ILLINOIS TOOL WORKS INC
Form 424B5
February 19, 2014
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Filed Pursuant to Rule 424(b)(5)

Registration No. 333-183449

CALCULATION OF REGISTRATION FEE

Title of Each Class of Securities Offered	Amount to be Registered	Proposed Maximum Offering Price per Note	Maximum Aggregate Offering Price	Amount of Registration Fee(1)
0.900% Notes due 2017	$650,000,000	99.861%	$649,096,500	$83,603.63
1.950% Notes due 2019	$650,000,000	99.871%	$649,161,500	$83,612.00
3.500% Notes due 2024	$700,000,000	99.648%	$697,536,000	$89,842.64
Total	$2,000,000,000		$1,995,794,000	$257,058.27

(1) Calculated in accordance with Rule 457(r).

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Prospectus Supplement

(To Prospectus dated August 21, 2012)

$2,000,000,000

ILLINOIS TOOL WORKS INC.

$650,000,000 0.900% Notes due 2017

$650,000,000 1.950% Notes due 2019

$700,000,000 3.500% Notes due 2024

This is an offering by Illinois Tool Works Inc. of $650,000,000 aggregate principal amount of 0.900% notes due 2017 (the 2017 notes), $650,000,000 aggregate principal amount of 1.950% notes due 2019 (the 2019 notes), and $700,000,000 aggregate principal amount of 3.500% notes due 2024 (the 2024 notes). The 2017 notes, the 2019 notes and the 2024 notes are collectively referred to as the notes.

Interest on the notes will be paid semi-annually in arrears on March 1 and September 1 of each year, beginning on September 1, 2014. The 2017 notes will mature on February 25, 2017, the 2019 notes will mature on March 1, 2019 and the 2024 notes will mature on March 1, 2024. We may redeem the notes, at any time in whole or from time to time in part, at the redemption prices described in this prospectus supplement under the caption Description of Notes Optional Redemption.

The notes will be our unsecured senior debt obligations and will rank equally with all of our other unsecured senior indebtedness from time to time outstanding. The notes will not be convertible or exchangeable.

We do not intend to apply for listing of the notes on any securities exchange. Currently, there is no public market for the notes.

Investing in our notes involves risks that are described under Risk Factors beginning on page S-6 of this prospectus supplement.

	Public offering price(1)	Underwriting discount	Proceeds, before expenses, to us
Per 2017 Note	99.861%	0.250%	99.611%
Total for 2017 Notes	$ 649,096,500	$ 1,625,000	$ 647,471,500
Per 2019 Note	99.871%	0.350%	99.521%
Total for 2019 Notes	$ 649,161,500	$ 2,275,000	$ 646,886,500
Per 2024 Note	99.648%	0.450%	99.198%
Total for 2024 Notes	$ 697,536,000	$ 3,150,000	$ 694,386,000
Total	$ 1,995,794,000	$ 7,050,000	$ 1,988,744,000

(1) Plus accrued interest, if any, from February 25, 2014, if settlement occurs after that date.

Neither the Securities and Exchange Commission nor any state securities commission has approved or disapproved of these securities or determined if this prospectus supplement or the accompanying prospectus is truthful or complete. Any representation to the contrary is a criminal offense.

We expect that delivery of the notes will be made to investors in book-entry form through the facilities of The Depository Trust Company and its direct and indirect participants, including Clearstream Banking, *société anonyme*, and Euroclear Bank, S.A./N.V., as operator of the Euroclear System, on or about February 25, 2014.

Joint Book-Running Managers

BofA Merrill Lynch **Citigroup** **Goldman, Sachs & Co.** **J.P. Morgan**

Co-Managers

HSBC **Mizuho Securities** **SOCIETE GENERALE**
Wells Fargo Securities

Banca IMI **Barclays** **BBVA**
BMO Capital Markets **COMMERZBANK** **Danske Markets Inc.**
ING **Loop Capital Markets** **nabSecurities, LLC**
US Bancorp

Prospectus Supplement dated February 18, 2014

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You should rely only on the information contained or incorporated by reference in this prospectus supplement and the accompanying prospectus. We have not, and the underwriters have not, authorized any other person to provide you with different or additional information with respect to this offering. If any person provides you with different or inconsistent information, you should not rely on it. We are not, and the underwriters are not, making an offer to sell these securities in any jurisdiction where the offer or sale is not permitted. You should only assume that the information contained or incorporated by reference in this prospectus supplement and the accompanying prospectus is accurate as of the date on the front of the respective document. Our business, properties, financial condition, results of operations and prospects may have changed since those dates.

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ABOUT THIS PROSPECTUS SUPPLEMENT

This document is in two parts. The first part is this prospectus supplement, which contains the terms of this offering of notes. The second part is the prospectus dated as of August 21, 2012, which was originally filed as part of our Registration Statement on Form S-3.

This prospectus supplement may add to, update or change the information in the accompanying prospectus. If information in this prospectus supplement is inconsistent with information in the accompanying prospectus, this prospectus supplement will apply and will supersede that information in the accompanying prospectus.

It is important for you to read and consider all information contained or incorporated by reference in this prospectus supplement and the accompanying prospectus in making your investment decision. You should also read and consider the information in the documents to which we have referred you under Where You Can Find More Information in this prospectus supplement.

You should rely only on the information contained or incorporated by reference in this prospectus supplement, in the accompanying prospectus or in any free writing prospectus filed by us with the Securities and Exchange Commission (the SEC). We have not, and the underwriters have not, authorized anyone to provide you with different information. Neither the delivery of this prospectus supplement and the accompanying prospectus, nor any sale made hereunder, shall under any circumstances create any implication that there has been no change in our affairs since the date of this prospectus supplement, or that the information contained or incorporated by reference in this prospectus supplement or the accompanying prospectus is correct as of any time after the date of that information.

The distribution of this prospectus supplement and the accompanying prospectus and the offering of the notes in certain jurisdictions may be restricted by law. This prospectus supplement and the accompanying prospectus do not constitute an offer, or an invitation on behalf of us or the underwriters or any of them, to subscribe to or purchase any of the notes, and may not be used for or in connection with an offer or solicitation by anyone, in any jurisdiction in which such an offer or solicitation is not authorized or to any person to whom it is unlawful to make such an offer or solicitation. See Underwriting.

In this prospectus supplement and the accompanying prospectus, unless otherwise stated, references to we, us, our and the Company refer to Illinois Tool Works Inc. and its subsidiaries.

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FORWARD-LOOKING STATEMENTS

This prospectus supplement contains or incorporates by reference certain statements and information that are forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended (the Securities Act), and Section 21E of the Securities Exchange Act of 1934, as amended (the Exchange Act). These statements may be identified by the use of words such as believe, expect, plans, intends, may, strategy, pros estimate, project, target, anticipate, guidance, forecast, and other similar words, including, without limitation, statements regarding the expected acquisition or disposition of businesses, economic conditions in various geographic regions, the timing and amount of share repurchases, the Company s Enterprise Strategy and its ability to manage its strategic business initiatives and the timing and amount of benefits therefrom, the adequacy of internally generated funds and credit facilities, the ability to fund debt service obligations, the cost and availability of additional financing, the intention to refinance debt obligations, the Company s portion of future benefit payments related to pension and postretirement benefits, the availability of raw materials and energy, the expiration of any one of the Company s patents, the cost of compliance with environmental regulations, the likelihood of future goodwill or intangible asset impairment charges, the outcome of outstanding legal proceedings, the impact of adopting new accounting pronouncements and the estimated timing and amount related to the resolution of tax matters. These statements are subject to certain risks, uncertainties, and other factors, which could cause actual results to differ materially from those anticipated. Important risks that may influence future results include (1) weakness or downturns in the markets we serve, (2) changes or deterioration in international and domestic political and economic conditions, (3) disruptions to our business as we implement our enterprise initiatives, (4) market conditions and availability of financing to fund our planned repurchase of shares, (5) negative effects of divestitures, including EPS dilution and impairment charges, (6) the risk of intentional acts of our employees, agents or business partners that violate anti-corruption and other laws, (7) the unfavorable impact of foreign currency fluctuations, (8) potential negative impact of acquisitions on our profitability and return on invested capital, (9) decreases in credit availability, (10) raw material price increases and supply shortages, (11) an interruption in, or reduction in, introducing new products into our product lines, (12) unfavorable tax law changes and tax authority rulings, (13) financial market risks to our obligations under our defined benefit pension plans, and (14) potential adverse outcome in legal proceedings. The risks covered here are not all inclusive and given these and other possible risks and uncertainties, investors should not place undue reliance on forward-looking statements as a prediction of actual results.

These forward-looking statements are not guarantees of future performance and involve risks, assumptions and uncertainties, known or unknown to us, including, but not limited to, those described in the section of this prospectus supplement entitled Risk Factors appearing below and elsewhere in this prospectus supplement and in the documents incorporated by reference in this prospectus supplement. Should one or more of these risks or uncertainties materialize, or should underlying assumptions prove incorrect, actual results may vary materially from those indicated or anticipated by such forward-looking statements. You are cautioned not to place undue reliance on these forward-looking statements, which speak only as of the date they are made. Except to the extent required by law, we do not undertake, and expressly disclaim, any duty or obligation to update publicly any forward-looking statement after the date the statement is made, whether as a result of new information, future events, changes in assumptions or otherwise.

WHERE YOU CAN FIND MORE INFORMATION

We file annual, quarterly and current reports, proxy statements and other information with the SEC. You may read and copy any reports, statements or other information we file with the SEC at the SEC s public reference room at 100 F Street, N.E., Washington, D.C. 20549. Please call the SEC at 1-800-SEC-0330 for further information on the public reference room. Our filings also are available to the public on the Internet, through a database maintained by the SEC at http://www.sec.gov. In addition, reports, proxy statements and other information concerning us may be inspected at

the offices of the New York Stock Exchange, 20 Broad Street, New York, New York 10005.

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We filed a registration statement on Form S-3 to register with the SEC the securities described in this prospectus supplement and the accompanying prospectus. This prospectus supplement and the accompanying prospectus are part of that registration statement. As permitted by SEC rules, this prospectus supplement and the accompanying prospectus do not contain all the information contained in the registration statement or the exhibits to the registration statement. You may refer to the registration statement and accompanying exhibits for more information about us and our securities.

The SEC allows us to incorporate by reference into this document the information we file with the SEC. This means that we can disclose important information to you by referring you to other documents that we identify as part of this prospectus supplement and the accompanying prospectus. The information incorporated by reference is considered to be part of this prospectus supplement and the accompanying prospectus.

We incorporate by reference the documents listed below:

1. Annual Report on Form 10-K for the fiscal year ended December 31, 2013; and

2. Current Reports on Form 8-K filed on February 12, 2014 and February 13, 2014 (other than documents or information deemed to have been furnished and not filed in accordance with SEC rules).

We also incorporate by reference any future filings we make with the SEC under Sections 13(a), 13(c), 14 or 15(d) of the Securities Exchange Act of 1934, as amended (the Exchange Act) (other than documents or information deemed to have been furnished and not filed in accordance with SEC rules), on or after the date of this prospectus supplement until we have terminated the offering. Those documents will become a part of this prospectus supplement from the date that the documents are filed with the SEC. Information that becomes a part of this prospectus supplement after the date of this prospectus supplement will automatically update and may replace information in this prospectus supplement, the accompanying prospectus and information previously filed with the SEC.

You may request a copy of any of these documents from us without charge, excluding certain exhibits to the documents, by writing or telephoning us at the following address:

Maria C. Green, Secretary

Illinois Tool Works Inc.

3600 West Lake Avenue

Glenview, IL 60026

(847) 724-7500

Documents may also be available on our website at www.itw.com. We do not intend our website address to be an active link and information contained on our website does not constitute a part of this prospectus supplement or the accompanying prospectus (or any document incorporated by reference herein or therein), and you should not rely on that information in making your investment decision unless that information is also in this prospectus supplement or the accompanying prospectus or has been expressly incorporated by reference into this prospectus supplement or the accompanying prospectus.

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SUMMARY

The Company

We are a global manufacturer of a diversified range of industrial products and equipment with operations in 56 countries.

We periodically make changes to our management reporting structure to better align our business with Company objectives and operating strategies. Effective January 1, 2013, the Company made certain changes in how its operations are reported to senior management in order to better align its portfolio of businesses with its enterprise-wide portfolio management initiative. As a result of this reorganization, the Company s operations are internally reported as 28 operating segments to senior management as of December 31, 2013, which have been aggregated into the following seven external reportable segments: Automotive OEM; Test & Measurement and Electronics; Food Equipment; Polymers & Fluids; Welding; Construction Products; and Specialty Products.

The significant changes that resulted from this reorganization included the following:

- Certain businesses within the former Transportation segment, primarily related to the automotive aftermarket business, are reported in the Polymers & Fluids segment and the Transportation segment has been renamed Automotive OEM.

- The Welding business, which was formerly reported in the Power Systems & Electronics segment, is reported separately as the Welding segment.

- The Electronics business, which was formerly reported in the Power Systems & Electronics segment, has been combined with the Test & Measurement business, which was formerly reported in the All Other segment, to form a new Test & Measurement and Electronics segment.

- The All Other segment has been renamed Specialty Products.

The following is a description of the Company s seven reportable segments:

Automotive OEM: Businesses in this segment produce components and fasteners for automotive-related applications.

In the Automotive OEM segment, products and services include:

- plastic and metal components, fasteners and assemblies for automobiles, light trucks, and other industrial uses.

Test & Measurement and Electronics: Businesses in this segment produce equipment, consumables, and related software for testing and measuring of materials and structures, as well as equipment and consumables used in the production of electronic subassemblies and microelectronics.

In the Test & Measurement and Electronics segment, products include:

- equipment, consumables, and related software for testing and measuring of materials, structures, gases and fluids;
- electronic assembly equipment and related consumable solder materials;
- electronic components and component packaging;
- static control equipment and consumables used for contamination control in clean room environments; and
- pressure sensitive adhesives and components for telecommunications, electronics, medical and transportation applications.

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Food Equipment: Businesses in this segment produce commercial food equipment and provide related service.

In the Food Equipment segment, products and services include:

- warewashing equipment;
- cooking equipment, including ovens, ranges and broilers;
- refrigeration equipment, including refrigerators, freezers and prep tables;
- food processing equipment, including slicers, mixers and scales;
- kitchen exhaust, ventilation and pollution control systems; and
- food equipment service, maintenance and repair.

Polymers & Fluids: Businesses in this segment produce adhesives, sealants, lubrication and cutting fluids, janitorial and hygiene products, and fluids and polymers for auto aftermarket maintenance and appearance.

In the Polymers & Fluids segment, products include:

- adhesives for industrial, construction and consumer purposes;
- chemical fluids which clean or add lubrication to machines;
- epoxy and resin-based coating products for industrial applications;
- hand wipes and cleaners for industrial applications;
- fluids, polymers and other supplies for auto aftermarket maintenance and appearance;
- fillers and putties for auto body repair; and
- polyester coatings and patch and repair products for the marine industry.

Welding: Businesses in this segment produce arc welding equipment, consumables and accessories for a wide array of industrial and commercial applications.

In the Welding segment, products include:

- arc welding equipment;
- metal arc welding consumables and related accessories; and
- metal jacketing and other insulation products.

Construction Products: Businesses in this segment produce construction fastening systems and truss products.

In the Construction Products segment, products include:

- fasteners and related fastening tools for wood and metal applications;
- anchors, fasteners and related tools for concrete applications;
- metal plate truss components and related equipment and software; and
- packaged hardware, fasteners, anchors and other products for retail.

Specialty Products: Diversified businesses in this segment produce beverage packaging equipment and consumables, product coding and marking equipment and consumables, and appliance components and fasteners.

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In the Specialty Products segment, products include:

- line integration, conveyor systems and line automation for the food and beverage industries;
- plastic consumables that multi-pack cans and bottles and related equipment;
- foil, film and related equipment used to decorate consumer products;
- product coding and marking equipment and related consumables;
- plastic and metal fasteners and components for appliances;
- airport ground support equipment; and
- components for medical devices.

Recent Development   Entry Into Agreement to Sell Industrial Packaging Segment

In February 2013, we initiated a review process to explore strategic alternatives for our Industrial Packaging segment. In September 2013, our Board of Directors authorized a plan to commence a sale process and we classified the Industrial Packaging segment as held for sale beginning in the third quarter of 2013 and from that time no longer presented this segment as part of our continuing operations. On February 6, 2014, we announced our entry into a definitive agreement to sell the Industrial Packaging segment to The Carlyle Group for $3.2 billion. The transaction is subject to regulatory approval and customary closing conditions, and is expected to close by mid-2014. We intend to use proceeds from the sale to partially fund our plan to repurchase approximately 50 million shares of our common stock by the end of 2014 in order to offset the EPS dilution associated with this divestiture.

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The Offering

The following is a brief summary of some of the terms of the notes. For a more complete description of the terms of the notes see Description of Notes in this prospectus supplement and Description of Debt Securities in the accompanying prospectus.

Issuer	Illinois Tool Works Inc.
Notes Offered	$650,000,000 aggregate principal amount of 0.900% notes due 2017.
	$650,000,000 aggregate principal amount of 1.950% notes due 2019.
	$700,000,000 aggregate principal amount of 3.500% notes due 2024.
Maturity	The 2017 notes will mature on February 25, 2017, the 2019 notes will mature on March 1, 2019 and the 2024 notes will mature on March 1, 2024.
Interest Payment Dates	Interest on the notes is payable semi-annually in arrears on March 1 and September 1 of each year, beginning on September 1, 2014.
Ranking	The notes will be unsecured and rank equally with all of our other unsecured and unsubordinated indebtedness from time to time outstanding.
Use of Proceeds	We estimate that the net proceeds from the offering, after deducting the underwriters discount and estimated offering expenses payable by us, will be approximately $1,986.4 million. We intend to use these proceeds to repay short-term indebtedness we have incurred under our commercial paper program and for general corporate purposes.
Optional Redemption	We may redeem the notes, at any time in whole or from time to time in part, at the redemption prices described in this prospectus supplement. See Description of Notes Optional Redemption.
Certain Covenants	The indenture for the notes limits our ability to, among other things, engage in mergers, consolidations or similar transactions, create liens and

	engage in sale and leaseback transactions. See Description of Notes Covenants.
Further Issuances	We may from time to time, without the consent of the holders of the notes, issue additional notes with the same terms and conditions and with the same CUSIP number as the notes of that series so that the additional notes will be consolidated and form a single series with the previously outstanding notes of the applicable series. See Description of Notes General.
Book-Entry	The notes will be issued in book-entry form and will be represented by global securities deposited with, or on behalf of, The Depository Trust Company (DTC) and registered in the name of Cede & Co., DTC s nominee. See Description of Notes Book-Entry System.
	Beneficial interests in the notes will be shown on, and transfers will be effected only through, records maintained by DTC or its nominee

	and its direct and indirect participants, including the depositaries for Clearstream Banking, *société anonyme*, and Euroclear Bank, S.A./N.V.; and these interests may not be exchanged for certificated notes, except in limited circumstances.
Trustee	The Bank of New York Mellon Trust Company, N.A.
Risk Factors	See Risk Factors included in this prospectus supplement for a discussion of risks you should carefully consider before deciding to invest in the notes.

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RISK FACTORS

Investing in the notes involves a high degree of risk. You should carefully consider the risks described below and other information contained in this prospectus supplement, the accompanying prospectus and the documents incorporated by reference into this prospectus supplement before investing in the notes. The risks described below are not the only ones facing our company. Additional risks not presently known to us or that we currently consider less significant may also impair our business operations. Our business, financial condition, or results of operations could be materially adversely affected by any of these risks.

This prospectus supplement and the accompanying prospectus also contain or incorporate by reference forward-looking statements that involve risks and uncertainties. Our actual results could differ materially from those anticipated in such forward-looking statements as a result of certain factors, including the risks faced by us described below and elsewhere in this prospectus supplement and the accompanying prospectus. See Forward-Looking Statements.

Risks Related to Our Business

For a discussion of risks related to our business and operations, please see Item 1A. Risk Factors and Item 7. Management s Discussion and Analysis of Financial Condition and Results of Operations in our Annual Report on Form 10-K for our fiscal year ended December 31, 2013, which are incorporated by reference in this prospectus supplement, as well as similar disclosures contained in our filings with the SEC subsequent to the date of this prospectus supplement.

Risks Related to the Offering

The notes are subject to prior claims of any of our secured creditors.

The notes are our unsecured general obligations, ranking equally with other unsecured and unsubordinated debt but below any secured debt to the extent of the value of the assets constituting the security. The indenture governing the notes permits us and our subsidiaries to incur secured debt under specified circumstances. If we incur any debt secured by our assets or assets of our subsidiaries, these assets will be subject to the prior claims of our secured creditors.

In the event of a bankruptcy, liquidation, dissolution, reorganization or similar proceeding, our pledged assets would be available to satisfy obligations of the secured debt before any payment could be made on the notes. To the extent that such assets cannot satisfy in full our secured debt, the holders of such debt would have a claim for any shortfall that would rank equally in right of payment with the notes. In that case, we may not have sufficient assets remaining to pay amounts due on any or all of the notes.

The notes are effectively subordinated to the existing and future liabilities of our subsidiaries.

Our equity interest in our subsidiaries is subordinate to any debt and other liabilities and commitments of our subsidiaries to the extent of the value of the assets of such subsidiaries, whether or not secured. The notes will not be guaranteed by our subsidiaries and we may not have direct access to the assets of our subsidiaries unless these assets are transferred to us by dividend or otherwise. The ability of our subsidiaries to pay dividends or otherwise transfer assets to us is subject to various restrictions under applicable law. Our right to receive assets of any of our subsidiaries upon their bankruptcy, liquidation or reorganization, and therefore the right of the holders of the notes to participate in those assets, will be effectively subordinated to the claims of that subsidiary s creditors. In addition, even if we are a creditor of any of our subsidiaries, our right as a creditor would be subordinate to any security interest in the assets of

our subsidiaries and any debt of our subsidiaries senior to that held by us.

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Credit ratings of the notes may change and affect the market price and marketability of the notes.

Credit ratings are limited in scope, and do not address all material risks relating to an investment in the notes, but rather reflect only the view of each rating agency at the time the rating is issued. An explanation of the significance of such rating may be obtained from such rating agency. There can be no assurance that such credit ratings will remain in effect for any given period of time or that a rating will not be lowered, suspended or withdrawn entirely by the applicable rating agencies, if, in such rating agency s judgment, circumstances so warrant. Agency credit ratings are not a recommendation to buy, sell or hold any security. Actual or anticipated changes or downgrades in our credit ratings, including any announcement that our ratings are under further review for a downgrade, could affect the market price or marketability of the notes and increase our corporate borrowing costs.

The indenture does not restrict the amount of additional debt that we may incur.

The notes and indenture pursuant to which the notes will be issued do not place any limitation on the amount of unsecured debt that we or our subsidiaries may incur. Our incurrence of additional debt may have important consequences for you as a holder of the notes, including making it more difficult for us to satisfy our obligations with respect to the notes, a loss in the trading value of your notes, if any, and a risk that the credit rating of the notes is lowered or withdrawn.

An active trading market may not develop for the notes.

The notes are a new issue of securities with no established trading market. We do not intend to apply for listing of the notes on a national securities exchange. Certain of the underwriters have advised us that they presently intend to make a market in the notes as permitted by applicable law. However, the underwriters are not obligated to make a market in the notes and may cease their market-making activities at any time at their discretion without notice. In addition, the liquidity of the trading market in the notes and the market price quoted for the notes may be adversely affected by changes in the overall market for securities and by changes in the financial performance or prospects of our company or companies in our industry. As a result, no assurance can be given (i) that an active trading market will develop or be maintained for the notes, (ii) as to the liquidity of any market that does develop or (iii) as to your ability to sell any notes you may own or the price at which you may be able to sell your notes.

If trading markets do develop, changes in our ratings or the financial markets could adversely affect the market prices of the notes.

The market prices of the notes will depend on many factors, including, among others, the following:

- ratings on our debt securities assigned by rating agencies;
- the prevailing interest rates being paid by other companies similar to us;
- our results of operations, financial condition and prospects; and
- the condition of the financial markets.

The condition of the financial markets and prevailing interest rates have fluctuated in the past and are likely to fluctuate in the future, which could have an adverse effect on the market prices of the notes.

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USE OF PROCEEDS

The net proceeds to us from the sale of the notes will be approximately $1,986.4 million (after deducting the underwriting discount and our offering expenses). We intend to use the net proceeds from the sale of the notes to repay short-term indebtedness we have incurred under our commercial paper program and for general corporate purposes. The amount outstanding under our commercial paper program as of February 12, 2014, was approximately $2.1 billion, at a weighted average interest rate of 0.2% per year, which rate is subject to change over time. Pending application of the proceeds of sale of the notes, we intend to invest such proceeds in short-term investments.

RATIO OF EARNINGS TO FIXED CHARGES

Our consolidated ratio of earnings to fixed charges for each of the last five fiscal years is set forth below. You should read this table in conjunction with the consolidated financial statements and related notes to financial statements incorporated by reference in this prospectus. See Where You Can Find More Information in this prospectus supplement.

For the purpose of computing these ratios, earnings consists of income from continuing operations before income taxes and equity method earnings plus fixed charges and dividends of unconsolidated affiliates. Fixed charges consists of interest expense (which includes amortization of debt issuance costs) and an estimate of the interest within rental expense. The ratio was calculated by dividing the sum of the fixed charges into the sum of earnings. Interest related to income tax matters is included in income taxes in the consolidated statement of income and is excluded from the computation of fixed charges.

	Pro Forma	For the Years Ended December 31,				
	2013	2013	2012	2011	2010	2009
Ratio of earnings to fixed charges(1)	8.0x	9.3x	13.4x	10.3x	9.3x	6.1x

(1) Certain reclassifications of prior years data have been made to conform to current year reporting, including discontinued operations. In addition, we divested a 51% majority interest in our Decorative Surfaces segment on October 31, 2012, which, due to our continuing involvement through our remaining 49% interest, is presented in continuing operations prior to October 31, 2012. See Selected Consolidated Financial Data for more detail regarding discontinued operations and the Decorative Surfaces transaction.

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SELECTED CONSOLIDATED FINANCIAL DATA

The following table presents our selected consolidated financial data for the periods indicated. The consolidated statement of income and dividends declared data for each of the years in the three-year period ended December 31, 2013 and the consolidated statement of financial position data as of December 31, 2013 and 2012 have been derived from our audited consolidated financial statements appearing in our Annual Report on Form 10-K for the fiscal year ended December 31, 2013, which is incorporated by reference in this prospectus supplement. The consolidated statement of income data for the years ended December 31, 2010 and 2009 have been derived from our unaudited consolidated financial statements not included or incorporated by reference in this prospectus supplement or the accompanying prospectus. The consolidated statement of financial position data as of December 31, 2011, 2010 and 2009 and cash dividends declared data for each of the years in the two-year period ended December 31, 2010 have been derived from our audited consolidated financial statements not included or incorporated by reference in this prospectus supplement or the accompanying prospectus.

The selected historical consolidated financial data presented below should be read in conjunction with our audited consolidated financial statements and related notes to financial statements in Item 8. Financial Statements and Supplementary Data, as well as Management s Discussion and Analysis of Financial Condition and Results of Operations in our Annual Report on Form 10-K for the year ended December 31, 2013, which is incorporated by reference in this prospectus supplement and the accompanying prospectus. Our audited and unaudited consolidated financial information may not be indicative of our future performance.

	For the Years Ended December 31,				
In millions (except per share amounts)	**2013**	**2012**	**2011**	**2010**	**2009**
Operating revenues	$ 14,135	$ 14,791	$ 14,515	$ 12,265	$ 11,216
Income from continuing operations	1,630	2,233	1,775	1,258	889
Income per share from continuing operations:					
Basic	3.65	4.75	3.61	2.51	1.78
Diluted	3.63	4.72	3.59	2.50	1.77
Total assets at year-end	19,966	19,309	17,984	16,412	15,811
Long-term debt at year-end	2,793	4,589	3,488	2,542	2,861
Cash dividends declared per common share	1.60	1.48	1.40	1.30	1.24

Certain reclassifications of prior years data have been made to conform to current year reporting, including discontinued operations as discussed below.

We periodically review our operations for businesses that may no longer be aligned with our enterprise initiatives and long-term objectives. As a result, we may commit to a plan to exit or dispose of certain businesses and present them as discontinued operations. For businesses reported as discontinued operations in the statement of income, all related prior period income statement information has been restated to conform to the current year reporting of these businesses. Income from discontinued operations was $49 million, $637 million, $296 million, $245 million, and $84 million in the years 2013, 2012, 2011, 2010 and 2009, respectively.

On October 31, 2012, we divested a 51% majority interest in our Decorative Surfaces segment. Accordingly, we ceased consolidating the results of our Decorative Surfaces segment as of October 31, 2012 and now report our 49% ownership interest using the equity method of accounting. Due to our continuing involvement through our 49% interest, the historical operating results of Decorative Surfaces are presented in continuing operations. Effective November 1, 2012, Decorative Surfaces is no longer a reportable segment of the Company. See the Divestiture of

Majority Interest in Former Decorative Surfaces Segment note in Item 8. Financial Statements and Supplementary Data of our Annual Report on Form 10-K for the year ended December 31, 2013, which is incorporated by reference in this prospectus supplement, for further discussion of this transaction.

