VERIZON COMMUNICATIONS INC
Form 10-Q
November 06, 2006
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

(Mark one)
x QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d)

OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended September 30, 2006

OR

¨ TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d)

OF THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from to

Commission file number 1-8606

Verizon Communications Inc.

(Exact name of registrant as specified in its charter)

Delaware	**23-2259884**
(State of Incorporation)	(I.R.S. Employer Identification No.)
140 West Street **New York, New York** (Address of principal executive offices)	**10007** (Zip Code)

Registrant s telephone number (212) 395-1000

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

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

Large accelerated filer x Accelerated filer ¨ Non-accelerated filer ¨

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

At September 30, 2006, 2,919,515,293 shares of the registrant s Common Stock were outstanding, after deducting 48,137,145 shares held in treasury.

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Part I - Financial Information

Item 1. Financial Statements

Condensed Consolidated Statements of Income

Verizon Communications Inc. and Subsidiaries

(Dollars in Millions, Except Per Share Amounts) (Unaudited)	Three Months Ended September 30,		Nine Months Ended September 30,	
	2006	**2005**	**2006**	**2005**
Operating Revenues	$ 23,254	$ 18,486	$ 67,990	$ 54,221
Operating Expenses				
Cost of services and sales (exclusive of items shown below)	8,982	6,361	26,349	18,390
Selling, general and administrative expense	6,720	5,195	19,587	15,382
Depreciation and amortization expense	3,628	3,433	10,947	10,219
Sales of businesses, net				(530)
Total Operating Expenses	19,330	14,989	56,883	43,461
Operating Income	3,924	3,497	11,107	10,760
Equity in earnings of unconsolidated businesses	288	182	616	553
Other income and (expense), net	101	88	264	290
Interest expense	(572)	(525)	(1,798)	(1,601)
Minority interest	(1,088)	(748)	(2,942)	(2,069)
Income Before Provision For Income Taxes, Discontinued Operations and Cumulative Effect of Accounting Change	2,653	2,494	7,247	7,933
Provision for income taxes	(855)	(702)	(2,421)	(2,386)
Income Before Discontinued Operations and Cumulative Effect of Accounting Change	1,798	1,792	4,826	5,547
Income from discontinued operations, net of tax	124	77	381	192
Cumulative effect of accounting change, net of tax			(42)	
Net Income	$ 1,922	$ 1,869	$ 5,165	$ 5,739
Basic Earnings Per Common Share[(1)]				
Income before discontinued operations and cumulative effect of accounting change	$ .62	$ .65	$ 1.66	$ 2.00
Income from discontinued operations, net of tax	.04	.03	.13	.07
Cumulative effect of accounting change, net of tax			(.01)	
Net Income	$ .66	$ .68	$ 1.77	$ 2.07
Weighted-average shares outstanding (in millions)	2,907	2,765	2,911	2,767

Diluted Earnings Per Common Share[1]				
Income before discontinued operations and cumulative effect of accounting change	$ .62	$ .64	$ 1.65	$ 1.98
Income from discontinued operations, net of tax	.04	.03	.13	.07
Cumulative effect of accounting change, net of tax			(.01)	
Net Income	$ .66	$ .67	$ 1.76	$ 2.05
Weighted-average shares outstanding (in millions)	2,923	2,817	2,945	2,818
Dividends declared per common share	$ .405	$ .405	$ 1.215	$ 1.215

[1] Total per share amounts may not add due to rounding.

See Notes to Condensed Consolidated Financial Statements

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Condensed Consolidated Balance Sheets

Verizon Communications Inc. and Subsidiaries

(Dollars in Millions, Except Per Share Amounts) (Unaudited)	**At September 30, 2006**	**At December 31, 2005**
Assets		
Current assets		
Cash and cash equivalents	$ 1,846	$ 776
Short-term investments	1,589	2,498
Accounts receivable, net of allowances of $1,265 and $1,190	10,834	8,784
Inventories	1,650	1,714
Assets held for sale	3,597	3,336
Prepaid expenses and other	2,099	2,168
Total current assets	21,615	19,276
Plant, property and equipment	201,967	188,278
Less accumulated depreciation	120,565	115,125
	81,402	73,153
Investments in unconsolidated businesses	4,478	4,604
Wireless licenses	48,318	47,781
Goodwill	5,709	392
Other intangible assets, net	5,220	4,193
Other assets	18,937	18,731
Total assets	$ 185,679	$ 168,130
Liabilities and Shareowners Investment		
Current liabilities		
Debt maturing within one year	$ 11,529	$ 6,688
Accounts payable and accrued liabilities	14,501	12,066
Liabilities related to assets held for sale	2,065	1,865
Other	7,218	5,551
Total current liabilities	35,313	26,170
Long-term debt	30,154	31,569
Employee benefit obligations	20,231	18,198
Deferred income taxes	21,905	22,715
Other liabilities	4,274	3,363
Minority interest	27,523	26,435
Shareowners investment		
Series preferred stock ($.10 par value; none issued)		
Common stock ($.10 par value; 2,967,652,438 shares and 2,774,865,381 shares issued)	297	277

Contributed capital	31,423	25,369
Reinvested earnings	17,471	15,905
Accumulated other comprehensive loss	(1,516)	(1,783)
Common stock in treasury, at cost	(1,575)	(353)
Deferred compensation employee stock ownership plans and other	179	265
Total shareowners investment	46,279	39,680
Total liabilities and shareowners investment	$ 185,679	$ 168,130

See Notes to Condensed Consolidated Financial Statements

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Condensed Consolidated Statements of Cash Flows

