

CONTINENTAL AIRLINES INC /DE/
Form 10-Q
October 25, 2012
Table of Contents

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended September 30, 2012

OR

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

For the transition period from _____ to _____

Commission	Exact Name of Registrant as Specified in its Charter,	State of	I.R.S. Employer
File Number 001-06033	Principal Office Address and Telephone Number United Continental Holdings, Inc. 77 W. Wacker Drive, Chicago, Illinois 60601 (312) 997-8000	Incorporation Delaware	Identification No 36-2675207

Edgar Filing: CONTINENTAL AIRLINES INC /DE/ - Form 10-Q

001-11355	United Air Lines, Inc. 77 W. Wacker Drive, Chicago, Illinois 60601 (312) 997-8000	Delaware	36-2675206
001-10323	Continental Airlines, Inc. 1600 Smith Street, Dept HQSEO, Houston, Texas 77002 (713) 324-2950	Delaware	74-2099724

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

United Continental Holdings, Inc.	Yes <input checked="" type="checkbox"/> No <input type="checkbox"/>	United Air Lines, Inc.	Yes <input checked="" type="checkbox"/> No <input type="checkbox"/>
Continental Airlines, Inc.	Yes <input checked="" type="checkbox"/> No <input type="checkbox"/>		

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this Chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).

United Continental Holdings, Inc.	Yes <input checked="" type="checkbox"/> No <input type="checkbox"/>	United Air Lines, Inc.	Yes <input checked="" type="checkbox"/> No <input type="checkbox"/>
Continental Airlines, Inc.	Yes <input checked="" type="checkbox"/> No <input type="checkbox"/>		

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.

United Continental Holdings, Inc.	Large accelerated filer <input checked="" type="checkbox"/>	Accelerated filer <input type="checkbox"/>	Non-accelerated filer <input type="checkbox"/>	Smaller reporting company <input type="checkbox"/>
United Air Lines, Inc.	Large accelerated filer <input type="checkbox"/>	Accelerated filer <input type="checkbox"/>	Non-accelerated filer <input checked="" type="checkbox"/>	Smaller reporting company <input type="checkbox"/>
Continental Airlines, Inc.	Large accelerated filer <input type="checkbox"/>	Accelerated filer <input type="checkbox"/>	Non-accelerated filer <input checked="" type="checkbox"/>	Smaller reporting company <input type="checkbox"/>

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

United Continental Holdings, Inc.	Yes <input type="checkbox"/> No <input checked="" type="checkbox"/>
United Air Lines, Inc.	Yes <input type="checkbox"/> No <input checked="" type="checkbox"/>
Continental Airlines, Inc.	Yes <input type="checkbox"/> No <input checked="" type="checkbox"/>

The number of shares outstanding of each of the issuer's classes of common stock as of October 15, 2012 is shown below:

United Continental Holdings, Inc.	332,426,868 shares of common stock (\$0.01 par value)
United Air Lines, Inc.	205 (100% owned by United Continental Holdings, Inc.)

There is no market for United Air Lines, Inc. common stock.

Continental Airlines, Inc.	1,000 (100% owned by United Continental Holdings, Inc.)
----------------------------	---------------------------------------------------------

There is no market for Continental Airlines, Inc. common stock.

OMISSION OF CERTAIN INFORMATION

This combined Form 10-Q is separately filed by United Continental Holdings, Inc., United Air Lines, Inc. and Continental Airlines, Inc. United Air Lines, Inc. and Continental Airlines, Inc. meet the conditions set forth in General Instruction H(1)(a) and (b) of Form 10-Q and are therefore filing this form with the reduced disclosure format allowed under that General Instruction.

Table of Contents

United Continental Holdings, Inc.

United Air Lines, Inc.

Continental Airlines, Inc.

Report on Form 10-Q

For the Quarter Ended September 30, 2012

	Page
<u>PART I. FINANCIAL INFORMATION</u>	
<u>Item 1. Financial Statements</u>	3
United Continental Holdings, Inc.:	
<u>Statements of Consolidated Operations</u>	3
<u>Statements of Consolidated Comprehensive Income (Loss)</u>	4
<u>Consolidated Balance Sheets</u>	5
<u>Condensed Statements of Consolidated Cash Flows</u>	7
United Air Lines, Inc.:	
<u>Statements of Consolidated Operations</u>	8
<u>Statements of Consolidated Comprehensive Income (Loss)</u>	9
<u>Consolidated Balance Sheets</u>	10
<u>Condensed Statements of Consolidated Cash Flows</u>	12
Continental Airlines, Inc.:	
<u>Statements of Consolidated Operations</u>	13
<u>Statements of Consolidated Comprehensive Income (Loss)</u>	14
<u>Consolidated Balance Sheets</u>	15
<u>Condensed Statements of Consolidated Cash Flows</u>	17
<u>Combined Notes to Condensed Consolidated Financial Statements (United Continental Holdings, Inc., United Air Lines, Inc. and Continental Airlines, Inc.)</u>	18
<u>Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations</u>	36
<u>Item 3. Quantitative and Qualitative Disclosures About Market Risk</u>	49
<u>Item 4. Controls and Procedures</u>	49
<u>PART II. OTHER INFORMATION</u>	
<u>Item 1. Legal Proceedings</u>	50
<u>Item 1A. Risk Factors</u>	50
<u>Item 6. Exhibits</u>	51
<u>Signatures</u>	52
<u>Exhibit Index</u>	53

Table of Contents**PART I. FINANCIAL INFORMATION****ITEM 1. FINANCIAL STATEMENTS****UNITED CONTINENTAL HOLDINGS, INC.****STATEMENTS OF CONSOLIDATED OPERATIONS (UNAUDITED)****(In millions, except per share amounts)**

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2012	2011	2012	2011
Operating revenue:				
Passenger Mainline	\$ 6,993	\$ 7,237	\$ 19,891	\$ 19,780
Passenger Regional	1,781	1,772	5,159	4,916
Total passenger revenue	8,774	9,009	25,050	24,696
Cargo	246	283	775	882
Special revenue item (Note 10)				107
Other operating revenue	889	879	2,625	2,497
	9,909	10,171	28,450	28,182
Operating expense:				
Aircraft fuel	3,406	3,371	10,043	9,270
Salaries and related costs	2,038	2,020	5,959	5,742
Regional capacity purchase	628	619	1,887	1,807
Landing fees and other rent	504	476	1,476	1,451
Aircraft maintenance materials and outside repairs	469	447	1,308	1,330
Depreciation and amortization	379	384	1,137	1,157
Distribution expenses	356	377	1,038	1,102
Aircraft rent	245	255	747	760
Special charges (Note 10)	514	120	884	343
Other operating expenses	1,170	1,167	3,467	3,443
	9,709	9,236	27,946	26,405
Operating income	200	935	504	1,777
Nonoperating income (expense):				
Interest expense	(202)	(227)	(631)	(731)
Interest capitalized	9	10	26	24
Interest income	4	6	16	15
Miscellaneous, net	4	(64)	(7)	(94)
	(185)	(275)	(596)	(786)
Income (loss) before income taxes	15	660	(92)	991
Income tax expense	9	7	11	13
Net income (loss)	\$ 6	\$ 653	\$ (103)	\$ 978

Edgar Filing: CONTINENTAL AIRLINES INC /DE/ - Form 10-Q

Earnings (loss) per share, basic	\$ 0.02	\$ 1.97	\$ (0.31)	\$ 2.96
Earnings (loss) per share, diluted	\$ 0.02	\$ 1.69	\$ (0.31)	\$ 2.59

The accompanying Combined Notes to Consolidated Financial Statements are an integral part of these statements.

Table of Contents**UNITED CONTINENTAL HOLDINGS, INC.****STATEMENTS OF CONSOLIDATED COMPREHENSIVE INCOME (LOSS) (UNAUDITED)****(In millions)**

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2012	2011	2012	2011
Net income (loss)	\$ 6	\$ 653	\$ (103)	\$ 978
Other comprehensive income (loss), net:				
Fuel derivative financial instruments:				
Reclassification into earnings	38	(94)	107	(526)
Change in fair value	133	(181)	(36)	112
Employee benefit plans:				
Amortization of net actuarial items	4	(5)	13	(18)
Investments and other	5	(5)	14	
	180	(285)	98	(432)
Total comprehensive income (loss), net	\$ 186	\$ 368	\$ (5)	\$ 546

The accompanying Combined Notes to Consolidated Financial Statements are an integral part of these statements.

Table of Contents**UNITED CONTINENTAL HOLDINGS, INC.****CONSOLIDATED BALANCE SHEETS**

(In millions, except shares)

	(Unaudited) September 30, 2012	December 31, 2011
ASSETS		
Current assets:		
Cash and cash equivalents	\$ 5,129	\$ 6,246
Short-term investments	1,551	1,516
Total unrestricted cash, cash equivalents and short-term investments	6,680	7,762
Restricted cash	79	40
Receivables, less allowance for doubtful accounts (2012 \$12; 2011 \$7)	1,862	1,358
Aircraft fuel, spare parts and supplies, less obsolescence allowance (2012 \$111; 2011 \$89)	675	615
Deferred income taxes	641	615
Prepaid expenses and other	837	607
	10,774	10,997
Operating property and equipment:		
Owned		
Flight equipment	16,753	15,786
Other property and equipment	3,151	3,126
	19,904	18,912
Less Accumulated depreciation and amortization	(4,750)	(4,005)
	15,154	14,907
Purchase deposits for flight equipment	613	382
Capital leases		
Flight equipment	1,484	1,458
Other property and equipment	235	237
	1,719	1,695
Less Accumulated amortization	(676)	(565)
	1,043	1,130
	16,810	16,419
Other assets:		
Goodwill	4,523	4,523
Intangibles, less accumulated amortization (2012 \$762; 2011 \$670)	4,650	4,750
Restricted cash	392	529
Other, net	756	770
	10,321	10,572

\$ 37,905 \$ 37,988

(continued on next page)

Table of Contents**UNITED CONTINENTAL HOLDINGS, INC.****CONSOLIDATED BALANCE SHEETS**

(In millions, except shares)

	(Unaudited) September 30, 2012	December 31, 2011
LIABILITIES AND STOCKHOLDERS EQUITY		
Current liabilities:		
Advance ticket sales	\$ 3,849	\$ 3,114
Frequent flyer deferred revenue	2,405	2,405
Accounts payable	2,188	1,998
Accrued salaries and benefits	1,328	1,509
Current maturities of long-term debt	1,704	1,186
Current maturities of capital leases	120	125
Other	1,463	1,057
	13,057	11,394
Long-term debt	9,592	10,496
Long-term obligations under capital leases	828	928
Other liabilities and deferred credits:		
Frequent flyer deferred revenue	2,839	3,253
Postretirement benefit liability	2,461	2,407
Pension liability	1,788	1,862
Advanced purchase of miles	1,581	1,711
Deferred income taxes	1,649	1,603
Lease fair value adjustment, net	927	1,133
Other	1,356	1,395
	12,601	13,364
Commitments and contingencies		
Stockholders' equity:		
Preferred stock		
Common stock at par, \$0.01 par value; authorized 1,000,000,000 shares; outstanding 332,439,588 and 330,906,192 shares at September 30, 2012 and December 31, 2011, respectively	3	3
Additional capital invested	7,140	7,114
Retained deficit	(4,965)	(4,863)
Stock held in treasury, at cost	(32)	(31)
Accumulated other comprehensive loss	(319)	(417)
	1,827	1,806
	\$ 37,905	\$ 37,988

The accompanying Combined Notes to Consolidated Financial Statements are an integral part of these statements.

Table of Contents**UNITED CONTINENTAL HOLDINGS, INC.****CONDENSED STATEMENTS OF CONSOLIDATED CASH FLOWS (UNAUDITED)****(In millions)**

	Nine Months Ended September 30,	
	2012	2011
Cash Flows from Operating Activities:		
Net income (loss)	\$ (103)	\$ 978
Adjustments to reconcile net income (loss) to net cash provided (used) by operating activities		
Depreciation and amortization	1,137	1,157
Debt and lease discount amortization	(196)	(171)
Special items, non-cash portion	61	(15)
Other, net	112	112
Increase in advance ticket sales	735	762
Increase in receivables	(434)	(517)
Increase (decrease) in frequent flyer deferred revenue and advanced purchase of miles	(544)	82
Increase in other current assets	(452)	(209)
Increase in accounts payable	169	1
Increase in other liabilities	360	24
Decrease in fuel hedge collateral		(61)
Net cash provided by operating activities	845	2,143
Cash Flows from Investing Activities:		
Capital expenditures	(774)	(510)
Increase in short-term and other investments, net	(22)	(754)
Proceeds from sale of property and equipment	146	107
Aircraft purchase deposits paid, net	(253)	(121)
(Increase) decrease in restricted cash, net	98	(4)
Net cash used in investing activities	(805)	(1,282)
Cash Flows from Financing Activities:		
Payments of long-term debt	(1,158)	(1,925)
Proceeds from issuance of long-term debt	86	142
Principal payments under capital leases	(89)	(199)
Other, net	4	36
Net cash used in financing activities	(1,157)	(1,946)
Net decrease in cash and cash equivalents during the period	(1,117)	(1,085)
Cash and cash equivalents at beginning of the period	6,246	8,069
Cash and cash equivalents at end of the period	\$ 5,129	\$ 6,984
Investing and Financing Activities Not Affecting Cash:		
Property and equipment acquired through the issuance of debt	\$ 526	\$ 130
Special facility payment financing	101	

Edgar Filing: CONTINENTAL AIRLINES INC /DE/ - Form 10-Q

8% Contingent Senior Unsecured Notes, net of discount	48	49
Airport construction financing	31	
Reclassification of debt to advanced purchases of miles		270
Reclassification of debt discount to other assets		60
Interest paid in kind on UAL 6% Senior Notes		18

The accompanying Combined Notes to Consolidated Financial Statements are an integral part of these statements.

Table of Contents**UNITED AIR LINES, INC.****STATEMENTS OF CONSOLIDATED OPERATIONS (UNAUDITED)****(In millions)**

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2012	2011	2012	2011
Operating revenue:				
Passenger Mainline	\$ 3,734	\$ 4,007	\$ 10,587	\$ 10,812
Passenger Regional	1,027	1,078	2,936	2,995
Total passenger revenue	4,761	5,085	13,523	13,807
Cargo	157	177	505	535
Special revenue item (Note 10)				88
Other operating revenue	738	595	1,878	1,673
	5,656	5,857	15,906	16,103
Operating expense:				
Aircraft fuel	1,914	1,949	5,685	5,294
Salaries and related costs	1,046	1,092	3,166	3,117
Regional capacity purchase	387	407	1,152	1,190
Landing fees and other rent	271	246	807	773
Aircraft maintenance materials and outside repairs	313	299	862	881
Depreciation and amortization	232	228	695	684
Distribution expenses	172	194	526	580
Aircraft rent	78	82	234	243
Special charges (Note 10)	332	72	604	236
Other operating expenses	912	709	2,400	2,081
	5,657	5,278	16,131	15,079
Operating income (loss)	(1)	579	(225)	1,024
Nonoperating income (expense):				
Interest expense	(122)	(135)	(395)	(462)
Interest capitalized	4	6	10	12
Interest income		2	5	7
Miscellaneous, net	(1)	(35)	(8)	(43)
	(119)	(162)	(388)	(486)
Income (loss) before income taxes	(120)	417	(613)	538
Income tax expense	7	2	8	2
Net income (loss)	\$ (127)	\$ 415	\$ (621)	\$ 536

The accompanying Combined Notes to Consolidated Financial Statements are an integral part of these statements.

Table of Contents**UNITED AIR LINES, INC.****STATEMENTS OF CONSOLIDATED COMPREHENSIVE INCOME (LOSS) (UNAUDITED)****(In millions)**

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2012	2011	2012	2011
Net income (loss)	\$ (127)	\$ 415	\$ (621)	\$ 536
Other comprehensive income (loss), net:				
Fuel derivative financial instruments:				
Reclassification into earnings	23	(90)	55	(427)
Change in fair value	77	(91)	(13)	145
Employee benefit plans:				
Amortization of net actuarial items	(2)		(4)	(1)
Investments and other	3	(3)	7	(4)
	101	(184)	45	(287)
Total comprehensive income (loss), net	\$ (26)	\$ 231	\$ (576)	\$ 249

The accompanying Combined Notes to Consolidated Financial Statements are an integral part of these statements.

Table of Contents**UNITED AIR LINES, INC.****CONSOLIDATED BALANCE SHEETS**

(In millions, except shares)

	(Unaudited) September 30, 2012	December 31, 2011
ASSETS		
Current assets:		
Cash and cash equivalents	\$ 3,005	\$ 3,458
Short-term investments	346	275
Total unrestricted cash, cash equivalents and short-term investments	3,351	3,733
Restricted cash	79	40
Receivables from related parties (Note 11)	2,708	228
Receivables, less allowance for doubtful accounts (2012 \$10; 2011 \$5)	1,686	763
Deferred income taxes	316	348
Aircraft fuel, spare parts and supplies, less obsolescence allowance (2012 \$81; 2011 \$73)	379	340
Prepaid expenses and other	633	447
	9,152	5,899
Operating property and equipment:		
Owned		
Flight equipment	9,354	9,135
Other property and equipment	2,197	2,260
	11,551	11,395
Less Accumulated depreciation and amortization	(3,740)	(3,359)
	7,811	8,036
Purchase deposits for flight equipment	183	57
Capital leases		
Flight equipment	1,484	1,458
Other property and equipment	65	67
	1,549	1,525
Less Accumulated amortization	(649)	(548)
	900	977
	8,894	9,070
Other assets:		
Intangibles, less accumulated amortization (2012 \$575; 2011 \$534)	2,241	2,283
Receivables from related parties (Note 11)	448	
Restricted cash	275	393
Other, net	595	600
	3,559	3,276

\$ 21,605 \$ 18,245

(continued on next page)

Table of Contents**UNITED AIR LINES, INC.****CONSOLIDATED BALANCE SHEETS**

(In millions, except shares)

	(Unaudited) September 30, 2012	December 31, 2011
LIABILITIES AND STOCKHOLDER S DEFICIT		
Current liabilities:		
Advance ticket sales (Note 11)	\$ 3,776	\$ 1,652
Frequent flyer deferred revenue (Note 11)	2,405	1,484
Accounts payable	1,426	1,109
Accrued salaries and benefits	760	988
Current maturities of long-term debt	978	615
Current maturities of capital leases	116	122
Payables to related parties	105	104
Other	1,270	853
	10,836	6,927
Long-term debt	4,191	5,130
Long-term obligations under capital leases	652	735
Other liabilities and deferred credits:		
Frequent flyer deferred revenue (Note 11)	2,839	2,018
Postretirement benefit liability	2,156	2,115
Advanced purchase of miles (Note 11)	1,581	1,442
Deferred income taxes	692	707
Pension liability	84	92
Other	1,044	983
	8,396	7,357
Commitments and contingencies		
Stockholder s deficit:		
Common stock at par, \$5 par value; authorized 1,000 shares; issued and outstanding 205 shares at both September 30, 2012 and December 31, 2011		
Additional capital invested	3,442	3,432
Retained deficit	(5,829)	(5,208)
Accumulated other comprehensive loss	(83)	(128)
	(2,470)	(1,904)
	\$ 21,605	\$ 18,245

The accompanying Combined Notes to Consolidated Financial Statements are an integral part of these statements.

