ABBOTT LABORATORIES
Form 10-Q
August 05, 2014
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended June 30, 2014

OR

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

For the transition period from to

Commission File No. 1-2189

ABBOTT LABORATORIES

An Illinois Corporation

I.R.S. Employer Identification No.
36-0698440

100 Abbott Park Road

Abbott Park, Illinois 60064-6400

Telephone: **(847) 937-6l00**

Indicate by check mark whether the registrant: (l) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of l934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes x No o

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§ 229.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes x No o

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

Large Accelerated Filer x	Accelerated Filer o
Non-Accelerated Filer o (Do not check if a smaller reporting company)	Smaller reporting company o

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

As of June 30, 2014, Abbott Laboratories had 1,503,699,033 common shares without par value outstanding.

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Abbott Laboratories

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Abbott Laboratories and Subsidiaries

Condensed Consolidated Statement of Earnings

(Unaudited)

(dollars in millions except per share data; shares in thousands)

	Three Months Ended June 30 2014	Three Months Ended June 30 2013	Six Months Ended June 30 2014	Six Months Ended June 30 2013
Net Sales	$ 5,551	$ 5,446	$ 10,795	$ 10,824
Cost of products sold, excluding amortization of intangible assets	2,506	2,545	4,976	4,977
Amortization of intangible assets	161	197	335	396
Research and development	335	363	722	709
Selling, general and administrative	1,788	1,714	3,550	3,500
Total Operating Cost and Expenses	4,790	4,819	9,583	9,582
Operating Earnings	761	627	1,212	1,242
Interest expense	39	40	78	81
Interest (income)	(19)	(17)	(35)	(32)
Net foreign exchange loss (gain)	1	11	3	40
Other (income) expense, net	3	(8)	6	(2)
Earnings from Continuing Operations Before Taxes	737	601	1,160	1,155
Taxes on Earnings from Continuing Operations	277	125	361	134
Earnings from Continuing Operations	460	476	799	1,021
Earnings from Discontinued Operations, net of taxes	6		42	
Net Earnings	$ 466	$ 476	$ 841	$ 1,021
Basic Earnings Per Common Share				
Continuing Operations	$ 0.30	$ 0.30	$ 0.52	$ 0.65
Discontinued Operations			0.03	
Net Earnings	$ 0.30	$ 0.30	$ 0.55	$ 0.65
Diluted Earnings Per Common Share				
Continuing Operations	$ 0.30	$ 0.30	$ 0.52	$ 0.64
Discontinued Operations			0.03	
Net Earnings	$ 0.30	$ 0.30	$ 0.55	$ 0.64
Cash Dividends Declared Per Common Share	$ 0.22	$ 0.14	$ 0.44	$ 0.28
Average Number of Common Shares Outstanding Used for Basic Earnings Per Common Share	1,506,595	1,560,519	1,521,668	1,564,894
Dilutive Common Stock Options and Awards	10,451	16,165	10,605	16,726
Average Number of Common Shares Outstanding Plus Dilutive Common Stock Options and Awards	1,517,046	1,576,684	1,532,273	1,581,620

Outstanding Common Stock Options Having No Dilutive Effect	544	1,015	544	1,015

The accompanying notes to condensed consolidated financial statements are an integral part of this statement.

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Abbott Laboratories and Subsidiaries

Condensed Consolidated Statement of Comprehensive Income

(Unaudited)

(dollars in millions)

	Three Months Ended June 30 2014	Three Months Ended June 30 2013	Six Months Ended June 30 2014	Six Months Ended June 30 2013
Net Earnings	$ 466	$ 476	$ 841	$ 1,021
Less: Earnings from Discontinued Operations	6		42	
Earnings from Continuing Operations	460	476	799	1,021
Foreign currency translation gain (loss) adjustments	(19)	(360)	43	(750)
Net actuarial gains (losses) and amortization of net actuarial (losses) and prior service (cost) and credits, net of taxes of $7 and $15 in 2014 and $16 and $(7) in 2013	12	28	28	(13)
Unrealized gains (losses) on marketable equity securities, net of taxes of $(2) and $(2) in 2014 and $1 and $2 in 2013	(4)	2	(4)	3
Net adjustments for derivative instruments designated as cash flow hedges and other, net of taxes of $(2) and $(2) in 2014 and $(1) and $(6) in 2013	(7)	(3)	(7)	(23)
Other Comprehensive Income (Loss) from Continuing Operations	(18)	(333)	60	(783)
Comprehensive Income (Loss) from Continuing Operations	442	143	859	238
Comprehensive Income from Discontinued Operations	6		42	
Comprehensive Income	$ 448	$ 143	$ 901	$ 238