In February 2013, we initiated a review process to explore strategic alternatives for our Industrial Packaging segment. In September 2013, our Board of Directors authorized a plan to commence a sale process and we

classified the Industrial Packaging segment as held for sale beginning in the third quarter of 2013 and from that time no longer presented this segment as part of our continuing operations. On February 6, 2014, we announced our entry into a definitive agreement to sell the Industrial Packaging segment to The Carlyle Group for $3.2 billion. The transaction is subject to regulatory approval and customary closing conditions, and is expected to close by mid-2014.

In the third quarter of 2013, we also committed to plans for the divestiture of a construction distribution business previously included in the Construction Products segment and a specialty coatings business previously included in the Polymers & Fluids segment. The construction distribution and specialty coatings businesses were classified as held for sale beginning in the third quarter of 2013.

In the first quarter of 2013, we committed to plans for the divestiture of two transportation related businesses and a machine components business previously included in the Specialty Products segment, two construction distribution businesses previously included in the Construction Products segment, and a chemical manufacturing business previously included in the Polymers & Fluids segment. These businesses were classified as held for sale beginning in the first quarter of 2013.

These held for sale businesses discussed above, as well as certain previously divested businesses, are reported as discontinued operations in the statement of income. All related prior period income statement information has been restated to conform to the current year reporting of these businesses. Refer to the Discontinued Operations note in Item 8. Financial Statements and Supplementary Data of our Annual Report on Form 10-K for the year ended December 31, 2013, which is incorporated by reference in this prospectus supplement, for discussion of our discontinued operations.

Information on the comparability of results is included in Item 7. Management s Discussion and Analysis of Financial Condition and Results of Operations in our Annual Report on Form 10-K for the year ended December 31, 2013, which is incorporated by reference in this prospectus supplement.

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CAPITALIZATION

The following table sets forth our consolidated cash and equivalents and capitalization as of December 31, 2013 on a historical basis and on an as adjusted basis to give effect to the offering of the notes and the use of proceeds therefrom as described under Use of Proceeds. This table should be read in conjunction with our audited consolidated financial statements and related notes to financial statements in Item 8. Financial Statements and Supplementary Data, as well as Management s Discussion and Analysis of Financial Condition and Results of Operations in our Annual Report on Form 10-K for the year ended December 31, 2013, which is incorporated by reference in this prospectus supplement.

	As of December 31, 2013	
	Actual	**As Adjusted(1)**
	(In millions)	
Cash and equivalents	$ 3,618	$ 3,953
Debt:		
U.S. Dollar-denominated commercial paper	$ 1,652	$
5.15% notes due April 1, 2014	800	800
5.25% Euro notes due October 1, 2014	1,031	1,031
6.25% notes due April 1, 2019	700	700
4.88% senior notes due through December 31, 2020	7	7
3.375% notes due September 15, 2021	349	349
4.875% notes due September 15, 2041	641	641
3.9% notes due September 1, 2042	1,090	1,090
0.900% notes due February 25, 2017 offered hereby		649
1.950% notes due March 1, 2019 offered hereby		649
3.500% notes due March 1, 2024 offered hereby		698
Other borrowings	74	74
Total debt	6,344	6,688
Total stockholders equity	9,709	9,709
Total capitalization	$ 16,053	$ 16,397

(1) Assumes all commercial paper outstanding as of December 31, 2013 is repaid with the net proceeds from the offering. The amount outstanding under our commercial paper program as of February 12, 2014 was approximately $2.1 billion.

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DESCRIPTION OF NOTES

The following description of the terms of the notes offered hereby supplements, and to the extent it is inconsistent therewith replaces, the description of the general terms of debt securities set forth in the accompanying prospectus, to which description reference is hereby made. In this Description of Notes section, the terms we, our, us and ITW solely to Illinois Tool Works Inc. and not to its subsidiaries.

General

We will issue the notes as a series of debt securities under the Indenture dated November 1, 1986, as supplemented by a First Supplemental Indenture dated as of May 1, 1990, between us and The Bank of New York Mellon Trust Company, N.A., as successor trustee (the trustee), with certain terms of the notes being set forth in an officer s certificate (together, the indenture).

The notes will not have the benefit of any sinking fund and will not be convertible or exchangeable. We will issue the notes in minimum denominations of $2,000 and integral multiples of $1,000 in excess thereof. The notes will be issued in book-entry form only. At our option, we may redeem the notes prior to maturity at the redemption prices described below.

We may from time to time under the indenture, without the consent of the existing holders of notes, create and issue additional notes with the same terms and conditions and with the same CUSIP number as the notes of that series, except for issue date, issue price and the first payment of interest thereon. Additional notes issued in this manner will be consolidated with and will form a single series with the previously outstanding notes of the applicable series.

Ranking

The notes will be our direct, unsecured obligations. They will rank on a parity with all of our other unsecured and unsubordinated indebtedness from time to time outstanding.

Principal, Interest Payments and Maturity

The 2017 notes will initially be limited to $650,000,000 aggregate principal amount and will mature on February 25, 2017. The 2019 notes will initially be limited to $650,000,000 aggregate principal amount and will mature on March 1, 2019. The 2024 notes will initially be limited to $700,000,000 aggregate principal amount and will mature on March 1, 2024.

The notes of each series will bear interest at the applicable rate shown on the cover of this prospectus supplement, accruing from February 25, 2014 or the most recent interest payment date to which interest has been paid or provided for. We will pay interest on the notes semi-annually in arrears on March 1 and September 1 of each year, beginning on September 1, 2014, to persons in whose names the notes are registered at the close of business on the preceding February 15 or August 15, as the case may be. We will compute the amount of interest payable on the basis of a 360-day year of twelve 30-day months.

Principal of and any premium or interest on the notes will be payable, and the notes may be registered for transfer or exchanged without payment of any charge (other than any tax or other governmental charge payable in connection therewith), at our office or agency in Chicago, Illinois and any other location we designate. Initially, the trustee s offices in Chicago, Illinois and New York, New York will serve as our offices and agency for these purposes. However, we may elect that payment of interest on registered notes be made by check mailed to the address of the

appropriate person as it appears on the security register or by wire transfer as instructed by the appropriate person.

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If any interest payment date or maturity or redemption date falls on a day that is not a business day, then the payment will be made on the next business day without additional interest and with the same effect as if it were made on the originally scheduled date.

Optional Redemption

We may redeem the notes of each series at our option, in whole or in part, (i) in the case of the 2024 notes, on any date that is not less than three months prior to the stated maturity thereof and (ii) in the case of the 2017 notes and the 2019 notes, on any date that is prior to the stated maturity thereof, in each case, at our option at a redemption price equal to the greater of:

(1) 100% of the principal amount of the notes to be redeemed; or

(2) the sum of the present values of the remaining scheduled payments of principal and interest on the notes being redeemed on the date of redemption (exclusive of interest accrued to the date of redemption) discounted to the date of redemption on a semi-annual basis at the Treasury Rate (as defined below) plus 5 basis points for the 2017 notes, 10 basis points for the 2019 notes and 15 basis points for the 2024 notes, in each case as determined by a Reference Treasury Dealer (as defined below),

plus, in each case, accrued and unpaid interest on the principal amount being redeemed to the date of redemption.

At any time on or after the date that is three months prior to the maturity date of the 2024 notes, we may also redeem some or all of the maturing 2024 notes at our option, at a redemption price equal to 100% of the principal amount of the notes being redeemed plus accrued and unpaid interest on the notes to the date of redemption.

Notwithstanding the foregoing, installments of interest on notes that are due and payable on interest payment dates falling on or prior to a date of redemption will be payable on the interest payment date to the registered holders as of the close of business on the relevant record date according to the notes and the indenture. The redemption price will be calculated on the basis of a 360-day year consisting of twelve 30-day months.

Comparable Treasury Issue means the United States Treasury security selected by the Reference Treasury Dealer as having a maturity comparable to the remaining term of the series of the notes to be redeemed that would be utilized, at the time of selection and in accordance with customary financial practice, in pricing new issues of corporate debt securities of comparable maturity to the remaining term of such notes.

Comparable Treasury Price means, with respect to any redemption date, (i) the average of the Reference Treasury Dealer Quotations for such redemption date, after excluding the highest and lowest such Reference Treasury Dealer Quotations, or (ii) if we obtain fewer than four such Reference Treasury Dealer Quotations, the average of all such quotations, or (iii) if only one Reference Treasury Dealer Quotation is received, such quotation.

Primary Treasury Dealer means a primary United States government securities dealer in the United States.

Reference Treasury Dealer means (i) Citigroup Global Markets Inc., Goldman, Sachs & Co., J.P. Morgan Securities LLC and Merrill Lynch, Pierce, Fenner & Smith Incorporated (or their respective affiliates that are Primary Treasury Dealers) and their respective successors; provided, however, that if any of the foregoing shall cease to be a Primary Treasury Dealer, we will substitute therefor another Primary Treasury Dealer and (ii) any other Primary Treasury

Dealer(s) (in any case not less than two) selected by us.

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Reference Treasury Dealer Quotations means, with respect to each Reference Treasury Dealer and any redemption date, the average, as determined by us, of the bid and asked prices for the Comparable Treasury Issue (expressed in each case as a percentage of its principal amount) quoted in writing to us by such Reference Treasury Dealer at 3:30 p.m., New York City time, on the third business day preceding such redemption date.

Treasury Rate means, with respect to any redemption date, the rate per annum equal to the semi-annual equivalent yield to maturity (on a day count basis) of the Comparable Treasury Issue, assuming a price for the Comparable Treasury Issue (expressed as a percentage of its principal amount) equal to the Comparable Treasury Price for such redemption date.

We will, or will cause the trustee on our behalf to, mail notice of a redemption to holders of notes to be redeemed by first-class mail at least 30 and not more than 60 days prior to the date fixed for redemption. Unless we default in payment of the redemption price, on and after the redemption date, interest will cease to accrue on the notes or portions thereof called for redemption. On or before the redemption date, we will deposit with a paying agent (which may be the trustee) or set aside, segregate and hold in trust (if we are acting as paying agent), funds sufficient to pay the redemption price of, and accrued and unpaid interest on, such notes to be redeemed on that redemption date. If fewer than all of the notes are to be redeemed, the trustee will select, not more than 60 days prior to the redemption date, the particular notes or portions thereof for redemption from the outstanding notes of such series not previously called by such method as the trustee deems fair and appropriate and in accordance with the applicable procedures of the depositary; provided, however, that no notes of a principal amount of $2,000 or less shall be redeemed in part.

Covenants

The following covenants apply to the notes. Each of the covenants is subject to the provision for exempted indebtedness described below.

For your reference, we have provided below definitions of the capitalized terms used in the description of the covenants.

Limitation on Liens

We will not, nor will we permit any Restricted Subsidiary to, issue, assume or guarantee any debt for money borrowed if such debt is secured by a mortgage, security interest, lien, pledge or other encumbrance (referred to in this offering memorandum as a lien) on any Principal Property, or on any shares of stock or indebtedness of any Restricted Subsidiary, without in any such case effectively providing that the notes (and if we so choose, any other debt or obligation that ranks equally with the notes) are secured equally and ratably with, or prior to, such debt. These restrictions do not apply to debt secured by:

- liens on property of a corporation existing at the time it becomes a subsidiary or at the time it is merged into or consolidated with or purchased by us or a subsidiary;
- liens on property existing at the time of its acquisition and certain purchase money liens;
- liens securing the cost of construction of new plants, incurred within 180 days of completion of construction;

liens securing the debt of a Restricted Subsidiary owing to us or another Restricted Subsidiary;

liens in connection with the issuance of certain industrial revenue bonds or similar financings;

liens existing on the date of the indenture;

certain other liens specified in the indenture that are customarily exempted from restrictions in offerings of securities similar to the notes; and

any extensions, renewals or replacements, in whole or in part, of any lien referred to above, as long as the principal amount of debt secured by any such lien does not increase and the lien is limited to all or part of the same property that previously secured the lien.

Limitation on Sale and Lease-Back

We will not, nor will we permit any Restricted Subsidiary to, engage in a sale and lease-back transaction of any Principal Property (except for certain temporary leases and leases with a Restricted Subsidiary) unless:

we or the Restricted Subsidiary could (subject to the limitation on liens) incur debt secured by a lien on the Principal Property to be leased without equally and ratably securing the notes; or

within 180 days following such a transaction, we retire long-term debt equal to the value of the transaction.

Exempted Indebtedness

We and our Restricted Subsidiaries may incur debt and enter into sale and lease-back transactions without regard to the two covenants described above if the sum of such debt and the value of such sale and lease-back transactions on a cumulative basis does not exceed 10% of the Consolidated Net Tangible Assets (which is total assets less current liabilities, goodwill and other intangibles) as shown on our audited consolidated balance sheet in our latest annual report to our stockholders.

Definitions

Principal Property means any manufacturing plant or other facility within the United States that we or a subsidiary own or lease, unless our Board of Directors determines that the plant or facility, together with any others so determined, is not of material importance to the total business of us and our Restricted Subsidiaries.

Restricted Subsidiary means any subsidiary (other than a subsidiary principally engaged in leasing or financing installment receivables or financing operations outside the United States) that owns or leases a Principal Property if: (1) substantially all of its property is located in the United States, (2) substantially all of its business is carried on in the United States, or (3) it is incorporated in any State of the United States.

Consolidation or Merger

Under the terms of the indenture, we may consolidate or merge with another corporation or sell, convey or lease all or substantially all of our assets to another corporation or entity. The successor or acquiring corporation or entity must expressly assume all of our responsibilities and liabilities under the indenture, including the payment of all amounts due on the notes and performance of the covenants. If, upon any such consolidation, merger, sale, conveyance or lease, or upon any such consolidation, merger, sale, conveyance or lease with respect to a Restricted Subsidiary, any Principal Property or shares of stock or indebtedness of a Restricted Subsidiary would become subject to a lien that is not in favor of us, a Restricted Subsidiary or any such successor or acquiring corporation or entity, we must, before or at the time of such transaction, effectively provide that the notes will be secured (if we so choose, equally and ratably with any other obligation of us or a Restricted Subsidiary that ranks equally with the notes) by a direct lien on such Principal Property or shares of stock or indebtedness of a Restricted Subsidiary that is prior to all liens other than pre-existing liens on such Principal Property or shares of stock or indebtedness of a Restricted Subsidiary, and that will continue as long as such Principal Property, shares of stock or indebtedness is subject to the lien arising in such

transaction.

Events of Default

An event of default for any series of the notes includes the following:

- failure to pay any installment of interest on the notes of that series that continues for 30 days after such payment is due;

- failure to pay principal of or premium, if any, on the notes of that series when due;
- failure to perform any of the other covenants or agreements in the notes or in the indenture and relating to the notes of that series that continues for 60 days after notice to us by the trustee or holders of at least 25% in aggregate principal amount of the outstanding notes of that series; or
- certain events of bankruptcy, insolvency or reorganization of us.

An event of default with respect to a particular series of notes issued under the indenture does not necessarily constitute an event of default with respect to any other series. The indenture provides that the trustee will, with certain exceptions, notify the holders of the affected series of notes of the occurrence of any of the events of default listed above (not including any applicable grace period and irrespective of the giving of notice as described in the third bullet) known to the trustee within 90 days after the occurrence thereof. Except in the case of a default in the payment of principal of, or premium, if any, or interest on a series of the notes, the trustee may withhold notice if it determines in good faith that withholding notice is in the interest of the holders.

If an event of default is continuing for any series of the notes, the trustee or the holders of not less than 25% in aggregate principal amount of the affected series of notes then outstanding may declare the principal amount of that series of the notes to be due and payable immediately. In such a case, subject to certain conditions, the holders of a majority in aggregate principal amount of that series of the notes then outstanding can annul the declaration and waive past defaults.

We are required to provide an annual officers certificate to the trustee concerning our compliance with certain covenants we make in the indenture. Subject to the provisions of the indenture relating to the duties of the trustee, the trustee is not obligated to exercise any of its rights or powers at the request or direction of any of the holders of notes unless the holders have offered the trustee security or indemnity reasonably satisfactory to the trustee. The holders of a majority in principal amount of the outstanding notes of each series affected by an event of default may direct the time, method and place of conducting any proceeding for any remedy available to the trustee under the indenture or exercising any of the trustee s trusts or powers with respect to that series of the notes; however, the trustee may decline to follow such direction in certain circumstances.

Modification and Amendment of the Indenture

We may enter into supplemental indentures with the trustee without the consent of the holders of the notes to, among other things:

- evidence the assumption by a successor corporation of our obligations under the indenture;
- appoint additional or separate trustees to act under the indenture;
- add covenants for the protection of the holders of the notes; and

cure any ambiguity or correct any inconsistency in the indenture.

With the consent of the holders of a majority in aggregate principal amount of the securities of each affected series issued under the indenture at the time outstanding, we may execute supplemental indentures with the trustee to add provisions or change or eliminate any provision of the indenture or any supplemental indenture relating to such series or to modify the rights of the holders of those securities. However, no such supplemental indenture will (1) extend the fixed maturity of any securities, reduce the principal amount (including in the case of discounted securities the amount payable upon acceleration of the maturity thereof), reduce the rate or extend the time of payment of any interest, reduce any premium payable upon redemption, or change the currency in which any securities are payable, without the consent of each holder of affected securities, or (2) reduce the aforesaid majority in principal amount of the securities of any series, the consent of the holders of which is required for any such supplemental indenture, without the consent of the holders of all securities of such series.

Defeasance and Discharge of Indenture or Certain Obligations

At our option, we (1) will be discharged from all obligations under the indenture in respect of the notes of a series (except for certain obligations to register the transfer of or to exchange notes, replace stolen, lost or mutilated notes, maintain paying agencies and hold monies for payment in trust) or (2) need not comply with certain covenants of the indenture (including the limitation on liens and the limitation on sale and lease-back) and will not be limited by the restrictions in the indenture with respect to merger, consolidation or sale, conveyance or lease of substantially all of our assets, in each case if we irrevocably deposit with the trustee, in trust, money or U.S. government obligations (or a combination thereof) sufficient to pay the principal of and any premium or interest on the notes when due and satisfy other conditions in the indenture. In order to select either option, we must provide the trustee, among other things, a ruling from or published by the Internal Revenue Service (in the case of option 1) or an opinion of counsel (in the case of option 2) to the effect that holders of the notes will not recognize income, gain or loss for federal income tax purposes as a result of our exercise of the option, as if we had not exercised such option.

In the event we exercise our option under (2) above with respect to the notes and the notes of any series are declared due and payable because of the occurrence of any event of default other than default with respect to such obligations, the amount of money and U.S. government obligations on deposit with the trustee will be sufficient to pay amounts due on the notes of that series at the time of their stated maturity but may not be sufficient to pay amounts due on the notes of that series at the time of the acceleration resulting from such event of default. We would remain liable, however, for such payments.

Book-Entry System

Global Notes

We will issue the notes of each series in the form of one or more global notes in definitive, fully registered, book-entry form. The global notes will be deposited with or on behalf of DTC and registered in the name of Cede & Co., as nominee of DTC.

DTC, Clearstream and Euroclear

Beneficial interests in the global notes will be represented through book-entry accounts of financial institutions acting on behalf of beneficial owners as direct and indirect participants in DTC. Investors may hold interests in the global notes through either DTC (in the United States), Clearstream Banking, *société anonyme*, Luxembourg, which we refer to as Clearstream, or Euroclear Bank S.A./N.V., as operator of the Euroclear System, which we refer to as Euroclear, in Europe, either directly if they are participants in such systems or indirectly through organizations that are participants in such systems. Clearstream and Euroclear will hold interests on behalf of their participants through customers securities accounts in Clearstream s and Euroclear s names on the books of their United States depositaries, which in turn will hold such interests in customers securities accounts in the United States depositaries names on the books of DTC.

We have obtained the information in this section concerning DTC, Clearstream and Euroclear and the book-entry system and procedures from sources that we believe to be reliable, but we take no responsibility for the accuracy of this information.

We understand that:

DTC is a limited-purpose trust company organized under the New York Banking Law, a banking organization within the meaning of the New York Banking Law, a member of the Federal Reserve System, a clearing corporation within the meaning of the New York Uniform Commercial Code and a clearing agency registered under Section 17A of the Exchange Act.

DTC holds securities that its participants deposit with DTC and facilitates the settlement among participants of securities transactions, such as transfers and pledges, in deposited securities through electronic computerized book-entry changes in participants accounts, thereby eliminating the need for physical movement of securities certificates.

Direct participants of DTC include both U.S. and non-U.S. securities brokers and dealers, banks, trust companies, clearing corporations and other organizations, including Clearstream and Euroclear.

DTC is a wholly owned subsidiary of The Depository Trust & Clearing Corporation (DTCC). DTCC is the holding company for DTC, National Securities Clearing Corporation and Fixed Income Clearing Corporation, all of which are registered clearing agencies. DTCC is owned by the users of its regulated subsidiaries.

Access to the DTC system is also available to others such as securities brokers and dealers, banks and trust companies that clear through or maintain a custodial relationship with a direct participant, either directly or indirectly.

The rules applicable to DTC and its direct and indirect participants are on file with the SEC.
We understand that Clearstream is incorporated under the laws of Luxembourg as a professional depositary. Clearstream holds securities for its participating organizations and facilitates the clearance and settlement of securities transactions between its participants through electronic book-entry changes in accounts of its participants, thereby eliminating the need for physical movement of certificates. Clearstream provides to its participants, among other things, services for safekeeping, administration, clearance and settlement of internationally traded securities and securities lending and borrowing. Clearstream interfaces with domestic markets in several countries. As a registered bank, Clearstream is subject to regulation by the Luxembourg Commission for the Supervision of the Financial Section. Clearstream customers are recognized financial institutions around the world, including underwriters, securities brokers and dealers, banks, trust companies, clearing corporations and other organizations and may include the underwriters. Indirect access to Clearstream is also available to others, such as banks, brokers, dealers and trust companies that clear through or maintain a custodial relationship with a Clearstream customer either directly or indirectly.

We understand that Euroclear was created in 1968 to hold securities for participants of Euroclear and to clear and settle transactions between Euroclear participants through simultaneous electronic book-entry delivery against payment, thereby eliminating the need for physical movement of certificates and any risk from lack of simultaneous transfers of securities and cash. Euroclear provides various other services, including securities lending and borrowing and interfaces with domestic markets in several countries. Euroclear is operated by Euroclear Bank S.A./N.V., which we refer to as the Euroclear Operator, under contract with Euroclear Clearance Systems S.C., a Belgian cooperative corporation, which we refer to as the Cooperative . All operations are conducted by the Euroclear Operator, and all Euroclear securities clearance accounts and Euroclear cash accounts are accounts with the Euroclear Operator, not the Cooperative. Euroclear participants include banks (including central banks), securities brokers and dealers, and other professional financial intermediaries and may include the underwriters. Indirect access to Euroclear is also available to other firms that clear through or maintain a custodial relationship with a Euroclear participant, either directly or indirectly. Securities clearance accounts and cash accounts with the Euroclear Operator are governed by the Terms and Conditions Governing Use of Euroclear and the related operating procedures of Euroclear, and applicable Belgian

law (collectively, the Terms and Conditions). The Terms and Conditions govern transfers of securities and cash within Euroclear, withdrawals of securities and cash from Euroclear, and receipts of payments with respect to securities in Euroclear. All securities in Euroclear are held on a fungible basis without attribution of specific certificates to specific securities clearance accounts. The Euroclear Operator acts under the Terms and Conditions only on behalf of Euroclear participants, and has no records of or relationship with persons holding through Euroclear participants. Distributions with respect to the notes held beneficially through Euroclear will be credited to the cash accounts of Euroclear participants in accordance with the Terms and Conditions.

We understand that the Euroclear Operator is licensed by the Belgian Banking and Finance Commission to carry out banking activities on a global basis. As a Belgian bank, it is regulated and examined by the Belgian Banking and Finance Commission.

Purchases of notes under the DTC system must be made by or through direct participants, which will receive a credit for the notes in DTC s records. The ownership interest of each actual purchaser of notes is in turn to be recorded on the direct and indirect participants records. Beneficial owners of the notes will not receive written confirmation from DTC of their purchase, but beneficial owners are expected to receive written confirmations providing details of the transaction, as well as periodic statements of their holdings, from the direct or indirect participant through which the beneficial owner entered into the transaction. Transfers of ownership interests in the notes are to be accomplished by entries made on the books of direct and indirect participants acting on behalf of beneficial owners. Beneficial owners will not receive certificates representing their ownership interests in the notes, except in the event that use of the book-entry system for the notes is discontinued.

To facilitate subsequent transfers, all notes deposited by direct participants with DTC are registered in the name of DTC s partnership nominee, Cede & Co., or such other name as may be requested by an authorized representative of DTC. The deposit of notes with DTC and their registration in the name of Cede & Co. or such other nominee do not effect any change in beneficial ownership. DTC has no knowledge of the actual beneficial owners of the notes; DTC s records reflect only the identity of the direct participants to whose accounts such notes are credited, which may or may not be the beneficial owners. The direct and indirect participants will remain responsible for keeping account of their holdings on behalf of their customers.

Conveyance of notices and other communications by DTC to direct participants, by direct participants to indirect participants, and by direct participants and indirect participants to beneficial owners will be governed by arrangements among them, subject to any statutory or regulatory requirements as may be in effect from time to time. The laws of some jurisdictions may require that certain persons take physical delivery in definitive form of securities which they own. Consequently, those persons may be prohibited from purchasing beneficial interests in the global notes from any beneficial owner or otherwise.

Redemption notices shall be sent to DTC. If less than all of the notes within an issue are being redeemed, DTC s practice is to determine by lot the amount of the interest of each direct participant in such issue to be redeemed.

So long as DTC s nominee is the registered owner of the global notes, such nominee for all purposes will be considered the sole owner or holder of the notes for all purposes under the indenture. Except as provided below, beneficial owners will not be entitled to have any of the notes registered in their names, will not receive or be entitled to receive physical delivery of the notes in definitive form and will not be considered the owners or holders thereof under the indenture.

Neither DTC nor Cede & Co. (nor such other DTC nominee) will consent or vote with respect to the notes. Under its usual procedures, DTC mails an omnibus proxy to the issuer as soon as possible after the record date. The omnibus proxy assigns Cede & Co. s consenting or voting rights to those direct participants to whose accounts the notes are credited on the record date (identified in a listing attached to the omnibus proxy).

All payments on the global notes will be made to Cede & Co., or such other nominee as may be requested by an authorized representative of DTC. DTC s practice is to credit direct participants accounts upon DTC s receipt of funds and corresponding detail information from trustees or issuers on payment dates in accordance with their respective holdings shown on DTC s records. Payments by participants to beneficial owners will be governed by standing instructions and customary practices, as is the case with securities held for the accounts of customers in bearer form or

registered in street name, and will be the responsibility of such participant and not of DTC, the Trustee or us, subject to any statutory or regulatory requirements as may be in effect from time to time. Payment of principal and interest to Cede & Co. (or such other nominee as may be requested by an

authorized representative of DTC) shall be the responsibility of the Trustee or us, disbursement of such payments to direct participants shall be the responsibility of DTC, and disbursement of such payments to the beneficial owners shall be the responsibility of direct and indirect participants.

DTC may discontinue providing its service as securities depositary with respect to the notes at any time by giving reasonable notice to us or the Trustee. In addition, we may decide to discontinue use of the system of book-entry transfers through DTC (or a successor securities depositary). In the event that a successor securities depositary is not obtained under the above circumstances, or, alternatively, if an event of default with respect to the notes has occurred and is outstanding, note certificates in fully registered form are required to be printed and delivered to beneficial owners of the global notes representing such notes.

Distributions on the notes held beneficially through Clearstream will be credited to cash accounts of its customers in accordance with its rules and procedures, to the extent received by the United States depositary for Clearstream.

Distributions on the notes held beneficially through Euroclear will be credited to the cash accounts of its participants in accordance with the Terms and Conditions, to the extent received by the United States depositary for Euroclear.

Although we expect that DTC, Clearstream and Euroclear will agree to the foregoing procedures in order to facilitate transfers of interests in each global note among participants of DTC, Clearstream and Euroclear, DTC, Clearstream and Euroclear are under no obligation to perform or continue to perform such procedures, and such procedures may be discontinued at any time.

We have provided the descriptions of the operations and procedures of DTC, Clearstream and Euroclear in this prospectus supplement solely as a matter of convenience, and we make no representation or warranty of any kind with respect to these operations and procedures. These operations and procedures are solely within the control of those organizations and are subject to change by them from time to time. None of us, the underwriters or the trustee takes any responsibility for these operations or procedures, and you are urged to contact DTC, Clearstream and Euroclear or their participants directly to discuss these matters.

Clearance and Settlement Procedures

Initial settlement for the notes will be made in immediately available funds. Secondary market trading between DTC participants will occur in the ordinary way in accordance with DTC rules and will be settled in immediately available funds. Secondary market trading between Clearstream customers and/or Euroclear participants will occur in the ordinary way in accordance with the applicable rules and operating procedures of Clearstream and Euroclear, as applicable, and will be settled using the procedures applicable to conventional Eurobonds in immediately available funds.

Cross-market transfers between persons holding directly or indirectly through DTC, on the one hand, and directly or indirectly through Clearstream customers or Euroclear participants, on the other, will be effected through DTC in accordance with DTC rules on behalf of the relevant European international clearing system by the United States depositary. Such cross-market transactions, however, will require delivery of instructions to the relevant European international clearing system by the counterparty in such system in accordance with its rules and procedures and within its established deadlines (European time). The relevant European international clearing system will, if the transaction meets its settlement requirements, deliver instructions to the United States depositary to take action to effect final settlement on its behalf by delivering or receiving the notes in DTC, and making or receiving payment in accordance with normal procedures for same-day funds settlement applicable to DTC. Clearstream customers and Euroclear participants may not deliver instructions directly to their United States depositaries.