Table of Contents**UNITED AIR LINES, INC.****CONDENSED STATEMENTS OF CONSOLIDATED CASH FLOWS (UNAUDITED)****(In millions)**

	Nine Months Ended September 30,	
	2012	2011
Cash Flows from Operating Activities:		
Net income (loss)	\$ (621)	\$ 536
Adjustments to reconcile net income (loss) to net cash provided (used) by operating activities		
Depreciation and amortization	695	684
Debt and lease discount amortization	26	11
Special charges, non-cash portion	59	(19)
Other, net	78	109
Increase in advance ticket sales	2,124	579
Increase in receivables	(885)	(144)
Decrease in frequent flyer deferred revenue and advanced purchase of miles	(506)	(150)
Increase in other current assets	(392)	(88)
Increase in accounts payable	296	113
Increase (decrease) in other liabilities	390	(38)
Decrease in fuel hedge collateral		(61)
Increase in receivables from related parties	(543)	(93)
Increase (decrease) in payables to related parties	2	(1)
Net cash provided by operating activities	723	1,438
Cash Flows from Investing Activities:		
Capital expenditures	(391)	(332)
Increase in short-term and other investments, net	(64)	(180)
Proceeds from sale of property and equipment	56	15
Aircraft purchase deposits paid, net	(126)	(6)
(Increase) decrease in restricted cash, net	79	(28)
Net cash used in investing activities	(446)	(531)
Cash Flows from Financing Activities:		
Payments of long-term debt	(634)	(1,316)
Principal payments under capital leases	(88)	(198)
Other, net	(8)	12
Net cash used in financing activities	(730)	(1,502)
Net decrease in cash and cash equivalents	(453)	(595)
Cash and cash equivalents at beginning of the period	3,458	4,665
Cash and cash equivalents at end of the period	\$ 3,005	\$ 4,070
Investing and Financing Activities Not Affecting Cash:		
Transfer of OnePass frequent flyer liability and advanced purchase of miles from Continental (Note 11)	\$ 2,387	\$

Edgar Filing: CONTINENTAL AIRLINES INC /DE/ - Form 10-Q

8% Contingent Senior Unsecured Notes, net of discount	48	49
Interest paid in kind on UAL 6% Senior Notes		18

The accompanying Combined Notes to Consolidated Financial Statements are an integral part of these statements.

Table of Contents**CONTINENTAL AIRLINES, INC.****STATEMENTS OF CONSOLIDATED OPERATIONS (UNAUDITED)****(In millions, except per share amounts)**

	Three Months		Nine Months Ended	
	Ended		September 30,	
	September 30,	2011	2012	2011
	2012	2011	2012	2011
Operating revenue:				
Passenger Mainline	\$ 3,259	\$ 3,227	\$ 9,304	\$ 8,962
Passenger Regional	754	695	2,223	1,922
Total passenger revenue	4,013	3,922	11,527	10,884
Cargo	89	105	270	346
Special revenue item (Note 10)				19
Other operating revenue	411	345	1,226	965
	4,513	4,372	13,023	12,214
Operating expense:				
Aircraft fuel	1,493	1,422	4,359	3,976
Salaries and related costs	943	906	2,692	2,575
Regional capacity purchase	240	211	735	617
Landing fees and other rent	234	230	670	678
Aircraft maintenance materials and outside repairs	171	152	479	455
Depreciation and amortization	147	156	442	473
Distribution expenses	184	183	512	523
Aircraft rent	167	171	513	516
Special charges (Note 10)	182	48	280	107
Other operating expenses	549	533	1,604	1,531
	4,310	4,012	12,286	11,451
Operating income	203	360	737	763
Nonoperating income (expense):				
Interest expense	(81)	(88)	(241)	(259)
Interest capitalized	5	4	16	12
Interest income	5	3	11	7
Miscellaneous, net	(28)	(41)	14	(76)
	(99)	(122)	(200)	(316)
Income before income taxes	104	238	537	447
Income tax expense	2	2	3	6
Net income	\$ 102	\$ 236	\$ 534	\$ 441

The accompanying Combined Notes to Consolidated Financial Statements are an integral part of these statements.

Table of Contents**CONTINENTAL AIRLINES, INC.****STATEMENTS OF CONSOLIDATED COMPREHENSIVE INCOME (UNAUDITED)****(In millions)**

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2012	2011	2012	2011
Net income	\$ 102	\$ 236	\$ 534	\$ 441
Other comprehensive income (loss), net:				
Fuel derivative financial instruments:				
Reclassification into earnings	15	(4)	52	(99)
Change in fair value	56	(90)	(23)	(33)
Employee benefit plans:				
Amortization of net actuarial items	6	(5)	17	(17)
Investments and other	3	(2)	8	2
	80	(101)	54	(147)
Total comprehensive income, net	\$ 182	\$ 135	\$ 588	\$ 294

The accompanying Combined Notes to Consolidated Financial Statements are an integral part of these statements.

Table of Contents

CONTINENTAL AIRLINES, INC.
CONSOLIDATED BALANCE SHEETS

(In millions, except shares)

	(Unaudited) September 30, 2012	December 31, 2011
ASSETS		
Current assets:		
Cash and cash equivalents	\$ 2,119	\$ 2,782
Short-term investments	1,205	1,241
Total unrestricted cash, cash equivalents and short-term investments	3,324	4,023
Receivables, less allowance for doubtful accounts (2012 \$2; 2011 \$2)	176	595
Aircraft fuel, spare parts and supplies, less obsolescence allowance (2012 \$16; 2011 \$30)	296	275
Deferred income taxes	331	267
Prepaid expenses and other	193	165
	4,320	5,325
Operating property and equipment:		
Owned		
Flight equipment	7,399	6,651
Other property and equipment	954	866
	8,353	7,517
Less Accumulated depreciation and amortization	(1,009)	(646)
	7,344	6,871
Purchase deposits for flight equipment	430	324
Capital leases Other property and equipment	170	170
Less Accumulated amortization	(27)	(17)
	143	153
	7,917	7,348
Other assets:		
Goodwill	4,523	4,523
Intangibles, less accumulated amortization (2012 \$187; 2011 \$136)	2,411	2,469
Restricted cash	116	135
Other, net	364	364
	7,414	7,491
	\$ 19,651	\$ 20,164

(continued on next page)

Table of Contents

CONTINENTAL AIRLINES, INC.
CONSOLIDATED BALANCE SHEETS

(In millions, except shares)

	(Unaudited) September 30, 2012	December 31, 2011
LIABILITIES AND STOCKHOLDER S EQUITY		
Current liabilities:		
Payables to related parties (Note 11)	\$ 2,486	\$ 11
Advance ticket sales (Note 11)	73	1,462
Accounts payable	767	894
Current maturities of long-term debt	726	571
Accrued salaries and benefits	568	521
Current maturities of capital leases	4	3
Frequent flyer deferred revenue (Note 11)		921
Other	249	279
	4,873	4,662
Long-term debt	4,998	4,957
Long-term obligations under capital leases	176	193
Other liabilities and deferred credits:		
Pension liability	1,704	1,770
Payables to related parties (Note 11)	448	
Lease fair value adjustment, net	927	1,133
Deferred income taxes	887	820
Postretirement benefit liability	304	292
Frequent flyer deferred revenue (Note 11)		1,235
Advanced purchase of miles (Note 11)		270
Other	404	507
	4,674	6,027
Commitments and contingencies		
Stockholder s equity:		
Common stock at par, \$0.01 par value; authorized 1,000 shares; issued and outstanding 1,000 shares at both September 30, 2012 and December 31, 2011		
Additional capital invested	4,165	4,148
Retained earnings	1,008	474
Accumulated other comprehensive loss	(243)	(297)
	4,930	4,325
	\$ 19,651	\$ 20,164

The accompanying Combined Notes to Consolidated Financial Statements are an integral part of these statements.

Table of Contents**CONTINENTAL AIRLINES, INC.****CONDENSED STATEMENTS OF CONSOLIDATED CASH FLOWS (UNAUDITED)****(In millions)**

	Nine Months Ended September 30,	
	2012	2011
Cash Flows from Operating Activities:		
Net income	\$ 534	\$ 441
Adjustments to reconcile net income to net cash provided (used) by operating activities		
Depreciation and amortization	442	473
Debt and lease discount amortization	(222)	(182)
Special charges, non-cash portion	2	4
Other, net	49	30
Increase (decrease) in advance ticket sales	(1,389)	183
(Increase) decrease in receivables	451	(373)
Increase (decrease) in frequent flyer deferred revenue and advanced purchase of miles	(39)	233
Increase in other current assets	(72)	(83)
Decrease in accounts payable	(127)	(113)
Increase (decrease) in other liabilities	(44)	23
Decrease in receivables from related parties		3
Increase in payables to related parties	536	66
Net cash provided by operating activities	121	705
Cash Flows from Investing Activities:		
Capital expenditures	(383)	(178)
(Increase) decrease in short-term investments, net	43	(574)
Aircraft purchase deposits paid, net	(127)	(116)
Proceeds from sale of property and equipment	90	92
Decrease in restricted cash, net	19	25
Net cash used in investing activities	(358)	(751)
Cash Flows from Financing Activities:		
Payments of long-term debt	(524)	(609)
Proceeds from issuance of long-term debt	86	142
Other, net	12	23
Net cash used in financing activities	(426)	(444)
Net decrease in cash and cash equivalents	(663)	(490)
Cash and cash equivalents at beginning of the period	2,782	3,398
Cash and cash equivalents at end of the period	\$ 2,119	\$ 2,908
Investing and Financing Activities Not Affecting Cash:		
Transfer of frequent flyer liability and advanced purchase of miles to United (Note 11)	\$ 2,387	\$
Property and equipment acquired through the issuance of debt	526	130
Special facility payment financing	101	
Airport construction financing	31	

Reclassification of debt to advanced purchases of miles	270
Reclassification of debt discount to other assets	60

The accompanying Combined Notes to Consolidated Financial Statements are an integral part of these statements.

Table of Contents

UNITED CONTINENTAL HOLDINGS, INC.,

UNITED AIR LINES, INC. AND CONTINENTAL AIRLINES, INC.

COMBINED NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

United Continental Holdings, Inc. (together with its consolidated subsidiaries, UAL) is a holding company and its principal, wholly-owned subsidiaries are United Air Lines, Inc. (together with its consolidated subsidiaries, United) and Continental Airlines, Inc. (together with its consolidated subsidiaries, Continental). All significant intercompany transactions are eliminated.

This Quarterly Report on Form 10-Q is a combined report of UAL, United and Continental. We sometimes use the words we, our, us, and the Company for disclosures that relate to all of UAL, United and Continental. As UAL consolidates United and Continental for financial statement purposes, disclosures that relate to United and Continental activities also apply to UAL. When appropriate, UAL, United and Continental are named specifically for their related activities and disclosures.

Interim Financial Statements. The UAL, United and Continental unaudited condensed consolidated financial statements shown here have been prepared as required by the U.S. Securities and Exchange Commission (the SEC). Some information and footnote disclosures normally included in financial statements that comply with accounting principles generally accepted in the United States (GAAP) have been condensed or omitted as permitted by the SEC. The financial statements include all adjustments, including normal recurring adjustments and other adjustments, which are considered necessary for a fair presentation of the Company's financial position and results of operations. Certain prior year amounts have been reclassified to conform to the current year's presentation. These reclassifications were made to conform the financial statement presentation of UAL, United and Continental. The UAL, United and Continental financial statements should be read together with the information included in the Company's Annual Report on Form 10-K for the year ended December 31, 2011 (the 2011 Annual Report). UAL's quarterly financial data is subject to seasonal fluctuations and historically its second and third quarter financial results, which reflect higher travel demand, are better than its first and fourth quarter financial results.

NOTE 1 FREQUENT FLYER AND PASSENGER REVENUE ACCOUNTING

Frequent Flyer Awards. Effective January 1, 2012, the Company updated its estimated selling price for miles to the contractual rate at which we sell miles to our Star Alliance partners participating in reciprocal frequent flyer programs. This change in estimate has been applied prospectively effective January 1, 2012.

United and Continental account for miles sold and awarded that will never be redeemed by program members, which the Company refers to as breakage, using the redemption method. UAL reviews its breakage estimates annually based upon the latest available information regarding redemption and expiration patterns. The Company re-evaluated its population breakage estimates for Continental OnePass miles, which were previously not subject to an expiration policy, and increased the estimate of miles in the population expected to ultimately expire. As a result, the rate at which we recognize redeemed miles has increased.

The Company's estimate of the expected expiration of miles requires significant management judgment. Current and future changes to expiration assumptions, the expiration policy, program rules or program redemption opportunities may result in material changes to the deferred revenue balance as well as recognized revenues from the Company's frequent flyer program.

For the three and nine months ended September 30, 2012, the combined net impact of these changes to UAL, United and Continental were not material.

Passenger Revenue Accounting. The Company records an estimate of breakage revenue on the flight date for tickets that will expire unused. These estimates are based on the evaluation of actual historical results. During the three months ended September 30, 2012, Continental revised its estimate of breakage resulting in a reduction of passenger revenue of approximately \$60 million.

NOTE 2 NEW ACCOUNTING PRONOUNCEMENTS

In May 2011, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update No. 2011-04 (ASU 2011-04), *Fair Value Measurement: Amendments to Achieve Common Fair Value Measurements and Disclosure Requirements in U.S. GAAP and IFRS*. Some of the key amendments to the fair value measurement guidance include the highest and best use and valuation premise for nonfinancial assets, application to financial assets and financial liabilities with offsetting positions in market risks or counterparty credit risk, premiums or discounts in fair value measurement and fair value of an instrument classified in a reporting entity's shareholders' equity. Additional disclosures for fair

Edgar Filing: CONTINENTAL AIRLINES INC /DE/ - Form 10-Q

value measurements categorized in Level 3 of the fair value hierarchy include a quantitative disclosure of the unobservable inputs and assumptions used in the measurement, a description of the valuation processes in place, a narrative description of the sensitivity of the fair value to changes in unobservable inputs and interrelationships between those inputs and the level in the fair value hierarchy of

Table of Contents

items that are not measured at fair value in the consolidated balance sheet but whose fair value must be disclosed. ASU 2011-04 became effective for the Company's annual and interim periods beginning January 1, 2012, and the required disclosures are disclosed in Note 6 of this report.

NOTE 3 EARNINGS (LOSS) PER SHARE

The table below represents the computation of UAL basic and diluted earnings (loss) per share amounts and the number of securities that have been excluded from the computation of diluted earnings (loss) per share amounts because they were antidilutive (in millions, except per share amounts):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2012	2011	2012	2011
UAL basic earnings (loss) per share:				
Net income (loss)	\$ 6	\$ 653	\$ (103)	\$ 978
Less: Income allocable to participating securities		(2)		(3)
Earnings (loss) available to common stockholders	\$ 6	\$ 651	\$ (103)	\$ 975
Basic weighted average shares outstanding	331	330	331	329
Earnings (loss) per share, basic	\$ 0.02	\$ 1.97	\$ (0.31)	\$ 2.96
UAL diluted earnings (loss) per share:				
Earnings (loss) available to common stockholders	\$ 6	\$ 651	\$ (103)	\$ 975
Effect of UAL 4.5% Senior Limited-Subordination Convertible Notes		2		31
Effect of Continental 4.5% Convertible Notes		2		7
Effect of Continental 6% Convertible Junior Subordinated Debentures		4		
Effect of UAL 6% Senior Convertible Notes		4		13
Earnings (loss) available to common stockholders including the effect of dilutive securities	\$ 6	\$ 663	\$ (103)	\$ 1,026
UAL diluted shares outstanding:				
Basic weighted average shares outstanding	331	330	331	329
Effect of stock options	1	1		2
Effect of UAL 4.5% Senior Limited-Subordination Convertible Notes		5		13
Effect of Continental 4.5% Convertible Notes		12		12
Effect of Continental 6% Convertible Junior Subordinated Debentures		4		
Effect of UAL 6% Senior Convertible Notes		40		40
Diluted weighted average shares outstanding	332	392	331	396
Earnings (loss) per share, diluted	\$ 0.02	\$ 1.69	\$ (0.31)	\$ 2.59
UAL potentially dilutive shares excluded from diluted per share amounts:				
Restricted stock and stock options	5	7	6	6
UAL 4.5% Senior Limited-Subordination Convertible Notes	5		5	
Continental 4.5% Convertible Notes	12		12	
Continental 6% Convertible Junior Subordinated Debentures	4		4	4
UAL 6% Senior Convertible Notes	40		40	

UAL's 6% Senior Notes due 2031 (the "6% Senior Notes"), with a principal amount of \$652 million as of September 30, 2012, and the \$125 million of UAL's 8% Contingent Senior Notes (the "8% Notes") issued by UAL in January 2012, are redeemable with either cash or shares of UAL common stock, or in the case of mandatory redemption, a combination thereof, at UAL's option. The Company is obligated to issue an additional

Edgar Filing: CONTINENTAL AIRLINES INC /DE/ - Form 10-Q

\$62.5 million of the 8% Notes by February 2013, which are also redeemable on the same terms as the 6% Senior Notes and the other 8% Notes. These notes are not included in the diluted earnings (loss) per share calculation because it is UAL's intent to redeem these notes with cash if UAL were to decide to redeem these notes.