	June 30, 2014	December 31, 2013
Supplemental Accumulated Other Comprehensive Income (Loss) Information, net of tax:		
Cumulative foreign currency translation (loss) adjustments	$ (675)	$ (718)
Net actuarial (losses) and prior service cost and credits	(1,284)	(1,312)
Cumulative unrealized gains on marketable equity securities	9	13
Cumulative gains (losses) on derivative instruments designated as cash flow hedges and other	(2)	5

The accompanying notes to condensed consolidated financial statements are an integral part of this statement.

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Abbott Laboratories and Subsidiaries

Condensed Consolidated Balance Sheet

(Unaudited)

(dollars in millions)

	June 30, 2014	December 31, 2013
Assets		
Current Assets:		
Cash and cash equivalents	$ 3,570	$ 3,475
Investments, primarily bank time deposits and U.S. treasury bills	3,492	4,623
Trade receivables, less allowances of $354 in 2014 and $312 in 2013	4,056	3,986
Inventories:		
Finished products	1,920	1,866
Work in process	339	349
Materials	564	478
Total inventories	2,823	2,693
Prepaid expenses, deferred income taxes, and other receivables	4,065	4,032
Current assets held for disposition	252	438
Total Current Assets	18,258	19,247
Investments	130	119
Property and equipment, at cost	13,096	12,870
Less: accumulated depreciation and amortization	7,161	6,965
Net property and equipment	5,935	5,905
Intangible assets, net of amortization	5,428	5,735
Goodwill	9,751	9,772
Deferred income taxes and other assets	1,921	2,109
Non-current assets held for disposition	52	66
	$ 41,475	$ 42,953
Liabilities and Shareholders Investment		
Current Liabilities:		
Short-term borrowings	$ 3,953	$ 3,164
Trade accounts payable	1,062	1,026
Salaries, wages and commissions	828	906
Other accrued liabilities	3,247	3,500
Dividends payable	331	341
Income taxes payable	181	175
Current portion of long-term debt	9	9
Current liabilities held for disposition	242	386
Total Current Liabilities	9,853	9,507
Long-term debt	3,403	3,388
Post-employment obligations, deferred income taxes and other long-term liabilities	4,514	4,784
Non-current liabilities held for disposition	1	7
Commitments and Contingencies		
Shareholders Investment:		
Preferred shares, one dollar par value Authorized 1,000,000 shares, none issued		
Common shares, without par value Authorized - 2,400,000,000 shares Issued at stated capital amount - Shares: 2014: 1,691,263,815; 2013: 1,685,827,096	12,126	12,048
Common shares held in treasury, at cost - Shares: 2014: 187,564,782; 2013: 137,728,810	(8,709)	(6,844)
Earnings employed in the business	22,137	21,979

Accumulated other comprehensive income (loss)		(1,952)		(2,012)
Total Abbott Shareholders Investment		23,602		25,171
Noncontrolling Interests in Subsidiaries		102		96
Total Shareholders Investment		23,704		25,267
	$	41,475	$	42,953

The accompanying notes to condensed consolidated financial statements are an integral part of this statement.