Because of time-zone differences, credits of the notes received in Clearstream or Euroclear as a result of a transaction with a DTC participant will be made during subsequent securities settlement processing and dated the business day following the DTC settlement date. Such credits or any transactions in the notes settled during such processing will be reported to the relevant Clearstream customers or Euroclear participants on such business day. Cash received in Clearstream or Euroclear as a result of sales of the notes by or through a Clearstream customer or a Euroclear participant to a DTC participant will be received with value on the DTC settlement date but will be available in the relevant Clearstream or Euroclear cash account only as of the business day following settlement in DTC.

Although DTC, Clearstream and Euroclear have agreed to the foregoing procedures to facilitate transfers of the notes among participants of DTC, Clearstream and Euroclear, they are under no obligation to perform or continue to perform such procedures and such procedures may be changed or discontinued at any time.

Certificated Notes

If the depositary at any time notifies us that it is unwilling or unable to continue as a depositary, or if the depositary becomes ineligible to serve, and we do not appoint a successor depositary within 90 days, we will issue notes in definitive form in exchange for the global notes. In addition, we may at any time and in our sole discretion determine not to have any series of notes represented by one or more global notes and, in such event, we will issue notes of that series in definitive form in exchange for the global note or notes. In any such instance, if we issue registered notes in exchange for global notes, we will register the definitive notes in such names and in such denominations authorized under the indenture as the depositary, pursuant to instructions from its direct or indirect participants or otherwise, instructs the trustee. The trustee will deliver the registered definitive notes to or on the order of the persons in whose names they are registered.

Governing Law

The indenture and the notes will be governed by, and construed and enforced in accordance with, the laws of the State of Illinois applicable to agreements made or instruments entered into and, in each case, performed in said state.

Relationship with Trustee

The Bank of New York Mellon Trust Company, N.A. currently serves as the trustee with respect to certain of our other outstanding debt securities.

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MATERIAL UNITED STATES FEDERAL INCOME TAX CONSEQUENCES

The following discussion summarizes certain of the United States federal income tax consequences of the purchase, ownership and disposition of the notes. This summary:

- is based on the Internal Revenue Code of 1986, as amended (the Code), United States Treasury Regulations issued under the Code, judicial decisions and administrative pronouncements in effect as of the date of this prospectus supplement, all of which are subject to different interpretation or to change. Any such change may be applied retroactively and may adversely affect the federal income tax consequences described herein;

- addresses only tax consequences to investors that purchase the notes at their issue price, which will equal the first price to the public (not including bond houses, brokers or similar persons or organizations acting in the capacity of underwriters, placement agents or wholesalers) at which a substantial amount of the notes are sold for money, and hold the notes as capital assets within the meaning of Section 1221 of the Code (that is, for investment purposes);

- does not discuss all of the tax consequences that may be relevant to particular investors in light of their particular circumstances, including, but not limited to, the alternative minimum tax;

- does not discuss all of the tax consequences that may be relevant to investors that are subject to special treatment under the United States federal income tax laws (including, without limitation, insurance companies, financial institutions, tax-exempt organizations, Subchapter S Corporations, personal holding companies, trusts, estates, government agencies and instrumentalities, retirement plans, regulated investment companies, dealers in securities or currencies, holders whose functional currency for tax purposes is not the United States dollar, passive foreign investment companies, controlled foreign corporations, persons holding the notes as part of a hedge, straddle, constructive sale, conversion or other integrated transaction, former United States citizens or long-term residents subject to taxation as expatriates under Section 877 of the Code, part year non-resident aliens or traders in securities that have elected to use a mark-to-market method of accounting for their securities holdings);

- does not discuss the effect of other United States federal tax laws (such as estate and gift tax laws) except to the limited extent specifically indicated below, and does not discuss any state, local or foreign tax laws or tax treaties; and

- does not discuss the tax consequences to a person holding notes through a partnership (or other entity or arrangement classified as a partnership for United States federal income tax purposes), except to the limited extent specifically indicated below.

We have not sought and will not seek a ruling from the Internal Revenue Service (the IRS) with respect to any matters discussed in this section, and we cannot assure you that the IRS will not take a different position concerning the tax consequences of the purchase, ownership or disposition of the notes, or that any such position would not be sustained.

If a partnership (or other entity or arrangement classified as a partnership for United States federal income tax purposes) holds the notes, the tax treatment of a partner in the partnership generally will depend on the status of the partner and the activities of the partnership. If you are a partnership or a partner in a partnership (or other entity or arrangement classified as a partnership for United States federal income tax purposes) holding notes, you should consult your tax advisor regarding the tax consequences of the purchase, ownership or disposition of the notes.

Prospective investors should consult their own tax advisors with regard to the application of the tax consequences discussed below to their particular situation and the application of any other United States federal as well as state or local or foreign tax laws and tax treaties, including gift and estate tax laws.

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Certain United States Federal Income Tax Consequences To U.S. Holders

The following is a summary of certain United States federal income tax consequences of the purchase, ownership and disposition of the notes by a holder that is a U.S. Holder. For purposes of this summary, U.S. Holder means a beneficial owner of a note or notes that is for United States federal income tax purposes:

- an individual citizen or resident of the United States, including an alien individual who is a lawful permanent resident of the United States or who meets the substantial presence test under Section 7701(b)(3) of the Code;
- a corporation (or other entity taxable as a corporation for United States federal income tax purposes) created or organized in or under the laws of the United States (or any state thereof or the District of Columbia);
- an estate whose income is subject to United States federal income taxation regardless of its source; or
- a trust if (i) a court within the United States is able to exercise primary supervision over its administration and one or more United States persons (within the meaning of the Code) have the authority to control all of its substantial decisions, or (ii) such trust has a valid election in effect under applicable United States Treasury Regulations to be treated as a United States person.

Under the substantial presence test referred to above, an individual may, subject to certain exceptions, be deemed to be a resident of the United States by reason of being present in the United States for at least 31 days in the calendar year and for an aggregate of at least 183 days during a three-year period ending on the last day of the current calendar year (counting for such purposes all of the days present in the current year, one-third of the days present in the immediately preceding year and one-sixth of the days present in the second preceding year).

Treatment of Interest

General

Except as described below regarding original issue discount, stated interest on the notes will be taxable to a U.S. Holder as ordinary income as the interest is paid or accrues in accordance with the U.S. Holder s method of tax accounting.

If a portion of the price paid for a note will be allocable to interest that accrued prior to the date the note is purchased (pre-issuance accrued interest), we intend to take the position that, on the first interest payment date, a portion of the interest received in an amount equal to the pre-issuance accrued interest will be treated as a return of the pre-issuance accrued interest and not as a payment of interest on the note. Amounts treated as a return of pre-issuance accrued interest should not be taxable when received but should reduce the U.S. Holder s adjusted tax basis in the note by a corresponding amount.

Original Issue Discount

If the notes are issued with original issue discount (OID) for U.S. federal income tax purposes, special tax accounting rules apply. Under these rules, a U.S. Holder of notes may be required to recognize income in a taxable year in excess of the amount of cash received on the notes during such taxable year. In general, the notes will be treated as issued with OID if the issue price of the notes is less than their stated redemption price at maturity. If the amount of such OID is de minimis (i.e., less than 0.25% of the stated redemption price at maturity multiplied by the number of complete years from issuance to maturity), the special tax accounting rules applicable to OID will not apply. Regardless of the regular method of accounting used by a U.S. Holder for U.S federal income tax purposes, OID (other than de minimis amounts) generally must be accrued into gross income on a constant yield basis, in advance of the receipt of some or all of the cash attributable to such OID.

The issue price of debt securities is the initial offering price to the public at which a substantial amount of the debt securities is sold for cash (ignoring sales to bond houses, brokers or similar persons or organizations

acting in the capacity of underwriters, placement agents or wholesalers). The stated redemption price at maturity of debt securities is the sum of all payments to be made on the debt securities other than qualified stated interest payments. A qualified stated interest payment is stated interest that is unconditionally payable at least annually at a single fixed rate (appropriately taking into account the length of the interval between payments).

The notes are not expected to be issued with OID except that there may be a discount that constitutes a *de minimis* amount of OID. A U.S. Holder of notes with *de minimis* OID is generally required to include such amount in income (as capital gain), on a pro rata basis, as principal payments are made on the notes unless the U.S. Holder elects to apply the constant yield method. The rest of the disclosure assumes that the notes should not be considered to have OID.

Treatment of Dispositions of Notes

Upon the sale, exchange, retirement or other taxable disposition (collectively, a disposition) of a note, a U.S. Holder generally will recognize gain or loss equal to the difference, if any, between the amount received on such disposition (other than amounts received in respect of accrued and unpaid interest, which will generally be taxable to that U.S. Holder as ordinary interest income at that time if not previously included in the U.S. Holder s income) and the U.S. Holder s adjusted tax basis in the note. A U.S. Holder s adjusted tax basis in a note will be, in general, the cost of the note to the U.S. Holder. Gain or loss realized on the disposition of a note generally will be capital gain or loss, and will be long-term capital gain or loss if, at the time of such disposition, the note has been held for more than one year. Otherwise, such gain or loss generally will be short-term capital gain or loss, the deductibility of which is subject to limitations. Net long-term capital gain recognized by a non-corporate U.S. Holder generally is eligible for reduced rates of United States federal income taxation. The deductibility of capital losses is subject to limitations.

If a U.S. Holder disposes of a note between interest payment dates, a portion of the amount received by the U.S. Holder will reflect interest that has accrued on the note but has not been paid as of the disposition date. That portion is treated as ordinary interest income and not as sale proceeds.

Additional Tax on Net Investment Income

Certain U.S. Holders that are individuals, estates or trusts may be required to pay an additional 3.8% Medicare contribution tax on certain net investment income, which may include interest income on, and net gain from, the disposition of a note. In the case of an U.S. Holder that is an individual, the tax will be imposed on the lesser of (1) the such individual s net investment income and (2) the amount by which the individual s modified adjusted gross income exceeds $250,000 (if the individual is married and filing jointly or a surviving spouse), $125,000 (if the individual is married and filing separately) or $200,000 (in any other case). In the case of a estate or trust, the tax will be imposed on the lesser of (1) undistributed net investment income and (2) the excess adjusted gross income over the dollar amount at which the highest income tax bracket applicable to an estate or trust begins. U.S. Holders should consult their tax advisors regarding the effect, if any, of such additional tax on an investment in the notes based upon their particular circumstances.

Certain United States Federal Income and Estate Tax Consequences to Non-U.S. Holders

The following is a summary of the United States federal income and estate tax consequences of the purchase, ownership and disposition of the notes by a holder that is a Non-U.S. Holder. For purposes of this summary, Non-U.S. Holder means a beneficial owner of a note or notes, that is for United States federal income tax purposes, an individual, corporation, estate or trust (other than a trust that is treated as a flow-through entity for United States federal income tax purposes), who is not a U.S. Holder.

Special rules may apply to Non-U.S. Holders that are subject to special treatment under the Code, including controlled foreign corporations and passive foreign investment companies. Such Non-U.S. Holders should

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consult their own tax advisors to determine the United States federal, state, local, Non-United States, tax treaty and other tax consequences that may be relevant to them.

Treatment of Interest

Subject to the discussions below concerning backup withholding and FATCA (as defined below), a Non-U.S. Holder will not be subject to United States federal income or withholding tax in respect of interest income on the notes if the interest income qualifies for the portfolio interest exception. Generally, interest income will qualify for the portfolio interest exception if each of the following requirements is satisfied:

- the interest is not effectively connected with the conduct of a trade or business by the Non-U.S. Holder in the United States;
- the Non-U.S. Holder appropriately certifies its status as a non-United States person (as described below);
- the Non-U.S. Holder does not actually or constructively own 10% or more of the total combined voting power of our stock entitled to vote;
- the Non-U.S. Holder is not a controlled foreign corporation that is actually or constructively related to us through stock ownership; and
- the Non-U.S. Holder is not a bank which acquired the notes in consideration for an extension of credit made pursuant to a loan agreement entered into in the ordinary course of business.

The certification requirement referred to above generally will be satisfied if the Non-U.S. Holder timely provides us or our paying agent with a statement on IRS Form W-8BEN (or suitable substitute or successor form), together with all appropriate attachments, signed under penalties of perjury, identifying the Non-U.S. Holder and stating, among other things, that the Non-U.S. Holder is not a United States person (within the meaning of the Code). If the Non-U.S. Holder holds its notes through a financial institution or other agent acting on the holder s behalf, the Non-U.S. Holder will be required to provide appropriate documentation to that agent, and that agent will then be required to provide appropriate documentation to us or our paying agent (either directly or through other intermediaries). A non-U.S. Holder may be required to obtain a U.S. taxpayer identification number under certain circumstances. We may be required to report annually to the IRS and to each Non-U.S. Holder the amount of interest paid to, and the tax withheld, if any, with respect to each Non-U.S. Holder. Prospective Non-U.S. Holders should consult their tax advisors regarding this certification requirement, and alternative methods under applicable U.S. Treasury regulations for satisfying the certification requirement.

If the requirements of the portfolio interest exception are not satisfied with respect to a Non-U.S. Holder, payments of interest to that Non-U.S. Holder will be subject to a 30% United States federal withholding tax, unless another exemption or a reduced withholding rate applies. For example, an applicable income tax treaty may reduce or eliminate such tax, in which event a Non-U.S. Holder claiming the benefit of such treaty must provide the withholding agent with a properly executed IRS Form W-8BEN (or suitable substitute or successor form) claiming the benefit of the applicable tax treaty. Alternatively, an exemption applies to the 30% United States withholding tax if the interest

is effectively connected with the Non-U.S. Holder s conduct of a trade or business in the United States (and, if certain tax treaties apply, is attributable to a permanent establishment or a fixed base maintained by the Non-U.S. Holder within the United States) and the Non-U.S. Holder provides an appropriate statement to that effect on a properly executed IRS Form W-8ECI (or suitable substitute or successor form). These forms may be required to be periodically updated. In the latter case, such Non-U.S. Holder generally will be subject to United States federal income tax with respect to all income from the notes in the same manner as U.S. Holders, as described above, unless an applicable income tax treaty provides otherwise. In addition, such a Non-U.S. Holder that is classified as a corporation for United States federal income tax purposes may be subject to a branch profits tax with respect to any such United States trade or business income at a rate of 30% (or at a reduced rate under an applicable income tax treaty).

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Treatment of Dispositions of Notes

Subject to the discussions below concerning backup withholding and FATCA, a Non-U.S. Holder generally will not be subject to United States federal income tax or withholding tax on gain realized upon the disposition of a note unless:

- the Non-U.S. Holder is an individual present in the United States for 183 days or more in the taxable year of the disposition and certain other conditions are met (certain tax treaties may provide otherwise); or
- the gain is effectively connected with the Non-U.S. Holder s conduct of a trade or business in the United States (or, if certain tax treaties apply, is attributable to a permanent establishment maintained by the Non-U.S. Holder within the United States).

If the first exception applies, the Non-U.S. Holder generally will be subject to United States federal income tax at a rate of 30% (or at a reduced rate under an applicable income tax treaty) on the amount by which capital gains allocable to United States sources (including gains from the sale, exchange, retirement or other disposition of the notes) exceed capital losses allocable to United States sources in the taxable year of disposition. If the second exception applies, the Non-U.S. Holder generally will be subject to United States federal income tax with respect to such gain in the same manner as U.S. Holders, as described above, unless an applicable income tax treaty provides otherwise. Additionally, Non-U.S. Holders that are classified as corporations for United States federal income tax purposes could be subject to a branch profits tax with respect to such gain at a rate of 30% (or at a reduced rate under an applicable income tax treaty).

Treatment of Notes for United States Federal Estate Tax Purposes

A note held, or beneficially held, by an individual who is not a citizen or resident of the United States at the time of his or her death will not be includable in the individual s gross estate for United States federal estate tax purposes, provided that (i) the Non-U.S. Holder does not at the time of death actually or constructively own 10% or more of the combined voting power of all classes of our stock entitled to vote and (ii) at the time of death, payments with respect to such note would not have been effectively connected with the conduct by such holder of a trade or business in the United States. In addition, under the terms of an applicable estate tax treaty, United States federal estate tax may not apply with respect to a note.

United States Information Reporting Requirements and Backup Withholding Tax

U.S. Holders

We, or if a U.S. Holder holds notes through a broker or other securities intermediary, the intermediary, may be required to file information returns with respect to payments made to the U.S. Holder of interest, and, in some cases, disposition proceeds on the notes.

In addition, U.S. Holders may be subject to backup withholding at a current rate of 28% on those payments if they do not provide their taxpayer identification numbers in the manner required, fail to certify that they are not subject to backup withholding, fail to properly report in full their dividend and interest income, or otherwise fail to comply with the applicable requirements of backup withholding rules. Backup withholding is not an additional tax. Any amounts withheld under the backup withholding rules will be allowed as a credit against the U.S. Holder s United States federal

income tax liability or may entitle a U.S. Holder to a refund provided the required information is timely furnished to the IRS. Prospective U.S. Holders should consult their tax advisors concerning the application of information reporting and backup withholding rules.

Non-U.S. Holders

The rules concerning information reporting and backup withholding applicable to Non-U.S. Holders are as follows:

Interest payments received by a Non-U.S. Holder will be exempt from the usual backup withholding rules (see above) if such payments are subject to the 30% withholding tax on interest or if they are exempt from that tax by application of a tax treaty or the portfolio interest exception, where the Non-U.S. Holder satisfies the certification requirements described under Certain United States Federal Tax Consequences to Non-U.S. Holders Treatment of Interest above. The exemption does not apply if the withholding agent or an intermediary knows or has reason to know that the Non-U.S. Holder should be subject to the usual information reporting or backup withholding rules. In the event backup withholding applies to a Non-U.S. Holder, the amount of any backup withholding from a payment will be allowed as a credit against the Non-U.S. Holder s United States federal income tax liability and may entitle the Non-U.S. Holder to a refund provided the required information is timely furnished to the IRS. In addition, information reporting may still apply to payments of interest (on Form 1042-S) even if certification is provided and the interest is exempt from the 30% withholding tax. Copies of information returns reporting such interest payments and any withholding may also be made available to the tax authorities in the country in which the Non-U.S. Holder resides pursuant to a treaty or broad information exchange agreement; and

Sale proceeds received by a Non-U.S. Holder on a sale of notes through a broker may be subject to information reporting and/or backup withholding if the Non-U.S. Holder is not eligible for an exemption or does not provide the certification described under Certain United States Federal Tax Consequences to Non-U.S. Holders Treatment of Interest above. In particular, information reporting and backup withholding may apply if the Non-U.S. Holder uses the United States office of a broker, and information reporting (but generally not backup withholding) may apply if a Non-U.S. Holder uses the foreign office of a broker that has certain connections to the United States.

Prospective Non-U.S. Holders should consult their tax advisors concerning the application of information reporting and backup withholding rules.

FATCA Legislation

Sections 1471-1474 of the Code, U.S. Treasury regulations promulgated thereunder and official IRS guidance (FATCA), enacted as part of the Hiring Incentives to Restore Employment Act of 2010, generally imposes a U.S. federal withholding tax of 30% on certain payments of income made after June 30, 2014 and certain payments of gross proceeds made after December 31, 2016 to a foreign financial institution (as defined for this purpose under FATCA) unless the institution enters into an agreement with the U.S. tax authorities (or is subject to an applicable intergovernmental agreement) to withhold on certain payments and to collect and provide to the U.S. tax authorities (or local revenue authorities if required under an applicable intergovernmental agreement) substantial information regarding U.S. account holders of the institution and its affiliates (including certain account holders that are foreign entities with U.S. owners). FATCA also imposes a 30% withholding tax on certain payments of income made after June 30, 2014 and certain payments of gross proceeds made after December 31, 2016 to a non-financial foreign entity unless the entity timely provides the withholding agent with a certification that it does not have any substantial U.S. owners or a certification identifying its direct and indirect substantial U.S. owners as defined under FATCA and in either case, complies with certain other requirements including where such institution or entity is acting as an intermediary. The FATCA tax described above will not apply if the foreign financial institution or non-financial

foreign entity otherwise qualifies for an exemption and properly and timely certifies its exempt status to a withholding agent.

Under applicable United States Treasury Regulations, no FATCA withholding taxes will apply to payments made on, or gross proceeds from sales or other dispositions of, debt instruments that are issued on or before June 30, 2014 (unless the debt instruments are significantly modified (within the meaning of U.S. Treasury

regulation Section 1.1001-3) after that date). Accordingly, absent a material modification of the terms of the notes after June 30, 2014, we do not anticipate that payments of interest or gross proceeds from the redemption, retirement, sale or other disposition of a note will be subject to FATCA. Prospective Holders should consult with their tax advisors regarding FATCA as it applies to their investment in the notes.

Foreign financial institutions and non-financial foreign entities located in jurisdictions that have an intergovernmental agreement with the United States governing FATCA, may be subject to different rules. Application of this FATCA tax does not depend on whether the payment otherwise would be exempt from U.S. federal withholding tax under the other exemptions described above.

THE UNITED STATES FEDERAL INCOME AND ESTATE TAX DISCUSSION SET FORTH ABOVE IS INCLUDED FOR GENERAL INFORMATION ONLY, IS NOT TAX ADVICE AND MAY NOT BE APPLICABLE DEPENDING UPON A HOLDER S PARTICULAR SITUATION. HOLDERS SHOULD CONSULT THEIR TAX ADVISORS REGARDING THE TAX CONSEQUENCES TO THEM OF THE PURCHASE, OWNERSHIP AND DISPOSITION OF THE NOTES, INCLUDING THE TAX CONSEQUENCES UNDER UNITED STATES FEDERAL NON-INCOME, STATE, LOCAL, FOREIGN AND OTHER TAX LAWS AND TAX TREATIES (AND ANY PROPOSED CHANGES IN APPLICABLE LAW).

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UNDERWRITING

We intend to offer the notes through the underwriters. Subject to the terms and conditions described in an underwriting agreement among us and Citigroup Global Markets Inc., Goldman, Sachs & Co., J.P. Morgan Securities LLC and Merrill Lynch, Pierce, Fenner & Smith Incorporated, as representatives of the underwriters, we have agreed to sell to the underwriters, and the underwriters severally have agreed to purchase from us, the principal amounts of the notes listed opposite their names below.

Underwriter	Principal Amount of 2017 Notes	Principal Amount of 2019 Notes	Principal Amount of 2024 Notes
Citigroup Global Markets Inc.	$ 120,250,000	$ 120,250,000	$ 129,500,000
Goldman, Sachs & Co.	$ 120,250,000	$ 120,250,000	$ 129,500,000
J.P. Morgan Securities LLC	$ 120,250,000	$ 120,250,000	$ 129,500,000
Merrill Lynch, Pierce, Fenner & Smith Incorporated	$ 120,250,000	$ 120,250,000	$ 129,500,000
HSBC Securities (USA) Inc.	$ 26,000,000	$ 26,000,000	$ 28,000,000
Mizuho Securities USA Inc.	$ 26,000,000	$ 26,000,000	$ 28,000,000
SG Americas Securities, LLC	$ 26,000,000	$ 26,000,000	$ 28,000,000
Wells Fargo Securities, LLC	$ 26,000,000	$ 26,000,000	$ 28,000,000
Banca IMI S.p.A.	$ 6,500,000	$ 6,500,000	$ 7,000,000
Barclays Capital Inc.	$ 6,500,000	$ 6,500,000	$ 7,000,000
BBVA Securities Inc.	$ 6,500,000	$ 6,500,000	$ 7,000,000
BMO Capital Markets Corp.	$ 6,500,000	$ 6,500,000	$ 7,000,000
Commerz Markets LLC	$ 6,500,000	$ 6,500,000	$ 7,000,000
Danske Markets Inc.	$ 6,500,000	$ 6,500,000	$ 7,000,000
ING Financial Markets LLC	$ 6,500,000	$ 6,500,000	$ 7,000,000
Loop Capital Markets LLC	$ 6,500,000	$ 6,500,000	$ 7,000,000
nabSecurities, LLC	$ 6,500,000	$ 6,500,000	$ 7,000,000
U.S. Bancorp Investments, Inc.	$ 6,500,000	$ 6,500,000	$ 7,000,000
Total	$ 650,000,000	$ 650,000,000	$ 700,000,000

The underwriters have agreed to purchase all of the notes sold under the underwriting agreement if any of these notes are purchased. If an underwriter defaults, the underwriting agreement provides that the purchase commitments of the non-defaulting underwriters may be increased or the underwriting agreement may be terminated. The offering of the notes by the underwriters is subject to receipt and acceptance and subject to the underwriters right to reject any order in whole or in part.

We have agreed to indemnify the several underwriters against certain liabilities, including liabilities under the Securities Act or to contribute to payments the underwriters may be required to make in respect of those liabilities.

The underwriters are offering the notes, subject to prior sale, when, as and if issued to and accepted by them, subject to approval of legal matters by their counsel, including the validity of the notes, and other conditions contained in the

underwriting agreement, such as the receipt by the underwriters of officer s certificates and legal opinions. The underwriters reserve the right to withdraw, cancel or modify offers to the public and to reject orders in whole or in part.

We expect to deliver the notes against payment for the notes on or about the date specified in the last paragraph of the cover page of this prospectus supplement, which will be the fifth business day following the date of the pricing of the notes. Under Rule 15c6-1 of the Exchange Act, trades in the secondary market generally are required to settle in three business days, unless the parties to a trade expressly agree otherwise. Accordingly, purchasers who wish to trade notes on the date of pricing or the next succeeding business day will be required, by

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virtue of the fact that the notes initially will settle in T+5, to specify alternative settlement arrangements to prevent a failed settlement.

Commissions and Discounts

The underwriters have advised us that they propose initially to offer the notes to the public at the public offering price on the cover page of this prospectus supplement, and to dealers at that price less a concession not in excess of 0.150% of the principal amount of the 2017 notes, 0.200% of the principal amount of the 2019 notes and 0.250% of the principal amount of the 2024 notes. The underwriters may allow, and the dealers may reallow, to other dealers a discount not in excess of 0.100% of the principal amount of the 2017 notes, 0.150% of the principal amount of the 2019 notes and 0.200% of the principal amount of the 2024 notes. After the initial public offering, the public offering price and other selling terms may be changed.

The expenses of the offering, not including the underwriting discount, are estimated at $2.4 million and are payable by us.

New Issue of Notes

The notes are a new issue of securities with no established trading market. We do not intend to apply for listing of the notes on any securities exchange or for quotation of the notes on any automated dealer quotation system. We have been advised by certain of the underwriters that they presently intend to make a market in the notes after completion of the offering. However, they are under no obligation to do so and may discontinue any market-making activities at any time without any notice. We cannot assure the liquidity of the trading markets for the notes or that active public markets for the notes will develop. If active public trading markets for the notes do not develop, the market price and liquidity of the notes may be adversely affected.

Stabilization and Short Positions

In connection with the offering, the underwriters are permitted to engage in transactions that stabilize the market price of the notes. Such transactions consist of bids or purchases to peg, fix or maintain the price of the notes. If the underwriters create a short position in the notes in connection with the offering (i.e., if they sell more notes than are on the cover page of this prospectus supplement), the underwriters may reduce that short position by purchasing notes in the open market. Purchases of a security to stabilize the price or to reduce a short position could cause the price of the security to be higher than it might be in the absence of such purchases. The underwriters also may impose a penalty bid. This occurs when a particular underwriter repays to the underwriters a portion of the underwriting discount received by it because the representatives have repurchased notes sold by or for the account of such underwriter in stabilizing or short covering transactions.

Neither we nor any of the underwriters makes any representation or prediction as to the direction or magnitude of any effect that the transactions described above may have on the price of the notes. In addition, neither we nor any of the underwriters makes any representation that the underwriters will engage in these transactions or that these transactions, once commenced, will not be discontinued without notice.

Other Relationships

Certain of the underwriters and their respective affiliates have, from time to time, performed, and may in the future perform, various financial advisory and commercial and investment banking services for us, for which they received or will receive customary fees and expenses. The underwriters or their affiliates may provide credit to us or our

affiliates as lenders from time to time, including under our existing credit facility. In particular, the underwriters or their affiliates may hold outstanding commercial paper issued by us, which may be repaid with a portion of the net proceeds received by us from the sale of the notes. See Use of Proceeds.

In addition, in the ordinary course of their business activities, the underwriters and their affiliates may make or hold a broad array of investments and actively trade debt and equity securities (or related derivative securities)

and financial instruments (including bank loans) for their own account and for the accounts of their customers. Such investments and securities activities may involve securities and/or instruments of ours or our affiliates. If any of the underwriters or their affiliates have a lending relationship with us, certain of those underwriters or their affiliates routinely hedge, and certain other of those underwriters may hedge their credit exposure to us consistent with their customary risk management practices. Typically, such underwriters and their affiliates would hedge such exposure by entering into transactions which consist of either the purchase of credit default swaps or the creation of short positions in our securities, including potentially the notes offered hereby. Any such credit default swaps or short positions could adversely affect future trading prices of the notes offered hereby. The underwriters and their affiliates may also make investment recommendations and/or publish or express independent research views in respect of such securities or financial instruments and may hold, or recommend to clients that they acquire, long and/or short positions in such securities and instruments.

Banca IMI S.p.A. is not a U.S. registered broker-dealer, and will not effect any offers or sales of any notes in the United States unless it is through one or more U.S. registered broker-dealers as permitted by the regulations of the Financial Industry Regulatory Authority, Inc.