Table of Contents

During the second quarter of 2011, UAL repurchased at par value approximately \$570 million of the \$726 million outstanding principal amount of its 4.5% Senior Limited-Subordination Convertible Notes due 2021 (the 4.5% Notes) with cash after the 4.5% Notes were put to UAL by the noteholders. For the three and nine months ended September 30, 2011, the dilutive effect of the 4.5% Notes was excluded from the diluted earnings per share calculations from the date that notice was given of the Company's intent to pay the notes put to it in cash up to the June 30, 2011 repurchase date.

NOTE 4 INCOME TAXES

Our effective tax rates are lower than the federal statutory rate of 35% primarily because of the impact of changes to existing valuation allowances. We continue to provide a valuation allowance for our deferred tax assets in excess of deferred tax liabilities because we have concluded that it is more likely than not that such deferred tax assets will ultimately not be realized.

The ultimate realization of deferred tax assets is dependent upon the generation of future taxable income (including the reversals of deferred tax liabilities) during the periods in which those deferred tax assets will become deductible. The Company's management assesses available positive and negative evidence regarding the realizability of its deferred tax assets, and records a valuation allowance when it is more likely than not that all or a portion of the deferred tax assets will not be realized. To form a conclusion, management considers positive evidence in the form of reversing temporary differences, projections of future taxable income and tax planning strategies, and negative evidence such as recent history of losses. Although the Company was no longer in a three-year cumulative loss position at the end of 2011, management determined that the size and frequency of financial losses in recent years and the uncertainty associated with projecting future taxable income supported the conclusion that the valuation allowance was still needed on net deferred tax assets. If UAL achieves significant profitability in 2012 and the economic and industry outlook supports a continued expectation of profitability, then management will evaluate whether its recent history of profitability constitutes sufficient positive evidence to support a reversal of a portion, or all, of the remaining valuation allowance.

NOTE 5 EMPLOYEE BENEFIT PLANS

Defined Benefit Pension and Other Postretirement Benefit Plans. The Company's net periodic benefit cost includes the following components (in millions):

	Pension Benefits		Other Postretirement Benefits	
	Three Months Ended September 30,		Three Months Ended September 30,	
	2012	2011	2012	2011
UAL				
Service cost	\$ 25	\$ 22	\$ 11	\$ 11
Interest cost	45	44	30	32
Expected return on plan assets	(33)	(36)		(1)
Amortization of unrecognized (gain) loss and prior service cost	4	(5)		
Net periodic benefit costs	\$ 41	\$ 25	\$ 41	\$ 42
United				
Service cost	\$ 2	\$ 2	\$ 8	\$ 8
Interest cost	2	2	27	29
Expected return on plan assets	(2)	(3)		(1)
Amortization of unrecognized gain and prior service cost	(1)		(1)	
Net periodic benefit costs	\$ 1	\$ 1	\$ 34	\$ 36
Continental				
Service cost	\$ 23	\$ 20	\$ 3	\$ 3
Interest cost	43	42	3	3
Expected return on plan assets	(31)	(33)		
Amortization of unrecognized (gain) loss and prior service cost	5	(5)	1	

Edgar Filing: CONTINENTAL AIRLINES INC /DE/ - Form 10-Q

Net periodic benefit costs	\$ 40	\$ 24	\$ 7	\$ 6
----------------------------	-------	-------	------	------

Table of Contents

	Pension Benefits Nine Months Ended September 30,		Other Postretirement Benefits Nine Months Ended September 30,	
	2012	2011	2012	2011
UAL				
Service cost	\$ 75	\$ 66	\$ 37	\$ 35
Interest cost	137	133	93	95
Expected return on plan assets	(103)	(105)	(2)	(2)
Amortization of unrecognized (gain) loss and prior service cost	15	(17)	(2)	(1)
Net periodic benefit costs	\$ 124	\$ 77	\$ 126	\$ 127
United				
Service cost	\$ 6	\$ 5	\$ 26	\$ 25
Interest cost	6	7	82	85
Expected return on plan assets	(8)	(8)	(2)	(2)
Amortization of unrecognized gain and prior service cost	(1)	(1)	(3)	
Net periodic benefit costs	\$ 3	\$ 3	\$ 103	\$ 108
Continental				
Service cost	\$ 69	\$ 61	\$ 11	\$ 10
Interest cost	131	126	11	10
Expected return on plan assets	(95)	(97)		
Amortization of unrecognized (gain) loss and prior service cost	16	(16)	1	(1)
Net periodic benefit costs	\$ 121	\$ 74	\$ 23	\$ 19

During the nine months ended September 30, 2012, Continental contributed \$167 million to its tax-qualified defined benefit pension plans. Continental contributed an additional \$41 million to its tax-qualified defined benefit pension plans in October 2012.

Share-Based Compensation. In February 2012, UAL granted share-based compensation awards pursuant to the United Continental Holdings, Inc. 2008 Incentive Compensation Plan. These share-based compensation awards include approximately 0.5 million shares of restricted stock and 0.6 million restricted stock units (RSUs) that vest pro-rata over three years on the anniversary of the grant date. In addition, UAL granted 1.3 million performance-based RSUs that will vest based on UAL's return on invested capital for the three years ending December 31, 2014. If this performance condition is achieved, cash payments will be made after the end of the performance period based on the 20-day average closing price of UAL common stock immediately prior to the vesting date. The Company accounts for the RSUs as liability awards. The table below presents information related to share-based compensation (in millions):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2012	2011	2012	2011
Share-based compensation expense (a)	\$ 18	\$ 13	\$ 44	\$ 40

	September 30, 2012	December 31, 2011
Unrecognized share-based compensation expense	\$43	\$43

(a) Includes \$0 and \$7 million of expense recognized in integration-related costs for the three and nine months ended September 30, 2012, respectively. Includes \$3 million and \$12 million of expense recognized in integration-related costs for the three and nine months ended September 30, 2011, respectively.

Profit Sharing Plans. In 2012, substantially all employees participate in profit sharing, which pays 15% of total pre-tax earnings, excluding special items and share-based compensation expense, to eligible employees when pre-tax profit, excluding special items, profit sharing expense and share-based compensation program expense, exceeds \$10 million. Eligible U.S. co-workers in each participating work group receive a profit sharing payout using a formula based on the ratio of each qualified co-worker's annual eligible earnings to the eligible earnings of all qualified co-workers in all domestic workgroups. The international profit sharing plan pays eligible non-U.S. co-workers the same percentage of eligible pay that is calculated under the U.S. profit sharing plan. Profit sharing expense is recorded as a component of salaries and related costs in the consolidated statements of operations.

Table of Contents**NOTE 6 FINANCIAL INSTRUMENTS AND FAIR VALUE MEASUREMENTS**

The table below presents disclosures about the financial assets and financial liabilities measured at fair value on a recurring basis in the Company's financial statements as of September 30, 2012 and December 31, 2011 (in millions):

	Total	September 30, 2012			Total	December 31, 2011		
		Level 1	Level 2	Level 3		Level 1	Level 2	Level 3
UAL								
Cash and cash equivalents	\$ 5,129	\$ 5,129	\$	\$	\$ 6,246	\$ 6,246	\$	\$
Short-term investments:								
Asset-backed securities	647		647		478		478	
Corporate debt	340		340		515		515	
Certificates of deposit placed through an account registry service (CDARS)	404		404		355		355	
Auction rate securities	115			115	113			113
U.S. government and agency notes	15		15		22		22	
Other fixed income securities	30		30		33		33	
Enhanced equipment trust certificates (EETC)	62			62	60			60
Fuel derivatives, net	33		33		73		73	
Foreign currency derivatives					(1)		(1)	
Restricted cash	471	471			569	569		
United								
Cash and cash equivalents	\$ 3,005	\$ 3,005	\$	\$	\$ 3,458	\$ 3,458	\$	\$
Short-term investments:								
Asset-backed securities	16		16		29		29	
Corporate debt	140		140		138		138	
CDARS	156		156		87		87	
U.S. government and agency notes	8		8		5		5	
Other fixed income securities	26		26		16		16	
EETC	62			62	60			60
Fuel derivatives, net	24		24		44		44	
Restricted cash	354	354			433	433		
Continental								
Cash and cash equivalents	\$ 2,119	\$ 2,119	\$	\$	\$ 2,782	\$ 2,782	\$	\$
Short-term investments:								
Asset-backed securities	631		631		449		449	
Corporate debt	200		200		377		377	
CDARS	248		248		268		268	
Auction rate securities	115			115	113			113
U.S. government and agency notes	7		7		17		17	
Other fixed income securities	4		4		17		17	
Fuel derivatives, net	9		9		29		29	
Foreign currency derivatives					(1)		(1)	
Restricted cash	116	116			135	135		
Convertible debt derivative asset	202			202	193			193
Convertible debt option liability	(91)			(91)	(95)			(95)

Table of Contents

The tables below present disclosures about the activity for Level 3 financial assets and financial liabilities for the three and nine months ended September 30 (in millions):

UAL (a)	Three Months Ended September 30,			
	2012		2011	
	Auction Rate Securities	EETC	Auction Rate Securities	EETC
Balance at June 30	\$ 112	\$ 63	\$ 121	\$ 65
Settlements		(2)		(2)
Gains (losses):				
Reported in earnings unrealized	1		1	
Reported in other comprehensive income (loss)	2	1	(1)	(3)
Balance at September 30	\$ 115	\$ 62	\$ 121	\$ 60

(a) For 2012 and 2011, United's only Level 3 recurring measurements are the above EETCs.

UAL (a)	Nine Months Ended September 30,			
	2012		2011	
	Auction Rate Securities	EETC	Auction Rate Securities	EETC
Balance at January 1	\$ 113	\$ 60	\$ 119	\$ 66
Settlements		(5)		(4)
Gains (losses):				
Reported in earnings unrealized			2	
Reported in other comprehensive income (loss)	2	7		(2)
Balance at September 30	\$ 115	\$ 62	\$ 121	\$ 60

(a) For 2012 and 2011, United's only Level 3 recurring measurements are the above EETCs.

Continental	Three Months Ended September 30,					
	2012			2011		
	Auction Rate Securities	Convertible Debt Supplemental Derivative Asset (a)	Convertible Debt Conversion Option Liability (a)	Auction Rate Securities	Convertible Debt Supplemental Derivative Asset (a)	Convertible Debt Conversion Option Liability (a)
Balance at June 30	\$ 112	\$ 289	\$ (147)	\$ 121	\$ 251	\$ (143)
Sales						
Gains (losses):						
Reported in earnings unrealized	1	(87)	56	1	(52)	40
Reported in other comprehensive income (loss)	2			(1)		
Balance at September 30	\$ 115	\$ 202	\$ (91)	\$ 121	\$ 199	\$ (103)

Edgar Filing: CONTINENTAL AIRLINES INC /DE/ - Form 10-Q

- (a) These derivatives are not designated as hedges. The Convertible Debt Supplemental Derivative Asset is classified in Other Asset Other, net , and the Convertible Debt Conversion Option Liability is classified in Other liabilities and deferred credits Other in Continental s consolidated balance sheets. The earnings impact is classified in Nonoperating income (expense) Miscellaneous, net in Continental s statements of consolidated operations.

Table of Contents

	Nine Months Ended September 30,					
	Auction Rate Securities	2012 Convertible Debt Supplemental Derivative Asset (a)	Convertible Debt Conversion Option Liability (a)	Auction Rate Securities	2011 Convertible Debt Supplemental Derivative Asset (a)	Convertible Debt Conversion Option Liability (a)
Continental						
Balance at January 1	\$ 113	\$ 193	\$ (95)	\$ 119	\$ 286	\$ (164)
Sales						
Gains (losses):						
Reported in earnings unrealized		9	4	2	(87)	61
Reported in other comprehensive income (loss)	2					
Balance at September 30	\$ 115	\$ 202	\$ (91)	\$ 121	\$ 199	\$ (103)

(a) These derivatives are not designated as hedges. The Convertible Debt Supplemental Derivative Asset is classified in Other Asset Other, net, and the Convertible Debt Conversion Option Liability is classified in Other liabilities and deferred credits Other in Continental's consolidated balance sheets. The earnings impact is classified in Nonoperating income (expense) Miscellaneous, net in Continental's statements of consolidated operations.

As of September 30, 2012, Continental's auction rate securities, which had a par value of \$135 million, were variable-rate debt instruments with contractual maturities generally greater than ten years and with interest rates that reset every 7, 28 or 35 days, depending on the terms of the particular instrument. These securities are backed by pools of student loans guaranteed by state-designated guaranty agencies and reinsured by the U.S. government. All of the auction rate securities that Continental holds are senior obligations under the applicable indentures authorizing the issuance of the securities.

As of September 30, 2012, United's EETC securities had unrealized gains of \$1 million. All changes in the fair value of these investments have been classified within accumulated other comprehensive income.

Continental's debt-related derivatives presented in the tables above relate to (a) supplemental indenture agreements that provide that Continental's convertible debt, which was previously convertible into shares of Continental common stock, is convertible into shares of UAL common stock upon the terms and conditions specified in the indentures, and (b) the embedded conversion options in Continental's convertible debt that are required to be separated and accounted for as though they are free-standing derivatives as a result of the Continental debt becoming convertible into the common stock of a different reporting entity. These derivatives are reported in Continental's separate financial statements and eliminated in consolidation for UAL.

The table below presents the carrying values and estimated fair values of financial instruments not presented in the tables above as of September 30, 2012 and December 31, 2011 (in millions):

	Carrying Amount	Fair Value of Debt by Fair Value Hierarchy Level							
		September 30, 2012				December 31, 2011			
		Total	Level 1	Level 2	Level 3	Total	Level 1	Level 2	Level 3
UAL debt	\$ 11,296	\$ 12,320	\$ 7,015	\$ 5,305	\$ 11,682	\$ 11,992	\$ 859	\$ 11,133	
United debt	5,169	5,436	1,994	3,442	5,745	5,630		5,630	
Continental debt	5,724	6,050	4,187	1,863	5,528	5,503		5,503	

Table of Contents**Quantitative Information About Level 3 Fair Value Measurements as of September 30, 2012 (\$ in millions)**

Item	Fair Value at September 30, 2012	Valuation Technique	Unobservable Input	Range (Weighted Average)
Auction rate securities	\$ 115	Discounted Cash Flows	Credit risk premium (a) Illiquidity premium (b) Expected repayments (c)	1% 5% Assumed repayment in years 2013 through 2036
EETC	62	Discounted Cash Flows	Structure credit risk (d)	6% - 7% (7%)
Convertible debt derivative asset	202	Binomial Lattice Model	Expected volatility (e) Own credit risk (f)	45% - 60% (48%) 7% - 10% (8%)
Convertible debt option liability	(91)	Binomial Lattice Model	Expected volatility (e) Own credit risk (f)	45% - 60% (49%) 7% - 10% (8%)

- (a) Represents the credit risk premium component of the discount rate that the Company has determined market participants would use in pricing the investments.
- (b) Represents the illiquidity premium component of the discount rate that the Company has determined market participants would use in pricing the investments.
- (c) Represents the estimated timing of principal repayments used in the discounted cash flow model.
- (d) Represents the credit risk premium of the EETC structure above the risk-free rate that the Company has determined market participants would use in pricing the instruments.
- (e) Represents the range in volatility estimates that the Company has determined market participants would use when pricing the instruments.
- (f) Represents the range of Company-specific risk adjustments that the Company has determined market participants would use as a model input.

Valuation Processes Level 3 Measurements The Company's internal valuation group is responsible for determining the fair value of financial instruments. Depending on the instrument, the valuation group utilizes discounted cash flow methods or option pricing methods as indicated above. Valuations using discounted cash flow methods are generally conducted by the valuation group. Valuations using option pricing models are generally provided to the Company by third-party valuation experts. Each reporting period, the valuation group reviews the unobservable inputs used by third-party valuation experts for reasonableness utilizing relevant information available to the Company from other published sources. The Company has a formal process to review changes in fair value for satisfactory explanation.

Sensitivity Analysis Level 3 Measurements Changes in the unobservable input values would be unlikely to cause material changes in the fair value of the auction rate securities and EETCs.

The significant unobservable inputs used in the fair value measurement of the Continental convertible debt derivative assets and liabilities are the UAL stock expected volatility and the Company's own credit risk. Significant increases (decreases) in expected volatility would result in a higher (lower) fair value measurement. Significant increases (decreases) in the Company's own credit risk would result in a lower (higher) fair value measurement. A change in one of the inputs would not necessarily result in a directionally similar change in the other.

Table of Contents

Fair value of the financial instruments included in the tables above was determined as follows:

Description	Fair Value Methodology
<i>Cash and Cash Equivalents</i>	The carrying amounts approximate fair value because of the short-term maturity of these assets.
<i>Short - term Investments, Investments, and Restricted Cash</i>	Fair value is based on (a) the trading prices of the investment or similar instruments, (b) an income approach, which uses valuation techniques to convert future amounts into a single present amount based on current market expectations about those future amounts when observable trading prices are not available, or (c) internally-developed models of the expected future cash flows related to the securities. These assets have maturities of less than one year except for the EETCs, auction rate securities and corporate debt.
<i>Fuel Derivatives</i>	Derivative contracts are privately negotiated contracts and are not exchange traded. Fair value measurements are estimated with option pricing models that employ observable inputs. Inputs to the valuation models include contractual terms, market prices, yield curves, fuel price curves and measures of volatility, among others.
<i>Foreign Currency Derivatives</i>	Fair value is determined with a formula utilizing observable inputs. Significant inputs to the valuation models include contractual terms, risk-free interest rates and forward exchange rates.
<i>Debt</i>	Fair values were based on either market prices or the discounted amount of future cash flows using our current incremental rate of borrowing for similar liabilities.
<i>Convertible Debt Derivative Asset and Option Liability</i>	The Company used a binomial lattice model to value the conversion options and the supplemental derivative assets. Significant binomial model inputs that are not objectively determinable include volatility and discount rate.