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Abbott Laboratories and Subsidiaries

Condensed Consolidated Statement of Cash Flows

(Unaudited)

(dollars in millions)

	Six Months Ended June 30	
	2014	**2013**
Cash Flow From (Used in) Operating Activities:		
Net earnings	$ 841	$ 1,021
Adjustments to reconcile net earnings to net cash from operating activities -		
Depreciation	463	461
Amortization of intangibles	335	396
Share-based compensation	168	177
Trade receivables	(76)	(91)
Inventories	(141)	(232)
Other, net	(354)	(555)
Net Cash From Operating Activities	1,236	1,177
Cash Flow From (Used in) Investing Activities:		
Acquisitions of property and equipment	(513)	(565)
Sales (Purchases) of investment securities, net	1,119	(1,507)
Other	27	
Net Cash From (Used in) Investing Activities	633	(2,072)
Cash Flow From (Used in) Financing Activities:		
Proceeds from issuance of short-term debt and other	872	3,150
Transfer of cash and cash equivalents to AbbVie Inc.		(5,901)
Purchases of common shares	(2,193)	(1,215)
Proceeds from stock options exercised, including income tax benefit	226	142
Dividends paid	(676)	(444)
Net Cash (Used in) Financing Activities	(1,771)	(4,268)
Effect of exchange rate changes on cash and cash equivalents	(3)	(67)
Net Increase (Decrease) in Cash and Cash Equivalents	95	(5,230)
Cash and Cash Equivalents, Beginning of Year	3,475	10,802
Cash and Cash Equivalents, End of Period	$ 3,570	$ 5,572

The accompanying notes to condensed consolidated financial statements are an integral part of this statement.

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Abbott Laboratories and Subsidiaries

Notes to the Condensed Consolidated Financial Statements

June 30, 2014

(Unaudited)

Note 1 Basis of Presentation

The accompanying unaudited, condensed consolidated financial statements have been prepared pursuant to rules and regulations of the Securities and Exchange Commission and, therefore, do not include all information and footnote disclosures normally included in audited financial statements. However, in the opinion of management, all adjustments (which include only normal adjustments) necessary to present fairly the results of operations, financial position and cash flows have been made. It is suggested that these statements be read in conjunction with the financial statements included in Abbott s Annual Report on Form 10-K for the year ended December 31, 2013. The consolidated financial statements include the accounts of the parent company and subsidiaries, after elimination of intercompany transactions.

Note 2 Separation of AbbVie Inc.

On January 1, 2013, Abbott completed the separation of AbbVie Inc. (AbbVie), which was formed to hold Abbott s research-based proprietary pharmaceuticals business. Abbott and AbbVie entered into transitional services agreements prior to the separation pursuant to which Abbott and AbbVie are providing to each other, on an interim transitional basis, various services. Transition services may be provided for up to 24 months with an option for a one-year extension by the recipient. Services being provided by Abbott include certain information technology and back office support. Billings by Abbott under these transitional services agreements are recorded as a reduction of the costs to provide the respective service in the applicable expense category in the Condensed Consolidated Statement of Earnings. This transitional support will enable AbbVie to establish its stand-alone processes for various activities that were previously provided by Abbott and does not constitute significant continuing support of AbbVie s operations.

For a small portion of AbbVie s operations, the legal transfer of AbbVie s assets (net of liabilities) did not occur with the separation of AbbVie on January 1, 2013, in certain countries, due to the time required to transfer marketing authorizations and other regulatory requirements in each of these countries. Under the terms of the separation agreement with Abbott, AbbVie is subject to the risks and entitled to the benefits generated by these operations and assets. The majority of these operations were transferred to AbbVie in 2013 with the remainder expected to be transferred in 2014 or 2015. These assets and liabilities have been presented as held for disposition in the Condensed Consolidated Balance Sheet. At June 30, 2014, the assets and liabilities held for disposition consist of trade accounts receivable of $137 million, inventories of $89 million, equipment of $16 million, other assets of $62 million, trade accounts payable and accrued liabilities of $242 million and other liabilities of $1 million. Abbott s obligation to transfer the net assets held for disposition to AbbVie of $61 million is included in Other accrued liabilities.

Abbott has retained all liabilities for all U.S. federal and foreign income taxes on income prior to the separation, as well as certain non-income taxes attributable to AbbVie s business. AbbVie generally will be liable for all other taxes attributable to its business.