Verizon Communications Inc. and Subsidiaries

(Dollars in Millions) (Unaudited)	Nine Months Ended September 30, 2006	2005
Cash Flows from Operating Activities		
Net Income	$ 5,165	$ 5,739
Adjustments to reconcile net income to net cash provided by operating activities continuing operations:		
Depreciation and amortization	10,947	10,219
Sales of businesses, net		(530)
Employee retirement benefits	1,500	1,231
Deferred income taxes	(540)	(945)
Provision for uncollectible accounts	916	982
Equity in earnings of unconsolidated businesses	(616)	(553)
Cumulative effect of accounting change, net of tax	42	
Changes in current assets and liabilities, net of effects from acquisition/disposition of businesses	(1,601)	(1,916)
Other, net	2,123	773
Net cash provided by operating activities continuing operations	17,936	15,000
Net cash provided by operating activities discontinued operations	315	275
Net cash provided by operating activities	18,251	15,275
Cash Flows from Investing Activities		
Capital expenditures (including capitalized software)	(12,318)	(11,363)
Acquisitions, net of cash acquired, and investments	1,037	(4,630)
Proceeds from disposition of businesses		1,326
Net change in short-term investments	1,521	938
Other, net	576	293
Net cash used in investing activities continuing operations	(9,184)	(13,436)
Net cash used in investing activities discontinued operations	(138)	(189)
Net cash used in investing activities	(9,322)	(13,625)
Cash Flows from Financing Activities		
Proceeds from long-term borrowings	3,958	1,486
Repayments of long-term borrowings and capital lease obligations	(8,706)	(2,371)
Increase in short-term obligations, excluding current maturities	1,831	1,109
Dividends paid	(3,537)	(3,308)
Proceeds from sale of common stock	115	37
Purchase of common stock for treasury	(1,348)	(221)
Other, net	5	30
Net cash used in financing activities continuing operations	(7,682)	(3,238)
Net cash used in financing activities discontinued operations	(177)	(86)

Net cash used in financing activities	(7,859)	(3,324)
Increase (decrease) in cash and cash equivalents	1,070	(1,674)
Cash and cash equivalents, beginning of period	776	2,290
Cash and cash equivalents, end of period	$ 1,846	$ 616

See Notes to Condensed Consolidated Financial Statements

Notes to Condensed Consolidated Financial Statements

Verizon Communications Inc. and Subsidiaries

(Unaudited)

1. Basis of Presentation

The accompanying unaudited condensed consolidated financial statements have been prepared based upon Securities and Exchange Commission (SEC) rules that permit reduced disclosure for interim periods. These financial statements reflect all adjustments that are necessary for a fair presentation of results of operations and financial condition for the interim periods shown including normal recurring accruals and other items. The results for the interim periods are not necessarily indicative of results for the full year. For a more complete discussion of significant accounting policies and certain other information, you should refer to the financial statements included in the Verizon Communications Inc. (Verizon) Annual Report on Form 10-K for the year ended December 31, 2005.

We have reclassified prior year amounts to conform to the current year presentation.

2. Acquisitions

Completion of Merger with MCI

On February 14, 2005, Verizon announced that it agreed to acquire 100% of the outstanding common stock of MCI, Inc. (MCI) for a combination of Verizon common shares and cash. MCI was a global communications company that provided Internet, data and voice communication services to businesses and government entities throughout the world and consumers in the United States. After receiving the required state, federal and international regulatory approvals, Verizon and MCI closed the merger on January 6, 2006.

On April 9, 2005, Verizon entered into a stock purchase agreement with eight entities affiliated with Carlos Slim Helú to purchase 43.4 million shares of MCI common stock for $25.72 per share in cash plus an additional cash amount of 3% per annum from April 9, 2005, until the closing of the purchase of those shares. The transaction closed on May 17, 2005. The total cash payment was $1,121 million and the investment was accounted for as a cost investment. No payments were made under a provision that required Verizon to pay an additional amount at the end of one year to the extent that the price of Verizon s common stock exceeded $35.52 per share. We received the special dividend of $5.60 per MCI share on these 43.4 million MCI shares, or $243 million, on October 27, 2005.

Under the terms of the merger agreement, MCI shareholders received .5743 shares of Verizon common stock ($5,050 million in the aggregate) and cash of $2.738 ($779 million in the aggregate) for each of their MCI shares. The merger consideration was equal to $20.40 per MCI share, excluding the $5.60 per share special dividend paid by MCI to its shareholders on October 27, 2005. There was no purchase price adjustment.

The merger was accounted for using the purchase method in accordance with the Financial Accounting Standards Board Statement of Financial Accounting Standard (SFAS) No. 141, *Business Combinations* (SFAS No. 141), and the aggregate transaction value was $6,889 million, consisting of the cash and common stock issued at closing ($5,829 million), the consideration for the shares acquired from the Carlos Slim Helú entities, net of the special dividend paid by MCI ($973 million) and closing and other direct merger-related costs, including financial advisory, legal and accounting services. The number of shares issued was based on the Average Parent Stock Price, as defined in the merger agreement. The consolidated financial statements include the results of MCI s operations from the date of the close of the merger.

Prior to the merger, there were commercial transactions between us and the former MCI entities for telecommunications services at rates comparable to similar transactions with other third parties. Subsequent to the merger, these transactions are eliminated in consolidation.

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Reasons for the Merger

We believe that the merger will make us a more efficient competitor in providing a broad range of communications services and will result in several significant strategic benefits to us, including the following:

Strategic Position. Following the merger, it is expected that our core strengths in communication services will be enhanced by MCI s employee and business customer base, portfolio of advanced data and IP services and network assets.

Growth Platform. MCI s presence in the U.S. and international enterprise sector and its long haul fiber network infrastructure are expected to provide us with a stronger platform from which we can market our products and services.