Selling Restrictions

European Economic Area

This prospectus supplement and the accompanying prospectus are not a prospectus for the purposes of the Prospectus Directive (as defined below).

In relation to each Member State of the European Economic Area which has implemented the Prospectus Directive (each, a Relevant Member State), each underwriter has represented and agreed that with effect from and including the date on which the Prospectus Directive is implemented in that Relevant Member State (the Relevant Implementation Date) it has not made and will not make an offer of notes that are the subject of the offering contemplated by this prospectus supplement to the public in that Relevant Member State other than:

(a) to any legal entity which is a qualified investor as defined in the Prospectus Directive;

(b) to fewer than 100 or, if the Relevant Member State has implemented the relevant provision of the 2010 PD Amending Directive, 150, natural or legal persons (other than qualified investors as defined in the Prospectus Directive), as permitted under the Prospectus Directive, subject to obtaining the prior consent of the relevant Dealer or Dealers nominated by the Company for any such offer; or

(c) in any circumstances falling within Article 3(2) of the Prospectus Directive, provided that no such offer of bonds shall require the Company or any underwriter to publish a prospectus pursuant to Article 3 of the Prospectus Directive.

For the purposes of this provision, the expression an offer of notes to the public in relation to any notes in any Relevant Member State means the communication in any form and by any means of sufficient information on the terms of the offer and the notes to be offered so as to enable an investor to decide to purchase or subscribe the notes, as the same may be varied in that Member State by any measure implementing the Prospectus Directive in that Member State, the expression Prospectus Directive means Directive 2003/71/EC (and amendments thereto, including the 2010 PD Amending Directive, to the extent implemented in the Relevant Member State), and includes any relevant implementing measure in the Relevant Member State, and the expression 2010 PD Amending Directive means Directive 2010/73/EU.

United Kingdom

Each underwriter has represented and agreed that:

(a) it has only communicated or caused to be communicated and will only communicate or cause to be communicated an invitation or inducement to engage in investment activity (within the meaning of Section 21 of

the FSMA) received by it in connection with the issue or sale of the notes in circumstances in which Section 21(1) of the FSMA does not apply to us; and

(b) it has complied and will comply with all applicable provisions of the FSMA with respect to anything done by it in relation to the notes in, from or otherwise involving the United Kingdom.

Hong Kong

The notes may not be offered or sold in Hong Kong by means of any document other than (a) to professional investors as defined in the Securities and Futures Ordinance (Cap. 571, Laws of Hong Kong) and any rules made under that Ordinance; or (b) in other circumstances which do not result in the document being a prospectus as defined in the Companies Ordinance (Cap. 32, Laws of Hong Kong) of Hong Kong and no advertisement, invitation or document relating to the notes may be issued or may be in the possession of any person for the purpose of issue (in each case whether in Hong Kong or elsewhere) which is directed at, or the contents of which are likely to be accessed or read by, the public of Hong Kong (except if permitted to do so under the laws of Hong Kong) other than with respect to notes which are or are intended to be disposed of only to persons outside Hong Kong or only to professional investors as defined in the Securities and Futures Ordinance (Cap. 571, Laws of Hong Kong) and any rules made under that Ordinance.

Japan

The notes have not been and will not be registered under the Financial Instruments and Exchange Law of Japan and each underwriter has agreed that it will not offer or sell any notes, directly or indirectly, in Japan or to, or for the account or the benefit of, any resident of Japan (which term as used herein means any person resident in Japan, including any corporation or other entity organized under the laws of Japan), or to others for re-offering or resale, directly or indirectly, in Japan, or to or for the account or the benefit of, any resident of Japan, except pursuant to an exemption from the registration requirements of, and otherwise in compliance with, the Financial Instruments and Exchange Law and any other applicable laws, regulations and ministerial guidelines of Japan.

Singapore

This prospectus has not been registered as a prospectus under the Securities and Futures Act, Chapter 289 of Singapore (the SFA) by the Monetary Authority of Singapore, and the offer of the notes in Singapore is made primarily pursuant to the exemptions under Sections 274 and 275 of the SFA. Accordingly, the notes may not be offered or sold, or made the subject of an invitation for subscription or purchase, nor may this prospectus or any other document or material in connection with the offer or sale, or invitation for subscription or purchase of the notes be circulated or distributed, whether directly or indirectly, to any person in Singapore other than (i) to an institutional investor as defined in Section 4A of the SFA pursuant to Section 274 of the SFA, (ii) to an accredited investor as defined in Section 4A of the SFA or other relevant person as defined in Section 275(2) of the SFA, or to any person pursuant to an offer referred to in Section 275(1A) of the SFA, and in accordance with the conditions, specified in Section 275 of the SFA or (iii) otherwise pursuant to, and in accordance with the conditions of, any other applicable exemption or provision of the SFA.

Where the notes are subscribed or purchased under Section 275 by a relevant person which is: (a) a corporation (which is not an accredited investor) the sole business of which is to hold investments and the entire share capital of which is owned by one or more individuals, each of whom is an accredited investor; or (b) a trust (where the trustee is not an accredited investor) whose sole purpose is to hold investments and each beneficiary is an accredited investor, shares, debentures and units of shares and debentures of that corporation or the beneficiaries rights and interest in that

trust shall not be transferable for six months after that corporation or that trust has acquired the notes under Section 275 except: (1) to an institutional investor under Section 274 of the SFA or to a relevant person, or any person pursuant to Section 275(1A), and in accordance with the conditions, specified in Section 275 of the SFA; (2) where no consideration is given for the transfer; or (3) by operation of law.

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LEGAL MATTERS

Certain legal matters relating to the notes will be passed upon for us by Janet O. Love, Esq., Deputy General Counsel and Assistant Secretary, and Drinker Biddle & Reath LLP, Chicago, Illinois. Ms. Love is a participant in various of our employee benefit and incentive plans, including stock option plans, offered to employees. As of February 18, 2014, Ms. Love beneficially owns 4,597 shares of our common stock. Certain legal matters in connection with the securities offered hereby will be passed upon for the underwriters by Winston & Strawn LLP, Chicago, Illinois. Winston & Strawn LLP provides legal services to ITW and its subsidiaries from time to time.

EXPERTS

The financial statements incorporated in this prospectus supplement by reference from the Company s Annual Report on Form 10-K for the year ended December 31, 2013, and the effectiveness of Illinois Tool Works Inc. s internal controls over financial reporting have been audited by Deloitte & Touche LLP, an independent registered public accounting firm, as stated in their report, which is incorporated herein by reference. Such financial statements have been so incorporated in reliance upon the report of such firm given upon their authority as experts in accounting and auditing.

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PROSPECTUS

ILLINOIS TOOL WORKS INC.

Debt Securities

We may offer to sell from time to time debt securities. This prospectus provides you with a general description of the securities we may offer. We will provide you with the specific terms and the public offering prices of these securities in supplements to this prospectus. The prospectus supplements may also add, update or change information contained in this prospectus. You should read this prospectus and the applicable prospectus supplement, as well as the documents incorporated by reference in this prospectus and the applicable prospectus supplement, carefully before you invest.

The debt securities may be offered and sold to or through underwriters, dealers or agents as designated from time to time, or directly to one or more other purchasers or through a combination of such methods. See Plan of Distribution. If any underwriters, dealers or agents are involved in the sale of any of the securities, their names, and any applicable purchase price, fee, commission or discount arrangements between or among them, will be set forth, or will be calculable from the information set forth, in the applicable prospectus supplement.

This prospectus may not be used to offer and sell securities unless accompanied by a prospectus supplement.

You should carefully consider the risk factors included and incorporated by reference in this prospectus and the applicable prospectus supplement before you invest in our securities.

Neither the Securities and Exchange Commission nor any state securities commission has approved or determined if this prospectus is truthful or complete. Any representation to the contrary is a criminal offense.

The date of this prospectus is August 21, 2012.

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ABOUT THIS PROSPECTUS

This prospectus is part of a registration statement that we filed with the United States Securities and Exchange Commission, or the SEC, under a shelf registration process. Under this shelf registration process, we may sell debt securities under this prospectus in one or more offerings from time to time. This prospectus provides you with a general description of the debt securities we may offer. Each time we sell securities, we will provide a prospectus supplement containing specific information about the terms of that offering. The prospectus supplement may also add, update or change information contained in this prospectus, and accordingly, to the extent inconsistent, information in this prospectus is superseded by the information in the prospectus supplement. You should read both this prospectus and any prospectus supplement together with additional information described under the heading Where You Can Find More Information.

The prospectus supplement will describe: the terms of the debt securities offered, any initial public offering price, the price paid to us for the debt securities, the net proceeds to us, the manner of distribution and any underwriting compensation and the other specific material terms related to the offering of these securities. For more detail on the terms of the debt securities, you should read the exhibits filed with or incorporated by reference in our registration statement of which this prospectus forms a part.

In this prospectus we use the terms ITW, the Company, we, us, and our to refer to Illinois Tool Works Inc. and our consolidated subsidiaries. References to debt securities include any debt security that we might sell under this prospectus or any prospectus supplement. References to $ and dollars are to United States dollars.

This prospectus contains summaries of certain provisions contained in key documents described in this prospectus. All of the summaries are qualified in their entirety by the actual documents, which you should review before making your investment decision. Copies of the documents referred to herein have been filed, or will be filed or incorporated by reference as exhibits to the registration statement of which this prospectus is a part, and you may obtain copies of those documents as described below under Where You Can Find More Information.

Because we are a well-known seasoned issuer, as defined in Rule 405 of the Securities Act of 1933, as amended, or the Securities Act, we may add to this prospectus and offer additional securities by filing a prospectus supplement with the SEC at the time of the offer.

You should rely only on the information contained or incorporated by reference in this prospectus, in any accompanying prospectus supplement or in any free writing prospectus filed by us with the SEC. Neither we nor any underwriter has authorized anyone to provide you with different information. If anyone provides you with different or inconsistent information, you should not rely on it. We are not making an offer of these securities in any jurisdiction where the offer is not permitted. You should not assume that the information contained in or incorporated by reference in this prospectus, any prospectus supplement or any free writing prospectus is accurate as of any date other than their respective dates, regardless of the time of delivery of this prospectus or any sale of debt securities. Our business, financial condition, results of operations and prospects may have changed since those dates.

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WHERE YOU CAN FIND MORE INFORMATION

We file annual, quarterly and current reports, proxy statements and other information with the SEC. You may read and copy any reports, statements or other information we file with the SEC at the SEC s public reference room at 100 F Street, N.E., Washington, D.C. 20549. Please call the SEC at 1-800-SEC-0330 for further information on the public reference room. Our filings also are available to the public on the Internet, through a database maintained by the SEC at http://www.sec.gov. In addition, reports, proxy statements and other information concerning us may be inspected at the offices of the New York Stock Exchange, 20 Broad Street, New York, New York 10005.

We filed a registration statement on Form S-3 to register with the SEC the securities described in this prospectus. This prospectus is part of that registration statement. As permitted by SEC rules, this prospectus does not contain all the information contained in the registration statement or the exhibits to the registration statement. You may refer to the registration statement and accompanying exhibits for more information about us and our securities.

The SEC allows us to incorporate by reference into this document the information we file with the SEC. This means that we can disclose important information to you by referring you to other documents that we identify as part of this prospectus. The information incorporated by reference is considered to be part of this prospectus.

We incorporate by reference the documents listed below:

1. Annual Report on Form 10-K for the fiscal year ended December 31, 2011;

2. Quarterly Reports on Form 10-Q for the fiscal quarters ended March 31, 2012 and June 30, 2012; and

3. Current Reports on Form 8-K filed on January 13, 2012, February 7, 2012, February 13, 2012, February 23, 2012, April 6, 2012, May 10, 2012 and August 17, 2012 (other than documents or information deemed to have been furnished and not filed in accordance with SEC rules).

We also incorporate by reference any future filings we make with the SEC under Sections 13(a), 13(c), 14 or 15(d) of the Securities Exchange Act of 1934, as amended (the Exchange Act) (other than documents or information deemed to have been furnished and not filed in accordance with SEC rules), on or after the date of this prospectus until we have terminated the offering. Those documents will become a part of this prospectus from the date that the documents are filed with the SEC. Information that becomes a part of this prospectus after the date of this prospectus will automatically update and may replace information in this prospectus and information previously filed with the SEC.

You may request a copy of any of these documents from us without charge, excluding certain exhibits to the documents, by writing or telephoning us at the following address:

Maria C. Green, Secretary

Illinois Tool Works Inc.

3600 West Lake Avenue

Glenview, IL 60026

(847) 724-7500

Documents may also be available on our website at www.itw.com. We do not intend our website address to be an active link and information contained on our website does not constitute a part of this prospectus or any accompanying prospectus supplement (or any document incorporated by reference herein or therein), and you should not rely on that information in making your investment decision unless that information is also in this prospectus or has been expressly incorporated by reference into this prospectus.

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FORWARD-LOOKING STATEMENTS

This prospectus contains or incorporates by reference certain statements and information that are forward-looking statements within the meaning of Section 27A of the Securities Act and Section 21E of the Exchange Act. These statements may be identified by the use of words such as believe, expect, plans, intends, strategy, prospects, estimate, project, target, anticipate, guidance, forecast, and other sim without limitation, statements regarding the expected acquisition or disposition of businesses, the availability of raw materials and energy, the expiration of any one of our patents, the cost of compliance with environmental regulations, economic conditions in certain geographic regions, the adequacy of internally generated funds and credit facilities, the meeting of dividend payout objectives, the ability to fund debt service obligations, the likelihood of future goodwill or intangible asset impairment charges, our portion of future benefit payments related to pension and postretirement benefits, the availability of additional financing, the outcome of outstanding legal proceedings, the impact of adopting new accounting pronouncements and the estimated timing and amount related to the resolution of tax matters. These statements are subject to certain risks, uncertainties, and other factors, which could cause actual results to differ materially from those anticipated. Important risks that may influence future results include (1) weakness or downturns in the markets we serve, (2) changes or deterioration in international and domestic political and economic conditions, (3) potential negative impact of acquisitions on our profitability and return on invested capital, (4) the risk of intentional acts of our employees, agents or business partners that violate anti-corruption and other laws, (5) the unfavorable impact of foreign currency fluctuations, (6) decreases in credit availability, (7) raw material price increases and supply shortages, (8) an interruption in, or reduction in, introducing new products into our product lines, (9) an unfavorable environment for making acquisitions, domestic and international, including adverse accounting or regulatory requirements and market values of candidates, (10) unfavorable tax law changes and tax authority rulings, (11) financial market risks to our obligations under our defined benefit pension plans, and (12) potential adverse outcome in legal proceedings. The risks covered here are not all inclusive and given these and other possible risks and uncertainties, investors should not place undue reliance on forward-looking statements as a prediction of actual results.

These forward-looking statements are not guarantees of future performance and involve risks, assumptions and uncertainties, known or unknown to us, including, but not limited to, those described in Item 1A Risk Factors of our most recent Annual Report on Form 10-K and subsequent Quarterly Reports on Form 10-Q, in any prospectus supplement, and in other documents that we file or furnish with the Securities and Exchange Commission. Should one or more of these risks or uncertainties materialize, or should underlying assumptions prove incorrect, actual results may vary materially from those indicated or anticipated by such forward-looking statements. You are cautioned not to place undue reliance on these forward-looking statements, which speak only as of the date they are made. Except to the extent required by law, we do not undertake, and expressly disclaim, any duty or obligation to update publicly any forward-looking statement after the date the statement is made, whether as a result of new information, future events, changes in assumptions or otherwise.

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THE COMPANY

We are a multinational manufacturer of a diversified range of industrial products and equipment. As of December 31, 2011, our businesses operate in 58 countries and are reported internally as 52 operating segments to senior management. These operating segments have been aggregated into eight external reportable segments.

80/20 Business Process

A key element of our business strategy is our continuous 80/20 business process for both existing businesses and new acquisitions. The basic concept of this 80/20 business process is to focus on what is most important (the 20% of the items which account for 80% of the value) and to spend less time and resources on the less important (the 80% of the items which account for 20% of the value). Our operations use this 80/20 business process to simplify and focus on the key parts of their business, and as a result, reduce complexity that often disguises what is truly important. Our operations utilize the 80/20 process in various aspects of their business. Common applications of the 80/20 business process include:

- Simplifying product lines by reducing the number of products offered by combining the features of similar products, outsourcing products or, as a last resort, eliminating low-value products.
- Segmenting the customer base by focusing on the 80/20 customers separately and finding alternative ways to serve the 20/80 customers.
- Simplifying the supplier base by partnering with 80/20 suppliers and reducing the number of 20/80 suppliers.
- Designing business processes, systems and measurements around the 80/20 activities.

The result of the application of this 80/20 business process is that we have over time improved our long-term operating and financial performance. These 80/20 efforts can result in restructuring projects that reduce costs and improve margins. Corporate management works closely with those businesses that have operating results below expectations to help those businesses better apply this 80/20 business process and improve their results.

We were founded in 1912 and incorporated in Delaware in 1915. Our principal offices are located at 3600 West Lake Avenue, Glenview, Illinois 60026. Our telephone number is (847) 724-7500. We maintain a website at www.itw.com. We are not including the information contained on our website as a part of, or incorporating it by reference into, this prospectus.

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RATIO OF EARNINGS TO FIXED CHARGES

Our consolidated ratio of earnings to fixed charges for each of the last five fiscal years and for the six months ended June 30, 2012 is set forth below. You should read this table in conjunction with the consolidated financial statements and related notes to financial statements incorporated by reference in this prospectus. See Where You Can Find More Information.

For the purpose of computing these ratios, earnings consists of income from continuing operations before income taxes and equity method earnings plus fixed charges and dividends of unconsolidated affiliates. Fixed charges consists of interest expense (which includes amortization of debt issuance costs) and an estimate of the interest within rental expense. The ratio was calculated by dividing the sum of the fixed charges into the sum of earnings. Interest related to income tax matters is included in income taxes in the consolidated statement of income and is excluded from the computation of fixed charges.

	Six Months Ended June 30, 2012	Fiscal Year Ended December 31,				
		2011	2010	2009	2008	2007
Ratio of earnings to fixed charges[(1)]	11.8x	11.3x	10.1x	6.5x	11.9x	17.7x

(1) Certain reclassifications of prior years data have been made to conform to current year reporting, including discontinued operations. Fiscal years 2010 and 2009 have been restated for the elimination of the one-month lag for the reporting of our international operations outside of North America. See Item 8. Financial Statements and Supplementary Data of our Annual Report on Form 10-K for the year ended December 31, 2011 for more detail regarding discontinued operations and the elimination of the one-month lag.

USE OF PROCEEDS

Unless otherwise specified in the applicable prospectus supplement, the net proceeds from the sale of the securities to which this prospectus relates will be used for general corporate purposes. Until we apply the proceeds from the sale of the securities, we may temporarily invest any proceeds that are not immediately applied to the above purposes in United States government or agency obligations, commercial paper, money market accounts, short-term marketable securities, bank deposits or certificates of deposit, repurchase agreements collateralized by United States government or agency obligations or other short-term investments.

DESCRIPTION OF DEBT SECURITIES

The following summarizes the material provisions of the debt securities to which a prospectus supplement may relate. We may issue debt securities from time to time in one or more series. Each time we offer debt securities, the prospectus supplement related to that offering will describe the applicable terms.

As required by United States federal law for all bonds and notes of companies that are publicly offered, the debt securities will be governed by a document called an indenture. An indenture is a contract to be entered into by us and a financial institution, acting as trustee on your behalf. The indenture is subject to and governed by the Trust Indenture Act of 1939, as amended. The trustee has two main roles:

- First, subject to some limitations, the trustee can enforce your rights against us if we default.

- Second, the trustee performs for us certain administrative duties, which include sending you notices and, if the trustee also performs the service of paying agent, interest payments.

Because this section is a summary of the material terms, it does not describe every aspect of the debt securities. We urge you to read the indenture governing the debt securities because it, and not this description, defines your rights as a holder of debt securities. The indenture is filed as an exhibit to the registration statement

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of which this prospectus forms a part. This description is not complete and is subject to, and qualified in its entirety by reference to, all of the provisions of the indenture covering the debt securities, as described below, including definitions of some terms used in the indenture. The indenture is subject to any amendments or supplements that we may enter into from time to time, as permitted under the indenture.

References to ITW, we, us and our in this section are only to Illinois Tool Works Inc. and not to its subsidiaries.

General

Unless otherwise provided in the applicable prospectus supplement, the debt securities will be unsecured senior obligations of our company. As senior debt securities, they will rank equally with all of our other unsecured and unsubordinated indebtedness.

Our debt securities are effectively subordinated to all existing and future indebtedness and other liabilities, including trade payables and capital lease obligations, of any of our subsidiaries. This may affect your ability to receive payments on our debt securities.

The indenture provides for the issuance by us from time to time of debt securities in one or more series. The indenture does not limit the aggregate principal amount of debt securities we may issue under the indenture. In addition, the indenture does not limit the amount of other indebtedness or debt securities, other than certain secured indebtedness to the extent described in the prospectus supplement relating to that series of debt securities that may be issued by ITW or its subsidiaries.

The indenture sets forth the specific terms of any series of debt securities or provides that such terms will be set forth in, or determined pursuant to, one or more authorizing resolutions and an officers certificate or a supplemental indenture, if any, relating to that series.

You should read the prospectus supplement relating to a particular series of debt securities for the following terms of the series of debt securities offered by that prospectus supplement and this prospectus:

- the designation of the debt securities;

- the limit upon the aggregate principal amount of the debt securities;

- the rate or rates at which the debt securities will bear interest, if any, or the formula by which interest will accrue;

- the dates from which interest will accrue, the interest payment dates on which such interest will be payable, and the record date for the interest payable on any interest payment date;

- the maturity date of the debt securities;

- the period or periods within which, the price or prices at which, and the terms and conditions upon which, the debt securities may be redeemed, in whole or in part;

- our obligation, if any, to redeem or purchase the debt securities pursuant to a sinking, purchase or analogous fund or at the option of the holder thereof and the period or periods within which, the price or prices at which, and the terms and conditions upon which, the debt securities will be redeemed or purchased, in whole or in part, pursuant to any such obligation;

whether any of the debt securities may be redeemed at our option and, if so, the date or dates on which, the period or periods within which, the price or prices at which, and the other terms and conditions upon which the debt securities may be redeemed, in whole or in part;

if other than the principal amount, the portion of the principal amount of the debt securities that will be payable upon declaration of acceleration of maturity;

if other than denominations of $1,000, if registered, and $5,000, if unregistered, and any integral multiples of the applicable denominations for debt securities denominated in dollars, the denominations in which the debt securities will be issuable;

the form of security to be used to evidence ownership of the debt securities;

the place or places where the principal of (and premium, if any) and interest, if any, on the debt securities will be payable;

any additional offices or agencies maintained for the registration of transfer, exchange and payment of the debt securities;

whether the debt securities will be issued as registered securities or as unregistered securities, with or without coupons;

whether unregistered debt securities may be exchanged for registered debt securities and whether registered debt securities may be exchanged for unregistered debt securities and the circumstances under which and the place or places where any such exchanges, if permitted, may be made;

whether the debt securities will be issued in whole or in part in the form of one or more global securities and, in such case, the depositary for such global security or securities and whether any global securities of such series will be issuable initially in temporary form, and whether any global securities of such series will be issuable in definitive form, with or without coupons, and, if so, whether beneficial owners of interests in any such definitive global security may exchange such interests for debt securities of such series and the circumstances under which and the place or places where any such exchange may occur;

if other than dollars, the coin, or currency or currencies, or currency unit or units in which the debt securities will be denominated and in which payment of the principal, premium, and interest, if any, on the debt securities will be payable;

if the principal, premium, and interest, if any, on the debt securities are to be payable at the election of us or a holder thereof or under some or all other circumstances, in a coin, or currency or currencies, or currency unit or units other than that in which the debt securities are denominated, the period or periods within which, and the terms and conditions upon which, such election may be made, or the other circumstances under which any of the debt securities are to be so payable, and any provision requiring the holder thereof to bear currency exchange costs by deduction from such payments;

if the principal, premium, and interest, if any, on the debt securities may be determined with reference to a currency, currency unit, commodity or financial or non-financial index or indices, then the manner in which such amounts will be determined;

whether and under what circumstances and with what procedures and documentation we will pay additional amounts on any of the debt securities and coupons, if any, of such series to any holder who is a Non-U.S. Holder (as defined in the prospectus supplement relating to the debt securities), in respect of any tax, assessment or governmental charge withheld or deducted and, if so, whether we will have the option to redeem such debt securities rather than pay additional amounts (and the terms of any such option);

the person to whom any interest on any registered debt security will be payable, if other than the person in whose name that debt security is registered at the close of business on the record date for such interest, the manner in which, or the person to whom, any interest on any unregistered debt security of such series will be payable, if other than upon presentation and surrender of the coupons appertaining thereto as they mature, and the extent to which, or the manner in which, any interest payable on a temporary global security on an interest payment date will be paid if other than in the manner provided below;

- whether some of the provisions relating to the defeasance and discharge of the debt securities, or certain obligations relating thereto, described below under Defeasance and Discharge of Indenture or Certain Obligations will be applicable to the debt securities; and

- any other terms of the debt securities (which will not be inconsistent with the provisions of the indenture).

The principal, premium, and interest, if any, will be payable at the time or times and in the manner provided in the prospectus supplement relating to any series of debt securities. In the case of registered securities, interest on the debt securities will be payable on any interest payment date to the persons in whose names the debt securities are registered at the close of business on the record date. Any paying agents initially designated by us for the debt securities of a particular series will be named in the prospectus supplement relating to those debt securities. We may at any time designate additional paying agents or rescind the designation of any paying agent or approve a change in the office through which any paying agent acts.

The debt securities may be presented for transfer (duly endorsed or accompanied by a written instrument or instruments of transfer, if so required by us or the security registrar) or exchanged for other debt securities of the same series (of like aggregate principal amount and in any authorized denominations) at the office or agency maintained by us (initially the principal office of the trustee in Chicago, Illinois or another office designated by the trustee). The transfer or exchange will be made without service charge, but we may require payment of a sum sufficient to cover any tax or other governmental charge payable in connection with any registration of transfer or exchange of debt securities. We will not be required to (1) issue, register the transfer of, or exchange debt securities for a period of 15 days prior to the redemption of any of the debt securities of that series or (2) register the transfer of or exchange any debt security so selected for redemption in whole or in part, except the unredeemed portion of any debt security being redeemed in part.

We have appointed the trustee under the indenture as security registrar. Any transfer agent (in addition to the security registrar) initially designated by us for any series of debt securities will be named in the applicable prospectus supplement. We may at any time designate additional transfer agents or rescind the designation of any transfer agent or approve a change in the office through which any transfer agent acts, except that we will be required to maintain a transfer agent in each place of payment for the affected debt securities.

Unless otherwise indicated in the applicable prospectus supplement, the debt securities will be issued only in fully registered form, with or without coupons, in minimum denominations of $1,000 and integral multiples of $1,000 in excess thereof. The debt securities may be represented in whole or in part by one or more global debt securities registered in the name of a depositary or its nominee and, if so represented, interests in the global debt security will be shown on, and transfers will be effected only through, records maintained by the designated depositary and its participants as described below.

We may issue debt securities with terms different from those of debt securities that may already have been issued. There is no requirement that we issue debt securities in the future under the same indenture, and we may use other indentures or documentation, containing materially different provisions in connection with future issues of other debt securities.

We may issue the debt securities as original issue discount securities, which are debt securities, including any zero-coupon debt securities, that are issued and sold at a discount from their stated principal amount. Original issue discount securities provide that, upon acceleration of their maturity, an amount less than their principal amount will become due and payable. We will describe the United States federal income tax consequences and other considerations applicable to original issue discount securities in any prospectus supplement relating to them.

In addition, special United States federal income tax considerations or other restrictions or other terms applicable to any debt securities offered exclusively to foreigners or denominated in a currency other than United States dollars may also be set forth in the prospectus supplement, if applicable.

We will comply with Section 14(c) of the Exchange Act, and any other tender offer rules within the Exchange Act, which may then be applicable, if we are obligated to purchase debt securities at the option of the holders of the securities. Any obligation applicable to a series of debt securities will be described in the applicable prospectus supplement.

Unless otherwise described in a prospectus supplement relating to any series of debt securities, the indenture does not contain any provisions that would limit our ability to incur indebtedness or that would afford holders of debt securities protection in the event of a sudden and significant decline in our credit quality or a takeover, recapitalization or highly leveraged or similar transaction involving our company. Accordingly, we could in the future enter into transactions that could increase the amount of indebtedness outstanding at that time or otherwise affect our capital structure or credit rating. Reference is made to the prospectus supplement relating to the particular series of debt securities being offered for information about any deletions from, modifications or additions to the events of default described below or covenants of ITW in the indenture, including any addition of a covenant or other provisions providing event risk or similar protection.

Conversion and Exchange

If any debt securities are convertible, they may be convertible into or exchangeable for securities, property or cash, or a combination of the foregoing, and the prospectus supplement will explain the terms and conditions of such conversion or exchange, including:

- the securities, property or cash into which the debt securities are convertible or for which they are exchangeable;
- the conversion price or exchange ratio, or the calculation method for such price or ratio;
- the conversion or exchange period, or how such period will be determined;
- if conversion or exchange will be mandatory or at the option of the holder or our company;
- provisions for adjustment of the conversion price or the exchange ratio;
- provisions affecting conversion or exchange in the event of the redemption of the debt securities; and
- any other terms of the debt securities that are consistent with the provisions of the indenture.