Earnings from discontinued operations in the second quarter and first six months of 2014 reflect the recognition of $6 million and $42 million, respectively, of net tax benefits primarily as a result of the resolution of various tax positions related to AbbVie s operations for years prior to the separation.

Note 3 Supplemental Financial Information

Shares of unvested restricted stock that contain non-forfeitable rights to dividends are treated as participating securities and are included in the computation of earnings per share under the two-class method. Under the two-class method, net earnings are allocated between common shares and participating securities. Earnings from Continuing Operations allocated to common shares for the three months ended June 30, 2014 and 2013 were $458 million and $473 million, respectively and for the six months ended June 30, 2014 and 2013 were $795 million and $1.013 billion, respectively. Net earnings allocated to common shares for the three months ended June 30, 2014 and 2013 were $463 million and $473 million, respectively, and for the six months ended June 30, 2014 and 2013 were $837 million and $1.013 billion, respectively.

Other, net use of cash in Net cash from operating activities in the Condensed Consolidated Statement of Cash Flows for the first six months of 2014 and 2013 includes the effects of contributions to defined benefit plans of $330 million and $320 million, respectively, and to the post-employment medical and dental benefit plans of $40 million in each six month period, as well as the non-cash impact

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in the first six months of 2014 of approximately $70 million of tax benefits, net of cash refunded by taxing authorities, resulting from the resolution of various tax positions pertaining to prior years.

The components of long-term investments as of June 30, 2014 and December 31, 2013 are as follows:

(in millions)		June 30, 2014		December 31, 2013
Equity securities	$	95	$	93
Other		35		26
Total	$	130	$	119

Note 4 Changes in Accumulated Other Comprehensive Income (Loss)

The changes in accumulated other comprehensive income (loss) from continuing operations, net of income taxes, are as follows:

	Three Months Ended June 30							
	Cumulative Foreign Currency Translation Adjustments		Net Actuarial Losses and Prior Service Costs and Credits		Cumulative Unrealized Gains on Marketable Equity Securities		Cumulative Gains on Derivative Instruments Designated as Cash Flow Hedges	
(in millions)	2014	2013	2014	2013	2014	2013	2014	2013
Balance at March 31 (a)	$ (656)	$ (777)	$ (1,296)	$ (2,186)	$ 13	$ 32	$ 5	$ 38
Other comprehensive income (loss) before Reclassifications	(19)	(360)			1	7		12
Amounts reclassified from accumulated other comprehensive income (b)			12	28	(5)	(5)	(7)	(15)
Net current period comprehensive income from continuing operations	(19)	(360)	12	28	(4)	2	(7)	(3)
Balance at June 30 (a)	$ (675)	$ (1,137)	$ (1,284)	$ (2,158)	$ 9	$ 34	$ (2)	$ 35

	Six Months Ended June 30							
	Cumulative Foreign Currency Translation Adjustments		Net Actuarial Losses and Prior Service Costs and Credits		Cumulative Unrealized Gains on Marketable Equity Securities		Cumulative Gains on Derivative Instruments Designated as Cash Flow Hedges	
(in millions)	2014	2013	2014	2013	2014	2013	2014	2013
Balance at December 31, 2013 and 2012	$ (718)	$ (79)	$ (1,312)	$ (3,596)	$ 13	$ 31	$ 5	$ 50
Separation of AbbVie (a)		(308)		1,451				8

Other comprehensive income (loss) before Reclassifications	43	(750)		(69)	2	14	(1)	(5)
Amounts reclassified from accumulated other comprehensive income (b)			28	56	(6)	(11)	(6)	(18)
Net current period comprehensive income from continuing operations (a)	43	(750)	28	(13)	(4)	3	(7)	(23)
Balance at June 30	$ (675)	$ (1,137)	$ (1,284)	$ (2,158)	$ 9	$ 34	$ (2)	$ 35

(a) Prior year amounts have been appropriately revised to reflect a reclassification between Cumulative foreign currency translation adjustment and Net actuarial losses and prior service costs and credits.