Operational Benefits. We believe that we will achieve operational benefits through, among other things, eliminating duplicative staff and information and operation systems and to a lesser extent overlapping network facilities; reducing procurement costs; using the existing networks more efficiently; reducing line support functions; reducing general and administrative expenses; improving information systems; optimizing traffic flow; eliminating planned or potential Verizon capital expenditures for new long-haul network capability; and offering wireless capabilities to MCI s customers.

Allocation of the cost of the merger

In accordance with SFAS No. 141, the cost of the merger was preliminarily allocated to the assets acquired and liabilities assumed based on their fair values as of the close of the merger, with the amounts exceeding the fair value being recorded as goodwill. The process to identify and record the fair value of assets acquired and liabilities assumed included an analysis of the acquired fixed assets, including real and personal property; various contracts, including leases, contractual commitments, and other business contracts; customer relationships; investments; and contingencies.

The fair values of the assets acquired and liabilities assumed were preliminarily determined using one or more of three valuation approaches: market, income and cost. The selection of a particular method for a given asset depended on the reliability of available data and the nature of the asset, among other considerations. The market approach, which indicates value for a subject asset based on available market pricing for comparable assets, was utilized for certain acquired real property and investments. The income approach, which indicates value for a subject asset based on the present value of cash flow projected to be generated by the asset, was used for certain intangible assets such as customer relationships, as well as for favorable/unfavorable contracts. Projected cash flow is discounted at a required rate of return that reflects the relative risk of achieving the cash flow and the time value of money. Projected cash flows for each asset considered multiple factors, including current revenue from existing customers; distinct analysis of expected price, volume, and attrition trends; reasonable contract renewal assumptions from the perspective of a marketplace participant; expected profit margins giving consideration to marketplace synergies; and required returns to contributory assets. The cost approach, which estimates value by determining the current cost of replacing an asset with another of equivalent economic utility, was used for the majority of personal property. The cost to replace a given asset reflects the estimated reproduction or replacement cost for the property, less an allowance for loss in value due to depreciation or obsolescence, with specific consideration given to economic obsolescence if indicated.

As a result of the preliminary allocation of the cost of the merger, we recorded the assets acquired and liabilities assumed from MCI at their respective fair values as of the close of the merger. As the values of certain assets and liabilities are preliminary in nature, they are subject to adjustment as additional information is obtained, including, but not limited to, valuation and physical counts of property, plant and equipment, deferred taxes, the resolution of pre-acquisition tax and other contingencies, exiting certain contractual arrangements and the expected plans to rationalize the combined workforce. The valuations will be finalized within 12 months of the close of the merger. When the valuations are finalized, any changes to the preliminary valuation of assets acquired or liabilities assumed may result in material adjustments to the fair value of the identifiable intangible assets acquired and goodwill.

The following table summarizes the current preliminary allocation of the cost of the merger to the assets acquired, including cash of $2,361 million, and liabilities assumed as of the close of the merger. Certain of the amounts in the following table have been revised since the initial allocation to reflect information that has since become available. These amounts will likely continue to change until the valuation is finalized.

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(Dollars in Millions)

Assets acquired	
Current assets	$ 5,978
Property, plant & equipment	6,453
Intangible assets subject to amortization	
Customer relationships	1,162
Rights of way and other	202
Deferred income taxes and other assets	1,790
Goodwill	5,051
Total assets acquired	20,636
Liabilities assumed	
Current liabilities	6,047
Long-term debt	6,169
Deferred income taxes and other non-current liabilities	1,531
Total liabilities assumed	13,747
Purchase price	$ 6,889

The goodwill resulting from the merger with MCI was assigned to the Wireline segment, which includes the operations of the former MCI. The customer relationships are being amortized on a straight-line basis over 3-8 years based on whether the relationship is with a consumer or a business customer since this correlates to the pattern in which the economic benefits are expected to be realized.

In connection with the merger, we recorded $190 million of severance and severance-related costs and $382 million of contract termination costs in the above allocation of the cost of the merger in accordance with the Emerging Issues Task Force Issue (EITF) No. 95-3, Recognition of Liabilities in Connection with a Purchase Business Combination. We expect to pay $158 million of the severance and severance-related costs in 2006 with the remaining costs to be paid in 2007. We expect to pay $129 million of contract termination costs in 2006 and the remaining costs will be paid over the remaining contract periods through 2009. The following table summarizes the obligations recognized in connection with the MCI merger and the activity to date:

(Dollars in Millions)

	Beginning Balance	Payments	Other Increases (Decreases)	Ending Balance
Severance costs and contract termination costs	$ 459	$ (113)	$ 113	$ 459

Pro Forma Information

The following unaudited pro forma consolidated results of operations assume that the MCI merger was completed as of January 1 for the periods shown below:

(Dollars in Millions, Except Per Share Amounts)	Three Months Ended September 30, 2005	Nine Months Ended September 30, 2006	2005
Revenues	$ 22,454	$ 68,217	$ 66,614
Income before discontinued operations and cumulative effect of accounting change	$ 2,120	$ 4,826	$ 5,953
Net income	$ 2,193	$ 5,165	$ 6,227
Basic earnings per common share:			
	$ .72	$ 1.66	$ 2.03

Income before discontinued operations and cumulative effect of accounting change			
Net income	$ .75	$ 1.77	$ 2.13
Diluted earnings per common share:			
Income before discontinued operations and cumulative effect of accounting change	$ .72	$ 1.65	$ 2.01
Net income	$ .74	$ 1.76	$ 2.10