NOTE 7 HEDGING ACTIVITIES

Aircraft Fuel Hedges. The Company has a risk management strategy to hedge a portion of its price risk related to projected aircraft fuel requirements. The Company periodically enters into derivative contracts to mitigate the adverse financial impact of potential increases in the price of fuel. The Company does not enter into derivative instruments for speculative, non-risk management purposes.

Upon proper qualification, the Company accounts for certain fuel derivative instruments as cash flow hedges. All derivatives designated as hedges that meet certain requirements are granted special hedge accounting treatment. The types of instruments the Company utilizes that qualify for special hedge accounting treatment typically include swaps, call options and collars (which consist of a purchased call option and a sold put option). Generally, utilizing the special hedge accounting, all periodic changes in fair value of the derivatives designated as hedges that are considered to be effective are recorded in accumulated other comprehensive income (loss) (AOCI) until the underlying fuel is consumed and recorded in fuel expense. The Company is exposed to the risk that its hedges may not be effective in offsetting changes in the cost of fuel and that its hedges may not continue to qualify for special hedge accounting. Hedge ineffectiveness results when the change in the fair value of the derivative instrument exceeds the change in the value of the Company's expected future cash outlay to purchase and consume fuel. To the extent that the periodic changes in the fair value of the derivatives are not effective, that ineffectiveness is classified as other nonoperating income (expense).

The Company also utilizes certain derivative instruments that are economic hedges but do not qualify for hedge accounting under US GAAP. As with derivatives that qualify for hedge accounting, the purpose of these economic hedges is to mitigate the adverse financial impact of potential increases in the price of fuel. Currently, the only such economic hedges in the Company's hedging portfolio are three-way collars (which consist of a sold call option, a purchased call option, and a sold put option). The Company records changes in the fair value of three-way collars to other nonoperating income (expense).

The Company records each derivative instrument as a derivative asset or liability on a gross basis in its consolidated balance sheets and, accordingly, records any related collateral on a gross basis.

Table of Contents

As of September 30, 2012, our projected fuel requirements for the remainder of 2012 were hedged as follows:

	Maximum Price		Minimum Price	
	% of Expected Consumption	Weighted Average Price (per gallon)	% of Expected Consumption	Weighted Average Price (per gallon)
UAL (a)				
Heating oil collars	20%	\$ 3.56	20%	\$ 2.80
Brent crude oil collars	14	2.76	14	1.93
Diesel fuel collars	9	3.28	9	2.45
Diesel fuel call options	1	3.25	N/A	N/A
Total	44%		43%	

(a) As of September 30, 2012, UAL had also hedged 26% of its projected first half 2013 fuel consumption.

The following tables present information about the financial statement classification of the Company's derivatives (in millions):

Classification	Balance Sheet Location	September 30, 2012			December 31, 2011		
		UAL	United	Continental	UAL	United	Continental
Derivatives designated as cash flow hedges							
<i>Assets:</i>							
Fuel contracts due within one year	Receivables	\$ 27	\$ 17	\$ 10	\$ 77	\$ 48	\$ 29
<i>Liabilities:</i>							
Fuel contracts due within one year	Current liabilities: Other	\$ 7	\$ 4	\$ 3	\$ 4	\$ 4	\$
Derivatives not designated as hedges							
<i>Assets:</i>							
Fuel contracts due within one year	Receivables	\$ 17	\$ 13	\$ 4	\$	\$	\$
<i>Liabilities:</i>							
Fuel contracts due within one year	Current liabilities: Other	\$ 2	\$ 1	\$ 1	\$	\$	\$
Fuel contracts with maturities greater than one year	Other liabilities and deferred credits: Other	2	1	1			
Total liabilities		\$ 4	\$ 2	\$ 2	\$	\$	\$
Total derivatives							
<i>Assets:</i>							
Fuel contracts due within one year	Receivables	\$ 44	\$ 30	\$ 14	\$ 77	\$ 48	\$ 29
<i>Liabilities:</i>							
Fuel contracts due within one year	Current liabilities: Other	\$ 9	\$ 5	\$ 4	\$ 4	\$ 4	\$
Fuel contracts with maturities greater than one year	Other liabilities and deferred credits: Other	2	1	1			

Total liabilities	\$ 11	\$ 6	\$ 5	\$ 4	\$ 4	\$
-------------------	-------	------	------	------	------	----

Table of Contents

The following tables present the impact of derivative instruments and their location within the unaudited Statements of Consolidated Operations:

Derivatives designated as cash flow hedges

	Amount of Gain (Loss) Recognized in AOCI on Derivatives (Effective portion) Three Months Ended September 30,		Gain (Loss) Reclassified from AOCI into Income (Fuel Expense) Three Months Ended September 30,		Amount of Gain (Loss) Recognized in Income (Nonoperating Expense) (Ineffective Portion) Three Months Ended September 30,	
	2012	2011	2012	2011	2012	2011
Fuel contracts						
UAL	\$ 133	\$ (181)	\$ (38)	\$ 94	\$ 2	\$ (56)
United	77	(91)	(23)	90	1	(33)
Continental	56	(90)	(15)	4	1	(23)

	Amount of Gain (Loss) Recognized in AOCI on Derivatives (Effective portion) Nine Months Ended September 30,		Gain (Loss) Reclassified from AOCI into Income (Fuel Expense) Nine Months Ended September 30,		Amount of Loss Recognized in Income (Nonoperating Expense) (Ineffective Portion) Nine Months Ended September 30,	
	2012	2011	2012	2011	2012	2011
Fuel contracts						
UAL	\$ (36)	\$ 112	\$ (107)	\$ 526	\$ (2)	\$ (87)
United	(13)	145	(55)	427	(1)	(38)
Continental	(23)	(33)	(52)	99	(1)	(49)

Derivatives not designated as hedges

	Amount of Gain Recognized in Income (Nonoperating Expense) Three Months Ended September 30,		Amount of Gain Recognized in Income (Nonoperating Expense) Nine Months Ended September 30,	
	2012	2011	2012	2011
Fuel contracts				
UAL	\$ 10	\$	\$ 10	\$
United	8		8	
Continental	2		2	

Derivative Credit Risk and Fair Value

The Company is exposed to credit losses in the event of nonperformance by counterparties to its derivative instruments. While the Company records derivative instruments on a gross basis, the Company monitors its net derivative position with each counterparty to monitor credit risk. Based on the fair value of our fuel derivative instruments, our counterparties may require us to post collateral when the price of the underlying commodity decreases, and we may require our counterparties to provide us with collateral when the price of the underlying commodity increases. The following table presents information related to the Company's derivative credit risk as of September 30, 2012 (in millions):

UAL United Continental

Edgar Filing: CONTINENTAL AIRLINES INC /DE/ - Form 10-Q

Net derivative asset with counterparties	\$ 33	\$ 24	\$ 9
Collateral posted by the Company with its counterparties (a)			
Potential loss related to the failure of the Company's counterparties to perform	34	25	9

(a) Classified as a current receivable.

Table of Contents**NOTE 8 COMMITMENTS AND CONTINGENCIES**

General Guarantees and Indemnifications. In the normal course of business, the Company enters into numerous real estate leasing and aircraft financing arrangements that have various guarantees included in the contracts. These guarantees are primarily in the form of indemnities under which the Company typically indemnifies the lessors and any tax/financing parties against tort liabilities that arise out of the use, occupancy, operation or maintenance of the leased premises or financed aircraft. Currently, the Company believes that any future payments required under these guarantees or indemnities would be immaterial, as most tort liabilities and related indemnities are covered by insurance (subject to deductibles). Additionally, certain leased premises such as fueling stations or storage facilities include indemnities of such parties for any environmental liability that may arise out of or relate to the use of the leased premises.

Legal and Environmental Contingencies. The Company has certain contingencies resulting from litigation and claims incident to the ordinary course of business. Management believes, after considering a number of factors, including (but not limited to) the information currently available, the views of legal counsel, the nature of contingencies to which the Company is subject and prior experience, that the ultimate disposition of these contingencies will not materially affect the Company's consolidated financial position or results of operations.

The Company records liabilities for legal and environmental claims when a loss is probable and reasonably estimable. These amounts are recorded based on the Company's assessments of the likelihood of their eventual disposition.

Commitments. As of September 30, 2012, UAL, United and Continental had the following commitments to purchase aircraft:

UAL Aircraft Commitments. UAL had firm commitments to purchase 100 new Boeing 737 MAX 9 aircraft scheduled for delivery from 2018 through 2022. UAL also had options to purchase an additional 100 Boeing 737 MAX 9 aircraft. UAL had the right, and intends in the future, to assign its interest under the purchase agreement for the 737 MAX 9 aircraft with respect to one or more of the aircraft to either United or Continental.

United Aircraft Commitments. United had firm commitments to purchase 100 new aircraft (25 Boeing 787 aircraft, 50 Boeing 737-900ER aircraft and 25 Airbus A350XWB aircraft) scheduled for delivery from 2013 through 2019. United also had options and purchase rights for 164 additional Boeing and Airbus aircraft.

Continental Aircraft Commitments. Continental had firm commitments to purchase 68 new aircraft (44 Boeing 737 aircraft and 24 Boeing 787 aircraft) scheduled for delivery from October 1, 2012 through 2016. Continental also had options to purchase 83 Boeing aircraft. From October 1, 2012 through December 31, 2012, Continental expects to take delivery of six Boeing 737-900ER aircraft and four Boeing 787-8 aircraft.

Continental had arranged for EETC financing of 20 Boeing 737-900ER aircraft and six Boeing 787-8 aircraft scheduled for delivery through July 2013. In addition, United had secured considerable backstop financing commitments from its widebody aircraft and engine manufacturers, subject to certain customary conditions. See Note 9 of this report for additional information. However, UAL and United do not have backstop financing or any other financing currently in place for their firm narrowbody aircraft orders with Boeing, and Continental does not have backstop financing or any other financing currently in place for its other Boeing aircraft on order. Financing will be necessary to satisfy the Company's capital commitments for its firm order aircraft and other related capital expenditures. The Company can provide no assurance that any financing not already in place for aircraft and spare engine deliveries will be available to the Company on acceptable terms when necessary or at all.

UAL and Continental have concluded their discussions with Boeing regarding delays in delivery of certain Boeing 787 aircraft, and have reached a resolution with Boeing regarding compensation to be received in connection with those delays, which is reflected in the table below.

The table below summarizes the capital commitments of UAL, United and Continental as of September 30, 2012, which primarily relate to the acquisition of aircraft and related spare engines, aircraft improvements and acquisition of information technology services and assets. As UAL has the right, and intends in the future, to assign its interest under the purchase agreement for the 737 MAX 9 aircraft with respect to one or more of the aircraft to either United or Continental, but has not determined the actual assignment of the Boeing 737 MAX 9 aircraft between United and Continental, the table below assumes that 50% of the Boeing 737 MAX 9 order is assigned to United and 50% of the Boeing 737 MAX 9 order is assigned to Continental.

Table of Contents

	In billions		
	UAL	United	Continental
Last three months of 2012	\$ 0.9	\$ 0.3	\$ 0.6
2013	1.5	0.5	1.0
2014	1.7	0.8	0.9
2015	1.9	0.8	1.1
2016	2.8	2.0	0.8
After 2016	9.6	7.2	2.4
	\$ 18.4	\$ 11.6	\$ 6.8

Any incremental firm aircraft orders, including through the exercise of purchase options, will increase the total future capital commitments of the Company, United and/or Continental.

Credit Card Processing Agreements. United and Continental have agreements with financial institutions that process customer credit card transactions for the sale of air travel and other services. Under certain of United's and Continental's credit card processing agreements, the financial institutions either require, or under certain circumstances have the right to require, that United and Continental maintain a reserve equal to a portion of advance ticket sales that have been processed by that financial institution, but for which United and Continental have not yet provided the air transportation.

As of September 30, 2012, \$25 million was provided by the Company as a cash reserve for its credit card processing agreement with JPMorgan Chase Bank, N.A. and Paymentech, LLC. Our credit card processing agreement with JPMorgan Chase Bank, N.A. and Paymentech, LLC to process MasterCard/Visa transactions and our credit card processing agreement with American Express allow the applicable financial institution to require additional cash or other collateral reserves to be established or additional withholding of payments related to receivables collected if the Company does not maintain certain minimum levels of unrestricted cash, cash equivalents and short term investments. The Company's current level of unrestricted cash, cash equivalents and short term investments is substantially in excess of these minimum levels. The amount of required cash or other collateral reserves or withheld payments would be no more than the liability of the credit card processor for tickets purchased with the applicable credit cards for travel that had not occurred. In conjunction with the single passenger service system conversion in March 2012, all tickets sold since that date have been on United ticket stock. As a result, the advance ticket sales by Continental have diminished and are expected to be zero by March 2013.

Guarantees and Off-Balance Sheet Financing.

Guarantees. United and Continental are the guarantors of approximately \$270 million and \$1.6 billion, respectively, in aggregate principal amount of tax-exempt special facilities revenue bonds and interest thereon. These bonds, issued by various airport municipalities, are payable solely from rentals paid under long-term agreements with the respective governing bodies. The leasing arrangements associated with \$1.7 billion (\$270 million for United and \$1.4 billion for Continental) of these obligations are accounted for as operating leases with the associated expense recorded on a straight-line basis resulting in ratable accrual of the lease obligation over the expected lease term. The leasing arrangements associated with \$190 million (for Continental only) of these obligations are accounted for as capital leases. These bonds are due between 2015 and 2033.

In the Company's financing transactions that include loans, the Company typically agrees to reimburse lenders for any reduced returns with respect to the loans due to any change in capital requirements and, in the case of loans in which the interest rate is based on the London Interbank Offered Rate (LIBOR), for certain other increased costs that the lenders incur in carrying these loans as a result of any change in law, subject in most cases to obligations of the lenders to take certain limited steps to mitigate the requirement for, or the amount of, such increased costs. At September 30, 2012, UAL had \$2.6 billion of floating rate debt (consisting of United's \$1.9 billion and Continental's \$676 million of debt) and \$357 million of fixed rate debt (consisting of United's \$191 million and Continental's \$166 million of debt), with remaining terms of up to ten years, that are subject to these increased cost provisions. In several financing transactions involving loans or leases from non-U.S. entities, with remaining terms of up to nine years and an aggregate balance of \$2.9 billion (consisting of United's \$2.1 billion and Continental's \$762 million balance), the Company bears the risk of any change in tax laws that would subject loan or lease payments thereunder to non-U.S. entities to withholding taxes, subject to customary exclusions.

Houston Bush Terminal B Redevelopment Project. In May 2011, UAL, in partnership with the Houston Airport System, announced that it would begin construction of the first phase of a potential three-phase \$1 billion terminal improvement project for Terminal B at George Bush Intercontinental Airport (Houston Bush) by the end of 2011. In November 2011, the City of Houston issued approximately \$113 million of special facilities revenue bonds to finance the construction of a new south concourse at Houston Bush dedicated to the Company's regional jet operations. The bonds are guaranteed by Continental and

Table of Contents

are payable from certain rentals paid by Continental under a special facilities lease agreement with the City of Houston. Continental's initial commitment is to construct the first phase of the originally anticipated three-phase project. Continental's cost of construction of phase one of the project is currently estimated to be approximately \$100 million and is funded by special facilities revenue bonds. Construction of the remaining phases of the project, if any, will be based on demand over the next seven to 10 years, with phase one currently expected to be completed in late 2013.

Based on a qualitative assessment of the Houston Bush Terminal B Redevelopment Project, due to the fact that Continental is guaranteeing the special facilities revenue bonds and the requirement that Continental fund cost overruns with no stated limits, Continental is considered the owner of the property during the construction period for accounting purposes. As a result, the construction project is being treated as a financing transaction such that the property and related financing will be included on UAL's consolidated balance sheet as an asset under operating property and equipment and as a construction obligation under other long-term liabilities.

Credit Facilities. As of September 30, 2012 the Company had its entire commitment capacity of \$500 million available under the Credit and Guaranty Agreement, dated as of December 22, 2011 (the Revolving Credit Facility) with a syndicate of banks led by Citibank N.A., as administrative agent. The Revolving Credit Facility has an expiration date of January 30, 2015.

Labor Negotiations. As of September 30, 2012, UAL and its subsidiaries had approximately 88,000 active employees, of whom approximately 80% are represented by various labor organizations. On February 27, 2012, the pilots at both United and Continental agreed to an extension of their protocol for joint negotiations and continue to engage in joint bargaining with the Company for a combined collective bargaining agreement. On August 3, 2012, the Company announced it had reached an agreement in principle with respect to a new joint collective bargaining agreement with the Air Line Pilots Association, International (ALPA) representing pilots at United and Continental. The agreement in principle is subject to definitive documentation, and any such definitive documentation is subject to approvals by each of the United and Continental ALPA master executive councils and ratification by the Company's pilots. See Note 10 of this report for additional information related to negotiations with the pilots work group.

On February 28, 2012, the flight attendants at United ratified a new collective bargaining agreement and, on July 13, 2012, the flight attendants at Continental ratified a new collective bargaining agreement. On July 17, 2012, the Company reached a tentative agreement with its Continental Micronesia flight attendants, which was ratified on August 17, 2012. Joint negotiations will begin shortly for a joint collective bargaining agreement covering all of the Company's flight attendant work groups.

We are currently in the process of negotiating joint collective bargaining agreements with all of our represented employee groups, including our pilots, fleet and passenger service agents, reservations agents, flight attendants, technicians, dispatchers and storekeepers. Achieving joint collective bargaining agreements with our represented employee groups is likely to increase our labor costs, which increase could be material.

NOTE 9 DEBT

As of September 30, 2012, a substantial portion of our assets are pledged as collateral for our debt. These assets principally consist of aircraft and the related spare parts and engines, route authorities and loyalty program intangible assets. As of September 30, 2012, UAL, United and Continental were in compliance with their respective debt covenants.