(b) Reclassified amounts for foreign currency translation are recorded in the Condensed Consolidated Statement of Earnings as Net foreign exchange loss (gain); gains on marketable equity securities as Other (income) expense, net and cash flow hedges as Cost of products sold. Net actuarial losses and prior service cost is included as a component of net periodic benefit plan costs; see Note 11 for additional details.

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Note 5 Business Acquisitions

In August 2013, Abbott acquired 100 percent of IDEV Technologies, net of debt, for $310 million, in cash. The acquisition of IDEV Technologies expands Abbott s endovascular portfolio. The final allocation of the fair value at the date of acquisition resulted in non-deductible acquired in-process research and development of approximately $170 million which is accounted for as an indefinite-lived intangible asset until regulatory approval or discontinuation; non-deductible definite-lived intangible assets of approximately $66 million; non-deductible goodwill of approximately $112 million; and net deferred tax liabilities of $47 million. Acquired intangible assets consist of developed technology and are being amortized over 11 years.

In August 2013, Abbott acquired 100 percent of OptiMedica for $260 million, in cash, plus additional payments up to $150 million to be made upon completion of certain development, regulatory and sales milestones. The acquisition of OptiMedica provides Abbott with an immediate entry point into the laser assisted cataract surgery market. The final allocation of the fair value at the date of acquisition resulted in non-deductible definite-lived intangible assets of approximately $160 million; non-deductible acquired in-process research and development of approximately $60 million which is accounted for as an indefinite-lived intangible asset until regulatory approval or discontinuation; non-deductible goodwill of approximately $130 million; net deferred tax liabilities of $49 million; and contingent consideration of approximately $70 million. The fair value of the contingent consideration was determined based on an independent appraisal. Acquired intangible assets consist of developed technology and are being amortized over 18 years.

Note 6 Goodwill and Intangible Assets

The total amount of goodwill reported was $9.751 billion at June 30, 2014 and $9.772 billion at December 31, 2013. In the six months ended June 30, 2014, foreign currency translation adjustments increased goodwill by approximately $5 million, while purchase price allocation adjustments associated with recent acquisitions decreased goodwill by approximately $26 million. The amount of goodwill related to reportable segments at June 30, 2014 was $3.0 billion for the Established Pharmaceutical Products segment, $286 million for the Nutritional Products segment, $444 million for the Diagnostic Products segment, and $3.1 billion for the Vascular Products segment. There was no reduction of goodwill relating to impairments.

The gross amount of amortizable intangible assets, primarily product rights and technology was $12.3 billion as of June 30, 2014 and $12.2 billion as of December 31, 2013, and accumulated amortization was $7.0 billion as of June 30, 2014 and $6.8 billion as of December 31, 2013. Indefinite-lived intangible assets, which relate to in-process research and development acquired in a business combination, was approximately $114 million at June 30, 2014 and $266 million at December 31, 2013. The change reflects the movement of an IDEV-related intangible asset, *Supera,* to amortizable assets due to the receipt of regulatory approval in the first quarter of 2014. Abbott s estimated annual amortization expense for intangible assets is approximately $655 million in 2014, $615 million in 2015, $590 million in 2016, $575 million in 2017 and $500 million in 2018. Amortizable intangible assets are amortized over 2 to 20 years (weighted average 11 years).

Note 7 Restructuring Plans

In the first six months of 2014, Abbott management approved plans to streamline various operations in order to reduce costs and improve efficiencies in Abbott s vascular, diagnostics and nutritional businesses. Abbott recorded employee related severance and other charges of approximately $80 million in 2014. Approximately $17 million is recognized in Cost of products sold, $41 million is recognized in Research and development and approximately $22 million is recognized in Selling, general and administrative expense. The following summarizes the activity for these restructurings:

(in millions)		
Restructuring charges recorded in 2014	$	80
Payments and other adjustments		(20)
Accrued balance at June 30, 2014	$	60

In 2014 and 2013, Abbott management approved plans to reduce costs and improve efficiencies across various functional areas. In 2013, Abbott management also approved plans to streamline certain manufacturing operations in order to reduce costs and improve efficiencies in Abbott s established pharmaceuticals business. In 2012, Abbott management approved plans to streamline various commercial operations in order to reduce costs and improve efficiencies in Abbott s core diagnostics, established pharmaceuticals and nutritionals businesses. Additional charges of approximately $76 million were recognized in 2014 of which approximately $2 million is recorded in Cost of products sold and approximately $74 million in Selling, general and administrative expense.