The unaudited pro forma information presents the combined operating results of Verizon and the former MCI, with the results prior to the acquisition date adjusted to include the pro forma impact of: the elimination of transactions between Verizon and the former MCI; the adjustment of amortization of intangible assets and depreciation of fixed assets based on the preliminary purchase price allocation; the elimination of merger expenses incurred by the former MCI; the elimination of the loss on the early redemption of MCI s debt; the adjustment of interest expense reflecting the redemption of all of MCI s debt and the replacement of that debt with $4 billion of new debt issued in February 2006 at Verizon s weighted average borrowing rate; and to reflect the impact of income taxes on the pro forma adjustments utilizing Verizon s statutory tax rate of 40%. The unaudited pro forma results for the three and nine months ended September 30, 2005 include ($4) million, and $82 million, respectively, for discontinued operations that were sold by MCI during the first quarter of 2005. The unaudited pro forma results for the three and nine months ended September 30, 2005 include $188 million of net tax benefits resulting from tax reserve adjustments recognized by the former MCI in the third quarter of 2005, including audit settlements and other activity in the period.

The unaudited pro forma consolidated basic and diluted earnings per share for the nine months ended September 30, 2006 and the three and nine months ended September 30, 2005 are based on the consolidated basic and diluted weighted average shares of Verizon and the former MCI. The historical basic and diluted weighted average shares of the former MCI were converted for the actual number of shares issued upon the closing of the merger.

The unaudited pro forma results are presented for illustrative purposes only and do not reflect the realization of potential cost savings, or any related integration costs. Certain cost savings may result from the merger; however, there can be no assurance that these cost savings will be achieved. Cost savings, if achieved, could result from, among other things, the reduction of overhead expenses, including employee levels and the elimination of duplicate facilities and capital expenditures. These pro forma results do not purport to be indicative of the results that would have actually been obtained if the merger occurred as of the beginning of each of the periods presented, nor does the pro forma data intend to be a projection of results that may be obtained in the future.

Other Acquisitions

In August 2002, Verizon Wireless and Price Communications Corp. (Price) combined Price s wireless business with a portion of Verizon Wireless. The resulting limited partnership, Verizon Wireless of the East LP (VZ East), is controlled and managed by Verizon Wireless. In exchange for its contributed assets, Price received a limited partnership interest in the new partnership which was exchangeable into the common stock of Verizon Wireless if an initial public offering of that stock occurred, or into the common stock of Verizon on the fourth anniversary of the asset contribution date. On August 15, 2006, Verizon delivered 29.5 million shares of newly-issued Verizon common stock to Price valued at $1,007 million in exchange for Price s limited partnership interest in VZ East. As a result of acquiring Price s limited partnership interest, Verizon recorded goodwill of $345 million in the third quarter of 2006 attributable to its Domestic Wireless segment.

We also completed other immaterial acquisitions in our Verizon Wireless and Information Services segments.

3. Stock-Based Compensation

Effective January 1, 2006, we adopted SFAS No. 123(R), *Share-Based Payment* utilizing the modified prospective method. SFAS No. 123(R) requires the measurement of stock-based compensation expense based on the fair value of the award on the date of grant. Under the modified prospective method, the provisions of SFAS No. 123(R) apply to all awards granted or modified after the date of adoption. The impact to Verizon primarily resulted from Verizon Wireless, for which we recorded a $42 million cumulative effect of accounting change as of January 1, 2006, net of taxes and after minority interest, to recognize the effect of initially measuring the outstanding liability for Value Appreciation Rights (VARs) of the Verizon Wireless joint venture, at fair value utilizing a Black-Scholes model.

Previously, effective January 1, 2003, we adopted the fair value recognition provisions of SFAS No. 123, *Accounting for Stock-Based Compensation* using the prospective method (as permitted under SFAS No. 148, *Accounting for Stock-Based Compensation Transition and Disclosure*) for all new awards granted, modified or settled after January 1, 2003.

Verizon Communications Long Term Incentive Plan

The Verizon Communications Long Term Incentive Plan (the Plan), effective January 1, 2001, permits the grant of nonqualified stock options, incentive stock options, restricted stock, restricted stock units, performance shares, performance share units and other awards. The maximum number of shares for awards is 200 million.

Restricted Stock Units

The Plan provides for grants of restricted stock units (RSUs) that vest at the end of the third year of the grant. The RSUs are classified as liability awards because the RSUs will be paid in cash upon vesting. The RSU award liability is measured at its fair value at the end of each reporting period and, therefore, will fluctuate based on the performance of Verizon s stock.

Included in Verizon s stock-based compensation expense in the third quarter of 2006 and for the nine months ended September 30, 2006 is a portion of the cost related to restricted stock granted in 2006, 2005 and 2004.

Changes in Verizon s Restricted Stock Units outstanding for the nine months ended September 30, 2006 were as follows:

(Shares in Thousands)	Restricted Stock Units	Weighted Average Grant-Date Fair Value
Outstanding restricted stock units at beginning of year	6,869	$ 36.12
Granted	8,322	31.73
Cancellations/Forfeitures	(344)	35.29
Outstanding restricted stock units, September 30, 2006	14,847	$ 33.67

Performance Share Units

The Plan also provides for grants of performance share units (PSU) that vest at the end of the third year of the grant. The 2006, 2005 and 2004 performance share units will be paid in cash upon vesting. The 2003 PSUs were paid out in February 2006 in Verizon shares.

The target award is determined at the beginning of the period and can increase (to a maximum 200% of the target) or decrease (to zero) based on a key performance measure, Total Shareholder Return (TSR). At the end of the period, the PSU payment is determined by comparing Verizon s TSR to the TSR of a predetermined peer group and the S&P 500 companies. All payments are subject to approval by the Board s Compensation Committee. The PSUs are classified as liability awards because the PSU awards will be paid in cash upon vesting. The PSU award liability is measured at its fair value at the end of each reporting period and, therefore, will fluctuate based on the performance of Verizon s stock as well as Verizon s TSR relative to the peer group s TSR and S&P 500 TSR.