Continental EETCs. In March 2012, Continental created two pass-through trusts that issued an aggregate principal amount of \$892 million of pass-through certificates. Proceeds from the sale of the certificates are used to purchase equipment notes issued by Continental. Of the \$892 million in proceeds raised by the pass-through trusts, Continental had received \$577 million as of September 30, 2012, in exchange for Continental's issuance of an equivalent principal amount of equipment notes, which has been recorded as debt. The remaining amount is expected to be received during the last three months of this year as aircraft are delivered to Continental and Continental issues equipment notes to the trusts. Continental records the debt obligation upon issuance of the equipment notes rather than upon the initial issuance of the pass-through certificates. The proceeds have been and are expected to be used to fund the acquisition of new aircraft, and in the case of currently owned aircraft, for general corporate purposes.

In October 2012, Continental created two pass-through trusts, one of which issued \$712 million aggregate principal amount of Class A pass-through certificates with a stated interest rate of 4% and the second of which issued \$132 million aggregate principal amount of Class B pass-through certificates with a stated interest rate of 5.5%. The proceeds of the issuance of the Class A and Class B pass-through certificates, which amounted to \$844 million, will be used to purchase equipment notes issued by Continental. Continental has not yet received any of the proceeds raised by the pass-through trusts. Continental expects to receive the proceeds from the issuance starting in the fourth quarter of 2012 and continuing through the first seven months of 2013 as aircraft are delivered to Continental and Continental issues equipment notes to the trusts. Continental records the debt obligation upon issuance of the equipment notes rather than upon the initial issuance of the pass-through

certificates. The proceeds are expected to be used to fund the acquisition of new aircraft.

Table of Contents

The Company evaluated whether the pass-through trusts formed are variable interest entities (VIEs) required to be consolidated by the Company under applicable accounting guidance, and determined that the pass-through trusts are VIEs. The Company determined that it does not have a variable interest in the pass-through trusts. The Company does not invest in or obtain a financial interest in the pass-through trusts. Rather, Continental has an obligation to make interest and principal payments on its equipment notes held by the pass-through trusts. The Company did not intend to have any voting or non-voting equity interest in the pass-through trusts or to absorb variability from the pass-through trusts. Based on this analysis, the Company determined that it is not required to consolidate the pass-through trusts.

8% Contingent Senior Notes. UAL is obligated under an indenture to issue to the Pension Benefit Guaranty Corporation (PBGC) up to \$500 million aggregate principal amount of 8% Notes in up to eight equal tranches of \$62.5 million if certain financial triggering events occur (with each tranche issued no later than 45 days following the end of any applicable fiscal year).

During 2011, a financial triggering event under the 8% Notes indenture occurred at both June 30, 2011 and December 31, 2011 and, as a result, UAL issued two tranches of \$62.5 million each of the 8% Notes in January 2012, which were recorded during 2011 at their fair value of \$88 million as a component of integration costs. In addition, at June 30, 2012, a financial triggering event under the 8% Notes indenture occurred and, as a result, UAL is obligated to issue an additional tranche of \$62.5 million of the 8% Notes by February 2013. UAL recorded a liability for the fair value of the obligation of \$48 million during the second quarter of 2012.

Special Facility Revenue Refunding Bonds. In August 2012, the New Jersey Economic Development Authority (the Authority) issued approximately \$101 million of special facility revenue bonds (the 2012 Bonds) to provide funds for the defeasance of approximately \$100 million of the Authority s previously issued and outstanding special facility revenue bonds maturing on September 15, 2012 (the Refunded Bonds). The Refunded Bonds were guaranteed by Continental and payable from certain rental payments made by Continental pursuant to two lease agreements between the Authority and Continental. The 2012 Bonds are payable from certain loan repayments made by Continental under a loan agreement between Continental and the Authority. The 2012 Bonds are recorded by Continental as unsecured long-term debt.

NOTE 10 SPECIAL ITEMS

Special Revenue. During the second quarter of 2011, the Company modified the previously existing United and Continental co-branded credit card agreements with Chase Bank USA, N.A. This modification resulted in the following one-time adjustment to decrease frequent flyer deferred revenue and increase special revenue in accordance with ASU 2009-13 for the nine months ended September 30, 2011 as follows (in millions):

	UAL	United	Continental
Special revenue item	\$ 107	\$ 88	\$ 19

Table of Contents

Special Charges. For the three and nine months ended September 30, special charges consisted of the following (in millions):

	Three Months Ended September 30,			Nine Months Ended September 30,		
	UAL	United	Continental	UAL	United	Continental
2012						
Labor agreement costs	\$ 454	\$ 296	\$ 158	\$ 454	\$ 296	\$ 158
Integration-related costs	60	36	24	331	205	126
Voluntary severance and benefits				125	125	
Gains on sale of assets and other special charges, net				(26)	(22)	(4)
Subtotal special charges	514	332	182	884	604	280
Income tax benefit				(2)		(2)
Total special charges, net of income taxes	\$ 514	\$ 332	\$ 182	\$ 882	\$ 604	\$ 278
2011						
Integration-related costs	\$ 123	\$ 72	\$ 51	\$ 347	\$ 236	\$ 111
Gains on aircraft sales	(3)		(3)	(4)		(4)
Total	\$ 120	\$ 72	\$ 48	\$ 343	\$ 236	\$ 107

On August 3, 2012, the Company announced it had reached an agreement in principle with respect to a new joint collective bargaining agreement with ALPA representing pilots at United and Continental. The Company recorded \$454 million of expense in the third quarter associated with lump sum cash payments that would be made in conjunction with the ratification of the contract and the completion of the integrated pilot seniority list. This charge also includes costs associated with changes to existing pilot disability plans negotiated in connection with the agreement in principle. The lump sum payments are not in lieu of future pay increases and were accrued in the third quarter as a result of the payments becoming probable, primarily due to reaching the agreement in principle. The agreement in principle is subject to definitive documentation, and any such definitive documentation is subject to approvals by each of the United and Continental ALPA master executive councils and ratification by the Company's pilots. The Company currently expects to make cash payments of approximately \$250 million in late 2012 or early 2013 relating to these charges and the balance in subsequent periods.

Integration-related costs include compensation costs related to systems integration and training, costs to repaint aircraft and other branding activities, costs to write-off or accelerate depreciation on systems and facilities that are no longer used or planned to be used for significantly shorter periods, relocation costs for employees and severance primarily associated with administrative headcount reductions.

In addition, financial triggering events under the 8% Notes indenture occurred at both June 30, 2012 and 2011 and as a result, UAL became obligated to issue one tranche of \$62.5 million in aggregate principal amount of the 8% Notes with respect to each of these financial triggering events. The obligation to issue these tranches was recorded at their fair values of \$48 million and \$49 million as of June 30, 2012 and 2011, respectively. Both obligations described above were recorded as integration-related costs because the financial results of UAL, excluding Continental's results, would not have resulted in triggering events under the 8% Notes indenture.

During the nine months ended September 30, 2012, the Company recorded \$125 million of severance and benefits associated with three voluntary employee programs. During the first quarter of 2012, approximately 400 mechanics offered to retire early in exchange for a cash severance payment that was based on the number of years of service each employee had accumulated. The Company also offered a voluntary leave of absence program that approximately 1,800 flight attendants accepted, which allows for continued medical coverage during the leave of absence period. During the second quarter of 2012, as part of the recently amended collective bargaining agreement with the Association of Flight Attendants, the Company offered a voluntary program for flight attendants at United to retire early in exchange for a cash severance payment. The payments are dependent on the number of years of service each employee has accumulated. Approximately 1,300 flight attendants accepted this program and the expense for this voluntary program is approximately \$76 million.

In addition, the Company sold nine aircraft during the first nine months of 2012. The Company also made adjustments to certain legal reserves.

Edgar Filing: CONTINENTAL AIRLINES INC /DE/ - Form 10-Q

The Company expects to consolidate its headquarters facilities by mid-2013. During the consolidation process, the Company expects to record special charges for accelerated depreciation and lease expense on unused facilities associated with the facility that it vacates. The Company estimates that future charges will be approximately \$45 million to \$65 million in total, which are expected to be recorded in late 2012 through 2013.

Table of Contents***Accruals***

The accrual for severance and medical costs was \$59 million, \$42 million and \$17 million related to UAL, United and Continental, respectively, as of September 30, 2012. In addition, the accrual balance of future lease payments on permanently grounded aircraft was \$6 million for both UAL and United as of September 30, 2012.

The severance-related accrual as of September 30, 2012, which primarily relates to the integration of United and Continental, is expected to be paid through 2014. Lease payments for grounded aircraft are expected to continue through 2013.

At September 30, 2011, the accrual balance for severance and medical costs was \$73 million, \$42 million and \$31 million related to UAL, United and Continental, respectively. In addition, the accrual balance of future lease payments on permanently grounded aircraft was \$31 million for both UAL and United as of September 30, 2011.

NOTE 11 RELATED PARTY TRANSACTIONS***Intercompany transactions United and Continental***

United and Continental perform services for one another including various aircraft maintenance services, aircraft ground handling and jet fuel provisions at certain airports. For the three and nine months ended September 30, 2012, United provided \$196 million and \$317 million of services to Continental, respectively, and Continental provided \$61 million and \$155 million of services to United, respectively. These amounts do not include interline billings, which are common among airlines for various transportation-related services. Many of these transactions are routinely settled through the clearing house, which is customarily used in the monthly settlement of such items. Transactions not settled through the clearing house are typically settled in cash on a quarterly basis. As of September 30, 2012, Continental had a net current payable of \$2.5 billion to United primarily related to the transfer of the current portion of the frequent flyer liability and the cash transfer from United in conjunction with the conversion to the new passenger service system, as described below. In addition, Continental had a \$448 million noncurrent payable to United associated with the transfer of the long-term portion of the frequent flyer liability at September 30, 2012.

Frequent flyer program transition

In the first quarter of 2012, the Company moved to a single loyalty program. Continental's loyalty program formally ended in the first quarter of 2012, at which point United automatically enrolled Continental OnePass program members in the MileagePlus program and deposited into those MileagePlus accounts award miles equal to these members' OnePass award miles balance. In March 2012, the related frequent flyer deferred revenue and advance purchase of miles liabilities for the OnePass program was transferred to United with a corresponding liability recorded by Continental payable to United for assuming the frequent flyer obligations. No gain or loss was incurred from the transaction as the liabilities were transferred at their respective net book value. The obligation associated with this transfer will be settled by Continental through future redemptions by MileagePlus members on Continental operated flights.

Passenger service system and ticket stock integration

In March 2012, Continental and United converted to a single passenger service system, allowing the Company to operate using a single reservations system, carrier code, flight schedule, website and departure control system. In conjunction with the conversion to a single passenger service system, all tickets are now sold by United. As a result, the air traffic liability of Continental is diminishing as tickets previously sold by Continental are used or refunded and United's advanced ticket sales liability and associated cash receipts from the ticket sales will increase accordingly. Subsequent to the system conversion, United transferred cash to Continental each month, such transfers being netted against amounts owed to Continental for segments flown by Continental on United ticket stock. Revenue will continue to be recorded by the carrier that is operating the flight.

Revenue and expense allocation

In November 2011, the Company received a single operating certificate from the Federal Aviation Administration. The Company plans to merge Continental and United into one legal entity. Once this legal merger occurs, the financial statements of United and Continental will be combined at their historical cost for all periods presented beginning on October 1, 2010, the date on which Continental became a wholly-owned subsidiary of UAL, and there will no longer be a requirement to separately report the historical financial statements of Continental.

Edgar Filing: CONTINENTAL AIRLINES INC /DE/ - Form 10-Q

Until Continental and United are merged into one legal entity, revenue and expenses will continue to be recorded by each entity based on either specific identification of the related transaction, where applicable, or appropriate allocations based on metrics that are systematic and rational. Certain revenues and expenses that were previously recorded based on a specific identification were allocated in March 2012 in connection with the conversion to a single passenger service system. We believe the allocated amounts will generally be comparable to historical amounts.

Table of Contents

Each airline will continue to record actual expenses for aircraft that are owned or leased and passenger revenue will be determined on an actual basis for the carrier operating the flight. The table below illustrates a summary of the primary allocation metrics to be used:

Account	Allocation metric between subsidiaries
<i>Operating revenue:</i>	
Passenger	Actual ticket revenue based on specifically identified flights operated by each carrier. Frequent flyer component of passenger revenue is allocated to Continental based on historic revenue passenger miles (RPMs) split between carriers and rate at which outstanding frequent flyer liability was transferred from Continental to United at single passenger service system conversion for calculating frequent flyer impact. Regional revenue, based on the carrier that contracted with the regional carrier
Cargo	Actual by operating carrier
Other operating	Passenger related based on passenger revenue and other based on passengers enplaned or other similar criteria
<i>Operating expense:</i>	
Aircraft fuel	Actual by operating carrier
Salaries and related costs	Actual for operational workgroups and allocation based on historical RPMs for administrative personnel. Profit sharing expense is allocated based on the proportional profit of each operating entity
Regional capacity purchase	Actual based on specific identification of the carrier that contracted with regional carrier for flying
Landing fees and other rent	Allocation based on passengers enplaned
Aircraft maintenance materials and outside repairs	Actual based on the specific identification of each carrier's aircraft
Depreciation and amortization	Specific identification of carriers' operational assets (i.e. flight equipment) and intangible assets and allocation based on historical RPMs for other assets
Distribution expenses	Allocation based on passenger revenue
Aircraft rent	Actual based on specific identification of each carrier's aircraft
Special charges	Specific identification. Labor agreement costs are allocated based on salaries of respective work groups
Other operating expenses	Specific identification where applicable and allocation based on historical RPMs for other
Total net revenue allocated from United to Continental amounted to \$332 million and \$760 million for the three and nine months ended September 30, 2012, respectively.	

Total net expenses allocated from United to Continental amounted to \$109 million and \$232 million for the three and nine months ended September 30, 2012, respectively.

Table of Contents

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS.

Overview

United Continental Holdings, Inc. (together with its consolidated subsidiaries, "UAL") is a holding company and its principal, wholly-owned subsidiaries are United Air Lines, Inc. (together with its consolidated subsidiaries, "United") and Continental Airlines, Inc. (together with its consolidated subsidiaries, "Continental"). All significant intercompany transactions are eliminated.

This Quarterly Report on Form 10-Q is a combined report of UAL, United and Continental. We sometimes use the words "we," "our," "us," and "the Company" for disclosures that relate to all of UAL, United and Continental. As UAL consolidates United and Continental for financial statement purposes, disclosures that relate to United and Continental activities also apply to UAL. When appropriate, UAL, United and Continental are named specifically for their related activities and disclosures.

The Company transports people and cargo through its mainline operations, which utilize jet aircraft with at least 100 seats, and regional operations, which utilize smaller aircraft that are operated under contract by United Express carriers. The Company serves virtually every major market around the world, either directly or through participation in Star Alliance®, the world's largest airline alliance. The Company offers approximately 5,600 daily departures to 378 destinations.

Third Quarter Financial Highlights

UAL's third quarter 2012 net income was \$520 million, or \$1.35 diluted earnings per share, excluding \$514 million of special charges, net of tax. Including special charges, UAL's third quarter 2012 net income was \$6 million, or \$0.02 diluted earnings per share.

UAL's passenger revenue decreased 2.6% during the third quarter of 2012 as compared to the third quarter of 2011.

UAL's third quarter 2012 fuel cost increased 1.0% year-over-year.

UAL's unrestricted liquidity was \$7.2 billion, including \$500 million of undrawn commitments under a revolving credit facility.

Third Quarter Operational Highlights

UAL's traffic and capacity decreased 1.5% and 1.4%, respectively, during the third quarter of 2012 as compared to the third quarter of 2011. The Company's load factor for the third quarter of 2012 was 85.2%.

For the quarter ended September 30, 2012, the Company recorded a U.S. Department of Transportation on-time arrival rate of 72.4% and a system completion factor of 98.6%.

The Company took delivery of one new Boeing 787-8 aircraft and three new Boeing 737-900ER aircraft during the third quarter of 2012.

Outlook

In order to generate sustained profitability over the business cycle, the Company manages its capacity to meet balance with expected demand for travel. The Company has reduced and plans to reduce full year 2012 consolidated capacity by reducing flight frequencies, indefinitely postponing the start of flights to certain markets and exiting less profitable markets. For the first nine months of 2012, consolidated capacity decreased 0.6% compared to the nine months ended September 30, 2011, and, as compared to 2011 capacity, the Company expects full-year

Edgar Filing: CONTINENTAL AIRLINES INC /DE/ - Form 10-Q

2012 consolidated capacity to decrease 1.0% to 1.2% year-over-year, with full-year 2012 domestic capacity to decrease 1.8% to 2.0% and full-year 2012 international capacity to be between a decrease of 0.1% and an increase of 0.1%. The Company is also analyzing the removal of certain less fuel-efficient aircraft from its fleet and other cost-saving measures.

Integration

The Company has made significant progress in integrating its products, services, policies and a number of information technology systems. During the third quarter, the Company continued to redeploy aircraft across its global network, better matching aircraft and demand on a route by route basis. In August 2012, the Company reached an agreement in principle with respect to a new joint collective bargaining agreement with the Air Line Pilots Association, International representing pilots at United and Continental.

RESULTS OF OPERATIONS

The following discussion provides an analysis of UAL's results of operations and reasons for material changes therein for the three and nine months ended September 30, 2012 as compared to the corresponding periods in 2011.