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The following summarizes the activity for the first six months of 2014 related to these restructuring actions and the status of the related accrual as of June 30, 2014:

(in millions)		
Accrued balance at December 31, 2013	$	148
Restructuring charges recorded in 2014		76
Payments and other adjustments		(42)
Accrued balance at June 30, 2014	$	182

In 2013 and prior years, Abbott management approved plans to realign its vascular manufacturing operations in order to reduce costs. The following summarizes the activity for the first six months of 2014 related to these restructuring actions and the status of the related accrual as of June 30, 2014:

(in millions)		
Accrued balance at December 31, 2013	$	20
Restructuring charges recorded in 2014		
Payments and other adjustments		(1)
Accrued balance at June 30, 2014	$	19

In 2011 and 2008, Abbott management approved plans to streamline global manufacturing operations, reduce overall costs, and improve efficiencies in Abbott s core diagnostics business. The following summarizes the activity for the first six months of 2014 related to these restructuring actions and the status of the related accrual as of June 30, 2014:

(in millions)		
Accrued balance at December 31, 2013	$	41
Restructuring charges recorded in 2014		
Payments and other adjustments		(8)
Accrued balance at June 30, 2014	$	33

Note 8 Incentive Stock Programs

In the first six months of 2014, Abbott granted 3,721,084 stock options, 546,800 restricted stock awards and 5,318,607 restricted stock units under its incentive stock programs. At June 30, 2014, approximately 110 million shares were reserved for future grants. Information regarding the number of stock options outstanding and exercisable at June 30, 2014 is as follows:

		Outstanding		**Exercisable**
Number of shares		40,505,063		33,055,510
Weighted average remaining life (*years*)		4.3		3.3
Weighted average exercise price	$	27.38	$	25.36
Aggregate intrinsic value (*in millions*)	$	551	$	517

The total unrecognized share-based compensation cost at June 30, 2014 amounted to approximately $222 million which is expected to be recognized over the next three years.

Note 9 Financial Instruments, Derivatives and Fair Value Measures

Certain Abbott foreign subsidiaries enter into foreign currency forward exchange contracts to manage exposures to changes in foreign exchange rates for anticipated intercompany purchases by those subsidiaries whose functional currencies are not the U.S. dollar. These contracts, with notional amounts totaling approximately $140 million at June 30, 2014 and December 31, 2013, respectively, are designated as cash flow hedges of the variability of the cash flows due to changes in foreign exchange rates and are recorded at fair value. Accumulated gains and losses as of June 30, 2014 will be included in Cost of products sold at the time the products are sold, generally through the next twelve months. The amount of hedge ineffectiveness was not significant in 2014 and 2013.

Abbott enters into foreign currency forward exchange contracts to manage currency exposures for foreign currency denominated third-party trade payables and receivables, and for intercompany loans and trade accounts payable where the receivable or payable is denominated in a currency other than the functional currency of the entity. For intercompany loans, the contracts require Abbott to

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sell or buy foreign currencies, primarily European currencies and Japanese yen, in exchange for primarily U.S. dollars and other European currencies. For intercompany and trade payables and receivables, the currency exposures are primarily the U.S. dollar, European currencies and Japanese yen. At June 30, 2014 and December 31, 2013, Abbott held $13.1 billion and $13.8 billion, respectively, of such foreign currency forward exchange contracts.

Abbott has designated foreign denominated short-term debt as a hedge of the net investment in a foreign subsidiary of approximately $523 million and approximately $505 million as of June 30, 2014 and December 31, 2013, respectively. Accordingly, changes in the reported value of this debt due to changes in exchange rates are recorded in Accumulated other comprehensive income (loss), net of tax.