Such terms may also include provisions under which the number or amount of other securities or property to be received by the holders of such debt securities upon conversion or exchange would be calculated according to the market price of such other securities or property as of a time stated in the prospectus supplement.

Global Securities

The debt securities of a series may be issued in whole or in part in the form of one or more global debt securities (each a Global Security) that will be deposited with, or on behalf of, a depositary identified in the prospectus supplement relating to that particular series.

The specific terms of a depositary arrangement with respect to a series of debt securities will be described in the prospectus supplement relating to that particular series. We anticipate that the following provisions will apply to all depositary arrangements.

Upon the issuance of a Global Security, the depositary for the Global Security or its nominee will credit, on its book-entry registration and transfer system, the respective principal amounts of the debt securities represented by the Global Security. These accounts will be designated by the underwriters or agents with respect to such debt securities or by us if the debt securities are offered and sold directly by us. Ownership of beneficial interests in a Global Security will be limited to persons that may hold interests through participants. Ownership of beneficial

interests in such a Global Security will be shown on, and the transfer of that ownership will be effected only through, records maintained by the depositary or its nominee (with respect to interests of participants) for such Global Security and on the records of participants (with respect to interests of persons other than participants). The laws of some states require that some purchasers of securities take physical delivery of such securities in definitive form. These limits and laws may impair the ability to transfer beneficial interests in a Global Security.

So long as the depositary for a Global Security, or its nominee, is the registered owner of the Global Security, such depositary or such nominee, as the case may be, will be considered the sole owner or holder of the debt securities represented by the Global Security for all purposes under the indenture governing these debt securities. Except as provided below, owners of beneficial interests in a Global Security will not be entitled to have debt securities of the series represented by the Global Security registered in their names, will not receive or be entitled to receive physical delivery of debt securities of a series in definitive form and will not be considered the owners or holders of the debt securities under the indenture.

Principal of, any premium and interest on, and any additional amounts with respect to debt securities registered in the name of a depositary or its nominee will be made to the depositary or its nominee, as the case may be, as the registered owner of the Global Security representing the debt securities. None of ITW, the trustee, the paying agent or the security registrar will have any responsibility or liability for any aspect of the records relating to or payments made on account of beneficial ownership interests of the Global Security for the debt securities or for maintaining, supervising or reviewing any records relating to the beneficial ownership interests.

We expect that the depositary for a series of debt securities or its nominee, upon receipt of any payment of principal of, premium, if any, or interest on, or additional amounts with respect to debt securities, will credit participants accounts with payments in amounts proportionate to their respective beneficial interest in the principal amount of the Global Security for the debt securities as shown on the records of the depositary or its nominee. We also expect that payments by participants to owners of beneficial interests in the Global Security held through the participants will be governed by standing instructions and customary practices, as is now the case with securities held for the accounts of customers registered in street name, and will be the sole responsibility of the participants.

The indenture provides that if (1) the depositary for a series of debt securities notifies us that it is unwilling or unable to continue as depositary or if the depositary ceases to be eligible under the indenture and a successor depositary is not appointed by us within 90 days of written notice or (2) we determine that the debt securities of a particular series will no longer be represented by Global Securities and execute and deliver to the trustee a company order to that effect, the Global Securities will be exchanged for debt securities of the series in definitive form and in an aggregate principal amount equal to the principal amount of the Global Securities being exchanged. The definitive debt securities will be registered in such name or names as the depositary instructs the trustee. We expect that these instructions may be based upon directions received by the depositary from participants with respect to ownership of beneficial interests in Global Securities.

Consolidation or Merger

Under the terms of the indenture, we may consolidate or merge with another corporation or sell, convey or lease all or substantially all of our assets to another corporation or entity. The successor or acquiring corporation or entity must expressly assume all of our responsibilities and liabilities under the indenture, including the payment of all amounts due on any outstanding series of debt securities and performance of the covenants. If, upon any such consolidation, merger, sale, conveyance or lease, or upon any such consolidation, merger, sale, conveyance or lease with respect to a Restricted Subsidiary (as defined below), any Principal Property (as defined below) or shares of stock or indebtedness of a Restricted Subsidiary would become subject to a lien that is not in favor of us, a Restricted Subsidiary or any such successor or acquiring corporation or entity, we must, before or at the time of such transaction, effectively provide that any series of debt securities outstanding under the indenture will be secured (if we so choose, equally and ratably with any other obligation of us or a Restricted

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Subsidiary that ranks equally with such debt securities) by a direct lien on such Principal Property or shares of stock or indebtedness of a Restricted Subsidiary that is prior to all liens other than pre-existing liens on such Principal Property or shares of stock or indebtedness of a Restricted Subsidiary, and that will continue as long as such Principal Property, shares of stock or indebtedness is subject to the lien arising in such transaction. As used herein, Restricted Subsidiary means any subsidiary (other than a subsidiary principally engaged in leasing or financing installment receivables or financing operations outside the United States) that owns or leases a Principal Property if: (1) substantially all of its property is located in the United States, (2) substantially all of its business is carried on in the United States, or (3) it is incorporated in any State of the United States. Principal Property means any manufacturing plant or other facility within the United States that we or a subsidiary own or lease, unless our Board of Directors determines that the plant or facility, together with any others so determined, is not of material importance to the total business of us and our Restricted Subsidiaries.

Events of Default

Each of the following events will constitute an event of default under the indenture with respect to any series of debt securities issued:

- failure to pay any installment of interest on the debt of that series that continues for 30 days after such payment is due;
- failure to pay principal of or premium, if any, on the debt securities of that series when due;
- failure to perform any of the other covenants or agreements in the debt securities or in the indenture and relating to the debt securities of that series that continues for 60 days after notice to us by the trustee or holders of at least 25% in aggregate principal amount of the outstanding debt securities of that series; or
- certain events of bankruptcy, insolvency or reorganization of us.

An event of default with respect to a particular series of debt securities issued under the indenture does not necessarily constitute an event of default with respect to any other series. The indenture provides that the trustee will, with certain exceptions, notify the holders of the affected series of debt securities of the occurrence of any of the events of default listed above (not including any applicable grace period and irrespective of the giving of notice as described in the third bullet) known to the trustee within 90 days after the occurrence thereof. Except in the case of a default in the payment of principal of, or premium, if any, or interest on a series of the debt securities, the trustee may withhold notice if it determines in good faith that withholding notice is in the interest of the holders.

If an event of default is continuing for any series of the debt securities, the trustee or the holders of not less than 25% in aggregate principal amount of the affected series of debt securities then outstanding may declare the principal amount of that series of the debt securities to be due and payable immediately. In such a case, subject to certain conditions, the holders of a majority in aggregate principal amount of that series of the debt securities then outstanding can annul the declaration and waive past defaults.

We are required to provide an annual officers certificate to the trustee concerning our compliance with certain covenants we make in the indenture. Subject to the provisions of the indenture relating to the duties of the trustee, the trustee is not obligated to exercise any of its rights or powers at the request or direction of any of the holders of debt securities unless the holders have offered the trustee security or indemnity reasonably satisfactory to the trustee. The holders of a majority in principal amount of the outstanding debt securities of each series affected by an event of default may direct the time, method and place of conducting any proceeding for any remedy available to the trustee under the indenture or exercising any of the trustee s trusts or powers with respect to that series of the debt securities; however, the trustee may decline to follow such direction in certain circumstances.

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Modification and Amendment of Indenture

We may enter into supplemental indentures with the trustee without the consent of the holders of any series of debt securities to, among other things:

- evidence the assumption by a successor corporation of our obligations under the indenture;
- appoint additional or separate trustees to act under the indenture;
- add covenants for the protection of the holders of the debt securities; and
- cure any ambiguity or correct any inconsistency in the indenture.

With the consent of the holders of a majority in aggregate principal amount of the securities of each affected series issued under the indenture at the time outstanding, we may execute supplemental indentures with the trustee to add provisions or change or eliminate any provision of the indenture or any supplemental indenture relating to such series or to modify the rights of the holders of those securities. However, no such supplemental indenture will (1) extend the fixed maturity of any securities, reduce the principal amount (including in the case of discounted securities the amount payable upon acceleration of the maturity thereof), reduce the rate or extend the time of payment of any interest, reduce any premium payable upon redemption, or change the currency in which any securities are payable, without the consent of each holder of affected securities, or (2) reduce the aforesaid majority in principal amount of the securities of any series, the consent of the holders of which is required for any such supplemental indenture, without the consent of the holders of all securities of such series.

Defeasance and Discharge of Indenture or Certain Obligations

At our option, we (1) will be discharged from all obligations under the indenture in respect of the debt securities of a series (except for certain obligations to register the transfer of or to exchange debt securities, replace stolen, lost or mutilated debt securities, maintain paying agencies and hold monies for payment in trust) or (2) need not comply with certain covenants of the indenture (including the limitation on liens and the limitation on sale and lease-back) and will not be limited by the restrictions in the indenture with respect to merger, consolidation or sale, conveyance or lease of substantially all of our assets, in each case if we irrevocably deposit with the trustee, in trust, money or U.S. government obligations (or a combination thereof) sufficient to pay the principal of and any premium or interest on the notes when due and satisfy other conditions in the indenture. In order to select either option, we must provide the trustee, among other things, a ruling from or published by the Internal Revenue Service (in the case of option 1) or an opinion of counsel (in the case of option 2) to the effect that holders of the debt securities will not recognize income, gain or loss for Federal income tax purposes as a result of our exercise of the option, as if we had not exercised such option.

In the event we exercise our option under (2) above with respect to any series of debt securities and the debt securities of such series are declared due and payable because of the occurrence of any event of default other than default with respect to such obligations, the amount of money and U.S. government obligations on deposit with the trustee will be sufficient to pay amounts due on the debt securities of that series at the time of their stated maturity but may not be sufficient to pay amounts due on the debt securities of that series at the time of the acceleration resulting from such event of default. We would remain liable, however, for such payments.

Governing Law

The indenture and the debt securities will be governed by, and construed and enforced in accordance with, the laws of the State of Illinois applicable to agreements made or instruments entered into and, in each case, performed in said state.

Relationship with the Trustee

The trustee under the indenture, The Bank of New York Mellon Trust Company, N.A., currently serves as the trustee with respect to certain of our other outstanding debt securities.

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PLAN OF DISTRIBUTION

We may sell our securities on a continuous or delayed basis in any one or more of the following ways from time to time: (i) through agents; (ii) to or through underwriters; (iii) through brokers or dealers; (iv) directly by us to purchasers; or (v) through a combination of any of these methods of sale. The applicable prospectus supplement will contain the terms of the transaction, the place and time of delivery of the securities, the name or names of any underwriters, dealers, agents and the respective amounts of securities underwritten or purchased by them, the initial public offering price of the securities, and the applicable agent s commission, dealer s purchase price or underwriter s discount. Any dealers and agents participating in the distribution of the securities may be deemed to be underwriters, and compensation received by them on resale of the securities may be deemed to be underwriting discounts.

Any initial offering price, dealer purchase price, discount or commission may be changed from time to time.

The securities may be distributed from time to time in one or more transactions, at negotiated prices, at a fixed or fixed prices (that may be subject to change), at market prices prevailing at the time of sale, at various prices determined at the time of sale or at prices related to prevailing market prices.

Offers to purchase securities may be solicited directly by us or by agents designated by us from time to time. Any such agent may be deemed to be an underwriter, as that term is defined in the Securities Act, of the securities so offered and sold.

If underwriters are utilized in the sale of any securities in respect of which this prospectus is being delivered, such securities will be acquired by the underwriters for their own account and may be resold from time to time in one or more transactions, including negotiated transactions, at fixed public offering prices or at varying prices determined by the underwriters at the time of sale. Securities may be offered to the public either through underwriting syndicates represented by managing underwriters or directly by one or more underwriters.

If a dealer is utilized in the sale of the securities in respect of which this prospectus is delivered, we will sell such securities to the dealer, as principal. The dealer may then resell such securities to the public at varying prices to be determined by such dealer at the time of resale. Transactions through brokers or dealers may include block trades in whicflows associated with purchasing and selling fuel derivatives are classified as Other operating cash flows in the unaudited Condensed Consolidated Statement of Cash Flows. The following table presents the location of all assets and liabilities associated with the Company’s derivative instruments within the unaudited Condensed Consolidated Balance Sheet:

		Asset derivatives		Liability derivatives	
(in millions)	Balance Sheet location	Fair value at 6/30/2013	Fair value at 12/31/2012	Fair value at 6/30/2013	Fair value at 12/31/2012
Derivatives designated as hedges*					
Fuel derivative contracts (gross)	Prepaid expenses and other current assets	$17	$—	$6	$—
Fuel derivative contracts (gross)	Other assets	23	355	7	16
Fuel derivative contracts (gross)	Accrued liabilities	19	—	72	—
Fuel derivative contracts (gross)	Other noncurrent liabilities	111	—	30	—
Interest rate derivative contracts	Other assets	22	31	—	—
Interest rate derivative contracts	Other noncurrent liabilities	—	—	90	126
Total derivatives designated as hedges		$192	$386	$205	$142
Derivatives not designated as hedges*					
Fuel derivative contracts (gross)	Prepaid expenses and other current assets	$114	$375	$95	$327
Fuel derivative contracts (gross)	Other assets	24	233	31	351

Fuel derivative contracts (gross)	Accrued liabilities	68	10	106	60
Fuel derivative contracts (gross)	Other noncurrent liabilities	38	—	159	—
Total derivatives not designated as hedges		$244	$618	$391	$738
Total derivatives		$436	$1,004	$596	$880

* Represents the position of each trade before consideration of offsetting positions with each counterparty and does not include the impact of cash collateral deposits provided to or received from counterparties. See discussion of credit risk and collateral following in this Note.

In addition, the Company had the following amounts associated with fuel derivative instruments and hedging activities in its unaudited Condensed Consolidated Balance Sheet:

(in millions)	Balance Sheet location	June 30, 2013	December 31, 2012
Cash collateral deposits provided to counterparties for fuel contracts- noncurrent	Offset against Other noncurrent liabilities	$10	$—
Cash collateral deposits provided to counterparties for interest rate contracts - noncurrent	Offset against Other noncurrent liabilities	41	89
Cash collateral deposits provided to counterparties for fuel contracts - current	Offset against Accrued liabilities	55	—
Due to third parties for fuel contracts	Accrued liabilities	8	—
Receivable from third parties for fuel contracts - current	Accounts and other receivables	35	—
Receivable from third parties for fuel contracts - noncurrent	Other assets	27	54
Prepaid settlements for fuel contracts - current	Prepaid expenses and other current assets	—	15

All of the Company's fuel derivative instruments and interest rate swaps are subject to agreements that follow the netting guidance in the applicable accounting for derivatives and hedging. The types of derivative instruments the Company has determined are subject to netting requirements in the accompanying unaudited Condensed Consolidated Balance Sheet are those in which the Company pays or receives cash for transactions with the same counterparty that settle on the same day and in the same currency via one net payment or receipt. For cash collateral held by the Company or provided to counterparties, the Company nets such amounts against the fair value of the Company's derivative portfolio by each counterparty. The Company has elected to utilize netting for both its fuel derivative instruments and interest rate swap agreements and also classifies such amounts as either current or noncurrent, based on the net fair value position with each of the Company's counterparties in the unaudited Condensed Consolidated Balance Sheet.

The Company's application of its netting policy associated with cash collateral differs depending on whether its derivative instruments are in a net asset position or a net liability position. If its fuel derivative instruments are in a net asset position with a counterparty, cash collateral amounts held are first netted against current outstanding derivative amounts associated with that counterparty until that balance is zero, and then any remainder is applied against the fair value of noncurrent outstanding derivative instruments. If the Company's fuel derivative instruments are in a net liability position with the counterparty, cash collateral amounts provided are first netted against noncurrent outstanding derivative amounts associated with that counterparty until that balance is zero, and then any remainder is applied against the fair value of current outstanding derivative instruments. At June 30, 2013, $65 million in cash collateral deposits had been provided by the Company associated with its outstanding fuel derivative instruments. No letters of credit or aircraft collateral were provided by or held by the Company at June 30, 2013. At December 31, 2012, no cash collateral deposits, letters of credit, and/or aircraft collateral were provided by or held by the Company associated with its outstanding fuel derivative instruments.

The Company also has agreements with each of its counterparties associated with its outstanding interest rate swap agreements in which cash collateral may be required based on the fair value of outstanding derivative instruments, as well as the Company's and its counterparty's credit ratings. The Company has also elected to present its interest rate swap agreement cash collateral utilizing a net presentation. As of June 30, 2013, $39 million had been provided to one counterparty associated with interest rate derivatives based on the Company's outstanding net liability derivative position with that counterparty. In addition, in connection with interest rate swaps entered into by AirTran, $2 million

had been provided to one counterparty at June 30, 2013, as a result of the outstanding net liability derivative position with that counterparty. The outstanding interest rate net derivative positions with all other counterparties at June 30, 2013, were assets to the Company.

The Company has the following recognized financial assets and financial liabilities resulting from those transactions that meet the scope of the disclosure requirements as necessitated by applicable accounting guidance for balance sheet offsetting:

Offsetting of derivative assets
(in millions)

		(i)	(ii)	(iii) = (i) + (ii)	(i)	(ii)	(iii) = (i) + (ii)
		June 30, 2013			December 31, 2012		
Description	Balance Sheet location	Gross amounts of recognized assets	Gross amounts offset in the Balance Sheet	Net amounts of assets presented in the Balance Sheet	Gross amounts of recognized assets	Gross amounts offset in the Balance Sheet	Net amounts of assets presented in the Balance Sheet
Fuel derivative contracts	Prepaid expenses and other current assets	$131	$(101)	$30 (a)	$375	$(327)	$48 (a)
Fuel derivative contracts	Other assets	$47	$(38)	$9	$588	$(367)	$221
Fuel derivative contracts	Accrued liabilities	$87	$(87)	$—	$10	$(10)	$—
Fuel derivative contracts	Other noncurrent liabilities	$149	$(149)	$—	$—	$—	$—
Interest rate derivative contracts	Other assets	$22	$—	$22	$31	$—	$31

(a) Amounts included in Prepaid expenses and other current assets.

Offsetting of derivative liabilities
(in millions)

		(i)	(ii)	(iii) = (i) + (ii)	(i)	(ii)	(iii) = (i) + (ii)
		June 30, 2013			December 31, 2012		
Description	Balance Sheet location	Gross amounts of recognized liabilities	Gross amounts offset in the Balance Sheet	Net amounts of liabilities presented in the Balance Sheet	Gross amounts of recognized liabilities	Gross amounts offset in the Balance Sheet	Net amounts of liabilities presented in the Balance Sheet
Fuel derivative contracts	Prepaid expenses and other current assets	$101	$(101)	$—	$327	$(327)	$—
Fuel derivative contracts	Other assets	$38	$(38)	$—	$367	$(367)	$—
Fuel derivative	Accrued liabilities	$178	$(142)	$36	$60	$(10)	$50

contracts							
Fuel derivative contracts	Other noncurrent liabilities	$189	$(159)	$30	$—	$—	$—
Interest rate derivative contracts	Other noncurrent liabilities	$90	$(41)	$49	$126	$(89)	$37

The net amounts of derivative assets and liabilities are reconciled to the individual line item amounts presented in the unaudited Condensed Consolidated Balance Sheet in Note 7.

The following tables present the impact of derivative instruments and their location within the unaudited Condensed Consolidated Statement of Comprehensive Income for the three and six months ended June 30, 2013 and 2012:

Derivatives in cash flow hedging relationships

	(Gain) loss recognized in AOCI on derivatives (effective portion)		(Gain) loss reclassified from AOCI into income (effective portion)(a)		(Gain) loss recognized in income on derivatives (ineffective portion)(b)	
	Three months ended June 30,		Three months ended June 30,		Three months ended June 30,	
(in millions)	2013	2012	2013	2012	2013	2012
Fuel derivative contracts	$189 *	$279 *	$37 *	$28 *	$3	$8
Interest rate derivatives	(11)*	12 *	4 *	4 *	(1)	—
Total	$178	$291	$41	$32	$2	$8

*Net of tax

(a) Amounts related to fuel derivative contracts and interest rate derivatives are included in Fuel and oil and Interest expense, respectively.

(b) Amounts are included in Other (gains) losses, net.

Derivatives in cash flow hedging relationships

	(Gain) loss recognized in AOCI on derivatives (effective portion)		(Gain) loss reclassified from AOCI into income (effective portion)(a)		(Gain) loss recognized in income on derivatives (ineffective portion)(b)	
	Six months ended June 30,		Six months ended June 30,		Six months ended June 30,	
(in millions)	2013	2012	2013	2012	2013	2012
Fuel derivative contracts	$218 *	$143 *	$63 *	$51 *	$12	$40
Interest rate derivatives	(14)*	10 *	9 *	8 *	(1)	—
Total	$204	$153	$72	$59	$11	$40

*Net of tax

(a) Amounts related to fuel derivative contracts and interest rate derivatives are included in Fuel and oil and Interest expense, respectively.

(b) Amounts are included in Other (gains) losses, net.

Derivatives not in cash flow hedging relationships

	(Gain) loss recognized in income on derivatives		
	Three months ended June 30,		Location of (gain) loss recognized in income on derivatives
(in millions)	2013	2012	
Fuel derivative contracts	$32	$40	Other (gains) losses, net

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Derivatives not in cash flow hedging relationships

(in millions)	(Gain) loss recognized in income on derivatives Six months ended June 30, 2013	2012	Location of (gain) loss recognized in income on derivatives
Fuel derivative contracts	$(28)	$(169)	Other (gains) losses, net

The Company also recorded expense associated with premiums paid for fuel derivative contracts that settled/expired during the three months ended June 30, 2013 and 2012 of $12 million and $12 million, respectively, and the six months ended June 30, 2013 and 2012 of $17 million and $18 million, respectively. These amounts are excluded from the Company's measurement of effectiveness for related hedges and are included as a component of Other (gains) losses, net, in the unaudited Condensed Consolidated Statement of Comprehensive Income.

The fair values of the derivative instruments, depending on the type of instrument, were determined by the use of present value methods or option value models with assumptions about commodity prices based on those observed in underlying markets or provided by third parties. Included in the Company's cumulative net unrealized losses from fuel hedges as of June 30, 2013, were approximately $101 million in unrealized losses, net of taxes, which are expected to be realized in earnings during the twelve months subsequent to June 30, 2013. In addition, as of June 30, 2013, the Company had already recognized cumulative net gains due to ineffectiveness and derivatives that did not qualify for hedge accounting treatment totaling $32 million, net of taxes. These net gains were recognized during the three months ended June 30, 2013 and prior periods, and are reflected in Retained earnings as of June 30, 2013, but the underlying derivative instruments will not expire/settle until third quarter 2013 or future periods.

Interest rate swaps

The Company is party to certain interest rate swap agreements that are accounted for as either fair value hedges or cash flow hedges, as defined in the applicable accounting guidance for derivative instruments and hedging. The interest rate swap agreements accounted for as fair value hedges qualify for the "shortcut" method of accounting for hedges, which dictates that the hedges are assumed to be perfectly effective, and, thus, there is no ineffectiveness to be recorded in earnings. For the Company's interest rate swap agreements accounted for as cash flow hedges, ineffectiveness is required to be measured at each reporting period. The ineffectiveness associated with all of the Company's, including AirTran's, interest rate cash flow hedges for all periods presented was not material.

Credit risk and collateral

Credit exposure related to fuel derivative instruments is represented by the fair value of contracts that are an asset to the Company at the reporting date. At such times, these outstanding instruments expose the Company to credit loss in the event of nonperformance by the counterparties to the agreements. However, the Company has not experienced any significant credit loss as a result of counterparty nonperformance in the past. To manage credit risk, the Company selects and periodically reviews counterparties based on credit ratings, limits its exposure with respect to each counterparty, and monitors the market position of the fuel hedging program and its relative market position with each counterparty. At June 30, 2013, the Company had agreements with all of its active counterparties containing early termination rights and/or bilateral collateral provisions whereby security is required if market risk exposure exceeds a specified threshold amount based on the counterparty credit rating. The Company also had agreements with counterparties in which cash deposits, letters of credit, and/or pledged aircraft are required to be posted whenever the net fair value of derivatives associated with those counterparties exceeds specific thresholds. The following table provides the fair values of fuel derivatives, amounts posted as collateral, and applicable collateral posting threshold amounts as of June 30, 2013, at which such postings are triggered:

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(in millions)	Counterparty (CP) A	B	C	D	E	F	Other(a)	Total
Fair value of fuel derivatives	$(85)	$(18)	$(12)	$(6)	$16	$9	$4	$(92)
Cash collateral held (by) CP	(55)	(10)	—	—	—	—	—	(65)
Aircraft collateral pledged to CP	—	—	—	—	—	—	—	—
Letters of credit (LC)	—	—	—	—	—	—	—	—
Option to substitute LC for aircraft	(340) to (740)(d)	>(125)(d)	N/A	N/A	N/A	N/A		
Option to substitute LC for cash	N/A	N/A	(100) to (150)(e)	N/A	>(50)(e)	N/A		
If credit rating is investment grade, fair value of fuel derivative level at which:								
Cash is provided to CP	(40) to (340) or >(740)	0 to (125) or >(625)	>(50)	>(75)	>(50)	>(50)		
Cash is received from CP	>75	>150	>175(c)	>125(c)	>200	>30		
Aircraft or cash can be pledged to CP as collateral	(340) to (740)(d)	(125) to (625)(d)	N/A	N/A	N/A	N/A		
If credit rating is non-investment grade, fair value of fuel derivative level at which:								
Cash is provided to CP	(40) to (340) or >(740)	0 to (125) or >(625)	(b)	(b)	(b)	(b)		
Cash is received from CP	(b)	(b)	(b)	(b)	(b)	(b)		
Aircraft can be pledged to CP as collateral	(340) to (740)	(125) to (625)	N/A	N/A	N/A	N/A		

(a) Individual counterparties with fair value of fuel derivatives <$20 million.
(b) Cash collateral is provided at 100 percent of fair value of fuel derivative contracts.
(c) Thresholds may vary based on changes in credit ratings within investment grade.
(d) The Company has the option of providing cash, letters of credit, or pledging aircraft as collateral. No letters of credit or aircraft were pledged as collateral with such counterparties as of June 30, 2013.
(e) The Company has the option of providing cash or letters of credit as collateral. No letters of credit were pledged as collateral with such counterparties as of June 30, 2013.

6. COMPREHENSIVE INCOME (LOSS)

Comprehensive income (loss) includes changes in the fair value of certain financial derivative instruments that qualify for hedge accounting, unrealized gains and losses on certain investments, and actuarial gains/losses arising from the Company’s postretirement benefit obligation. The differences between Net income and Comprehensive income (loss) for the three and six months ended June 30, 2013 and 2012 were as follows:

Three months ended June 30,

(in millions)	2013	2012
NET INCOME	$224	$228
Unrealized loss on fuel derivative instruments, net of deferred taxes of ($90) and ($156)	(152)	(251)
Unrealized gain (loss) on interest rate derivative instruments, net of deferred taxes of $9 and ($5)	15	(8)
Other, net of deferred taxes of $ - and ($3)	—	(4)
Total other comprehensive loss	$(137)	$(263)
COMPREHENSIVE INCOME (LOSS)	$87	$(35)

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(in millions)	Six months ended June 30, 2013	2012
NET INCOME	$283	$327
Unrealized loss on fuel derivative instruments, net of deferred taxes of ($91) and ($57)	(155)	(92)
Unrealized gain (loss) on interest rate derivative instruments, net of deferred taxes of $15 and ($1)	23	(2)
Other, net of deferred taxes of $2 and ($1)	3	(2)
Total other comprehensive loss	$(129)	$(96)
COMPREHENSIVE INCOME	$154	$231

A rollforward of the amounts included in AOCI, net of taxes, is shown below for the three and six months ended June 30, 2013:

(in millions)	Fuel derivatives	Interest rate derivatives	Defined benefit pension items	Other	Deferred tax	Accumulated other comprehensive income (loss)
Balance at March 31, 2013	$(107)	$(94)	$26	$(3)	$67	$(111)
Changes in fair value	(301)	18	—	—	105	(178)
Reclassification to earnings	59	6	—	—	(24)	41
Balance at June 30, 2013	$(349)	$(70)	$26	$(3)	$148	$(248)

(in millions)	Fuel derivatives	Interest rate derivatives	Defined benefit pension items	Other	Deferred tax	Accumulated other comprehensive income (loss)
Balance at December 31, 2012	$(103)	$(108)	$26	$(8)	$74	$(119)
Changes in fair value	(347)	24	—	5	117	(201)
Reclassification to earnings	101	14	—	—	(43)	72
Balance at June 30, 2013	$(349)	$(70)	$26	$(3)	$148	$(248)

The following tables illustrate the significant amounts reclassified out of each component of AOCI for the three and six months ended June 30, 2013:

Three months ended June 30, 2013

(in millions) AOCI components	Amounts reclassified from AOCI	Affected line item in the unaudited Condensed Consolidated Statement of Comprehensive Income
Unrealized gain on fuel derivative instruments	$59	Fuel and oil expense
	$22	Less: Tax Expense
	$37	Net of tax
Unrealized gain on interest rate derivative instruments	$6	Interest expense
	$2	Less: Tax Expense
	$4	Net of tax

Total reclassifications for the period	$41	Net of tax

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Six months ended June 30, 2013

(in millions) AOCI components	Amounts reclassified from AOCI	Affected line item in the unaudited Condensed Consolidated Statement of Comprehensive Income
Unrealized gain on fuel derivative instruments	$101	Fuel and oil expense
	$38	Less: Tax Expense
	$63	Net of tax
Unrealized gain on interest rate derivative instruments	$14	Interest expense
	$5	Less: Tax Expense
	$9	Net of tax
Total reclassifications for the period	$72	Net of tax

7. SUPPLEMENTAL FINANCIAL INFORMATION

(in millions)	June 30, 2013	December 31, 2012
Fuel derivative contracts	$9	$221
Interest rate derivative contracts	22	31
Receivable from third parties for fuel contracts - noncurrent	27	54
Intangible assets	127	138
Non-current investments	41	41
Other	158	148
Other assets	$384	$633

(in millions)	June 30, 2013	December 31, 2012
Retirement plans	$222	$135
Aircraft rentals	130	139
Vacation pay	281	270
Health	61	70
Fuel derivative contracts	36	50
Workers compensation	156	159
Accrued taxes	119	67
Other	202	212
Accrued liabilities	$1,207	$1,102

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(in millions)	June 30, 2013	December 31, 2012
Postretirement obligation	$162	$148
Non-current lease-related obligations	340	376
Airport construction obligation	404	331
Other deferred compensation	147	141
Fuel derivative contracts	30	—
Interest rate derivative contracts	49	37
Other	79	91
Other non-current liabilities	$1,211	$1,124

For further details on fuel derivative and interest rate derivative contracts, see Note 5.