Table of Contents**Third Quarter 2012 Compared to Third Quarter 2011**

UAL recorded net income of \$6 million in the third quarter of 2012 as compared to net income of \$653 million in the third quarter of 2011. Excluding special items, UAL had net income of \$520 million in the third quarter of 2012 as compared to net income of \$773 million in the third quarter of 2011. See **Reconciliation of GAAP to non-GAAP Financial Measures** at the end of this item for additional information related to non-GAAP financial measures. We consider a key measure of our performance to be operating income, which was \$200 million for the third quarter of 2012, as compared to \$935 million for the third quarter of 2011. Significant components of our operating results for the three months ended September 30 are as follows (in millions, except percentage changes):

	2012	2011	Increase (Decrease)	% Increase (Decrease)
Operating Revenue	\$ 9,909	\$ 10,171	\$ (262)	(2.6)
Operating Expenses	9,709	9,236	473	5.1
Operating Income	200	935	(735)	(78.6)
Nonoperating Expense	(185)	(275)	(90)	(32.7)
Income Tax Expense	9	7	2	28.6
Net Income	\$ 6	\$ 653	\$ (647)	(99.1)

Certain consolidated statistical information for UAL's operations for the three months ended September 30 is as follows:

	2012	2011	Increase (Decrease)	% Increase (Decrease)
Passengers (thousands) (a)	37,588	38,019	(431)	(1.1)
Revenue Passenger Miles (RPMs) (millions) (b)	56,021	56,853	(832)	(1.5)
Available Seat Miles (ASMs) (millions) (c)	65,734	66,635	(901)	(1.4)
Passenger load factor (d)	85.2%	85.3%	(0.1) pts.	N/A
Passenger revenue per available seat mile (PRASM) (cents)	13.35	13.52	(0.17)	(1.3)
Average yield per revenue passenger mile (cents) (e)	15.66	15.85	(0.19)	(1.2)
Cost per available seat mile (CASM) (cents)	14.77	13.86	0.91	6.6
Average price per gallon of fuel, including fuel taxes	\$ 3.19	\$ 3.16	\$ 0.03	0.9
Fuel gallons consumed (millions)	1,069	1,066	3	0.3
Average full-time equivalent employees	85,400	82,300	3,100	3.8

- (a) The number of revenue passengers measured by each flight segment flown.
(b) The number of scheduled miles flown by revenue passengers.
(c) The number of seats available for passengers multiplied by the number of scheduled miles those seats are flown.
(d) Revenue passenger miles divided by available seat miles.
(e) The average passenger revenue received for each revenue passenger mile flown.

Operating Revenue

The table below shows year-over-year comparisons by type of operating revenue for the three months ended September 30 (in millions, except for percentage changes):

	2012	2011	Increase (Decrease)	% Change
Passenger Mainline	\$ 6,993	\$ 7,237	\$ (244)	(3.4)

Edgar Filing: CONTINENTAL AIRLINES INC /DE/ - Form 10-Q

Passenger Regional	1,781	1,772	9	0.5
Total passenger revenue	8,774	9,009	(235)	(2.6)
Cargo	246	283	(37)	(13.1)
Other operating revenue	889	879	10	1.1
	\$ 9,909	\$ 10,171	\$ (262)	(2.6)

NM- Not meaningful

Table of Contents

The table below presents selected passenger revenue and operating data, broken out by geographic region, expressed as third quarter year-over-year changes:

	Domestic	Pacific	Atlantic	Latin	Total Mainline	Regional	Consolidated
Increase (decrease) from 2011:							
Passenger revenue (in millions)	\$ (203)	\$ 144	\$ (139)	\$ (46)	\$ (244)	\$ 9	\$ (235)
Passenger revenue	(5.8)%	11.0%	(8.0)%	(6.8)%	(3.4)%	0.5%	(2.6)%
Average fare per passenger	(1.3)%	2.8%	(4.4)%	(7.4)%	(0.2)%	(2.6)%	(1.5)%
Yield	(2.6)%	7.2%	(3.7)%	(9.4)%	(1.5)%	(0.9)%	(1.2)%
PRASM	(4.2)%	9.9%	(4.5)%	(8.3)%	(2.0)%	1.6%	(1.3)%
Average stage length	2.9%	0.8%	0.2%	2.7%	2.4%	(1.1)%	1.2%
Passengers	(4.5)%	8.0%	(3.8)%	0.6%	(3.2)%	3.2%	(1.1)%
RPMs (traffic)	(3.2)%	3.6%	(4.5)%	2.9%	(1.9)%	1.4%	(1.5)%
ASMs (capacity)	(1.7)%	1.0%	(3.7)%	1.6%	(1.4)%	(1.1)%	(1.4)%
Passenger load factor (points)	(1.4)	2.1	(0.7)	1.1	(0.4)	2.0	(0.1)

Consolidated passenger revenue in the third quarter of 2012 decreased 2.6% as compared to the year-ago period due to a reduction in capacity which resulted in a decline in the number of passengers flown year-over-year. Additionally, the consolidated average fare per passenger and yield declined 1.5% and 1.2%, respectively, during the third quarter of 2012 versus the same period in 2011.

Cargo revenue decreased \$37 million, or 13.1%, in the third quarter of 2012 as compared to the year-ago period due to lower volumes on freight across all regions except Latin America.

Operating Expenses

The table below includes data related to UAL's operating expenses for the three months ended September 30 (in millions, except for percentage changes):

	2012	2011	Increase (Decrease)	% Change
Aircraft fuel	\$ 3,406	\$ 3,371	\$ 35	1.0
Salaries and related costs	2,038	2,020	18	0.9
Regional capacity purchase	628	619	9	1.5
Landing fees and other rent	504	476	28	5.9
Aircraft maintenance materials and outside repairs	469	447	22	4.9
Depreciation and amortization	379	384	(5)	(1.3)
Distribution expenses	356	377	(21)	(5.6)
Aircraft rent	245	255	(10)	(3.9)
Special charges	514	120	394	NM
Other operating expenses	1,170	1,167	3	0.3
	\$ 9,709	\$ 9,236	\$ 473	5.1

Aircraft fuel expense increased \$35 million, or 1.0%, year-over-year due primarily to fuel hedge losses in the current quarter versus gains in the third quarter of 2011. The table below presents the significant changes in aircraft fuel cost per gallon in the three month period ended September 30, 2012 as compared to the year-ago period:

Table of Contents

	(In millions)			Average price per gallon		
	2012	2011	% Change	2012	2011	% Change
Total aircraft fuel purchase cost excluding fuel hedge impacts	\$ 3,368	\$ 3,465	(2.8)	\$ 3.15	\$ 3.25	(3.1)
Fuel hedge gains (losses) reported in fuel expense	(38)	94	NM	(0.04)	0.09	NM
Fuel expense as reported	3,406	3,371	1.0	3.19	3.16	0.9
Fuel hedge non-cash mark-to-market gains (losses) (a)	12	(56)	NM	0.02	(0.05)	NM
Fuel expense including all fuel hedge impacts	\$ 3,394	\$ 3,427	(1.0)	\$ 3.17	\$ 3.21	(1.2)
Total fuel consumption (gallons)	1,069	1,066	0.3			

(a) Includes ineffectiveness gains (losses) and non-cash mark-to-market gains (losses) on all open fuel hedge positions. These amounts are recorded in Nonoperating income (expense): Miscellaneous, net.

Salaries and related costs increased \$18 million, or 0.9%, in the third quarter of 2012 as compared to the year-ago period due to several factors, including a 3.8% increase in the number of average full-time employees, higher pay rates primarily driven by new joint collective bargaining agreements, and overtime for airport and call center employees related to our conversion to a single passenger service system offset by decreases in profit sharing.

Landing fees and other rent increased \$28 million, or 5.9%, in the third quarter of 2012 as compared to the year-ago period primarily due to credits (refunds) received in 2011 as a result of certain airports' audits of prior period payment, and an increase in such fees paid in 2012 as compared to 2011.

Aircraft maintenance materials and outside repairs increased \$22 million, or 4.9%, in the third quarter of 2012 as compared to the year-ago period due primarily to higher rates on maintenance contracts.

Distribution expenses decreased \$21 million, or 5.6%, in the third quarter of 2012 as compared to the year-ago period due to reduced fees with our online ticket agents, lower credit card discount fees driven by legislation reducing costs on debit card sales, and lower volume of global distribution systems fees paid in 2012 as compared to 2011.

Details of UAL's special charges include the following for the three months ended September 30 (in millions):

	2012	2011
Labor agreement costs	\$ 454	\$
Integration-related costs	60	123
Gains on sale of assets and other special charges, net		(3)
Special charges	\$ 514	\$ 120

See Note 10 to the financial statements included in Part I, Item I of this report.

Nonoperating Income (Expense). The following table illustrates the year-over-year dollar and percentage changes in UAL's nonoperating income (expense) for the three months ended September 30 (in millions, except for percentage changes):

	2012	2011	Increase (Decrease)	% Change
Interest expense	\$ (202)	\$ (227)	\$ (25)	(11.0)
Interest capitalized	9	10	(1)	(10.0)
Interest income	4	6	(2)	(33.3)

Edgar Filing: CONTINENTAL AIRLINES INC /DE/ - Form 10-Q

Miscellaneous, net	4	(64)	(68)	NM
Total	\$ (185)	\$ (275)	\$ (90)	(32.7)

Interest expense decreased \$25 million, or 11.0%, in the third quarter of 2012, compared to the year-ago period primarily due to a decrease in debt outstanding during the third quarter of 2012 as compared to debt outstanding during the year-ago period.

Table of Contents

During the third quarter of 2012, miscellaneous, net included a fuel hedge ineffectiveness gain of \$2 million primarily resulting from an increase in fuel hedge values in excess of the increase in aircraft fuel prices as compared to a fuel hedge ineffectiveness loss of \$56 million in the year ago period. Third quarter 2012 miscellaneous, net also included mark-to-market gains of \$10 million from derivatives not qualifying for hedge accounting as compared to \$0 in the year ago period.

Income Taxes. Our effective tax rates are lower than the federal statutory rate of 35% primarily because of the impact of changes to existing valuation allowances. We continue to provide a valuation allowance for our deferred tax assets in excess of deferred tax liabilities because management has concluded that it is more likely than not that such deferred tax assets will ultimately not be realized. See Note 4 to the financial statements contained in Part I, Item 1 of this report for information related to this matter.

First Nine Months 2012 Compared to First Nine Months 2011

UAL recorded a net loss of \$103 million in the first nine months of 2012 as compared to net income of \$978 million in the first nine months of 2011. Excluding special items, UAL had net income of \$779 million in the first nine months of 2012 as compared to net income of \$1.2 billion in the first nine months of 2011. See Reconciliation of GAAP to non-GAAP Financial Measures at the end of this item for additional information related to non-GAAP financial measures. We consider a key measure of our performance to be operating income, which was \$504 million for the first nine months of 2012, as compared to \$1.8 billion for the first nine months of 2011. Significant components of our operating results for the first nine months of 2012 are as follows (in millions, except percentage changes):

	2012	2011	Increase (Decrease)	% Increase (Decrease)
Operating Revenue	\$ 28,450	\$ 28,182	\$ 268	1.0
Operating Expenses	27,946	26,405	1,541	5.8
Operating Income	504	1,777	(1,273)	(71.6)
Nonoperating Expense	(596)	(786)	(190)	(24.2)
Income Tax Expense	11	13	(2)	(15.4)
Net Income (Loss)	\$ (103)	\$ 978	\$ (1,081)	NM

NM - Not meaningful

Certain consolidated statistical information for UAL's operations for the nine months ended September 30 is as follows:

	2012	2011	Increase (Decrease)	% Increase (Decrease)
Passengers (thousands) (a)	107,186	107,608	(422)	(0.4)
RPMs (millions) (b)	157,619	158,062	(443)	(0.3)
ASMs (millions) (c)	190,694	191,814	(1,120)	(0.6)
Passenger load factor (d)	82.7%	82.4%	0.3 pts.	N/A
PRASM (cents)	13.14	12.87	0.27	2.1
Average yield per revenue passenger mile (cents) (e)	15.89	15.62	0.27	1.7
CASM (cents)	14.65	13.77	0.88	6.4
Average price per gallon of fuel, including fuel taxes	\$ 3.27	\$ 3.02	\$ 0.25	8.3
Fuel gallons consumed (millions)	3,071	3,069	2	0.1
Average full-time equivalent employees	84,600	81,500	3,100	3.8

Edgar Filing: CONTINENTAL AIRLINES INC /DE/ - Form 10-Q

- (a) The number of revenue passengers measured by each flight segment flown.
- (b) The number of scheduled miles flown by revenue passengers.
- (c) The number of seats available for passengers multiplied by the number of scheduled miles those seats are flown.
- (d) Revenue passenger miles divided by available seat miles.
- (e) The average passenger revenue received for each revenue passenger mile flown.

Table of Contents**Operating Revenue**

The table below shows year-over-year comparisons by type of operating revenue for the nine months ended September 30 (in millions, except for percentage changes):

	2012	2011	Increase (Decrease)	% Change
Passenger Mainline	\$ 19,891	\$ 19,780	\$ 111	0.6
Passenger Regional	5,159	4,916	243	4.9
Total passenger revenue	25,050	24,696	354	1.4
Cargo	775	882	(107)	(12.1)
Special revenue item		107	(107)	NM
Other operating revenue	2,625	2,497	128	5.1
	\$ 28,450	\$ 28,182	\$ 268	1.0

The table below presents selected passenger revenue and operating data, broken out by geographic region, expressed as year-over-year changes for the nine months ended September 30, 2012 compared to the nine months ended September 30, 2011:

	Domestic	Pacific	Atlantic	Latin	Total Mainline	Regional	Consolidated
Increase (decrease) from 2011:							
Passenger revenue (in millions)	\$ (142)	\$ 344	\$ (99)	\$ 8	\$ 111	\$ 243	\$ 354
Passenger revenue	(1.4)%	9.9%	(2.2)%	0.4%	0.6%	4.9%	1.4%
Average fare per passenger	2.0%	3.3%	0.3%	(0.7)%	2.8%	1.4%	1.8%
Yield	0.5%	5.5%	0.5%	(3.3)%	1.1%	3.2%	1.7%
PRASM	0.3%	5.5%	0.3%	(1.6)%	1.1%	6.1%	2.1%
Average stage length	2.8%	2.2%	0.9%	2.8%	3.0%	(2.5)%	1.3%
Passengers	(3.4)%	6.5%	(2.5)%	1.2%	(2.2)%	3.5%	(0.4)%
RPMs (traffic)	(1.9)%	4.2%	(2.7)%	3.9%	(0.6)%	1.7%	(0.3)%
ASMs (capacity)	(1.7)%	4.1%	(2.5)%	2.0%	(0.5)%	(1.1)%	(0.6)%
Passenger load factor (points)	(0.3)		(0.2)	1.4		2.2	0.3

Consolidated passenger revenue in the first nine months of 2012 increased 1.4% as compared to the year-ago period primarily due to increases in consolidated average fare per passenger and yield, which increased by 1.8% and 1.7%, respectively. Passenger revenue increased in 2011 as a result of certain accounting changes. In conjunction with these changes, the Company recorded a special adjustment in 2011 to decrease frequent flyer deferred revenue and increase revenue by \$107 million in connection with a modification to its co-branded credit card agreement with Chase Bank USA, N.A.

Cargo revenue decreased \$107 million, or 12.1%, in the first nine months of 2012 as compared to the year-ago period due to lower volumes on freight and mail across all regions.

Other operating revenue increased \$128 million, or 5.1%, in the first nine months of 2012 as compared to the year-ago period primarily due to an increase in sales volume of miles to third parties.

Table of Contents**Operating Expenses**

The table below includes data related to UAL's operating expenses for the nine months ended September 30 (in millions, except for percentage changes):

	2012	2011	Increase (Decrease)	% Change
Aircraft fuel	\$ 10,043	\$ 9,270	\$ 773	8.3
Salaries and related costs	5,959	5,742	217	3.8
Regional capacity purchase	1,887	1,807	80	4.4
Landing fees and other rent	1,476	1,451	25	1.7
Aircraft maintenance materials and outside repairs	1,308	1,330	(22)	(1.7)
Depreciation and amortization	1,137	1,157	(20)	(1.7)
Distribution expenses	1,038	1,102	(64)	(5.8)
Aircraft rent	747	760	(13)	(1.7)
Special charges	884	343	541	NM
Other operating expenses	3,467	3,443	24	0.7
	\$ 27,946	\$ 26,405	\$ 1,541	5.8

Aircraft fuel expense increased \$773 million, or 8.3%, year-over-year due to fuel hedge losses in the first nine months of 2012 versus gains in the first nine months of 2011. The table below presents the significant changes in aircraft fuel cost per gallon in the nine months ended September 30, 2012 as compared to the year-ago period.

	(In millions)			Average price per gallon		
	2012	2011	% Change	2012	2011	% Change
Total aircraft fuel purchase cost excluding fuel hedge impacts	\$ 9,936	\$ 9,796	1.4	\$ 3.24	\$ 3.19	1.6
Fuel hedge gains (losses) reported in fuel expense (a)	(107)	526	NM	(0.03)	0.17	NM
Fuel expense as reported	10,043	9,270	8.3	3.27	3.02	8.3
Settled fuel hedge losses not recorded in fuel expense (b)	(1)	(5)	NM			NM
Fuel expense including all gains (losses) from settled fuel hedges	10,044	9,275	8.3	3.27	3.02	8.3
Fuel hedge non-cash mark-to-market gains (losses) (c)	9	(82)	NM		(0.03)	NM
Fuel expense including all fuel hedge impacts	\$ 10,035	\$ 9,357	7.2	\$ 3.27	\$ 3.05	7.2
Total fuel consumption (gallons)	3,071	3,069	0.1			

(a) Includes gains (losses) from settled hedges that were designated for hedge accounting.

(b) Includes ineffectiveness gains (losses) and gains (losses) on derivatives not designated for hedge accounting. These amounts are recorded in Nonoperating income (expense): Miscellaneous, net.

(c) Includes ineffectiveness gains (losses) and non-cash mark-to-market gains (losses) on all open fuel hedge positions. These amounts are recorded in Nonoperating income (expense): Miscellaneous, net.

Salaries and related costs increased \$217 million, or 3.8%, in the first nine months of 2012 as compared to the year-ago period due to several factors including a 3.8% increase in the number of average full-time employees, higher pay rates primarily driven by new collective bargaining agreements, and additional overtime for airport and call center employees related to our conversion to a single passenger service system.

Regional capacity purchase increased \$80 million, or 4.4%, in the first nine months of 2012 as compared to the year-ago period primarily due to contractual amendments with one of our regional carrier partners to shift the arrangement from a prorate agreement to a capacity purchase

agreement and also due to an increase in the contractual rates with such regional carrier partner.

Distribution expenses decreased \$64 million, or 5.8%, in the first nine months of 2012 as compared to the year-ago period due to reduced fees with our online ticket agents, lower credit card discount fees driven by legislation reducing costs on debit card sales and lower volume of global distribution systems fees paid in 2012 as compared to 2011.