Changes in Verizon s Performance Share Units outstanding for the nine months ended September 30, 2006 were as follows:

(Shares in Thousands)	Performance Share Units	Weighted Average Grant-Date Fair Value
Outstanding performance share units at beginning of period	19,091	$ 36.84

Granted	12,734	31.82
Payments	(3,607)	38.54
Cancellations/Forfeitures	(1,089)	37.56
Outstanding performance share units, September 30, 2006	27,129	$ 34.23

As of September 30, 2006, unrecognized compensation expense related to the unvested portion of Verizon s RSUs and PSUs was approximately $504 million and is expected to be recognized over a weighted-average period of approximately 2 years.

MCI Restricted Stock Plan

MCI s Management Restricted Stock Plan (MRSP) provides for the granting of stock-based compensation to management. Following the acquisition by Verizon on January 6, 2006, awards outstanding under the MRSP were converted into 3,456,108 shares of Verizon common stock in accordance with the Merger Agreement. MCI has not issued new MRSP shares since February 2005.

Changes in the MRSP s restricted stock outstanding for the nine months ended September 30, 2006 were as follows:

(Shares in Thousands)	Restricted Stock	Weighted Average Grant-Date Fair Value
Outstanding restricted stock at beginning of year		$
Acquisition by Verizon	3,456	30.75
Payments	(2,530)	30.75
Cancellations/Forfeitures	(46)	30.75
Outstanding restricted stock, September 30, 2006	880	$ 30.75

As of September 30, 2006, unrecognized compensation expense related to the unvested portion of the MRSP restricted stock was approximately $12 million and is expected to be recognized over a weighted-average period of approximately 2 years.

Verizon Wireless Long-Term Incentive Plan

The 2000 Verizon Wireless Long-Term Incentive Plan (the Wireless Plan) provides compensation opportunities to eligible employees and other participating affiliates of the Cellco Partnership, d.b.a. Verizon Wireless (the Partnership). The Wireless Plan provides rewards that are tied to the long-term performance of the Partnership. Under the Wireless Plan, Value Appreciation Rights (VARs) are granted to eligible employees. The aggregate number of VARs that may be issued under the Wireless Plan is approximately 343 million. The Company has not issued new VARs since 2004.

VARs reflect the change in the value of the Partnership, as defined in the Wireless Plan, similar to stock options. Once VARs become vested, employees can exercise their VARs and receive a payment that is equal to the difference between the VAR price on the date of grant and the VAR price on the date of exercise, less applicable taxes. VARs are fully exercisable three years from the date of grant with a maximum term of 10 years. All VARs are granted at a price equal to the estimated fair value of the Partnership, as defined in the Wireless Plan, at the date of the grant.

With the adoption of SFAS No. 123(R), the Partnership began estimating the fair value of VARs granted using a Black-Scholes option valuation model. The following table summarizes the assumptions used in the model during the three and nine months ended September 30, 2006:

	Ranges
Risk-free rate	4.7% - 5.2%
Expected term (in years)	1.3 -3.5
Expected volatility	17.6% - 22.3%
Expected dividend yield	n/a

The risk-free rate is based on the U.S. Treasury yield curve in effect at the time of the grant. The expected term of the VARs granted was estimated using a combination of the simplified method as prescribed in Staff Accounting Bulletin (SAB) No. 107, Share Based Payments, historical experience, and management judgment. Expected volatility was based on a blend of the historical and implied volatility of publicly traded peer companies for a period equal to the VARs expected life, ending on the day of the grant, and calculated on a monthly basis. The

Partnership does not pay dividends.

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Changes in the VARs outstanding for the nine months ended September 30, 2006 were as follows:

(Shares in Thousands)	VARs	Weighted Average Grant-Date Fair Value
Outstanding rights at beginning of year	108,923	$ 17.12
Exercised	(5,836)	12.77
Cancellations/Forfeitures	(6,327)	23.40
Outstanding rights, September 30, 2006	96,760	$ 16.97

As of September 30, 2006, unrecognized compensation expense related to the unvested portion of the VARs was approximately $95 million and is expected to be recognized over a weighted-average period of less than one year.

Other Stock-Based Compensation Expense

After-tax compensation expense for other stock based compensation including RSUs, PSUs, MRSPs and VARs described above included in net income as reported for the three and nine months ended September 30, 2006 was $187 million and $433 million, respectively. For the three and nine months ended September 30, 2005, after-tax compensation expense for other stock based compensation was $116 million and $315 million, respectively.

Stock Options

The Verizon Long Term Incentive Plan provides for grants of stock options to employees at an option price per share of 100% of the fair market value of Verizon Stock on the date of grant. Each grant has a 10 year life, vesting equally over a three year period, starting at the date of the grant. We have not granted new stock options since 2004.

Included in Verizon s stock-based compensation expense for the nine months ended September 30, 2006 is the applicable portion of the cost related to 2003 stock option grants. The stock options granted before 2003 were fully vested as of the beginning of 2005.

Changes in Verizon s stock options outstanding for the nine months ended September 30, 2006 were as follows:

(Shares in Thousands)	Stock Options	Weighted Average Exercise Price
Options outstanding, beginning of year	250,976	$ 47.62
Exercised	(1,689)	32.28
Cancelled	(22,044)	44.53
Options outstanding, September 30, 2006	227,243	$ 48.03
Options exercisable, September 30, 2006	222,702	$ 48.26

The weighted average remaining contractual term was 4.1 years for stock options outstanding and exercisable as of September 30, 2006. The total intrinsic value was approximately $19 million for stock options outstanding and exercisable as of September 30, 2006. The total intrinsic value for stock options exercised during the nine months ended September 30, 2006 was $4.7 million. The total intrinsic value for stock options exercised during the nine months ended September 30, 2005 was $6.4 million.