Other Operating Expenses
Other operating expenses consist of distribution costs, advertising expenses, personnel expenses, professional fees, and other operating costs, none of which individually exceed 10 percent of Operating expenses.

8. LEASES

On July 9, 2012, the Company signed an agreement with Delta Air Lines, Inc. and Boeing Capital Corp. to lease or sublease all 88 of AirTran's Boeing 717-200 aircraft ("B717s") to Delta, with the first delivery expected to occur in August 2013, at a rate of approximately three B717s per month. A total of 78 of the B717s are on operating lease, eight are owned, and two are currently classified as capital leases.

The B717s add complexity to the Company's operations, as Southwest Airlines has historically operated an all-Boeing 737 fleet. From a fleet management perspective, the transition of approximately three B717s per month to Delta beginning in August 2013 allows the Company to minimize the impact of this transaction on operations, as the B717 capacity lost is expected to be replaced through the capacity gained as a result of (i) the Company's modification of the retirement dates for a portion of its 737-300 and 737-500 aircraft and (ii) its receipt of new 737 deliveries from Boeing or its acquisition of used 737s.

The Company will lease and/or sublease all 88 of the B717s to Delta at agreed-upon lease rates. In addition, the Company will pay the majority of the costs to convert the aircraft to the Delta livery and perform certain maintenance checks prior to the delivery of each aircraft. The agreement to pay these conversion and maintenance costs is a "lease incentive" under applicable accounting guidance. The sublease terms for the 78 B717s currently on operating lease and the two B717s currently classified as capital leases coincide with the Company's remaining lease terms for these aircraft from the original lessor, which range from approximately 6 years to approximately 12 years. The lease terms for the eight B717s that are owned by the Company are for a period of seven years, after which Delta will have the option to purchase the aircraft at the then-prevailing market value. The Company will account for the lease and sublease transactions with Delta as operating leases, except for the two aircraft classified by the Company as capital leases. The subleases of these two aircraft will be accounted for as direct financing leases. There are no contingent payments and no significant residual value conditions associated with the transaction.

The accounting for this transaction is based on the guidance provided for lease transactions. For the components of this transaction finalized in third quarter 2012 and with respect to which the lease inception has been deemed to occur, the Company recorded a charge of approximately $137 million during third quarter 2012. The charge represents the

remaining estimated cost, at the scheduled date of delivery of each B717 to Delta (including the conversion, maintenance, and other contractual costs to be incurred), of the Company's lease of the 78 B717s that are currently accounted for as operating leases, net of the future sublease income from Delta and the remaining unfavorable aircraft lease liability established as of the acquisition date. The charges recorded by the Company for this transaction were included as a component of Acquisition and integration costs in the Company's unaudited Condensed Consolidated

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Statement of Comprehensive Income and were included as a component of Other, net in Cash flows from operating activities in the Company's unaudited Condensed Consolidated Statement of Cash Flows, and the corresponding liability for this transaction is included as a component of Current liabilities and Other noncurrent liabilities in the Company's unaudited Condensed Consolidated Balance Sheet. See Note 2 for further information on the Company's Acquisition and integration costs. The Company may also incur other costs associated with this transaction, such as contract termination costs with certain aircraft maintenance vendors. Two of these vendor maintenance contracts have stated termination penalties totaling approximately $106 million if the Company were to terminate such contracts; however, termination of these contracts has not occurred, and any charges would only be recorded at the time of contract termination or at the time any associated charges become probable and estimable.

9. COMMITMENTS AND CONTINGENCIES

Commitments
During 2008, the City of Dallas approved the Love Field Modernization Program ("LFMP"), a project to reconstruct Dallas Love Field ("Airport") with modern, convenient air travel facilities. Pursuant to a Program Development Agreement ("PDA") with the City of Dallas and the Love Field Airport Modernization Corporation (or "LFAMC," a Texas non-profit "local government corporation" established by the City to act on the City's behalf to facilitate the development of the LFMP), the Company is managing this project. Major construction commenced during 2010. New ticketing and checkin areas opened during fourth quarter 2012, and 11 new gates and new concessions opened on April 16, 2013. Another new gate opened in July 2013, and full completion of the project is scheduled for second half 2014. The project consists of the complete replacement of gate facilities with a new 20-gate facility, including infrastructure, systems and equipment, aircraft parking apron, fueling system, roadways and terminal curbside, baggage handling systems, passenger loading bridges and support systems, and other supporting infrastructure.

It is currently expected that the total construction costs associated with the LFMP project will be approximately $519 million. Although the City of Dallas has received commitments from various sources that are expected to fund portions of the LFMP project, including the Federal Aviation Administration ("FAA"), the Transportation Security Administration, and the City's Aviation Fund, the majority of the funds used are from the issuance of bonds. During fourth quarter 2010, $310 million of such bonds were issued by the LFAMC, and the Company has guaranteed principal and interest payments on the bonds. An additional tranche of such bonds totaling $146 million was issued during second quarter 2012, and the Company has guaranteed the principal and interest payments on these bonds as well. The Company currently expects that as a result of the funding commitments from the above mentioned sources and the bonds that have been issued thus far, no further bond issuances and related guarantees from the Company will be required to complete the LFMP project.

In conjunction with the Company's significant presence at Dallas Love Field, its rights to occupy 16 of the available gates upon completion of the facility, and other factors, the Company agreed to manage the majority of the LFMP project. Based on these facts, the Company has evaluated its ongoing accounting requirements in consideration of accounting guidance provided for lessees involved in asset construction. The Company has recorded and will continue to record an asset and corresponding obligation for the cost of the LFMP project as the construction of the facility occurs. As of June 30, 2013, the Company had recorded LFMP construction costs of $404 million classified as both an asset as a component of Ground property and equipment and a corresponding liability as a component of Other non-current liabilities, respectively, in its unaudited Condensed Consolidated Balance Sheet. Upon completion of different phases of the LFMP project, the Company has placed the associated assets in service and has begun depreciating the assets over their estimated useful lives. The amount of depreciation recorded for the three and six months ended June 30, 2013, associated with the LFMP project was not material. The corresponding LFMP liabilities

will be reduced primarily through the Company's airport rental payments to the City of Dallas as the construction costs of the project are passed through to the Company via recurring airport rates and charges.

Contingencies

The Company is from time to time subject to various legal proceedings and claims arising in the ordinary course of business, including, but not limited to, examinations by the IRS. The Company's management does not expect that

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the outcome in any of its currently ongoing legal proceedings or the outcome of any adjustments presented by the IRS, individually or collectively, will have a material adverse effect on the Company's financial condition, results of operations, or cash flow.

10. FAIR VALUE MEASUREMENTS

Accounting standards pertaining to fair value measurements establish a three-tier fair value hierarchy, which prioritizes the inputs used in measuring fair value. These tiers include: Level 1, defined as observable inputs such as quoted prices in active markets; Level 2, defined as inputs other than quoted prices in active markets that are either directly or indirectly observable; and Level 3, defined as unobservable inputs in which little or no market data exists, therefore requiring an entity to develop its own assumptions.

As of June 30, 2013, the Company held certain items that are required to be measured at fair value on a recurring basis. These included cash equivalents, short-term investments (primarily treasury bills, commercial paper, and certificates of deposit), certain noncurrent investments, interest rate derivative contracts, fuel derivative contracts, and available-for-sale securities. The majority of the Company’s short-term investments consist of instruments classified as Level 1. However, the Company has certificates of deposit, commercial paper, and Eurodollar time deposits that are classified as Level 2, due to the fact that the fair value for these instruments is determined utilizing observable inputs in non-active markets. Noncurrent investments consist of certain auction rate securities, primarily those collateralized by student loan portfolios, which are guaranteed by the U.S. Government. Other available-for-sale securities primarily consist of investments associated with the Company’s excess benefit plan.

The Company’s fuel and interest rate derivative instruments consist of over-the-counter contracts, which are not traded on a public exchange. Fuel derivative instruments include swaps, as well as different types of option contracts, whereas interest rate derivatives consist solely of swap agreements. See Note 5 for further information on the Company’s derivative instruments and hedging activities. The fair values of swap contracts are determined based on inputs that are readily available in public markets or can be derived from information available in publicly quoted markets. Therefore, the Company has categorized these swap contracts as Level 2. The Company’s Treasury Department, which reports to the Chief Financial Officer, determines the value of option contracts utilizing an option pricing model based on inputs that are either readily available in public markets, can be derived from information available in publicly quoted markets, or are provided by financial institutions that trade these contracts. The option pricing model used by the Company is an industry standard model for valuing options and is the same model used by the broker/dealer community (i.e., the Company’s counterparties). The inputs to this option pricing model are the option strike price, underlying price, risk free rate of interest, time to expiration, and volatility. Because certain inputs used to determine the fair value of option contracts are unobservable (principally implied volatility), the Company has categorized these option contracts as Level 3. Volatility information is obtained from external sources, but is analyzed by the Company for reasonableness and compared to similar information received from other external sources. The fair value of option contracts considers both the intrinsic value and any remaining time value associated with those derivatives that have not yet settled. The Company also considers counterparty credit risk and its own credit risk in its determination of all estimated fair values. To validate the reasonableness of the Company’s option pricing model, on a monthly basis, the Company compares its option valuations to third party valuations. If any significant differences were to be noted, they would be researched in order to determine the reason. However, historically, no significant differences have been noted. The Company has consistently applied these valuation techniques in all periods presented and believes it has obtained the most accurate information available for the types of derivative contracts it holds.

The Company's investments associated with its excess benefit plan consist of mutual funds that are publicly traded and for which market prices are readily available. This plan is a non-qualified deferred compensation plan designed to hold Employee contributions in excess of limits established by Section 415 of the Internal Revenue Code of 1986, as amended. Payments under this plan are made based on the participant's distribution election and plan balance. Assets related to the funded portion of the deferred compensation plan are held in a rabbi trust, and the Company remains liable to these participants for the unfunded portion of the plan. The Company records changes in the fair value of the liability and the asset in the Company's earnings.

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All of the Company's auction rate security instruments, totaling $36 million (net) at June 30, 2013, are classified as available-for-sale securities and are reflected at their estimated fair value in the unaudited Condensed Consolidated Balance Sheet. In prior periods, due to the auction process which took place every 30-35 days for most securities, quoted market prices were readily available, which would have qualified as Level 1. However, due to events in credit markets beginning during first quarter 2008, the auction events for these remaining instruments failed, and have continued to fail through the current period. Therefore, the Company's Treasury Department determines the estimated fair values of these securities utilizing a discounted cash flow analysis. The Company has performed, and routinely updates, a valuation for each of its auction rate security instruments, considering, among other items, the collateralization underlying the security investments, the expected future cash flows, including the final maturity, associated with the securities, estimates of the next time the security is expected to have a successful auction or return to full par value, forecasted reset rates based on the London Interbank Offered Rate ("LIBOR") or the issuer's net loan rate, and a counterparty credit spread. To validate the reasonableness of the Company's discounted cash flow analyses, the Company compares its valuations to third party valuations on a quarterly basis.

In association with its estimate of fair value related to auction rate security instruments as of June 30, 2013, the Company has previously recorded a temporary unrealized decline in fair value of $14 million, with an offsetting entry to AOCI. The Company continues to believe that this decline in fair value is due entirely to market liquidity issues, because the underlying assets for the majority of these auction rate securities held by the Company are currently rated investment grade by Moody's, Standard and Poor's, and Fitch and are almost entirely backed by the U.S. Government. The range of maturities for the Company's auction rate securities are from 5 years to 34 years. Considering the relative insignificance of these securities in comparison to the Company's liquid assets and other sources of liquidity, the Company has no current intention of selling these securities nor does it expect to be required to sell these securities before a recovery in their cost basis. At the time of the first failed auctions during first quarter 2008, the Company held a total of $463 million in auction rate securities and, since that time, has been able to sell $413 million of these instruments at par value.

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The following tables present the Company's assets and liabilities that are measured at fair value on a recurring basis at June 30, 2013, and December 31, 2012:

		Fair value measurements at reporting date using:		
		Quoted prices in active markets for identical assets	Significant other observable inputs	Significant unobservable inputs
Description	June 30, 2013	(Level 1)	(Level 2)	(Level 3)
Assets	(in millions)			
Cash equivalents				
Cash equivalents (a)	$1,214	$1,214	$—	$—
Commercial paper	260	—	260	—
Certificates of deposit	15	—	15	—
Short-term investments:				
Treasury bills	1,660	1,660	—	—
Certificates of deposit	244	—	244	—
Noncurrent investments (b)				
Auction rate securities	36	—	—	36
Interest rate derivatives (see Note 5)	22	—	22	—
Fuel derivatives:				
Swap contracts (c)	60	—	60	—
Option contracts (c)	119	—	—	119
Swap contracts (d)	3	—	3	—
Option contracts (d)	220	—	—	220
Other available-for-sale securities	55	50	—	5
Total assets	$3,908	$2,924	$604	$380
Liabilities				
Fuel derivatives:				
Swap contracts (c)	$(7)	$—	$(7)	$—
Option contracts (c)	(119)	—	—	(119)
Swap contracts (d)	(72)	—	(72)	—
Option contracts (d)	(296)	—	—	(296)
Interest rate derivatives (see Note 5)	(90)	—	(90)	—
Deferred compensation	(143)	(143)	—	—
Total liabilities	$(727)	$(143)	$(169)	$(415)

(a) Cash equivalents are primarily composed of money market investments.
(b) Noncurrent investments are included in Other assets in the unaudited Condensed Consolidated Balance Sheet.
(c) In the unaudited Condensed Consolidated Balance Sheet amounts are presented as a net asset, and are also net of cash collateral provided to counterparties. See Note 5.
(d) In the unaudited Condensed Consolidated Balance Sheet amounts are presented as a net liability, and are also net of cash collateral provided to counterparties. See Note 5.

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		Fair value measurements at reporting date using:		
Description	December 31, 2012	Quoted prices in active markets for identical assets (Level 1)	Significant other observable inputs (Level 2)	Significant unobservable inputs (Level 3)
Assets	(in millions)			
Cash equivalents				
Cash equivalents (a)	$829	$829	$—	$—
Commercial paper	170	—	170	—
Certificates of deposit	34	—	34	—
Eurodollar Time Deposits	80	—	80	—
Short-term investments:				
Treasury bills	1,624	1,624	—	—
Certificates of deposit	233	—	233	—
Noncurrent investments (b)				
Auction rate securities	36	—	—	36
Interest rate derivatives (see Note 5)	31	—	31	—
Fuel derivatives:				
Swap contracts (c)	113	—	113	—
Option contracts (c)	850	—	—	850
Option contracts (d)	10	—	—	10
Other available-for-sale securities	49	44	—	5
Total assets	$4,059	$2,497	$661	$901
Liabilities				
Fuel derivatives:				
Swap contracts (c)	$(57)	$—	$(57)	$—
Option contracts (c)	(637)	—	—	(637)
Swap contracts (d)	(56)	—	(56)	—
Option contracts (d)	(4)	—	—	(4)
Interest rate derivatives (see Note 5)	(126)	—	(126)	—
Deferred Compensation	(137)	(137)	—	—
Total liabilities	$(1,017)	$(137)	$(239)	$(641)

(a) Cash equivalents are primarily composed of money market investments.
(b) Noncurrent investments are included in Other assets in the unaudited Condensed Consolidated Balance Sheet.
(c) In the unaudited Condensed Consolidated Balance Sheet amounts are presented as a net asset. See Note 5.
(d) In the unaudited Condensed Consolidated Balance Sheet amounts are presented as a net liability. See Note 5.

The Company had no transfers of assets or liabilities between any of the above levels during the six months ended June 30, 2013, or the year ended December 31, 2012. The following tables present the Company’s activity for items measured at fair value on a recurring basis using significant unobservable inputs (Level 3) for the three and six months ended June 30, 2013:

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(in millions)	Fair value measurements using significant unobservable inputs (Level 3) Fuel derivatives	Auction rate securities	Other securities	Total
Balance at March 31, 2013	$199	$38	$5	$242
Total gains or (losses) (realized or unrealized)				
Included in earnings	(16)	—	—	(16)
Included in other comprehensive income	(299)	(2)	—	(301)
Purchases	86 (a)	—	—	86
Sales	(70) (a)	—	—	(70)
Settlements	24	—	—	24
Balance at June 30, 2013	$(76)	$36 (b)	$5	$(35)
The amount of total losses for the period included in earnings attributable to the change in unrealized gains or losses relating to assets still held at June 30, 2013	$(27)	$—	$—	$(27)

(a) The purchase and sale of fuel derivatives are recorded gross based on the structure of the derivative instrument and whether a contract with multiple derivatives is purchased as a single instrument or separate instruments.
(b) Included in Other assets in the unaudited Condensed Consolidated Balance Sheet.

(in millions)	Fair value measurements using significant unobservable inputs (Level 3) Fuel derivatives	Auction rate securities	Other securities	Total
Balance at December 31, 2012	$219	$36	$5	$260
Total gains or (losses) (realized or unrealized)				
Included in earnings	11	—	—	11
Included in other comprehensive income	(345)	—	—	(345)
Purchases	275 (a)	—	—	275
Sales	(283) (a)	—	—	(283)
Settlements	47	—	—	47
Balance at June 30, 2013	$(76)	$36 (b)	$5	$(35)
The amount of total losses for the period included in earnings attributable to the change in unrealized gains or losses relating to assets still held at June 30, 2013	$(74)	$—	$—	$(74)

(a) The purchase and sale of fuel derivatives are recorded gross based on the structure of the derivative instrument and whether a contract with multiple derivatives is purchased as a single instrument or separate instruments.
(b) Included in Other assets in the unaudited Condensed Consolidated Balance Sheet.

The significant unobservable input used in the fair value measurement of the Company's derivative option contracts is implied volatility. Holding other inputs constant, a significant increase (decrease) in implied volatility would result in a significantly higher (lower) fair value measurement, respectively, for the Company's derivative option contracts. The significant unobservable inputs used in the fair value measurement of the Company's auction rate securities are time to

principal recovery, an illiquidity premium, and counterparty credit spread. Holding other inputs constant, a significant increase (decrease) in such unobservable inputs would result in a significantly lower (higher) fair value measurement, respectively.

The following table presents a range of the unobservable inputs utilized in the fair value measurements of the Company's assets and liabilities classified as Level 3 at June 30, 2013:

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Quantitative information about Level 3 fair value measurements

	Valuation technique	Unobservable input	Period (by year)	Range
Fuel derivatives	Option model	Implied volatility	Third quarter 2013	12-26%
			Fourth quarter 2013	17-28%
			2014	16-28%
			2015	15-22%
			2016	16-21%
			2017	16-19%
Auction rate securities	Discounted cash flow	Time to principal recovery		5-8 years
		Illiquidity premium		3-4%
		Counterparty credit spread		1-3%

All settlements from fuel derivative contracts that are deemed "effective" are included in Fuel and oil expense in the period the underlying fuel is consumed in operations. Any "ineffectiveness" associated with hedges, including amounts that settled in the current period (realized), and amounts that will settle in future periods (unrealized), is recorded in earnings immediately as a component of Other (gains) losses, net. See Note 5 for further information on hedging. Any gains and losses (realized and unrealized) related to other investments are reported in Other operating expenses and were immaterial for the three and six months ended June 30, 2013 and 2012.

The carrying amounts and estimated fair values of the Company's long-term debt (including current maturities), as well as the applicable fair value hierarchy tier, at June 30, 2013, are presented in the table below. The fair values of the Company's publicly held long-term debt are determined based on inputs that are readily available in public markets or can be derived from information available in publicly quoted markets; therefore, the Company has categorized these agreements as Level 2. Six of the Company's debt agreements are not publicly held. The Company has determined the estimated fair value of this debt to be Level 3, as certain inputs used to determine the fair value of these agreements are unobservable. The Company utilizes indicative pricing from counterparties and a discounted cash flow method to estimate the fair value of the Level 3 items.

(in millions)	Carrying value	Estimated fair value	Fair value level hierarchy
5.25% Notes due 2014	362	376	Level 2
5.75% Notes due 2016	322	355	Level 2
5.25% Convertible Senior Notes due 2016	116	143	Level 2
5.125% Notes due 2017	326	347	Level 2
Fixed-rate 717 Aircraft Notes payable through 2017 - 10.38%	56	54	Level 2
French Credit Agreements due 2018 - 1.12%	51	51	Level 3
Fixed-rate 737 Aircraft Notes payable through 2018 - 7.02%	33	34	Level 3
Term Loan Agreement due 2019 - 6.315%	226	228	Level 3
Term Loan Agreement due 2019 - 6.84%	90	96	Level 3
Term Loan Agreement due 2020 - 5.223%	432	402	Level 3
Floating-rate 737 Aircraft Notes payable through 2020	359	352	Level 3
Pass Through Certificates due 2022 - 6.24%	385	440	Level 2
7.375% Debentures due 2027	137	145	Level 2

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

Relevant comparative operating statistics for the three and six months ended June 30, 2013 and 2012 are included below. The Company provides these operating statistics because they are commonly used in the airline industry and, as such, allow readers to compare the Company’s performance against its results for the prior year period, as well as against the performance of the Company’s peers.

	Three months ended June 30,		
	2013	2012	Change
Revenue passengers carried	28,960,367	28,859,348	0.4 %
Enplaned passengers	35,530,779	35,210,151	0.9 %
Revenue passenger miles (RPMs) (000s)(1)	27,929,506	27,206,498	2.7 %
Available seat miles (ASMs) (000s)(2)	34,231,243	33,230,589	3.0 %
Load factor(3)	81.6 %	81.9 %	(0.3) pts
Average length of passenger haul (miles)	964	943	2.2 %
Average aircraft stage length (miles)	708	699	1.3 %
Trips flown	343,592	352,726	(2.6)%
Average passenger fare	151.23	150.65	0.4 %
Passenger revenue yield per RPM (cents)(4)	15.68	15.98	(1.9)%
Operating revenue per ASM (cents)(5)	13.56	13.89	(2.4)%
Passenger revenue per ASM (cents)(6)	12.79	13.08	(2.2)%
Operating expenses per ASM (cents)(7)	12.30	12.51	(1.7)%
Operating expenses per ASM, excluding fuel (cents)	7.95	7.76	2.4 %
Operating expenses per ASM, excluding fuel and profitsharing (cents)	7.72	7.54	2.4 %
Fuel costs per gallon, including fuel tax	3.11	3.25	(4.3)%
Fuel costs per gallon, including fuel tax, economic	3.06	3.22	(5.0)%
Fuel consumed, in gallons (millions)	478	483	(1.0)%
Active fulltime equivalent Employees	45,216	46,128	(2.0)%
Aircraft in service at period-end(8)	696	695	0.1 %

	Six months ended June 30,			
	2013	2012	Change	
Revenue passengers carried	54,164,301	54,420,170	(0.5	)%
Enplaned passengers	66,243,404	66,364,573	(0.2	)%
Revenue passenger miles (RPMs) (000s)(1)	51,686,249	50,891,364	1.6	%
Available seat miles (ASMs) (000s)(2)	65,032,668	63,863,482	1.8	%
Load factor(3)	79.5 %	79.7 %	(0.2	) pts
Average length of passenger haul (miles)	954	935	2.0	%
Average aircraft stage length (miles)	701	692	1.3	%
Trips flown	662,106	686,622	(3.6	)%
Average passenger fare	151.73	148.80	2.0	%
Passenger revenue yield per RPM (cents)(4)	15.90	15.91	(0.1	)%
Operating revenue per ASM (cents)(5)	13.42	13.48	(0.4	)%
Passenger revenue per ASM (cents)(6)	12.64	12.68	(0.3	)%
Operating expenses per ASM (cents)(7)	12.65	12.72	(0.6	)%
Operating expenses per ASM, excluding fuel (cents)	8.12	7.89	2.9	%
Operating expenses per ASM, excluding fuel and profitsharing (cents)	7.98	7.78	2.6	%
Fuel costs per gallon, including fuel tax	3.23	3.32	(2.7	)%
Fuel costs per gallon, including fuel tax, economic	3.17	3.33	(4.8	)%
Fuel consumed, in gallons (millions)	910	926	(1.7	)%
Active fulltime equivalent Employees	45,216	46,128	(2.0	)%
Aircraft in service at period-end(8)	696	695	0.1	%

(1) A revenue passenger mile is one paying passenger flown one mile. Also referred to as "traffic," which is a measure of demand for a given period.
(2) An available seat mile is one seat (empty or full) flown one mile. Also referred to as "capacity," which is a measure of the space available to carry passengers in a given period.
(3) Revenue passenger miles divided by available seat miles.
(4) Calculated as passenger revenue divided by revenue passenger miles. Also referred to as "yield," this is the average cost paid by a paying passenger to fly one mile, which is a measure of revenue production and fares.
(5) Calculated as operating revenue divided by available seat miles. Also referred to as "operating unit revenues," this is a measure of operating revenue production based on the total available seat miles flown during a particular period.
(6) Calculated as passenger revenue divided by available seat miles. Also referred to as “passenger unit revenues,” this is a measure of passenger revenue production based on the total available seat miles flown during a particular period.
(7) Calculated as operating expenses divided by available seat miles. Also referred to as "unit costs" or "cost per available seat mile," this is the average cost to fly an aircraft seat (empty or full) one mile, which is a measure of cost efficiencies.
(8) Includes leased aircraft and excludes aircraft that are not available for service or are held in storage, for sale, or for return to the lessor.

Reconciliation of Reported Amounts to non-GAAP Financial Measures (unaudited) (in millions, except per share and per ASM amounts)

	Three months ended June 30,		Percent	Six months ended June 30,		Percent
	2013	2012	Change	2013	2012	Change
Fuel and oil expense, unhedged	$1,442	$1,544		$2,847	$3,022	
Add: Fuel hedge losses included in Fuel and oil expense	47	33		99	65	
Fuel and oil expense, as reported	$1,489	$1,577		$2,946	$3,087	
Add (Deduct): Net impact from fuel contracts	(20)	(14)		(49)	10	
Fuel and oil expense, non-GAAP	$1,469	$1,563	(6.0)	$2,897	$3,097	(6.5)
Total operating expenses, as reported	$4,210	$4,156		$8,224	$8,125	
Add (Deduct): Reclassification between Fuel and oil and Other (gains) losses, net, associated with current period settled contracts	7	(10)		7	(12)	
Add (Deduct): Contracts settling in the current period, but for which gains and/or (losses) have been recognized in a prior period*	(27)	(4)		(56)	22	
Deduct: Acquisition and integration costs	(26)	(11)		(39)	(24)	
Total operating expenses, non-GAAP	$4,164	$4,131	0.8	$8,136	$8,111	0.3
Operating income, as reported	$433	$460		$503	$481	
Add (Deduct): Reclassification between Fuel and oil and Other (gains) losses, net, associated with current period settled contracts	(7)	10		(7)	12	
Add (Deduct): Contracts settling in the current period, but for which gains and/or (losses) have been recognized in a prior period*	27	4		56	(22)	
Add: Acquisition and integration costs	26	11		39	24	
Operating income, non-GAAP	$479	$485	(1.2)	$591	$495	19.4
Net income, as reported	$224	$228		$283	$327	
Add (Deduct): Mark-to-market impact from fuel contracts settling in future periods	25	50		(35)	(156)	
Add: Ineffectiveness from fuel hedges settling in future periods	3	8		12	39	
Add (Deduct): Other net impact of fuel contracts settling in the current or a prior period (excluding reclassifications)	27	4		56	(22)	
Add (Deduct): Income tax impact of fuel contracts	(21)	(24)		(12)	52	

Add: Acquisition and integration costs, net (a)	16	7		24	15	
Net income, non-GAAP	$274	$273	0.4	$328	$255	28.6
Net income per share, diluted, as reported	$0.31	$0.30		$0.39	$0.43	
Add (Deduct): Net impact to net income above from fuel contracts divided by dilutive shares	0.05	0.05		0.03	(0.12)	
Add: Impact of special items, net (a)	0.02	0.01		0.03	0.02	
Net income per share, diluted, non-GAAP	$0.38	$0.36	5.6	$0.45	$0.33	36.4
Operating expenses per ASM (cents)	12.30	12.51		12.65	12.72	
Deduct: Fuel expense divided by ASMs	(4.35)	(4.75)		(4.53)	(4.83)	
Deduct: Impact of special items	(0.08)	(0.03)		(0.06)	(0.04)	
Operating expenses per ASM, non-GAAP, excluding fuel and special items (cents)	7.87	7.73	1.8	8.06	7.85	2.7

* As a result of prior hedge ineffectiveness and/or contracts marked to market through earnings.