Table of Contents

Details of UAL's special charges include the following for the nine months ended September 30 (in millions):

	2012	2011
Labor agreement costs	\$ 454	\$
Integration-related costs	331	347
Voluntary severance and benefits	125	
Gains on sale of assets and other special charges, net	(26)	(4)
Special charges	\$ 884	\$ 343

See Note 10 to the financial statements included in Part I, Item I of this report.

Nonoperating Income (Expense). The following table illustrates the year-over-year dollar and percentage changes in UAL's nonoperating income (expense) for the first nine months September 30 (in millions, except for percentage changes):

	2012	2011	Increase (Decrease)	% Change
Interest expense	\$ (631)	\$ (731)	\$ (100)	(13.7)
Interest capitalized	26	24	2	8.3
Interest income	16	15	1	6.7
Miscellaneous, net	(7)	(94)	(87)	(92.6)
Total	\$ (596)	\$ (786)	\$ (190)	(24.2)

Interest expense decreased \$100 million, or 13.7%, in the first nine months of 2012, compared to the year-ago period primarily due to a decrease in debt outstanding during the first nine months of 2012 as compared to debt outstanding during the year-ago period.

During the first nine months of 2012, miscellaneous, net included a fuel hedge ineffectiveness loss of \$2 million primarily resulting from a decrease in fuel hedge ineffectiveness as compared to a loss of \$87 million in the year-ago period. The first nine months of 2012 miscellaneous, net also included mark-to-market gains of \$10 million from derivatives not qualifying for hedge accounting as compared to \$0 in the year ago period.

Income Taxes. Our effective tax rates are lower than the federal statutory rate of 35% primarily because of the impact of changes to existing valuation allowances. We continue to provide a valuation allowance for our deferred tax assets in excess of deferred tax liabilities because management has concluded that it is more likely than not that such deferred tax assets will ultimately not be realized. See Note 4 to the financial statements contained in Part I, Item 1 of this report for information related to this matter.

LIQUIDITY AND CAPITAL RESOURCES**Current Liquidity**

As of September 30, 2012, UAL had \$6.7 billion in unrestricted cash, cash equivalents and short-term investments, as compared to \$7.8 billion at December 31, 2011. At September 30, 2012, UAL also had \$471 million of restricted cash and cash equivalents, which is primarily collateral for performance bonds, letters of credit, estimated future workers' compensation claims and credit card processing agreements. As of September 30, 2012, the Company had its entire commitment capacity of \$500 million under the Revolving Credit Facility available for letters of credit or borrowings.

As is the case with many of our principal competitors, we have a high proportion of debt compared to capital. We have a significant amount of fixed obligations, including debt, aircraft leases and financings, leases of airport property and other facilities, and pension funding obligations. At September 30, 2012, UAL had approximately \$12.2 billion of debt and capital lease obligations, including \$1.8 billion that will become due in the next 12 months. In addition, we have substantial non-cancelable commitments for capital expenditures, including the acquisition of new

aircraft and related spare engines.

The Company will continue to evaluate opportunities to repurchase its debt in open market transactions to reduce its indebtedness and the amount of interest paid on its indebtedness.

As of September 30, 2012, UAL had firm commitments to purchase 100 Boeing 737 MAX 9 aircraft scheduled for delivery from 2018 through 2022. UAL also had options to purchase an additional 100 Boeing 737 MAX 9 aircraft. UAL had the right, and intends in the future, to assign its interest under the purchase agreement for the 737 MAX 9 aircraft with respect to one or more of the aircraft to either United or Continental.

Table of Contents

As of September 30, 2012, United had firm commitments to purchase 100 new aircraft (25 Boeing 787 aircraft, 50 Boeing 737-900ER aircraft and 25 Airbus A350XWB aircraft) scheduled for delivery from 2013 through 2019. United also had options and purchase rights for 164 additional Boeing and Airbus aircraft.

As of September 30, 2012, Continental had firm commitments to purchase 68 new aircraft (44 Boeing 737 aircraft and 24 Boeing 787 aircraft) scheduled for delivery from October 1, 2012 through 2016. Continental also had options to purchase 83 Boeing aircraft. From October 1, 2012 through December 31, 2012, Continental expects to take delivery of six Boeing 737-900ER aircraft and four Boeing 787-8 aircraft.

Continental had arranged for enhanced equipment trust certificate (EETC) financing of 20 Boeing 737-900ER aircraft and six Boeing 787-8 aircraft scheduled for delivery through July 2013. In addition, United had secured considerable backstop financing commitments from its widebody aircraft and engine manufacturers, subject to certain customary conditions. See Note 9 to the financial statements included in Part I, Item I of this report for additional information. However, UAL and United do not have backstop financing or any other financing currently in place for their firm narrowbody aircraft orders with Boeing, and Continental does not have backstop financing or any other financing currently in place for its other Boeing aircraft on order. Financing will be necessary to satisfy the Company's capital commitments for its firm order aircraft and other related capital expenditures. The Company can provide no assurance that any financing not already in place for aircraft and spare engine deliveries will be available to the Company on acceptable terms when necessary or at all.

UAL and Continental have concluded their discussions with Boeing regarding delays in delivery of certain Boeing 787 aircraft, and have reached a resolution with Boeing regarding compensation to be received in connection with those delays.

As of September 30, 2012, the Company has total capital commitments primarily related to aircraft and related spare engines, aircraft improvements and acquisition of information technology services and assets of approximately \$18.4 billion, of which approximately \$0.9 billion, \$1.5 billion, \$1.7 billion, \$1.9 billion, \$2.8 billion and \$9.6 billion are due in the last three months of 2012, 2013, 2014, 2015, 2016 and thereafter, respectively.

Any incremental firm aircraft orders, including through the exercise of purchase options, will increase the total future capital commitments of the Company, United and/or Continental.

As of September 30, 2012, a substantial portion of UAL's assets, principally aircraft, aircraft spare parts, route authorities and certain other intangible assets, were pledged under various loan and other agreements. We must sustain our profitability and/or access the capital markets to meet our significant long-term debt and capital lease obligations and future commitments for capital expenditures, including the acquisition of aircraft and related spare engines.

Credit Ratings. As of the filing date of this report, UAL, United and Continental had the following corporate credit ratings:

	S&P	Moody's	Fitch
UAL	B	B2	B
United	B	B2	B
Continental	B	B2	B

These credit ratings are below investment grade levels. Downgrades from these rating levels, among other things, could restrict the availability, or increase the cost of future financing for the Company.

Sources and Uses of Cash

Operating Activities. UAL's cash flow provided by operations for the nine months ended September 30, 2012 was \$845 million compared to \$2.1 billion in the same period in 2011. The decrease is attributable to a decrease in the Company's net income year-over-year and the cash flow impact of certain working capital items.

Investing Activities. UAL's capital expenditures, net of financings, were \$774 million and \$510 million in the nine months ended September 30, 2012 and 2011, respectively. UAL's capital expenditures for the nine months ended September 30, 2012 were primarily attributable to the purchase of new Boeing aircraft and other fleet-related expenditures to improve the onboard experience of our existing aircraft.

Edgar Filing: CONTINENTAL AIRLINES INC /DE/ - Form 10-Q

In addition to capital expenditures during the nine months ended September 30, 2012, Continental acquired four aircraft through the issuance of debt, as discussed under *Financing Activities* below.

The purchase of short-term investments decreased to \$22 million in the nine months ended September 30, 2012 from \$754 million in the nine months ended September 30, 2011.

Table of Contents

Financing Activities. In March 2012, Continental created two pass-through trusts which issued an aggregate principal amount of \$892 million of pass-through certificates. Proceeds from the sale of the certificates are used to purchase equipment notes issued by Continental. Of the \$892 million in proceeds raised by the pass-through trusts, Continental had received \$577 million as of September 30, 2012, in exchange for Continental's issuance of an equivalent principal amount of equipment notes, which has been recorded as debt. The remaining amount is expected to be received during the last three months of this year as aircraft are delivered to Continental and Continental issues equipment notes to the trusts. Continental records the debt obligation upon issuance of the equipment notes rather than upon the initial issuance of the pass-through certificates. The proceeds have been and are expected to be used to fund the acquisition of new aircraft, and in the case of currently owned aircraft, for general corporate purposes.

In October 2012, Continental created two pass-through trusts, one of which issued \$712 million aggregate principal amount of Class A pass-through certificates with a stated interest rate of 4% and the second of which issued \$132 million aggregate principal amount of Class B pass-through certificates with a stated interest rate of 5.5%. The proceeds of the issuance of the Class A and Class B pass-through certificates, which amounted to \$844 million, will be used to purchase equipment notes issued by Continental. Continental has not yet received any of the proceeds raised by the pass-through trusts. Continental expects to receive the proceeds from the issuance starting in the fourth quarter of 2012 and continuing through the first seven months of 2013 as aircraft are delivered to Continental and Continental issues equipment notes to the trusts. Continental records the debt obligation upon issuance of the equipment notes rather than upon the initial issuance of the pass-through certificates. The proceeds are expected to be used to fund the acquisition of new aircraft.

During the nine months ended September 30, 2012, UAL made debt and capital lease payments of \$1.2 billion. These payments include \$195 million related to Continental's Series 2002-1 EETCs.

In August 2012, the New Jersey Economic Development Authority (the Authority) issued approximately \$101 million of special facility revenue bonds (the 2012 Bonds) to provide funds for the defeasance of approximately \$100 million of the Authority's previously issued and outstanding special facility revenue bonds maturing on September 15, 2012 (the Refunded Bonds). The Refunded Bonds were guaranteed by Continental and payable from certain rental payments made by Continental pursuant to two lease agreements between the Authority and Continental. The 2012 Bonds are payable from certain loan repayments made by Continental under a loan agreement between Continental and the Authority. The 2012 Bonds are recorded by Continental as unsecured long-term debt.

Commitments, Contingencies and Liquidity Matters

As described in the 2011 Annual Report, the Company's liquidity may be adversely impacted by a variety of factors, including, but not limited to, obligations associated with fuel hedge settlements and related collateral requirements, pension funding obligations, reserve requirements associated with credit card processing agreements, guarantees, commitments and contingencies. See the 2011 Annual Report and Notes 5, 7, 8 and 9 to the financial statements contained in Part I, Item 1 of this report for information related to these matters.

United and Continental Results of Operations

In November 2011, the Company received a single operating certificate from the Federal Aviation Administration. The Company plans to merge Continental and United into one legal entity. Once this legal merger occurs, the financial statements of United and Continental will be combined at their historical cost for all periods presented beginning on October 1, 2010, the date on which Continental became a wholly-owned subsidiary of UAL, and there will no longer be a requirement to separately report the historical financial statements of Continental.

Until Continental and United are merged into one legal entity, revenue and expenses will continue to be recorded by each entity based on either specific identification of the related transaction, where applicable, or appropriate allocations based on metrics that are systematic and rational. Each airline will continue to record actual expenses for aircraft that are owned or leased and passenger revenue will be determined on an actual basis for the carrier operating the flight.

Table of Contents**United**

The following table presents information related to United's results of operations for the three and nine months ended September 30 (in millions, except percentage changes):

	Three Months Ended September 30,			Nine Months Ended September 30,		
	2012	2011	% Change	2012	2011	% Change
Operating Revenue:						
Passenger revenue	\$ 4,761	\$ 5,085	(6.4)	\$ 13,523	\$ 13,807	(2.1)
Special revenue items			NM		88	NM
Cargo and other revenue	895	772	15.9	2,383	2,208	7.9
Total revenue	\$ 5,656	\$ 5,857	(3.4)	\$ 15,906	\$ 16,103	(1.2)
Operating Expenses:						
Aircraft fuel	\$ 1,914	\$ 1,949	(1.8)	\$ 5,685	\$ 5,294	7.4
Salaries and related costs	1,046	1,092	(4.2)	3,166	3,117	1.6
Regional capacity purchase	387	407	(4.9)	1,152	1,190	(3.2)
Landing fees and other rent	271	246	10.2	807	773	4.4
Aircraft maintenance materials and outside repairs	313	299	4.7	862	881	(2.2)
Depreciation and amortization	232	228	1.8	695	684	1.6
Distribution expenses	172	194	(11.3)	526	580	(9.3)
Aircraft rent	78	82	(4.9)	234	243	(3.7)
Special charges	332	72	NM	604	236	NM
Other operating expenses	912	709	28.6	2,400	2,081	15.3
Total operating expenses	\$ 5,657	\$ 5,278	7.2	\$ 16,131	\$ 15,079	7.0
Operating income (loss)	\$ (1)	\$ 579	NM	\$ (225)	\$ 1,024	NM
Nonoperating expense	(119)	(162)	(26.5)	(388)	(486)	(20.2)
RPMs	30,702	31,992	(4.0)	86,763	88,638	(2.1)
ASMs	35,783	37,226	(3.9)	104,344	106,614	(2.1)

United had operating losses of \$1 million and \$225 million in the third quarter and first nine months of 2012, respectively, as compared to operating income of \$579 million and \$1 billion in the third quarter and first nine months of 2011, respectively. As compared to the third quarter of 2011, United's consolidated revenue decreased \$201 million, or 3.4%, to \$5.7 billion for the three months ended September 30, 2012. United's consolidated revenue decreased 1.2% for the nine months ended September 30, 2012 as compared to the year-ago period. These decreases are due to a decline in capacity in the third quarter and first nine months of 2012 as compared to the same periods in 2011 in addition to a one-time special revenue item in 2011.

Aircraft fuel expense decreased 1.8% and increased 7.4% in the third quarter and first nine months of 2012, respectively, as compared to the year-ago periods, which was primarily driven by volatility in market prices for aircraft fuel, as highlighted in the fuel table in *Operating Expenses*, above. Fuel hedge losses were \$23 million in the three months ended September 30, 2012, compared to fuel hedge gains of \$90 million in the three months ended September 30, 2011.

Other operating expenses increased \$203 million, or 28.6%, in the third quarter of 2012 as compared to the year-ago period, and increased \$319 million, or 15.3%, in the first nine months of 2012 as compared to 2011. These increases are primarily due to intercompany fuel transactions that are eliminated upon consolidation of the Company's financial results.

United's nonoperating expense decreased \$43 million, or 26.5%, in the third quarter of 2012 as compared to the year-ago period, and decreased \$98 million, or 20.2%, in the first nine months of 2012 as compared to the first nine months of 2011. This decrease is due to a reduction in interest expense as a result of a decrease in the principal amount of debt outstanding year-over-year in addition to larger fuel hedge ineffectiveness losses experienced in 2011.

Table of Contents**Continental**

The following table presents information related to Continental's results of operations for the three and nine months ended September 30 (in millions, except percentage changes):

	Three Months Ended September 30,			Nine Months Ended September 30,		
	2012	2011	% Change	2012	2011	% Change
Operating Revenue:						
Passenger revenue	\$ 4,013	\$ 3,922	2.3	\$ 11,527	\$ 10,884	5.9
Special revenue items			NM		19	NM
Cargo and other revenue	500	450	11.1	1,496	1,311	14.1
Total revenue	\$ 4,513	\$ 4,372	3.2	\$ 13,023	\$ 12,214	6.6
Operating Expenses:						
Aircraft fuel	\$ 1,493	\$ 1,422	5.0	\$ 4,359	\$ 3,976	9.6
Salaries and related costs	943	906	4.1	2,692	2,575	4.5
Regional capacity purchase	240	211	13.7	735	617	19.1
Landing fees and other rent	234	230	1.7	670	678	(1.2)
Aircraft maintenance materials and outside repairs	171	152	12.5	479	455	5.3
Depreciation and amortization	147	156	(5.8)	442	473	(6.6)
Distribution expenses	184	183	0.5	512	523	(2.1)
Aircraft rent	167	171	(2.3)	513	516	(0.6)
Special charges	182	48	NM	280	107	NM
Other operating expenses	549	533	3.0	1,604	1,531	4.8
Total operating expenses	\$ 4,310	\$ 4,012	7.4	\$ 12,286	\$ 11,451	7.3
Operating income	\$ 203	\$ 360	(43.6)	\$ 737	\$ 763	(3.4)
Nonoperating expense	(99)	(122)	(18.9)	(200)	(316)	(36.7)
RPMs	25,319	24,861	1.8	70,856	69,424	2.1
ASMs	29,951	29,409	1.8	86,350	85,200	1.3

Continental's operating income in the third quarter and first nine months of 2012 were \$203 million and \$737 million, respectively, as compared to operating income of \$360 million and \$763 million, respectively, in the third quarter and first nine months of 2011. As compared to the third quarter of 2011, Continental's consolidated revenue increased \$141 million, or 3.2%, to \$4.5 billion for the three months ended September 30, 2012. These improvements were largely due to year-over-year capacity discipline, which in turn resulted in higher fares, stronger yields and increased traffic, as compared to the same period in 2011. Similarly, Continental's consolidated revenue increased \$809 million, or 6.6%, to \$13 billion for the nine months ended September 30, 2012 as compared to the year-ago period.

Aircraft fuel expense increased approximately 5.0% and 9.6% in the third quarter and first nine months of 2012, respectively, as compared to the same periods in 2011, primarily due to volatility in the market prices of aircraft fuel. Fuel hedge losses were \$15 million and \$52 million in the third quarter and first nine months of 2012, respectively.

Regional capacity purchase expense increased by 13.7% and 19.1% in the third quarter and first nine months of 2012, respectively, as compared to the year-ago periods, which was primarily due to a contractual amendment with one of our regional carrier partners to shift the arrangement from a prorate agreement to a capacity purchase agreement.

Nonoperating expense includes a \$1 million gain from fuel hedge ineffectiveness in the third quarter of 2012 as compared to a \$23 million loss from fuel hedge ineffectiveness in the year ago period. Nonoperating expense also includes a \$1 million loss from fuel hedge ineffectiveness in the first nine months of 2012 as compared to a \$49 million loss from fuel hedge ineffectiveness in the first nine months of 2011. Continental's nonoperating expense in the three months ended September 30, 2012 also includes a net loss of \$31 million associated with marking to market the fair value of derivative assets and liabilities related to agreements that provide for Continental's convertible debt to be settled with UAL.

Edgar Filing: CONTINENTAL AIRLINES INC /DE/ - Form 10-Q

common stock. This net loss and the related derivatives are reflected only in the Continental stand-alone financial statements. See Note 7 to the financial statements included in Part I, Item 1 of this report for additional information.

