our customers' or our suppliers' confidential or proprietary information, cause a disruption to our manufacturing and other operations, result in release of employee personal data, or cause us to incur increased information technology protection costs, any of which could adversely affect our operating results and our reputation.

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 (1)	Approximate Dollar Value of Shares May Yet Be Purchased Under the Plans or Programs (1)
July 1, 2014 through July 31, 2014	7,981,490	$ 48.18	7,981,490	4.16 billion
August 1, 2014 through August	6,087,231	46.89	6,087,231	3.87 billion

31, 2014								
September 1, 2014 through September 30, 2014	—		—	—		3.87	billion
Total	14,068,721	(2)	$ 47.62	14,068,721	(2)	3.87	billion (3)

(1) All purchases during the quarter were made under the authorization from our board of directors to purchase up to $5.0 billion of additional shares of TI common stock announced on February 21, 2013.

(2) All purchases during the quarter were open-market purchases.

(3) As of September 30, 2014, this amount consisted of the remaining portion of the $5.0 billion authorized in February 2013. No expiration date has been specified for this authorization.

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) o 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).
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 Dieg Incorporated with and into the Registrant, dated August 27, 2002 (incorporated by reference to Exhibit 3(q) of the Registrant's Annual Repor 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).
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(a)	Certification of Chief Executive Officer of Periodic Report Pursuant to Rule 13a-15(e) or Rule 15d-15(e).
31(b)	Certification of Chief Financial Officer of Periodic Report Pursuant to Rule 13a-15(e) or Rule 15d-15(e).
32(a)	Certification by Chief Executive Officer of Periodic Report Pursuant to 18 U.S.C. Section 1350.
32(b)	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 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 markets such as personal electronics, especially the mobile phone sector, and industrial;
- 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;
- Violations of or changes in the complex laws, regulations and policies to which our global operations are subject, and 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;
- Financial difficulties of our distributors or their promotion of competing product lines to TI's detriment;
- A loss suffered by a customer or distributor of TI with respect to TI-consigned inventory;
- 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;
- 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: October 31, 2014

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