For the three and nine months ended September 30, 2006, the amount of cash received from the exercise of stock options was approximately $46 million and $53 million, respectively, and the related tax benefits for the three and nine months ended September 30, 2006 were approximately $1.6 million and $1.8 million, respectively. For the three and nine months ended September 30, 2005, the amount of cash received from the exercise of stock options was approximately $6 million and $33 million, respectively, and the related tax benefits were approximately $0.1 million and $2.4 million, respectively.

For the three and nine months ended September 30, 2006, after-tax compensation expense for stock options was $6 million and $24 million, respectively. For the three and nine months ended September 30, 2005, after-tax compensation expense for stock options was $16 million and $46 million, respectively.

As of September 30, 2006, unrecognized compensation expense related to the unvested portion of stock options was approximately $14 million and is expected to be recognized over the next six months.

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4. Strategic Actions

Merger Integration Costs

During the three and nine months ended September 30, 2006, we recorded pretax charges of $25 million ($16 million after-tax) and $157 million ($99 million after-tax), respectively, related to integration costs associated with the MCI merger that closed on January 6, 2006. These costs are primarily comprised of advertising and other costs related to re-branding initiatives and systems integration activities. There were no similar charges incurred during the comparable periods in 2005.

Facility and Employee-Related Items

During the three and nine months ended September 30, 2006, we recorded pretax charges of $48 million ($31 million after-tax) and $138 million ($88 million after-tax), respectively, in connection with the relocation of several functions to Verizon Center.

During the third quarter of 2006, we recorded net pretax pension settlement losses of $29 million ($17 million after-tax), related to employees that received lump-sum distributions during 2006 primarily resulting from our separation plans. These charges were recorded in accordance with SFAS No. 88, *Employ*ers *Accounting for Settlements and Curtailments of Defined Benefit Pension Plans and for Termination Benefits,* which requires that settlement losses be recorded once prescribed payment thresholds have been reached. There were no similar items incurred during the comparable period in 2005.

During the second quarter of 2006, we recorded pretax charges of $300 million ($186 million after-tax), for employee severance and severance-related costs in connection with the involuntary separation of approximately 3,200 employees, the majority of whom were separated in the second and third quarters. The remaining employees will be separated during the fourth quarter of 2006.

During the third quarter of 2005, we recorded a net pretax gain of $64 million ($37 million after-tax) in connection with the relocation of several functions to Verizon Center, including a pretax gain of $120 million ($72 million after-tax) related to the sale of a New York City office building, partially offset by a pretax charge of $56 million ($35 million after-tax) primarily associated with relocation-related employee severance costs and related activities.

Tax Matters

During the third quarter of 2005, we recorded a tax benefit of $94 million in connection with capital gains and prior year investment losses and a tax benefit of $21 million related to the repatriation of prior year foreign earnings.

During the second quarter of 2005, as a result of the capital gain realized in connection with the sale of our Hawaii businesses, we recorded a tax benefit of $242 million related to capital losses incurred in previous years.

Also during the second quarter of 2005, we recorded a net tax provision of $232 million related to the repatriation of foreign earnings under the provisions of the American Jobs Creation Act of 2004, for two of Verizon s foreign investments. There were no similar tax matters during the comparable periods in 2006.

Other Special Items

During the third quarter of 2005, we recorded a pretax impairment charge of $125 million ($125 million after-tax) pertaining to our leasing operations for aircraft leases involved in recent airline bankruptcy proceedings. There were no similar items incurred during the comparable period in 2006.

5. Discontinued Operations and Sales of Businesses, Net

Discontinued Operations

Verizon Dominicana C. por A. and Telecomunicaciones de Puerto Rico, Inc.

During the second quarter of 2006, we reached definitive agreements to sell our interests in our Caribbean and Latin American telecommunications operations in three separate transactions to América Móvil, S.A. de C.V. (América Móvil), a wireless service provider throughout Latin America, and a company owned jointly by Teléfonos de México, S.A. de C.V. (Telmex) and América Móvil. We have agreed to sell our 100 percent indirect interest in

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Verizon Dominicana C. por A. (Verizon Dominicana) and our 52 percent interest in Telecomunicaciones de Puerto Rico, Inc. (TELPRI) to América Móvil. An entity jointly owned by América Móvil and Telmex has agreed to purchase our indirect 28.5 percent interest in Compañía Anónima Nacional Teléfonos de Venezuela (CANTV).

Upon closing, the transactions are expected to result in pretax proceeds of approximately $3,700 million, prior to purchase price adjustments as defined in the sale agreements. Each transaction is subject to separate regulatory approvals and none of the sales is contingent on the closing of any of the other transactions. We expect to close the sale of our interest in TELPRI in 2006 or 2007. In September 2006, we extended the expiration date of the Verizon Dominicana and CANTV transactions until December 29, 2006. The transactions are expected to close subject to the receipt of regulatory approvals. Although we anticipate pretax gains on the transactions, in the case of Verizon Dominicana, the U.S. taxes that will become payable and be recorded at the time the transaction closes will significantly exceed the amount of the pretax gain. In addition, the government tax authority in the Dominican Republic has issued an assessment of capital gains tax in connection with the proposed transaction. We believe that the assessment is without merit, have filed an appeal and are contesting it vigorously. We are unable to predict the ultimate outcome of this proceeding or its effect on the transaction.