Abbott is a party to interest rate swap contracts totaling approximately $1.5 billion at June 30, 2014 and December 31, 2013 to manage its exposure to changes in the fair value of fixed-rate debt. These contracts are designated as fair value hedges of the variability of the fair value of fixed-rate debt due to changes in the long-term benchmark interest rates. The effect of the hedge is to change a fixed-rate interest obligation to a variable rate for that portion of the debt. Abbott records the contracts at fair value and adjusts the carrying amount of the fixed-rate debt by an offsetting amount. No hedge ineffectiveness was recorded in income in 2014 or 2013 for these hedges.

The following table summarizes the amounts and location of certain derivative financial instruments as of June 30, 2014 and December 31, 2013:

	Fair Value - Assets			Fair Value - Liabilities		
(in millions)	**June 30, 2014**	**Dec. 31, 2013**	**Balance Sheet Caption**	**June 30, 2014**	**Dec. 31, 2013**	**Balance Sheet Caption**
Interest rate swaps designated as fair value hedges	$ 106	$ 87	Deferred income taxes and other assets	$	$	Post-employment obligations, deferred income taxes and other long-term liabilities
Foreign currency forward exchange contracts:						
Hedging instruments	4	14	Prepaid expenses, deferred income taxes, and other receivables			Other accrued liabilities
Others not designated as hedges	67	70	Prepaid expenses, deferred income taxes, and other receivables	24	75	Other accrued liabilities
Debt designated as a hedge of net investment in a foreign subsidiary			n/a	523	505	Short-term borrowings
	$ 177	$ 171		$ 547	$ 580	

The following table summarizes the activity for foreign currency forward exchange contracts designated as cash flow hedges, debt designated as a hedge of net investment in a foreign subsidiary and the amounts and location of income (expense) and gain (loss) reclassified into income in the second quarter and first six months of 2014 and 2013 and for certain other derivative financial instruments. The amount of hedge ineffectiveness was not significant in 2014 and 2013 for these hedges.

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	Gain (loss) Recognized in Other Comprehensive Income (loss)				Income (expense) and Gain (loss) Reclassified into Income				
	Three Months Ended June 30		Six Months Ended June 30		Three Months Ended June 30		Six Months Ended June 30		Income Statement
(in millions)	2014	2013	2014	2013	2014	2013	2014	2013	Caption
Foreign currency forward exchange contracts designated as cash flow hedges	$ (3)	$ 14	$ (1)	$ 31	$ 3	$ 11	$ 6	$ 14	Cost of products sold
Debt designated as a hedge of net investment in a foreign subsidiary	(7)	25	(18)	75	n/a	n/a	n/a	n/a	n/a
Interest rate swaps designated as fair value hedges	n/a	n/a	n/a	n/a	8	(71)	19	(81)	Interest expense
Foreign currency forward exchange contracts not designated as hedges	n/a	n/a	n/a	n/a	(10)	50	(23)	140	Net foreign exchange loss (gain)

The interest rate swaps are designated as fair value hedges of the variability of the fair value of fixed-rate debt due to changes in the long-term benchmark interest rates. The hedged debt is marked to market, offsetting the effect of marking the interest rate swaps to market.

The carrying values and fair values of certain financial instruments as of June 30, 2014 and December 31, 2013 are shown in the following table. The carrying values of all other financial instruments approximate their estimated fair values. The counterparties to financial instruments consist of select major international financial institutions. Abbott does not expect any losses from nonperformance by these counterparties.

	June 30, 2014		December 31, 2013	
(in millions)	Carrying Value	Fair Value	Carrying Value	Fair Value
Long-term Investment Securities:				
Equity securities	$ 95	$ 95	$ 93	$ 93
Other	35	31	26	24
Total Long-term Debt	(3,412)	(4,033)	(3,397)	(3,930)
Foreign Currency Forward Exchange Contracts:				
Receivable position	71	71	84	84
(Payable) position	(24)	(24)	(75)	(75)
Interest Rate Hedge Contracts:				
Receivable position	106	106	87	87

The fair value of the debt was determined based on significant other observable inputs, including current interest rates.