(a) Amounts net of tax.

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Note Regarding Use of Non-GAAP Financial Measures

The Company's unaudited Condensed Consolidated Financial Statements are prepared in accordance with GAAP. These GAAP financial statements include (i) unrealized non-cash adjustments and reclassifications, which can be significant, as a result of accounting requirements and elections made under accounting pronouncements relating to derivative instruments and hedging and (ii) other charges the Company believes are not indicative of its ongoing operational performance.

As a result, the Company also provides financial information in this filing that was not prepared in accordance with GAAP and should not be considered as an alternative to the information prepared in accordance with GAAP. The Company provides supplemental non-GAAP financial information, including results that it refers to as "economic," which the Company's management utilizes to evaluate its ongoing financial performance and the Company believes provides greater transparency to investors as supplemental information to its GAAP results. The Company's economic financial results differ from GAAP results in that they only include the actual cash settlements from fuel hedge contracts - all reflected within Fuel and oil expense in the period of settlement. Thus, Fuel and oil expense on an economic basis reflects the Company’s actual net cash outlays for fuel during the applicable period, inclusive of settled fuel derivative contracts. Any net premium costs paid related to option contracts are reflected as a component of Other (gains) losses, net, for both GAAP and non-GAAP (including economic) purposes in the period of contract settlement. The Company believes these economic results provide a better measure of the impact of the Company's fuel hedges on its operating performance and liquidity since they exclude the unrealized, non-cash adjustments and reclassifications that are recorded in GAAP results in accordance with accounting guidance relating to derivative instruments, and they reflect all cash settlements related to fuel derivative contracts within Fuel and oil expense. This enables the Company's management, as well as investors, to consistently assess the Company's operating performance on a year-over-year or quarter-over-quarter basis after considering all efforts in place to manage fuel expense. However, because these measures are not determined in accordance with GAAP, such measures are susceptible to varying calculations and not all companies calculate the measures in the same manner. As a result, the aforementioned measures, as presented, may not be directly comparable to similarly titled measures presented by other companies.

Further information on (i) the Company's fuel hedging program, (ii) the requirements of accounting for derivative instruments, and (iii) the causes of hedge ineffectiveness and/or mark-to-market gains or losses from derivative instruments is included in the Company’s Annual Report on Form 10-K for the fiscal year ended December 31, 2012, and Note 5 to the unaudited Condensed Consolidated Financial Statements.

In addition to its “economic” financial measures, as defined above, the Company has also provided other non-GAAP financial measures, including results that it refers to as "excluding special items," as a result of items that the Company believes are not indicative of its ongoing operations. These include expenses associated with the Company’s acquisition and integration of AirTran. The Company believes that evaluation of its financial performance can be enhanced by a presentation of results that exclude the impact of these items in order to evaluate the results on a comparative basis with results in prior periods that do not include such items and as a basis for evaluating operating results in future periods. As a result of the Company’s acquisition of AirTran, which closed on May 2, 2011, the Company has incurred and expects to continue to incur substantial charges associated with integration of the two companies. While the Company cannot predict the exact timing or amounts of such charges, it does expect to treat these charges as special items in its future presentation of non-GAAP results. See Note 2 and Note 8 to the unaudited Condensed Consolidated Financial Statements for further information on the AirTran acquisition.

Material Changes in Results of Operations

Overview

The Company recorded second quarter and year to date GAAP and non-GAAP results for 2013 and 2012 as follows:

(in millions, except per share amounts)	Three months ended June 30,			Six months ended June 30,		
GAAP	2013	2012	Percent Change	2013	2012	Percent Change
Operating income	433	460	(5.9)	$503	$481	4.6
Net income	$224	$228	(1.8)	$283	$327	(13.5)
Net income per share, diluted	0.31	0.30	3.3	0.39	0.43	(9.3)
Non-GAAP						
Operating income	479	485	(1.2)	$591	$495	19.4
Net income	$274	$273	0.4	$328	$255	28.6
Net income per share, diluted	0.38	0.36	5.6	0.45	0.33	36.4

See the previous Note Regarding Use of Non-GAAP Financial Measures.

The Company's GAAP results for both the three and six months ended June 30, 2013 and 2012 were significantly impacted by the non-cash adjustments recorded as a result of the Company's portfolio of future derivative contracts utilized to hedge against jet fuel price volatility, as well as acquisition and integration costs associated with the Company's 2011 acquisition of AirTran. See Note 5 to the unaudited Condensed Consolidated Financial Statements for further information on fuel hedging and Note 2 for further information on the acquisition of AirTran. Excluding the impact of these items, the Company's net income on a non-GAAP basis for the second quarter of 2013 increased slightly versus the same period of 2012 to a Company record $274 million. For the six months ended June 30, 2013, also on a non-GAAP basis, the Company's net income increased 29 percent compared to the same prior year period, due primarily to a combination of higher passenger revenues and lower fuel costs.
The Company continued to make progress in second quarter 2013 on its five major strategic initiatives, which include:

1. The complete integration of AirTran into Southwest's operations by the end of 2014;
2. The continued growth of Southwest's Rapid Rewards frequent flyer program;
3. The continued addition of the Boeing 737-800, a larger aircraft, within the Company's fleet;
4. The modernization of the Company's entire fleet to produce both better revenue and cost efficiencies; and
5. The design and building of a new reservations system and international capabilities.

The Company reached a major milestone by completing the connection of the Southwest and AirTran networks during second quarter 2013. As of April 14th, Customers can now fly between any of the combined 97 Southwest and AirTran destinations on a single itinerary. During second quarter 2013, the Company also completed the conversion of five additional AirTran cities to the Southwest network-Charlotte, North Carolina; Rochester, New York; Flint, Michigan; Portland, Maine; and Wichita, Kansas. Also, on April 14, 2013, Southwest began daily service to San Juan, Puerto Rico, from Orlando and Tampa Bay, Florida, Southwest's first scheduled service outside of the continental United States. These flights are in addition to AirTran's existing service between San Juan and Atlanta, Georgia, Baltimore/Washington, and Fort Lauderdale/Hollywood, Florida. With respect to its AirTran integration initiative, the Company is experiencing substantial financial benefits associated with the recent connection of the Southwest and AirTran networks. The Company estimates it achieved approximately $95 million in net synergies during second quarter 2013, and continues to make progress towards its goal of producing approximately $400 million in total annualized net synergies from the AirTran acquisition by the end of 2013.

One of the next large phases of the Company's integration effort will be to optimize its operations in Atlanta in the fall of 2013. The Company will be transitioning Atlanta to a point-to-point operation, similar to other large Southwest cities, which is expected to enable efficiencies related to the scheduling of aircraft, flight crews, and ground staff.
The Company added three more of the larger 737-800 aircraft to its active fleet during the second quarter of 2013. The 737-800 aircraft provides both improved revenue opportunities and operational flexibility. As of June 30, 2013, the Company's fleet included 43 of the 737-800s, all of which have been placed in service over the last 15 months. During second quarter of 2013, the Company also continued to modernize its fleet through (i) the lease of one additional used 737-700 from a third party which is currently expected to enter active service during third quarter 2013, (ii) the retirement of two older Boeing 737-300s from the Company's fleet, (iii) the transition of one Boeing 717-200 out of active service as part of the Company's lease/sublease agreement with Delta, (iv) the retrofit of an additional 44 Southwest 737-700s with the Company's new Evolve interior, which completed the retrofitting of the Southwest 737-700 fleet, and (v) the retrofit of 14 of the planned 78 737-300 aircraft with the Company's new Evolve interior, with the remaining 64 expected to be completed in late 2013. The Company also converted one AirTran 737-700 to the Southwest livery during the second quarter of 2013.
The Company also continues to return significant value to its Shareholders. During second quarter 2013, the Company announced and completed an accelerated share repurchase program for approximately $251 million, or approximately 18 million shares, which brings total share repurchases during the first six months of 2013 to approximately $351 million, or approximately 27 million shares. The accelerated share repurchase was part of a total share repurchase authorization of $1.5 billion, of which approximately $975 million, or approximately 100 million shares, has now been completed in aggregate. During second quarter 2013, the Company's Board of Directors also authorized a four-fold increase in the Company's quarterly common stock dividend, from $.01 per share to $.04 per share. On an annualized basis, this new dividend amount provides an approximate $100 million return to Shareholders.
At the current time, the Company plans to continue its route network and schedule optimization efforts, but does not intend to grow its overall fleet size for 2013. During the second half of 2013, the Company currently expects to receive an additional nine new 737-800 aircraft from Boeing. During 2013, the Company also expects to continue to retire some of its older 737-300 and 737-500 aircraft, and transition a number of 717-200 aircraft out of the fleet as part of the Company's lease/sublease agreement with Delta. See Note 8 to the unaudited Condensed Consolidated Financial Statements. The Company currently expects 2013 ASMs to increase a modest two percent compared to ASMs flown during 2012 as a result of larger gauge aircraft. For 2014, the Company currently plans to keep its capacity in line with 2013 as it continues to optimize its network and execute on its strategic plan.
Comparison of three months ended June 30, 2013 to three months ended June 30, 2012

Operating Revenues

Operating revenues for second quarter 2013 increased by $27 million, or 0.6 percent, compared to second quarter 2012. The majority of the increase was due to a $33 million, or 0.8 percent, increase in Passenger revenues. The Company believes the lingering effects of government sequestration and higher taxes continued to be a drag on year-over-year revenue trends. In addition, the Company has a greater number of markets under development as the Company is in the midst of integrating AirTran, launching new city-pairs, and optimizing the combined networks. However, second quarter revenues and passenger traffic still reached Company record levels. The Company maintained strong load factors and ended the quarter with a record June load factor of 85.0 percent, which is notable considering the increasing mix of larger gauge 737-800 aircraft and Evolve -700 aircraft. The Company's addition of the larger gauge 737-800 aircraft over the past 15 months as well as the increased seat density created by the additional seats added to the Company's fleet from Evolve retrofits were contributing factors to the 2.4 percent year-over-year decline in unit revenues. However, as a result of the improvement in unit costs from the increased seating capacity, the Company believes these initiatives had a net positive impact to its second quarter operating results. Despite the 2.4 percent year-over-year decline in second quarter unit revenues, trends improved throughout the quarter. Third quarter 2013 revenue trends are encouraging thus far. July unit revenues are above last year's July, benefiting from the connection of the Southwest and AirTran networks and the Company's continued network

optimization, current bookings for the remainder of the third quarter also look solid.

During second quarter 2013, Southwest announced its implementation of a No Show policy that applies to nonrefundable fares that are not canceled or changed by a Customer at least ten minutes prior to a flight's scheduled departure. If a Customer has booked a nonrefundable fare anywhere in his/her itinerary and that portion of the flight is not used and not canceled or changed by the Customer at least ten minutes prior to scheduled departure, all unused funds on the full itinerary will be lost, and the remaining reservation will be canceled. The policy applies to reservations made or changed on or after Friday, May 10, 2013, for travel on or after Friday, September 13, 2013. This policy does not apply to military fares, senior fares, or travel during certain irregular operations, including severe weather conditions. The No Show policy will not impact Customers who simply cancel a Wanna Get Away® or DING!® fare at least ten minutes prior to scheduled departure; in this case, Customers may reuse their funds toward future travel on Southwest, without a change fee, as they have always done. Customers who are traveling on a fully refundable itinerary that does not contain a Wanna Get Away or DING! fare will continue to have the option of either requesting a refund or holding funds for future travel. Based on the Company's revenue recognition policy, revenue would be recorded at the flight date for a Customer that does not change his/her itinerary and loses their funds. The Company is unable to estimate the impact of this change in policy on future Passenger revenues at the current time. Freight revenues for second quarter 2013 increased by $1 million, or 2.4 percent, compared to second quarter 2012, primarily due to an increase in rates charged versus second quarter 2012. Other revenues for second quarter 2013 decreased by $7 million, or 3.1 percent, compared to second quarter 2012, primarily due to a decline in ancillary revenues. The majority of the decline in ancillary revenues was due to the conversion of AirTran aircraft into the Southwest livery and the adoption of Southwest fee policies for a larger portion of Customers. The Company currently expects such trend to continue as the integration process continues, and intends, upon full integration of AirTran, to have a consistent product offering. Based on current trends, the Company expects third quarter 2013 Freight and Other revenues will decrease from third quarter 2012.

Operating expenses

Operating expenses for second quarter 2013 increased by $54 million, or 1.3 percent, compared to second quarter 2012, while capacity increased 3.0 percent over the same prior year period. Historically, except for changes in the price of fuel, changes in Operating expenses for airlines are largely driven by changes in capacity, or ASMs. The following table presents the Company's Operating expenses per ASM for the second quarters of 2013 and 2012, followed by explanations of these changes on a per-ASM basis and/or on a dollar basis:

(in cents, except for percentages)	Three months ended June 30, 2013		2012		Per-ASM change		Percent change	
Salaries, wages, and benefits	3.79	¢	3.68	¢	0.11	¢	3.0	%
Fuel and oil	4.35		4.75		(0.40	)	(8.4	)
Maintenance materials and repairs	0.82		0.87		(0.05	)	(5.7	)
Aircraft rentals	0.27		0.27		—		—	
Landing fees and other rentals	0.85		0.78		0.07		9.0	
Depreciation and amortization	0.62		0.61		0.01		1.6	
Acquisition and integration	0.08		0.03		0.05		166.7	
Other operating expenses	1.52		1.52		—		—	
Total	12.30	¢	12.51	¢	(0.21	)¢	(1.7	)%

On a dollar basis, Operating expenses increased by 1.3 percent for second quarter 2013 compared to second quarter 2012, primarily due to higher Salaries, wages, and benefits expenses and higher Landing fees and other rentals, but were largely offset by lower fuel costs. Operating expenses per ASM (unit costs) for second quarter 2013 decreased 1.7 percent compared to second quarter 2012, primarily due to a decrease in Fuel and oil expense. On a non-GAAP basis, the Company's second quarter 2013 Operating expenses per ASM, excluding fuel and special items, increased

1.8 percent compared to second quarter 2012, primarily due to higher Salaries, wages, and benefits expenses. Based

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on current cost trends and benefits from our fleet modernization efforts, the Company expects third quarter 2013 unit costs, excluding fuel, special items, and profitsharing, to increase slightly from third quarter 2012's 7.72 cents. See the previous Note Regarding Use of Non-GAAP Financial Measures.

Salaries, wages, and benefits expense for second quarter 2013 increased by $76 million, or 6.2 percent, compared to second quarter 2012. Salaries, wages, and benefits expense per ASM for second quarter 2013 increased 3.0 percent compared to second quarter 2012. On both a dollar and a per ASM basis, approximately 40 percent of the increase was a result of higher contractual wage rates for a large portion of the Company's unionized workforce compared to second quarter 2012. The remainder of the increase was due to a variety of smaller items, including additional headcount associated with more Boeing 737-800s added to the Company's fleet over the past 12 months, as those are larger gauge aircraft which require the presence of a fourth flight attendant for each trip, and additional flight crew training costs incurred in preparation for future Southwest overwater and international flights. Based on current cost trends and anticipated capacity, the Company expects Salaries, wages, and benefits expense per ASM in third quarter 2013, excluding profitsharing, to be comparable to second quarter 2013's Salaries, wages, and benefits expense per ASM, excluding profitsharing.

Fuel and oil expense for second quarter 2013 decreased by $88 million, or 5.6 percent, compared to second quarter 2012. On a per-ASM basis, second quarter 2013 Fuel and oil expense decreased 8.4 percent versus second quarter 2012. Excluding the impact of hedging in both periods, both the nominal dollar and unit cost decreases were attributable to a lower fuel cost per gallon and to better efficiency. Approximately 80 percent of the dollar change was attributable to a lower fuel cost per gallon, and approximately 20 percent was related to better fuel efficiency. The Company's average economic jet fuel cost per gallon, including fuel tax, decreased 5.0 percent on a year-over-year basis, from $3.22 in second quarter 2012 to $3.06 in second quarter 2013. In addition, fuel gallons consumed decreased 1.0 percent compared to second quarter 2012, while year-over-year capacity increased 3.0 percent. The improvement in fuel efficiency was primarily due to the Company's continued replacement of older Classic (737-300s and 737-500s) aircraft with new Next Generation 737s. As a result of the Company's fuel hedging program and inclusive of accounting for derivatives and hedging, the Company recognized net losses totaling $47 million in second quarter 2013 in Fuel and oil expense relating to fuel derivative instruments versus net losses totaling $33 million recognized in Fuel and oil expense in second quarter 2012. These totals are inclusive of cash settlements realized from the expiration/settlement of fuel derivatives, which were $27 million paid to counterparties in second quarter 2013 versus $19 million paid to counterparties in second quarter 2012. These totals exclude gains and/or losses recognized from hedge ineffectiveness and from derivatives that do not qualify for hedge accounting, which impacts are recorded as a component of Other (gains) losses, net. See Note 5 to the unaudited Condensed Consolidated Financial Statements.

As of July 22, 2013, on an economic basis, the Company had derivative contracts in place related to expected future fuel consumption as follows:

Period	Average percent of estimated fuel consumption covered by fuel derivative contracts at varying WTI/Brent crude-equivalent price levels
Second half 2013	Approx. 80% to 85%
2014	Approx. 35%
2015	Approx. 35%
2016	Approx. 30%
2017	Approx. 50%

As a result of applying hedge accounting in prior periods the Company has amounts “frozen” in Accumulated other comprehensive income (loss) (“AOCI”), and these amounts will be recognized in earnings in future periods when the

underlying fuel derivative contracts settle. The following table displays the Company's estimated fair value of remaining fuel derivative contracts (not considering the impact of the cash collateral provided to or received from counterparties- See Note 5 to the unaudited Condensed Consolidated Financial Statements for further information), as well as the

amount of deferred gains/losses in AOCI at June 30, 2013, and the expected future periods in which these items are expected to settle and/or be recognized in earnings (in millions):

Year	Fair value (liability) of fuel derivative contracts at June 30, 2013	Amount of gains (losses) deferred in AOCI at June 30, 2013 (net of tax)
Remainder of 2013	$(93)	$(93)
2014	50	(18)
2015	(9)	(71)
2016	16	(24)
2017	(56)	(13)
Total	$(92)	$(219)

Based on forward market prices and the amounts in the above table (and excluding any other subsequent changes to the fuel hedge portfolio), the Company's jet fuel costs per gallon could exceed market (i.e., unhedged) prices during some of these future periods. This is based primarily on expected future cash settlements associated with fuel derivatives, but excludes any impact associated with the ineffectiveness of fuel hedges or fuel derivatives that are marked to market because they do not qualify for hedge accounting. See Note 5 to the unaudited Condensed Consolidated Financial Statements for further information. Assuming no changes to the Company's current fuel derivative portfolio, but including all previous hedge activity for fuel derivatives that have not yet settled, and considering only the expected net cash payments related to hedges that will settle, the Company is providing a sensitivity table for third quarter 2013, fourth quarter 2013, and full year 2013 jet fuel prices at different crude oil assumptions as of July 22, 2013, and for expected premium costs associated with settling contracts each period.

	Estimated economic jet fuel price per gallon, including taxes		
Average Brent Crude Oil price per barrel	3Q 2013 (2)	4Q 2013	Full Year 2013
$85	$2.85 - $2.90	$2.85 - $2.90	$3.00 - $3.05
$95	$2.90 - $2.95	$2.90 - $2.95	$3.05 - $3.10
Current Market (1)	$3.05 - $3.10	$3.05 - $3.10	$3.10 - $3.15
$115	$3.15 - $3.20	$3.25 - $3.30	$3.20 - $3.25
$125	$3.25 - $3.30	$3.35 - $3.40	$3.25 - $3.30
Estimated Premium Costs (3)	$22 million	$22 million	$60 million

(1) Brent crude oil average market prices as of July 22, 2013 were approximately $107 and $105 per barrel for third and fourth quarter 2013, respectively.
(2) The Company has approximately 80 percent of its third quarter 2013 estimated fuel consumption covered by fuel derivative contracts with approximately 70 percent at varying Gulf Coast jet fuel-equivalent prices and the remainder at varying Brent crude oil-equivalent prices. The Company has approximately 85 percent of its fourth quarter 2013 estimated fuel consumption covered by fuel derivative contracts with approximately 75 percent at varying Gulf Coast jet fuel-equivalent prices and the remainder at varying Brent crude oil-equivalent prices. The economic fuel price per gallon sensitivities provided above assume the relationship between Brent crude oil and refined products based on market prices as of July 22, 2013.
(3) Premium costs are recognized as a component of Other (gains) losses net.

Maintenance materials and repairs expense for second quarter 2013 decreased by $10 million, or 3.4 percent, compared to second quarter 2012. On a per-ASM basis, Maintenance materials and repairs expense for second quarter

2013 decreased 5.7 percent compared to second quarter 2012. These decreases were primarily attributable to fewer second quarter 2013 engine repairs associated with the Company's 737-300 and 737-500 fleet. The Company currently expects Maintenance materials and repairs expense per ASM for third quarter 2013 to be comparable to second quarter 2013 based on currently scheduled aircraft maintenance events.

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Aircraft rentals expense for second quarter 2013 increased by $2 million, or 2.2 percent, compared to second quarter 2012, primarily due to expense associated with five Boeing 737-800 aircraft received in the latter part of second quarter 2012 that are accounted for as operating leases. On a per-ASM basis compared to second quarter 2012, Aircraft rentals expense in second quarter 2013 was relatively flat. The Company currently expects Aircraft rentals expense per ASM for third quarter 2013 to be comparable to second quarter 2013.

Landing fees and other rentals expense for second quarter 2013 increased by $32 million, or 12.3 percent, compared to second quarter 2012. On a per-ASM basis compared to second quarter 2012, Landing fees and other rentals expense increased 9.0 percent. The majority of these increases were due to higher rental rates charged by several airports over the last twelve months, a portion of which was due to additional space occupied by the Company in some locations, and a portion of which was attributable to higher debt service costs passed through to the airlines in certain cities. The Company currently expects Landing fees and other rentals expense per ASM for third quarter 2013 to increase compared to third quarter 2012 as the escalation in airport costs is expected to be only partially offset by a year-over-year increase in ASMs.

Depreciation and amortization expense for second quarter 2013 increased by $11 million, or 5.4 percent, compared to second quarter 2012. On a per-ASM basis, Depreciation and amortization expense increased 1.6 percent compared to second quarter 2012. Both of these increases were primarily due to depreciation associated with large software projects that have been placed into service over the past twelve months. For third quarter 2013, the Company currently expects Depreciation and amortization expense per ASM to be comparable to third quarter 2012.

For second quarter 2013, the Company incurred $26 million of Acquisition and integration costs related to the acquisition of AirTran compared to $11 million in second quarter 2012. The second quarter 2013 costs primarily consisted of Employee training, technology integration projects, and facility integration expenses. See Note 2 to the unaudited Condensed Consolidated Financial Statements.

Other operating expenses for second quarter 2013 increased by $16 million, or 3.2 percent, compared to second quarter 2012. Approximately 30 percent of this increase was the result of increased winterization costs associated with late spring storms in early second quarter 2013, and approximately 30 percent was the result of costs associated with increased Customer usage of WiFi onboard the Company's 737-700 and 737-800 aircraft. The remainder of the increase was due to immaterial individual contributors. On a per-ASM basis, Other operating expenses were comparable to second quarter 2012. For third quarter 2013, the Company currently expects Other operating expenses per ASM to increase as compared to third quarter 2012.

Other

Other expenses (income) include interest expense, capitalized interest, interest income, and other gains and losses. Interest expense for second quarter 2013 decreased by $5 million, or 13.2 percent, compared to second quarter 2012, primarily due to the repayment of AirTran aircraft financing facilities during the first quarter of 2013. For third quarter 2013, the Company expects interest expense to be comparable to second quarter 2013 as a result of the repayment of this debt.

Other (gains) losses, net, primarily includes amounts recorded as a result of the Company's hedging activities. See Note 5 to the unaudited Condensed Consolidated Financial Statements for further information on the Company's hedging activities. The following table displays the components of Other (gains) losses, net, for the three months ended June 30, 2013 and 2012:

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(in millions)	Three months ended June 30, 2013	2012
Mark-to-market impact from fuel contracts settling in future periods	$25	$50
Ineffectiveness from fuel hedges settling in future periods	3	8
Realized ineffectiveness and mark-to-market (gains) or losses	7	(10)
Premium cost of fuel contracts	12	12
Other	—	2
	$47	$62

Income Taxes

The Company's effective tax rate was approximately 38.3 percent in second quarter 2013, compared to 38.0 percent in second quarter 2012. The Company currently projects a full year 2013 effective tax rate of approximately 38 to 40 percent based on currently forecasted financial results.

Comparison of six months ended June 30, 2013 to six months ended June 30, 2012

Operating Revenues

Operating revenues for the six months ended June 30, 2013, increased by $121 million, or 1.4 percent, compared to the first six months of 2012. The majority of the increase was due to a $121 million, or 1.5 percent, increase in Passenger revenues. The majority of the increase in Passenger revenues was attributable to a 1.8 percent increase in capacity, as both load factor and passenger yields remained relatively flat with the same prior year period. The Company's load factor for the six months ended June 30, 2013, was relatively flat compared to the first six months of 2012.

Freight revenues for the six months ended June 30, 2013, increased by $3 million, or 3.8 percent, compared to the first six months of 2012, primarily due to an increase in rates charged versus the prior year. Other revenues for the six months ended June 30, 2013, decreased by $3 million, or 0.7 percent, compared to the first six months of 2012, primarily due to a decline in ancillary revenues. The majority of the decline in ancillary revenues was due to the conversion of AirTran aircraft into Southwest and the adoption of Southwest fee policies for a larger portion of Customers.

Operating expenses

Operating expenses for the six months ended June 30, 2013, increased by $99 million, or 1.2 percent, compared to the first six months of 2012, while capacity increased 1.8 percent over the same prior year period. Historically, except for changes in the price of fuel, changes in Operating expenses for airlines are largely driven by changes in capacity, or ASMs. The following table presents the Company's Operating expenses per ASM for the first six months of 2013 and 2012, followed by explanations of these changes on a per-ASM basis and/or on a dollar basis:

(in cents, except for percentages)	Six months ended June 30, 2013	2012	Per-ASM change	Percent change
Salaries, wages, and benefits	3.81 ¢	3.70 ¢	0.11 ¢	3.0 %
Fuel and oil	4.53	4.83	(0.30)	(6.2)
Maintenance materials and repairs	0.88	0.88	—	—
Aircraft rentals	0.28	0.28	—	—
Landing fees and other rentals	0.86	0.80	0.06	7.5
Depreciation and amortization	0.65	0.63	0.02	3.2
Acquisition and integration	0.06	0.04	0.02	50.0
Other operating expenses	1.58	1.56	0.02	1.3
Total	12.65 ¢	12.72 ¢	(0.07)¢	(0.6)%

On a dollar basis, Operating expenses increased by 1.2 percent for the first six months of 2013 compared to the first six months of 2012, primarily due to higher Salaries, wages, and benefits expenses and higher Landing fees and other rentals, but were largely offset by lower fuel costs. Operating expenses per ASM (unit costs) for the first six months of 2013 decreased 0.6 percent compared to the first six months of 2012, primarily due to a decrease in Fuel and oil expense. On a non-GAAP basis, the Company's Operating expenses per ASM for the first six months of 2013, excluding fuel and special items, increased 2.7 percent compared to the first six months of 2012, primarily due to higher Salaries, wages, and benefits expenses. See the previous Note Regarding Use of Non-GAAP Financial Measures.

Salaries, wages, and benefits expense for the six months ended June 30, 2013, increased by $118 million, or 5.0 percent, compared to the six months ended June 30, 2012. Salaries, wages, and benefits expense per ASM for the first six months of 2013 increased 3.0 percent compared to the first six months of 2012. Approximately 65 percent of these increases were a result of higher contractual wage rates for a large portion of the Company's workforce compared to the six months ended June 30, 2012, and the majority of the remaining increases were a result of higher contributions to Employee retirement plans, including profitsharing and 401(k) matching contributions. The Company’s profitsharing expense is based on profits that exclude the unrealized gains and/or losses the Company records for its fuel hedging program as well as Acquisition and integration costs.

Fuel and oil expense for the six months ended June 30, 2013, decreased by $141 million, or 4.6 percent, compared to the six months ended June 30, 2012. On a per-ASM basis, for the first six months of 2013, Fuel and oil expense decreased 6.2 percent versus the first six months of 2012. Excluding the impact of hedging in both periods, both the nominal dollar and unit cost decreases were attributable to a lower fuel cost per gallon and to better efficiency. Approximately 70 percent of the dollar change was attributable to a lower fuel cost per gallon and approximately 25 percent was related to better fuel efficiency. The Company's average economic jet fuel cost per gallon, including fuel tax, decreased 4.8 percent on a year-over-year basis, from $3.33 during the six months ended June 30, 2012, to $3.17 during the six months ended June 30, 2013. In addition, fuel gallons consumed decreased 1.7 percent compared to the six months ended June 30, 2012, while year-over-year capacity increased 1.8 percent. The improvement in fuel efficiency was primarily due to the Company's continued replacement of older Classic (737-300s and 737-500s) aircraft with new Next Generation 737s including 28 of the larger gauge 737-800 aircraft added into service during the last twelve months. As a result of the Company's fuel hedging program and inclusive of accounting for derivatives and hedging, the Company recognized net losses totaling $99 million during the six months ended June 30, 2013 in Fuel and oil expense relating to fuel derivative instruments versus net losses totaling $64 million recognized in Fuel and oil expense in the six months ended June 30, 2012. These totals are inclusive of cash settlements realized from the expiration/settlement of fuel derivatives, which were $50 million paid to counterparties in the first six months of 2013, versus $74 million paid to counterparties in the first six months of 2012. These totals exclude gains and/or losses recognized from hedge ineffectiveness and from derivatives that do not qualify for hedge accounting, which impacts

are recorded as a component of Other (gains) losses, net. See Note 5 to the unaudited Condensed Consolidated Financial Statements.