In accordance with SFAS No. 144, *Accounting for the Impairment or Disposal of Long-Lived Assets*, we have classified the results of operations of Verizon Dominicana and TELPRI as discontinued operations in the unaudited condensed consolidated statements of income. In addition, the assets and liabilities of Verizon Dominicana and TELPRI are aggregated and disclosed as current assets and current liabilities in the unaudited condensed consolidated balance sheets. Our investment in CANTV continues to be accounted for as an equity method investment in continuing operations. Additional detail related to the assets and liabilities of Verizon Dominicana and TELPRI are as follows:

(Dollars in Millions)	At September 30, 2006	At December 31, 2005
Current assets	$ 467	$ 508
Plant, property and equipment, net	2,223	2,152
Other non-current assets	907	676
Total assets	$ 3,597	$ 3,336
Current liabilities	$ 350	$ 758
Long-term debt	575	300
Other non-current liabilities	1,140	807
Total liabilities	$ 2,065	$ 1,865

Related to the assets and liabilities above is $881 million and $897 million included as Accumulated Other Comprehensive Loss in the Condensed Consolidated Balance Sheets as of September 30, 2006 and December 31, 2005, respectively, comprised of foreign currency translation adjustments and minimum pension liability adjustments.

Income from discontinued operations, net of tax presented in the Condensed Consolidated Statements of Income included the following:

(Dollars in Millions)	Three Months Ended September 30, 2006	Three Months Ended September 30, 2005	Nine Months Ended September 30, 2006	Nine Months Ended September 30, 2005
Operating Revenues	$ 544	$ 551	$ 1,759	$ 1,565
Income from operations	198	113	598	304
Provision for income taxes	(74)	(36)	(217)	(112)
Income from discontinued operations, net of tax	$ 124	$ 77	$ 381	$ 192

Sales of Businesses, Net

V*erizon Hawaii Inc.*

During the second quarter of 2005, we recorded a pretax gain of $530 million ($336 million after-tax) related to the sale of our wireline and directory businesses in Hawaii, including Verizon Hawaii Inc. which operated approximately 700,000 switched access lines, as well as the services and assets of Verizon Long Distance, Verizon Online, Verizon Information Services and Verizon Select Services Inc. in Hawaii, to an affiliate of The Carlyle Group.

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6. Goodwill and Other Intangible Assets

Goodwill

Changes in the carrying amount of goodwill for the nine months ended September 30, 2006, were as follows:

(Dollars in Millions)	Wireline	Wireless	Information Services	Total
Balance at December 31, 2005	$ 315	$	$ 77	$ 392
Acquisitions	5,051	345		5,396
Reclassifications and other	(75)		(4)	(79)
Balance at September 30, 2006	$ 5,291	$ 345	$ 73	$ 5,709

Other Intangible Assets

The major components and average useful lives of our other intangible assets follow:

	At September 30, 2006		At December 31, 2005	
(Dollars in Millions)	Gross Carrying Amount	Accumulated Amortization	Gross Carrying Amount	Accumulated Amortization
Amortized intangible assets:				
Customer lists and relationships (3 to 8 years)	$ 1,294	$ 236	$ 3,436	$ 3,279
Non-network internal-use software (1 to 7 years)	7,965	4,013	7,377	3,365
Other (1 to 25 years)	229	19	27	3
Total	$ 9,488	$ 4,268	$ 10,840	$ 6,647
Unamortized intangible assets:				
Wireless licenses	$ 48,318		$ 47,781	

Customer lists and relationships of $3,313 million became fully amortized and were written-off during the second quarter of 2006. Amortization expense was $337 million and $1,127 million for the three and nine months ended September 30, 2006, respectively. For the three and nine months ended September 30, 2005, amortization expense was $374 million and $1,109 million, respectively. Amortization expense is estimated to be $340 million for the remainder of 2006, $1,195 million in 2007, $1,034 million in 2008, $832 million in 2009 and $620 million in 2010.

7. Debt

Redemption of Debt Assumed in Merger

On January 17, 2006, Verizon announced offers to purchase two series of MCI senior notes, MCI $1,983 million aggregate principal amount of 6.688% Senior Notes Due 2009 and MCI $1,699 million aggregate principal amount of 7.735% Senior Notes Due 2014, at 101% of their par value. Due to the change in control of MCI that occurred in connection with the merger with Verizon on January 6, 2006, Verizon was required to make this offer to noteholders within 30 days of the closing of the merger. Noteholders tendered $165 million of the 6.688% Senior Notes. Separately, Verizon notified noteholders that MCI was exercising its right to redeem both series of Senior Notes prior to maturity under the optional redemption procedures provided in the indentures. The 6.688% Notes were redeemed on March 1, 2006, and the 7.735% Notes were redeemed on February 16, 2006.

In addition, on January 20, 2006, Verizon announced an offer to repurchase MCI $1,983 million aggregate principal amount of 5.908% Senior Notes Due 2007 at 101% of their par value. On February 21, 2006, $1,804 million of these notes were redeemed by Verizon. Verizon satisfied and discharged the indenture governing this series of notes shortly after the close of the offer for those noteholders who did not accept this offer.

We recorded pretax charges of $26 million ($16 million after-tax) during the first quarter of 2006 resulting from the extinguishment of debt assumed in connection with the completion of the MCI merger described above.