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The following table summarizes the bases used to measure certain assets and liabilities at fair value on a recurring basis in the balance sheet:

			Basis of Fair Value Measurement		
(in millions)	**Outstanding Balances**		**Quoted Prices in Active Markets**	**Significant Other Observable Inputs**	**Significant Unobservable Inputs**
June 30, 2014:					
Equity securities	$ 19		$ 19	$	$
Interest rate swap derivative financial instruments	106			106	
Foreign currency forward exchange contracts	71			71	
Total Assets	$ 196		$ 19	$ 177	**$**
Fair value of hedged long-term debt	$ 1,642		$	$ 1,642	$
Foreign currency forward exchange contracts	24			24	
Contingent consideration related to business combinations	75				75
Total Liabilities	$ 1,741		$	$ 1,666	75
December 31, 2013:					
Equity securities	$ 26		$ 26	$	$
Interest rate swap derivative financial instruments	87			87	
Foreign currency forward exchange contracts	84			84	
Total Assets	$ 197		$ 26	$ 171	$
Fair value of hedged long-term debt	$ 1,623		$	$ 1,623	$
Foreign currency forward exchange contracts	75			75	
Contingent consideration related to business combinations	208				208
Total Liabilities	$ 1,906		$	$ 1,698	$ 208

The fair value of the debt was determined based on the face value of the debt adjusted for the fair value of the interest rate swaps, which is based on a discounted cash flow analysis. The fair value of foreign currency forward exchange contracts is determined using a market approach, which utilizes values for comparable derivative instruments. The fair value of the contingent consideration was determined based on an independent appraisal adjusted for the time value of money, exchange, payments and other changes in fair value. The change in contingent consideration from the previous year end primarily reflects the payment of contingent consideration in the first six months of 2014.

Note 10 Litigation and Environmental Matters

Abbott has been identified as a potentially responsible party for investigation and cleanup costs at a number of locations in the United States and Puerto Rico under federal and state remediation laws and is investigating potential contamination at a number of company-owned locations. Abbott has recorded an estimated cleanup cost for each site for which management believes Abbott has a probable loss exposure. No individual site cleanup exposure is expected to exceed $4 million, and the aggregate cleanup exposure is not expected to exceed $15 million.

Abbott is involved in various claims and legal proceedings, and Abbott estimates the range of possible loss for its legal proceedings and environmental exposures to be from approximately $65 million to $90 million. The recorded accrual balance at June 30, 2014 for these proceedings and exposures was approximately $75 million. This accrual represents management s best estimate of probable loss, as defined by FASB ASC No. 450, Contingencies. Within the next year, legal proceedings may occur that may result in a change in the estimated loss accrued by Abbott. While it is not feasible to predict the outcome of all such proceedings and exposures with certainty, management believes that their ultimate disposition should not have a material adverse effect on Abbott s financial position, cash flows, or results of operations.

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Note 11 Post-Employment Benefits

Retirement plans consist of defined benefit, defined contribution, and medical and dental plans. Net cost recognized in continuing operations for the three months and six months ended June 30 for Abbott s major defined benefit plans and post-employment medical and dental benefit plans is as follows:

	Defined Benefit Plans				Medical and Dental Plans			
	Three Months Ended June 30		Six Months Ended June 30		Three Months Ended June 30		Six Months Ended June 30	
(in millions)	2014	2013	2014	2013	2014	2013	2014	2013
Service cost benefits earned during the period	$ 62	$ 76	$ 128	$ 152	$ 9	$ 11	$ 18	$ 23
Interest cost on projected benefit obligations	75	66	152	132	16	15	32	30
Expected return on plan assets	(113)	(94)	(226)	(187)	(9)	(9)	(19)	(18)
Net amortization of:								
Actuarial loss, net	24	40	49	80	4	8	9	16
Prior service cost (credit)		1	1	2	(9)	(8)	(18)	(16)
Net Cost	$							