Maintenance materials and repairs expense for the six months ended June 30, 2013, increased by $9 million, or 1.6 percent, compared to the six months ended June 30, 2012. This increase was primarily attributable to costs associated with the Company's Evolve aircraft interior retrofit program, which began in March 2012. On a per ASM basis compared to the six months ended June 30, 2012, Maintenance materials and repairs expense in the first six months of 2013 was relatively flat.

Aircraft rentals expense for the six months ended June 30, 2013, increased by $7 million, or 3.9 percent, compared to the six months ended June 30, 2012, primarily due to expense associated with five Boeing 737-800 aircraft received in the latter part of second quarter 2012 that are accounted for as operating leases. On a per-ASM basis compared to the six months ended June 30, 2012, Aircraft rentals expense in the first six months of 2013 was relatively flat.

Landing fees and other rentals expense for the six months ended June 30, 2013, increased by $45 million, or 8.8 percent, compared to the six months ended June 30, 2012. On a per-ASM basis, Landing fees and other rentals expense increased 7.5 percent compared to the six months ended June 30, 2012. The majority of these increases were due to higher rental rates charged by several airports over the last twelve months, a portion of which is due to additional space occupied by the Company in some locations, and a portion of which is attributable to higher debt service costs passed through to the airlines in certain cities.

Depreciation and amortization expense for the six months ended June 30, 2013, increased by $19 million, or 4.7 percent, compared to the six months ended June 30, 2012. Approximately 55 percent of this increase was due to depreciation associated with large software projects that have been placed into service over the past twelve months and approximately 40 percent was due to 28 737-800 aircraft being placed into service during the twelve months ended June 30, 2013. On a per-ASM basis, Depreciation and amortization expense increased 3.2 percent compared to the six months ended June 30, 2012, primarily due to depreciation associated with large software projects that have been placed into service over the past twelve months.

For the six months ended June 30, 2013, the Company incurred $39 million of Acquisition and integration costs related to the acquisition of AirTran compared to $24 million for the six months ended June 30, 2012. These 2013 costs primarily consisted of Employee training, technology integration projects, and facility integration expenses. See Note 2 to the unaudited Condensed Consolidated Financial Statements.

Other operating expenses for the six months ended June 30, 2013, increased by $27 million, or 2.7 percent, compared to the six months ended June 30, 2012, and increased 1.3 percent on a per-ASM basis compared to the six months ended June 30, 2012. Approximately 30 percent of these increases were the result of costs associated with increased Customer usage of WiFi onboard the Company's 737-700 and 737-800 aircraft and approximately 25 percent was the result of increased winterization costs at airports from more severe weather during the first six months of 2013 compared to the same period in 2012. The remainder of the increases was due to immaterial individual contributors.

Other

Other expenses (income) include interest expense, capitalized interest, interest income, and other gains and losses. Interest expense for the six months ended June 30, 2013, decreased by $15 million, or 19.5 percent, compared to the six months ended June 30, 2012, primarily due to the repayment of $385 million of 6.5% notes in March 2012.

Other (gains) losses, net, primarily includes amounts recorded as a result of the Company's hedging activities. See Note 5 to the unaudited Condensed Consolidated Financial Statements for further information on the Company's hedging activities. The following table displays the components of Other (gains) losses, net, for the the six months ended June 30, 2013 and 2012:

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	Six months ended June 30,	
(in millions)	2013	2012
Mark-to-market impact from fuel contracts settling in future periods	$(35)	$(156)
Ineffectiveness from fuel hedges settling in future periods	12	39
Realized ineffectiveness and mark-to-market (gains) or losses	7	(12)
Premium cost of fuel contracts	17	18
Other	—	2
	$1	$(109)

Income Taxes

The Company's effective tax rate was approximately 37.9 percent for the first six months of 2013, compared to 38.0 percent for the first six months of 2012.

Liquidity and Capital Resources

Net cash provided by operating activities was $778 million for the three months ended June 30, 2013, compared to $145 million provided by operating activities in the same prior year period. For the six months ended June 30, 2013, net cash provided by operating activities was $1.8 billion compared to $1.4 billion provided by operating activities in the first six months of 2012. The operating cash flows for the six months ended June 30, 2013, were largely impacted by the Company's results of operations (as adjusted for noncash depreciation and amortization expense), changes in Air traffic liability, and Accounts payable and accrued liabilities. For the six months ended June 30, 2013, in addition to the Company's net income (as adjusted for noncash depreciation and amortization expense), there was a $907 million increase in Air traffic liability, as a result of bookings for future travel and higher sales of points to business partners in the Company's frequent flyer program, and a net $282 million increase in cash flow associated with higher balances in Accounts payable and accrued liabilities due to timing of payments. For the six months ended June 30, 2012, there was a $693 million increase in Air traffic liability, as a result of bookings for future travel and a net $301 million increase in cash flow associated with higher balances in Accounts payable and accrued liabilities due to timing of payments. See Note 5 to the unaudited Condensed Consolidated Financial Statements for further information on the Company's derivatives and hedging activities. Net cash provided by operating activities is primarily used to finance capital expenditures, repay debt, and provide working capital.

Net cash used in investing activities during the three months ended June 30, 2013, totaled $300 million, versus $355 million used in investing activities in the same prior year period. For the six months ended June 30, 2013, net cash used in investing activities was $771 million compared to $368 million used in the same prior year period. Investing activities in both years included payments for new aircraft delivered to the Company and progress payments for future aircraft deliveries, as well as changes in the balance of the Company's short-term investments and noncurrent investments. During the six months ended June 30, 2013, the Company's transactions in short-term and noncurrent investments resulted in a net cash outflow of $44 million, versus a net cash inflow of $169 million during the same prior year period.

Net cash used in financing activities during the three months ended June 30, 2013, was $327 million, compared to $265 million used in financing activities for the same prior year period. For the six months ended June 30, 2013, net cash used in financing activities was $613 million compared to $748 million used in the same prior year period. During the six months ended June 30, 2013, the Company repaid $216 million in debt and capital lease obligations and repurchased approximately $351 million of its outstanding common stock through a share repurchase program. During the six months ended June 30, 2012, the Company repaid $469 million in debt and capital lease obligations that came due and repurchased approximately $275 million of its outstanding common stock through a share repurchase program.

The Company is a "well-known seasoned issuer" and currently has an effective shelf registration statement registering an indeterminate amount of debt and equity securities for future sales. The Company currently intends to use the

proceeds from any future securities sales off this shelf registration statement for general corporate purposes. The Company has not issued any securities under this shelf registration statement to date.

On April 2, 2013, the Company entered into a new $1 billion unsecured revolving credit facility expiring in April 2018, and terminated its previous facility, which would have expired in April 2016. Other than an increased borrowing capacity, this new facility is substantially the same as the previous facility. Interest on the facility is based on the Company's credit ratings at the time of borrowing. At the Company's current ratings, the interest cost would be LIBOR plus a spread of 150 basis points. The new facility also contains the same financial covenant as the previous facility, requiring a minimum coverage ratio of adjusted pre-tax income to fixed obligations, as defined. As of June 30, 2013, the Company was in compliance with this covenant and there were no amounts outstanding under the revolving credit facility.

Contractual Obligations and Contingent Liabilities and Commitments

The Company has contractual obligations and commitments primarily with regard to future purchases of aircraft, repayment of debt, and lease arrangements. During the six months ended June 30, 2013, the Company purchased nine new 737-800 aircraft from Boeing, and retired from service six of its older 737-300 and 737-500 aircraft and removed one of its 717-200 aircraft from active service. In addition, the Company also leased two 737-700 aircraft from a third party which were not yet placed into service as of June 30, 2013. During second quarter 2013, the Company announced modifications to its aircraft orders with Boeing and an agreement to purchase ten pre-owned 737-700 aircraft from a third party for delivery in 2014 and 2015. During July 2013, the Company entered into an agreement to lease two pre-owned 737-700 aircraft from a third party for delivery in 2014. The modifications with Boeing included the relinquishment of a total of ten options for Boeing Next Generation ("NG") aircraft, the exercise of five separate options for 737-800 aircraft, the conversion of five 737-700 firm orders to 737-800 deliveries, and the deferral and conversion of existing NG aircraft firm orders and options to 737 MAX options and firm orders in future years. The Company and Boeing also announced Southwest would be the launch Customer for the Boeing 737 MAX 7 series aircraft, with deliveries expected to begin in 2019. As of July 24, 2013, the Company had scheduled deliveries for Boeing 737-700, 737-800, 737 MAX 7, and 737 MAX 8 aircraft as follows:

	The Boeing Company 737 NG				The Boeing Company 737 MAX				
	-700 Firm Orders	-800 Firm Orders	Options	Additional -700 A/C	-7 Firm Orders	-8 Firm Orders	Options	Total	
2013	—	18	—	2	—	—	—	20	(3)
2014	—	36	—	7	—	—	—	43	
2015	36	—	—	5	—	—	—	41	
2016	31	—	12	—	—	—	—	43	
2017	15	—	12	—	—	14	—	41	
2018	10	—	12	—	—	13	—	35	
2019	—	—	—	—	15	10	—	25	
2020	—	—	—	—	14	22	—	36	
2021	—	—	—	—	1	33	18	52	
2022	—	—	—	—	—	30	19	49	
2023	—	—	—	—	—	14	23	37	
2024	—	—	—	—	—	14	23	37	
2025	—	—	—	—	—	—	36	36	
Through 2027	—	—	—	—	—	—	72	72	

Total	92 (1)	54	36	14	30	150 (2)	191	567

(1) The Company has flexibility to substitute 737-800s in lieu of 737-700 firm orders.

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(2) The Company has flexibility to substitute MAX 7 in lieu of MAX 8 firm orders beginning in 2019.
(3) Includes nine 737-800s and two leased 737-700s delivered through July 24, 2013.

The Company's financial commitments associated with the firm orders in the above aircraft table are as follows: $390 million remaining in 2013, $1.1 billion in 2014, $1.3 billion in 2015, $1.2 billion in 2016, $1.2 billion in 2017, and $7.0 billion thereafter.

For aircraft commitments with Boeing, the Company is required to make cash deposits towards the purchase of aircraft. These deposits are classified as Deposits on flight equipment purchase contracts in the unaudited Condensed Consolidated Balance Sheet until the aircraft is delivered, at which time deposits previously made are deducted from the final purchase price of the aircraft and are reclassified as Flight equipment.

The following table details information on the active aircraft in the Company's fleet that were in service as of June 30, 2013:

Type	Seats	Average Age (Yrs)	Number of Aircraft	Number Owned	Number Leased
717-200	117	12	87	8	79
737-300	137 or 143	20	123	75	48
737-500	122	22	19	10	9
737-700	137 or 143	9	424	379	45
737-800	175	1	43	38	5
TOTALS			696	510	186

The Company expects to incur no more than $550 million in Acquisition and integration costs associated with the AirTran acquisition, of which approximately $363 million has been recorded through June 30, 2013. These costs have been, and are expected to continue to be, funded with cash from operations. The Company believes that its current liquidity position, including unrestricted cash and short-term investments of $3.4 billion as of June 30, 2013, anticipated future internally generated funds from operations, and its fully available, unsecured revolving credit facility of $1 billion that expires in April 2018, will enable it to meet these future integration expenditures. However, if a liquidity need were to arise, the Company believes it has access to financing arrangements because of its current investment grade credit ratings, large value of unencumbered assets, and modest leverage, which should enable it to meet its ongoing capital, operating, and other liquidity requirements. The Company will continue to consider various borrowing or leasing options to maximize liquidity and supplement cash requirements as necessary.

In January 2008, the Company's Board of Directors authorized the repurchase of up to $500 million of the Company's common stock. Through February 15, 2008, the Company had repurchased 4.4 million shares for a total of approximately $54 million, at which time repurchases under the program were suspended. On August 5, 2011, the Company's Board of Directors authorized the Company to resume a share repurchase program and approved the Company's repurchase, on a discretionary basis, of a total of up to $500 million of the Company's common stock following such authorization. On May 16, 2012, the Company's Board of Directors increased the previous share repurchase authorization by $500 million. On May 15, 2013, the Company's Board of Directors further increased the previous share repurchase authorization by an additional $500 million to a total of $1.5 billion and, in a privately negotiated transaction, the Company entered into an agreement with a third party financial institution to repurchase $250 million of its common shares under an accelerated share repurchase program ("ASR Program") utilizing cash on hand. On May 15, 2013, pursuant to the ASR Program agreement, the Company advanced the $250 million to the financial institution and received approximately 17.9 million shares, which was recorded as a treasury share purchase for purposes of calculating earnings per share. The Company also made a $500 thousand additional payment to the third party financial institution under the terms of the agreement governing the ASR Program. The ASR Program was

completed on June 24, 2013, upon which a settlement of approximately 158 thousand shares were delivered to the Company. The final number of shares delivered upon settlement was determined based on a discount to the volume-weighted average price of the Company's common stock over the term of the ASR Program. Including purchases

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made under the ASR Program, the Company's cumulative purchases under all Board-authorized repurchases since the August 2011 authorization have totaled approximately 100 million shares for approximately $975 million of the $1.5 billion in total authorized by the Board.

Cautionary Statement Regarding Forward-Looking Statements

This Form 10-Q contains “forward-looking statements” within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934. Forward-looking statements are based on, and include statements about, the Company's estimates, expectations, beliefs, intentions, and strategies for the future, and the assumptions underlying these forward-looking statements. Specific forward-looking statements can be identified by the fact that they do not relate strictly to historical or current facts and include, without limitation, statements related to the following:

- the Company's strategic initiatives and related financial and operational goals and expectations;
- the integration of AirTran and the Company's related financial and operational goals and expectations, including, without limitation, anticipated integration timeframes and expected benefits and costs associated with the integration;
- the Company's network plans, opportunities, and expectations;
- the Company's fleet plans, including its fleet modernization and capacity plans and expectations;
- the Company's financial outlook and projected results of operations;
- the Company's plans and expectations with respect to managing risk associated with changing jet fuel prices;
- the Company's expectations with respect to liquidity and capital expenditures, including anticipated needs for, and sources of, funds;
- the Company's assessment of market risks; and
- the Company's plans and expectations related to legal proceedings.

While management believes these forward-looking statements are reasonable as and when made, forward-looking statements are not guarantees of future performance and involve risks and uncertainties that are difficult to predict. Therefore, actual results may differ materially from what is expressed in or indicated by the Company's forward-looking statements or from historical experience or the Company's present expectations. Factors that could cause these differences include, among others:

- demand for the Company's services and the impact of fuel prices and availability, economic conditions, and actions of competitors (including, without limitation, pricing, scheduling, and capacity decisions and consolidation and alliance activities) on the Company's business decisions, plans, and strategies;
- the Company's ability to effectively integrate AirTran and realize the expected synergies and other benefits from the acquisition;
- the Company's ability to timely and effectively implement, transition, and maintain the necessary information technology systems and infrastructure to support its operations and initiatives;
- the Company's ability to timely and effectively prioritize its strategic initiatives and related expenditures;
- changes in the price of aircraft fuel, the impact of hedge accounting, and any changes to the Company's fuel hedging strategies and positions;
- the Company's dependence on third parties with respect to certain of its initiatives, in particular its fleet plans;
- the impact of governmental action related to the Company's operations; and
- other factors as set forth in the Company's filings with the Securities and Exchange Commission, including the detailed factors discussed under the heading “Risk Factors” in the Company's Annual Report on Form 10-K for the year ended December 31, 2012.

Caution should be taken not to place undue reliance on the Company's forward-looking statements, which represent the Company's views only as of the date this report is filed. The Company undertakes no obligation to update

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publicly or revise any forward-looking statement, whether as a result of new information, future events or otherwise.

Item 3. Quantitative and Qualitative Disclosures About Market Risk

As discussed in Note 5 to the unaudited Condensed Consolidated Financial Statements, the Company endeavors to acquire jet fuel at the lowest possible cost and to reduce volatility in operating expenses through its fuel hedging program with the use of financial derivative instruments. At June 30, 2013, the estimated fair value of outstanding contracts, excluding the impact of cash collateral provided to or held by counterparties, was a liability of $92 million.

The Company's credit exposure related to fuel derivative instruments is represented by the fair value of contracts that are an asset to the Company. At such times, these outstanding instruments expose the Company to credit loss in the event of nonperformance by the counterparties to the agreements. As of June 30, 2013, the Company had five counterparties with which the derivatives held were a net asset, totaling $40 million, and five counterparties with which the derivatives held were a net liability, totaling a net $132 million liability. To manage credit risk, the Company selects and periodically reviews counterparties based on credit ratings, limits its exposure with respect to each counterparty, and monitors the market position of the fuel hedging program and its relative market position with each counterparty. However, if one or more of these counterparties were in a liability position to the Company and were unable to meet their obligations, any open derivative contracts with the counterparty could be subject to early termination, which could result in substantial losses for the Company. At June 30, 2013, the Company had agreements with all of its active counterparties containing early termination rights and/or bilateral collateral provisions whereby security is required if market risk exposure exceeds a specified threshold amount based on the counterparty's credit rating. The Company also had agreements with counterparties in which cash deposits, letters of credit, and/or pledged aircraft are required to be posted whenever the net fair value of derivatives associated with those counterparties exceeds specific thresholds.

At June 30, 2013, $65 million in cash deposits and no letters of credit or aircraft collateral were provided by the Company based on its outstanding fuel derivative instrument portfolio. Due to the terms of the Company's current fuel hedging agreements with counterparties and the types of derivatives held, in the Company's judgment, it does not have significant additional exposure to future cash collateral requirements. As an example, if market prices for the commodities used in the Company's fuel hedging activities were to decrease by 25 percent from market prices as of June 30, 2013, given the Company's current fuel derivative portfolio, its aircraft collateral facilities, and its investment grade credit rating, it would likely provide an additional $666 million in cash collateral, post $644 million in aircraft collateral, and post $50 million in letters of credit against these positions with its current counterparties. However, the Company would expect to also benefit from lower market prices paid for fuel used in its operations. See Note 5 to the unaudited Condensed Consolidated Financial Statements.

The Company is also subject to the risk that the fuel derivatives it uses to hedge against fuel price volatility do not provide adequate protection. A portion of the fuel derivatives in the Company's hedge portfolio are based on the market price of West Texas intermediate crude oil ("WTI"). In some periods, the spread between WTI and jet fuel has widened beyond historic norms, which has led to more ineffectiveness when measuring the Company's hedges. During those time periods, jet fuel prices have more closely correlated with changes in the price of Brent crude oil ("Brent"). The Company has attempted to mitigate some of this risk by entering into more fuel hedges based on Brent crude. Although the Company has some fuel derivatives based on the price of Brent, to the extent the spread between jet fuel and WTI continues to fluctuate, a portion of these changes in fair value of the Company's hedges could continue to experience ineffectiveness and not provide complete protection against jet fuel price volatility. In addition, to add further protection, the Company may periodically enter into jet fuel derivatives for short-term timeframes. Jet fuel is not widely traded on an organized futures exchange and, therefore, there are limited opportunities to hedge directly in jet fuel for time horizons longer than approximately six to twelve months into the future.

See Item 7A “Quantitative and Qualitative Disclosures About Market Risk” in the Company's Annual Report on Form 10-K for the year ended December 31, 2012, for further information about market risk, and Note 5 to the unaudited

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Condensed Consolidated Financial Statements in this Form 10-Q for further information about the Company's fuel derivative instruments.

Item 4. Controls and Procedures

Disclosure Controls and Procedures

The Company maintains disclosure controls and procedures (as defined in Rule 13a-15(e) of the Securities Exchange Act of 1934 (the "Exchange Act")) designed to provide reasonable assurance that the information required to be disclosed by the Company in the reports that it files or submits under the Exchange Act is recorded, processed, summarized, and reported within the time periods specified in the Securities and Exchange Commission's rules and forms. These include controls and procedures designed to ensure that this information is accumulated and communicated to the Company's management, including its Chief Executive Officer and Chief Financial Officer, as appropriate to allow timely decisions regarding required disclosure. Management, with the participation of the Chief Executive Officer and Chief Financial Officer, evaluated the effectiveness of the Company's disclosure controls and procedures as of June 30, 2013. Based on this evaluation, the Company's Chief Executive Officer and Chief Financial Officer have concluded that the Company's disclosure controls and procedures were effective as of June 30, 2013, at the reasonable assurance level.

Changes in Internal Control over Financial Reporting

There were no changes in the Company’s internal control over financial reporting (as defined in Rule 13a-15(f) under the Exchange Act) during the fiscal quarter ended June 30, 2013, that have materially affected, or are reasonably likely to materially affect, the Company’s internal control over financial reporting.

PART II. OTHER INFORMATION

Item 1. Legal Proceedings

A complaint alleging violations of federal antitrust laws and seeking certification as a class action was filed against Delta Air Lines, Inc. (“Delta”) and AirTran in the United States District Court for the Northern District of Georgia in Atlanta on May 22, 2009. The complaint alleged, among other things, that AirTran attempted to monopolize air travel in violation of Section 2 of the Sherman Act, and conspired with Delta in imposing $15-per-bag fees for the first item of checked luggage in violation of Section 1 of the Sherman Act. The initial complaint sought treble damages on behalf of a putative class of persons or entities in the United States who directly paid Delta and/or AirTran such fees on domestic flights beginning December 5, 2008. After the filing of the May 2009 complaint, various other nearly identical complaints also seeking certification as class actions were filed in federal district courts in Atlanta, Georgia; Orlando, Florida; and Las Vegas, Nevada. All of the cases were consolidated before a single federal district court judge in Atlanta. A Consolidated Amended Complaint was filed in the consolidated action on February 1, 2010, which broadened the allegations to add claims that Delta and AirTran conspired to reduce capacity on competitive routes and to raise prices in violation of Section 1 of the Sherman Act. In addition to treble damages for the amount of first baggage fees paid to AirTran and to Delta, the Consolidated Amended Complaint seeks injunctive relief against a broad range of alleged anticompetitive activities, as well as attorneys' fees. On August 2, 2010, the Court dismissed plaintiffs' claims that AirTran and Delta had violated Section 2 of the Sherman Act; the Court let stand the claims of a conspiracy with respect to the imposition of a first bag fee and the airlines' capacity and pricing decisions. On June 30, 2010, the plaintiffs filed a motion to certify a class, which AirTran and Delta have opposed. The Court has not yet ruled on the class certification motion. The original period for fact and expert discovery was scheduled to end on February 25, 2011, but on February 3, 2012, the Court granted plaintiffs' motion for supplemental discovery because Delta discovered that it had not produced certain electronic documents. The period for supplemental discovery against AirTran ended on May 3, 2012, but discovery disputes between plaintiffs and Delta have continued. On June 18, 2012, the parties filed a Stipulation and Order that plaintiffs have abandoned their claim that AirTran and Delta conspired to reduce capacity. On August 31, 2012, AirTran and Delta moved for summary judgment on all of plaintiffs' remaining claims, and the plaintiffs filed a supplemental brief on class certification. From September to November 2012, the plaintiffs filed a series of motions to compel Delta to produce additional documents and for sanctions based on alleged failures to produce electronic data. On November 19, 2012, the Court ordered plaintiffs to appoint an expert to examine Delta's production of electronic data and suspended the briefing schedule for the summary judgment motion until the expert has completed his work. The expert submitted a preliminary report, disputes have arisen concerning the expert's work, and the Court is deciding how to proceed. After disputes concerning the expert's work and Delta's discovery have been resolved, the parties will resume briefing defendants' motions for summary judgment and supplemental briefing on plaintiffs' motion for class certification. AirTran denies all allegations of wrongdoing, including those in the Consolidated Amended Complaint, and intends to defend vigorously any and all such allegations.

The Company is from time to time subject to various legal proceedings and claims arising in the ordinary course of business, including, but not limited to, examinations by the Internal Revenue Service.

The Company’s management does not expect that the outcome in any of its currently ongoing legal proceedings or the outcome of any proposed adjustments presented to date by the Internal Revenue Service, individually or collectively, will have a material adverse effect on the Company’s financial condition, results of operations, or cash flow.

Item 1A. Risk Factors

There have been no material changes to the factors disclosed in Item 1A. Risk Factors in the Company’s Annual Report on Form 10-K for the year ended December 31, 2012.

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds

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Issuer Purchases of Equity Securities (1)

Period	(a) Total number of shares purchased		(b) Average price paid per share (2)	(c) Total number of shares purchased as part of publicly announced plans or programs	(d) Maximum dollar value of shares that may yet be purchased under the plans or programs
April 1, 2013 through April 30, 2013	—		$—	—	$275,015,838
May 1, 2013 through May 31, 2013	17,882,690		$13.98	17,882,690	$524,515,838
June 1, 2013 through June 30, 2013	157,907	(3)	$—	157,907	$524,515,838
Total	18,040,597			18,040,597	

(1) In January 2008, the Company's Board of Directors authorized the repurchase of up to $500 million of the Company's common stock. Through February 15, 2008, the Company had repurchased 4.4 million shares for a total of approximately $54 million, at which time repurchases under the program were suspended. On August 5, 2011, the Company's Board of Directors authorized the Company to resume a share repurchase program and approved the Company's repurchase, on a discretionary basis, of a total of up to $500 million of the Company's common stock following such authorization. On May 16, 2012, the Company's Board of Directors increased the previous share repurchase authorization by an additional $500 million. On May 15, 2013, the Company's Board of Directors further increased the previous share repurchase authorization by an additional $500 million to a total of $1.5 billion and, in a privately negotiated transaction, the Company entered into the ASR Program with a third party financial institution to buy $250 million of its common shares utilizing cash on hand. Repurchases are made in accordance with applicable securities laws in open market, private, or accelerated repurchase transactions from time to time, depending on market conditions, and may be discontinued at any time.

(2) During May 2013, under the ASR Program, the Company paid $250 million and received an initial delivery of 17,882,690 shares. The Company also made a $500 thousand additional payment to the third party financial institution under the terms of the agreement governing the ASR Program. Upon completion of the ASR Program in June 2013, the Company received 157,907 additional shares of its common stock. The calculation of average price paid per share does not include amounts attributable to the shares delivered upon completion of the ASR Program or to the $500 thousand additional payment made by the Company. In total, the average purchase price per share for the 18,040,597 shares repurchased under the ASR Program, upon completion of the ASR Program in June 2013, was $13.89.

(3) Shares delivered by counterparty upon settlement of the ASR Program.

Item 3. Defaults Upon Senior Securities

None

Item 4. Mine Safety Disclosures

Not applicable

Item 5. Other Information

None

Item 6. Exhibits

3.1	Restated Certificate of Formation of the Company, effective May 18, 2012 (incorporated by reference to Exhibit 3.1 to the Company's Quarterly Report on Form 10-Q for the quarter ended June 30, 2012 (File No. 1-7259)).
3.2	Amended and Restated Bylaws of the Company, effective November 19, 2009 (incorporated by reference to Exhibit 3.1 to the Company's Current Report on Form 8-K dated November 19, 2009 (File No. 1-7259)).
10.1	Supplemental Agreement No. 82 to Purchase Agreement No. 1810, dated January 19, 1994, between The Boeing Company and the Company. (1)
10.2	Supplemental Agreement No. 83 to Purchase Agreement No. 1810, dated January 19, 1994, between The Boeing Company and the Company. (1)
10.3	Supplemental Agreement No. 1 to Purchase Agreement No. 3729, dated December 13, 2011, between The Boeing Company and the Company. (1)
10.4	Supplemental Agreement No. 2 to Purchase Agreement No. 3729, dated December 13, 2011, between The Boeing Company and the Company. (1)
31.1	Rule 13a-14(a) Certification of Chief Executive Officer.
31.2	Rule 13a-14(a) Certification of Chief Financial Officer.
32.1	Section 1350 Certifications of Chief Executive Officer and Chief Financial Officer. (2)
101.INS	XBRL Instance Document.
101.SCH	XBRL Taxonomy Extension Schema Document.
101.CAL	XBRL Taxonomy Extension Calculation Linkbase Document.
101.DEF	XBRL Taxonomy Extension Definition Linkbase Document.
101.LAB	XBRL Taxonomy Extension Labels Linkbase Document.
101.PRE	XBRL Taxonomy Extension Presentation Linkbase Document.

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(1) Pursuant to 17 CFR 240.24b-2, confidential information has been omitted and has been filed separately with the Securities and Exchange Commission pursuant to a Confidential Treatment Application filed with the Commission.

(2) Furnished, not filed.

SIGNATURES

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.

	SOUTHWEST AIRLINES CO.	
July 31, 2013	By	/s/ Tammy Romo
		Tammy Romo Chief Financial Officer (On behalf of the Registrant and in her capacity as Principal Financial and Accounting Officer)

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EXHIBIT INDEX

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