Table of Contents**RECONCILIATION OF GAAP TO NON-GAAP FINANCIAL MEASURES**

The non-GAAP financial measures in this report are presented because they provide management and investors the ability to measure and monitor UAL's performance on a consistent basis. UAL believes that adjusting for special items is useful to investors because they are non-recurring items not indicative of UAL's on-going performance. A reconciliation of net income (loss) and diluted earnings (loss) per share to the non-GAAP financial measure of net income and diluted earnings per share, excluding special items, for the three and nine months ended September 30 is as follows (in millions, except per share amounts):

	Three Months Ended September 30,			Nine Months Ended September 30,		
	Net Income 2012	Diluted Earnings per Share 2012	Net Income 2011	Net Income (Loss) 2012	Diluted Earnings (Loss) per Share 2012	Net Income 2011
Net income (loss) GAAP	\$ 6	\$ 0.02	\$ 653	\$ (103)	\$ (0.31)	\$ 978
Special revenue item						(107)
Special charges, net	514	1.33	120	882	2.37	343
Net income excluding special items non-GAAP	\$ 520	\$ 1.35	\$ 773	\$ 779	\$ 2.06	\$ 1,214

CRITICAL ACCOUNTING POLICIES

See *Critical Accounting Policies* in Management's Discussion and Analysis of Financial Condition and Results of Operations in the 2011 Annual Report for a discussion of the Company's critical accounting policies. See Note 1 to the financial statements included in Part I, Item I of this report for a discussion of changes in accounting for revenue for the Company's loyalty program.

FORWARD-LOOKING INFORMATION

Certain statements throughout Management's Discussion and Analysis of Financial Condition and Results of Operations and elsewhere in this report are forward-looking and thus reflect our current expectations and beliefs with respect to certain current and future events and financial performance. Such forward-looking statements are and will be subject to many risks and uncertainties relating to our operations and business environment that may cause actual results to differ materially from any future results expressed or implied in such forward-looking statements. Words such as *expects*, *will*, *plans*, *anticipates*, *indicates*, *believes*, *forecast*, *guidance*, *outlook* and similar expressions are intended to identify forward-looking statements.

Additionally, forward-looking statements include statements that do not relate solely to historical facts, such as statements which identify uncertainties or trends, discuss the possible future effects of current known trends or uncertainties, or which indicate that the future effects of known trends or uncertainties cannot be predicted, guaranteed or assured. All forward-looking statements in this report are based upon information available to us on the date of this report. We undertake no obligation to publicly update or revise any forward-looking statement, whether as a result of new information, future events, changed circumstances or otherwise, except as required by applicable law.

The Company's actual results could differ materially from these forward-looking statements due to numerous factors including, without limitation, the following: its ability to comply with the terms of its various financing arrangements; the costs and availability of financing; its ability to maintain adequate liquidity; its ability to execute its operational plans; its ability to control its costs, including realizing benefits from its resource optimization efforts, cost reduction initiatives and fleet replacement programs; its ability to utilize its net operating losses; its ability to attract and retain customers; demand for transportation in the markets in which it operates; an outbreak of a disease that affects travel demand or travel behavior; demand for travel and the impact that global economic conditions have on customer travel patterns; excessive taxation and the inability to offset future taxable income; general economic conditions (including interest rates, foreign currency exchange rates, investment or credit market conditions, crude oil prices, costs of aviation fuel and energy refining capacity in relevant markets); its ability to cost-effectively hedge against increases in the price of aviation fuel; any potential realized or unrealized gains or losses related to fuel or currency hedging programs; the effects of any hostilities, act of war or terrorist attack; the ability of other air carriers with whom the Company has alliances or partnerships to provide the services contemplated by the respective arrangements with such carriers; the costs and availability of aviation and other insurance; the costs associated with security measures and practices; industry consolidation or changes in airline alliances; competitive pressures on pricing and on demand; its capacity decisions and the capacity decisions of its competitors; U.S. or foreign governmental legislation, regulation and other actions (including open skies agreements and environmental regulations); labor costs; its ability to maintain

Edgar Filing: CONTINENTAL AIRLINES INC /DE/ - Form 10-Q

satisfactory labor relations and the results of the collective bargaining agreement process with its union groups; any disruptions to operations due to any potential actions by its labor groups; weather conditions; the possibility that expected merger synergies will not be realized or will not be realized within the expected time period; and other risks and uncertainties set forth under Item 1A, Risk Factors of the 2011 Annual Report, as well as other risks and uncertainties set forth from time to time in the reports the Company files with the SEC.

Table of Contents**ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK.**

There have been no material changes in market risk from the information provided in Item 7A. Quantitative and Qualitative Disclosures About Market Risk in our 2011 Annual Report except as follows:

Aircraft Fuel. As of September 30, 2012, UAL's projected consolidated fuel requirements for the remainder of 2012 were hedged as follows:

	Maximum Price		Minimum Price	
	% of Expected Consumption	Weighted Average Price (per gallon)	% of Expected Consumption	Weighted Average Price (per gallon)
UAL (a)				
Heating oil collars	20%	\$ 3.56	20%	\$ 2.80
Brent crude oil collars	14	2.76	14	1.93
Diesel fuel collars	9	3.28	9	2.45
Diesel fuel call options	1	3.25	N/A	N/A
Total	44%		43%	

(a) At September 30, 2012, UAL had also hedged 26% of its projected first half 2013 fuel consumption.

At September 30, 2012, UAL fuel derivatives were in a net asset position of \$33 million. See Note 7 to the financial statements included in Part I, Item 1 of this report for additional information related to fuel hedges.

Fuel derivative disclosures for United and Continental are omitted under the reduced disclosure format permitted by General Instruction H(2) of Form 10-Q.

ITEM 4. CONTROLS AND PROCEDURES.

UAL, United and Continental each maintain controls and procedures that are designed to ensure that information required to be disclosed in the reports filed or submitted to the SEC is recorded, processed, summarized and reported, within the time periods specified by the SEC's rules and forms, and is accumulated and communicated to management, including the Chief Executive Officer and Chief Financial Officer, as appropriate to allow timely decisions regarding required disclosure. The management of UAL, United and Continental, including the Chief Executive Officer and Chief Financial Officer, performed an evaluation to conclude with reasonable assurance that UAL's, United's and Continental's disclosure controls and procedures were designed and operating effectively to report the information each company is required to disclose in the reports they file with the SEC on a timely basis. Based on that evaluation, the Chief Executive Officer and the Chief Financial Officer of UAL, United and Continental have concluded that as of September 30, 2012, disclosure controls and procedures of each company were effective.

Changes in Internal Control over Financial Reporting during the Quarter Ended September 30, 2012

Except as set forth below, during the three months ended September 30, 2012, there were no changes in UAL's, United's or Continental's internal controls over financial reporting that materially affected, or are reasonably likely to materially affect, their internal controls over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f) under the Securities Exchange Act of 1934).

During the first quarter of 2012, we made certain changes to internal controls over financial reporting related to our revenue accounting system and our frequent flyer accounting systems. In connection with our conversion to a single passenger service system in March 2012, United converted from its former revenue accounting system to the Continental revenue accounting system and frequent flyer passenger database. During the second and third quarters of 2012, we continued to make additional enhancements to the revenue accounting system to improve our internal controls over financial reporting, including a reconciliation of open coupon detail to the general ledger balance of advanced ticket sales. The operating effectiveness of these changes to the internal controls over financial reporting will be evaluated as part of our annual assessment of the effectiveness of internal controls over financial reporting as of the end of fiscal year 2012.

Table of Contents**PART II. OTHER INFORMATION****ITEM 1. LEGAL PROCEEDINGS.**

The disclosures below include updates to certain legal proceedings included in the 2011 Annual Report. In addition to the legal proceedings below, UAL, United and Continental are parties to other legal proceedings as described in the 2011 Annual Report and in Part II, Item 1, Legal Proceedings, of the Company's Form 10-Q for each of the quarters ended March 31, 2012 and June 30, 2012.

EEOC Claim Under the Americans with Disabilities Act

On June 5, 2009, the U.S. Equal Employment Opportunity Commission (EEOC) filed a lawsuit on behalf of five named individuals and other similarly situated employees alleging that United's reasonable accommodation policy for employees with medical restrictions does not comply with the requirements of the Americans with Disabilities Act. The EEOC maintains that qualified disabled employees should be placed into available open positions for which they are minimally qualified, even if there are better qualified candidates for these positions. Under United's accommodation policy, employees who are medically restricted and who cannot be accommodated in their current position are given the opportunity to apply and compete for available positions. If the medically restricted employee is similarly qualified to others who are competing for an open position, under United's policy, the medically restricted employee will be given a preference for the position. If, however, there are candidates that have superior qualifications competing for an open position, then no preference will be given. United successfully transferred the venue of the case to the United States Federal Court for the Northern District of Illinois. On November 22, 2010, United filed a motion to dismiss the matter which the district court granted on February 3, 2011. On April 1, 2011, the EEOC appealed the dismissal to the Seventh Circuit Court of Appeals. On March 7, 2012, the Seventh Circuit Court of Appeals upheld the district court's decision dismissing the case. However, the three judge panel noted the split in the appellate court on this issue and potentially relevant precedent from the U.S. Supreme Court, and strongly recommended an *en banc* hearing of the case. On September 7, 2012, a unanimous Seventh Circuit overruled itself and previous Seventh Circuit precedent and held that there may be an obligation to place a minimally qualified disabled worker in a position over a more qualified non-disabled worker. The case was then remanded to the district court. The district court granted United's motion to stay this mandate during appeal and United anticipates filing a Petition for Certiorari with the Supreme Court of the United States within 90 days of the September 7th opinion.

ITEM 1A. RISK FACTORS.

See Part I, Item 1A., Risk Factors, of the 2011 Annual Report and Part II, Item 1A., Risk Factors, of the Company's Form 10-Q for the quarter ended March 31, 2012 for a detailed discussion of the risk factors affecting UAL, United and Continental. The disclosure below includes updates to certain risk factor disclosures included in the 2011 Annual Report, which are in addition to, and not in lieu of, those contained in the 2011 Annual Report.

Union disputes, employee strikes or slowdowns, and other labor-related disruptions, as well as the integration of the United and Continental workforces in connection with the Merger, present the potential for a delay in achieving expected Merger synergies, could adversely affect the Company's operations, and could result in increased costs that impair its financial performance.

United and Continental are both highly unionized companies. As of September 30, 2012, the Company and its subsidiaries had approximately 88,000 active employees, of whom approximately 80% were represented by various U.S. labor organizations.

The successful integration of United and Continental and achievement of the anticipated benefits of the combined company depend in part on integrating United and Continental employee groups and maintaining productive employee relations. In order to fully integrate the pre-Merger represented employee groups, the Company must negotiate a joint collective bargaining agreement covering each combined group. The process for integrating the labor groups of United and Continental is governed by a combination of the Railway Labor Act (the RLA), the McCaskill-Bond Amendment, and where applicable, the existing provisions of each company's collective bargaining agreements and union policy. A delay in or failure to integrate the United and Continental employee groups presents the potential for delays in achieving expected Merger synergies, increased operating costs and labor disputes that could adversely affect our operations.

We are currently in the process of negotiating joint collective bargaining agreements with all of our represented employee groups, including our pilots, fleet and passenger service agents, reservations agents, flight attendants, technicians, dispatchers and storekeepers. Achieving joint collective bargaining agreements with our represented employee groups is likely to increase our labor costs, which increase could be material.

On August 3, 2012, the Company announced that it had reached an agreement in principle with respect to a new joint collective bargaining agreement with the Air Line Pilots Association, International (ALPA) representing pilots at United and Continental. The agreement in principle

Edgar Filing: CONTINENTAL AIRLINES INC /DE/ - Form 10-Q

is subject to definitive documentation, and any such definitive documentation is subject to approvals by each of the United and Continental ALPA master executive councils and ratification by the Company's pilots.

Table of Contents

The Company can provide no assurance that a successful or timely resolution of labor negotiations for all amendable collective bargaining agreements will be achieved. There is a risk that unions or individual employees might pursue judicial or arbitral claims arising out of changes implemented as a result of the Merger. Employee dissatisfaction with the results of the seniority integration may lead to litigation that in some cases can delay implementation of the integrated seniority list. There is also a possibility that employees or unions could engage in job actions such as slow-downs, work-to-rule campaigns, sick-outs or other actions designed to disrupt United's and Continental's normal operations, in an attempt to pressure the companies in collective bargaining negotiations. Although the RLA makes such actions unlawful until the parties have been lawfully released to self-help, and United and Continental can seek injunctive relief against premature self-help, such actions can cause significant harm even if ultimately enjoined.

ITEM 6. EXHIBITS.

A list of exhibits included as part of this Form 10-Q is set forth in an Exhibit Index that immediately precedes the exhibits.

Table of Contents

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, each registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized. The signature for each undersigned company shall be deemed to relate only to matters having reference to such company or its subsidiaries.

United Continental Holdings, Inc.
(Registrant)

Date: October 25, 2012

By: /s/ John D. Rainey

John D. Rainey

Executive Vice President and Chief Financial Officer

(principal financial officer)

Date: October 25, 2012

By: /s/ Chris Kenny

Chris Kenny

Vice President and Controller

(principal accounting officer)

United Air Lines, Inc.
(Registrant)

Date: October 25, 2012

By: /s/ John D. Rainey

John D. Rainey

Executive Vice President and Chief Financial Officer

(principal financial officer)

Date: October 25, 2012

By: /s/ Chris Kenny

Chris Kenny

Vice President and Controller

(principal accounting officer)

Continental Airlines, Inc.
(Registrant)

Date: October 25, 2012

By: /s/ John D. Rainey

John D. Rainey

Edgar Filing: CONTINENTAL AIRLINES INC /DE/ - Form 10-Q

Executive Vice President and Chief Financial Officer

(principal financial officer)

Date: October 25, 2012

By: /s/ Chris Kenny

Chris Kenny

Vice President and Controller

(principal accounting officer)

Table of Contents**EXHIBIT INDEX**

Exhibit No.	Registrant	Exhibit
^10.1	UAL United	Purchase Agreement No. PA-03784 dated July 12, 2012 between The Boeing Company (Boeing) and United Air Lines, Inc.
^10.2	UAL United	Supplemental Agreement No. 01 to Purchase Agreement No. PA-03784 dated September 27, 2012 between Boeing and United Air Lines, Inc.
^10.3	UAL United Continental	Purchase Agreement No. PA-03776 dated July 12, 2012 between Boeing and United Continental Holdings, Inc.
^10.4	UAL United Continental	Letter Agreement No. 6-1162-KKT-080 dated July 12, 2012 among Boeing, United Continental Holdings, Inc., United Air Lines, Inc., and Continental Airlines, Inc.
^10.5	UAL Continental	Supplemental Agreement No. 59 to Purchase Agreement No. 1951 dated July 12, 2012 between Boeing and Continental Airlines, Inc.
^10.6	UAL United	Purchase Agreement No. 3860 dated September 27, 2012 between Boeing and United Air Lines, Inc.
12.1	UAL	United Continental Holdings, Inc. and Subsidiary Companies Computation of Ratio of Earnings to Fixed Charges and Ratio of Earnings to Fixed Charges and Preferred Stock Dividend Requirements
12.2	United	United Air Lines, Inc. and Subsidiary Companies Computation of Ratio of Earnings to Fixed Charges and Ratio of Earnings to Fixed Charges and Preferred Stock Dividend Requirements
12.3	Continental	Continental Airlines, Inc. and Subsidiary Companies Computation of Ratio of Earnings to Fixed Charges
31.1	UAL	Certification of the Principal Executive Officer of UAL Pursuant to 15 U.S.C. 78m(a) or 78o(d) (Section 302 of the Sarbanes-Oxley Act of 2002)
31.2	UAL	Certification of the Principal Financial Officer of UAL Pursuant to 15 U.S.C. 78m(a) or 78o(d) (Section 302 of the Sarbanes-Oxley Act of 2002)
31.3	United	Certification of the Principal Executive Officer of United Pursuant to 15 U.S.C. 78m(a) or 78o(d) (Section 302 of the Sarbanes-Oxley Act of 2002)
31.4	United	Certification of the Principal Financial Officer of United Pursuant to 15 U.S.C. 78m(a) or 78o(d) (Section 302 of the Sarbanes-Oxley Act of 2002)
31.5	Continental	Certification of the Principal Executive Officer of Continental Pursuant to 15 U.S.C. 78m(a) or 78o(d) (Section 302 of the Sarbanes-Oxley Act of 2002)
31.6	Continental	Certification of the Principal Financial Officer of Continental Pursuant to 15 U.S.C. 78m(a) or 78o(d) (Section 302 of the Sarbanes-Oxley Act of 2002)
32.1	UAL	Certification of the Chief Executive Officer and Chief Financial Officer of UAL Pursuant to 18 U.S.C. 1350 (Section 906 of the Sarbanes-Oxley Act of 2002)
32.2	United	Certification of the Chief Executive Officer and Chief Financial Officer of United Pursuant to 18 U.S.C. 1350 (Section 906 of the Sarbanes-Oxley Act of 2002)
32.3	Continental	Certification of the Chief Executive Officer and Chief Financial Officer of Continental Pursuant to 18 U.S.C. 1350 (Section 906 of the Sarbanes-Oxley Act of 2002)
99.1	United Continental	Unaudited Pro Forma Condensed Combined Financial Information of United and Continental
101.1	UAL United Continental	XBRL Instance Document

Table of Contents

101.2	UAL	
	United	
	Continental	XBRL Taxonomy Extension Schema Document
101.3	UAL	
	United	
	Continental	XBRL Taxonomy Extension Calculation Linkbase Document
101.4	UAL	
	United	
	Continental	XBRL Taxonomy Extension Definition Linkbase Document
101.5	UAL	
	United	
	Continental	XBRL Taxonomy Extension Labels Linkbase Document
101.6	UAL	
	United	
	Continental	XBRL Taxonomy Extension Presentation Linkbase Document

^ Confidential portion of this exhibit has been omitted and filed separately with the SEC pursuant to a request for confidential treatment.