Other Debt Redemptions/Prepayments

During the second quarter of 2006, we redeemed/prepaid several debt issuances, including: Verizon North Inc. $200 million 7.625% Series C debentures due May 15, 2026; Verizon Northwest Inc. $175 million 7.875% Series B

debentures due June 1, 2026; Verizon South Inc. $250 million 7.5% Series D debentures due March 15, 2026; Verizon California Inc. $25 million 9.41% Series W first mortgage bonds due 2014; Verizon California Inc. $30 million 9.44% Series X first mortgage bonds due 2015; Verizon Northwest Inc. $3 million 9.67% Series HH first mortgage bonds due 2010 and Contel of the South Inc. $14 million 8.159% Series GG first mortgage bonds due 2018. The gain/(loss) from these retirements was immaterial.

During the third quarter of 2005, we redeemed Verizon New England Inc. $250 million 6.875% debentures due October 1, 2023 resulting in a pretax charge of $10 million ($6 million after-tax) in connection with the early extinguishment of the debt.

Zero-Coupon Convertible Notes

Previously, Verizon Global Funding issued approximately $5,442 million in principal amount at maturity of zero-coupon convertible notes due 2021 which were callable by Verizon on or after May 15, 2006. On May 15, 2006, we redeemed the remaining $1,375 million accreted principal of the remaining outstanding zero-coupon convertible notes at a redemption price of $639.76 per $1,000 principal plus interest of approximately $0.5767 per $1,000 principal. The total payment on the date of redemption was approximately $1,377 million.

Issuance of Debt

In February 2006, Verizon issued $500 million of 5.35% notes due 2011, $1,250 million of 5.55% notes due 2016, $500 million of 5.85% notes due 2035 and $1,750 million of floating rate notes due 2007 resulting in cash proceeds of $3,958 million, net of discounts, issuance costs and the receipt of cash proceeds related to hedges on the interest rate of an anticipated financing.

Support Agreements and Guarantees

All of Verizon Global Funding s debt had the benefit of Support Agreements between us and Verizon Global Funding, which gave holders of Verizon Global Funding debt the right to proceed directly against us for payment of interest, premium (if any) and principal outstanding should Verizon Global Funding fail to pay. The holders of Verizon Global Funding debt did not have recourse to the stock or assets of most of our telephone operations; however, they did have recourse to dividends paid to us by any of our consolidated subsidiaries as well as assets not covered by the exclusion. On February 1, 2006, Verizon announced the merger of Verizon Global Funding into Verizon. As a result of the merger, all of Verizon Global Funding s debt has been assumed by Verizon by operation of law.

In addition, Verizon Global Funding had guaranteed the debt obligations of GTE Corporation (but not the debt of its subsidiary or affiliate companies) that were issued and outstanding prior to July 1, 2003. In connection with the merger of Verizon Global Funding into Verizon, Verizon has assumed this guarantee. As of September 30, 2006, $2,950 million principal amount of these obligations remained outstanding.

Verizon and NYNEX Corporation are the joint and several co-obligors of the 20-Year 9.55% Debentures due 2010 previously issued by NYNEX on March 26, 1990. As of September 30, 2006, $92 million principal amount of this obligation remained outstanding. NYNEX and GTE no longer issue public debt or file SEC reports. See Note 12 for information on guarantees of operating subsidiary debt listed on the New York Stock Exchange.

Debt Covenants

We and our consolidated subsidiaries are in compliance with all of our debt covenants.

8. Comprehensive Income

Comprehensive income consists of net income and other gains and losses affecting shareowners investment that, under accounting principles generally accepted in the United States, are excluded from net income.

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Changes in the components of other comprehensive income (loss) were as follows:

(Dollars in Millions)	Three Months Ended September 30, 2006	2005	Nine Months Ended September 30, 2006	2005
Net Income	$ 1,922	$ 1,869	$ 5,165	$ 5,739
Other Comprehensive Income (Loss), Net of Taxes				
Foreign currency translation adjustments	(36)	(96)	210	(641)
Unrealized gains on net investment hedges				2
Unrealized derivative gains on cash flow hedges		3	13	6
Unrealized gains (losses) on marketable securities	17	(4)	31	(23)
Minimum pension liability adjustment			13	(1)
	(19)	(97)	267	(657)
Total Comprehensive Income	$ 1,903	$ 1,772	$ 5,432	$ 5,082

The unrealized foreign currency translation loss in the third quarter of 2006 is primarily driven by the decline in the functional currency on our investment in Vodafone Omnitel N.V. (Vodafone Omnitel). The unrealized foreign currency translation gain in the nine months ended September 30, 2006 is primarily driven by the appreciation in the functional currency on our investment in Vodafone Omnitel. The unrealized foreign currency translation loss in 2005 was primarily driven by a decline in the functional currencies on our investments in Vodafone Omnitel and Verizon Dominicana.

During the third quarter of 2005, we entered into interest rate derivatives to limit our exposure to interest rate changes. In accordance with the provisions of SFAS No. 133, *Accounting for Derivative Instruments and Hedging Activities* (SFAS No. 133), and related amendments and interpretations, changes in fair value of these cash flow hedges due to interest rate fluctuations were recognized in Accumulated Other Comprehensive Loss. Also, during the second and third quarters of 2005, we entered into zero cost euro collars to hedge a portion of our net investment in Vodafone Omnitel. In accordance with the provisions of SFAS No. 133, changes in the fair value of these contracts due to exchange rate fluctuations are recognized in Accumulated Other Comprehensive Loss and offset the impact of foreign currency changes on the value of our net investment in the operation being hedged. As of September 30, 2006, our positions in the interest rate derivatives and the zero cost euro collars have been settled.

The components of Accumulated Other Comprehensive Loss are as follows:

(Dollars in Millions)	At September 30, 2006	At December 31, 2005
Foreign currency translation adjustments	$ (657)	$ (867)
Unrealized gains on net investment hedges	2	2
Unrealized derivative losses on cash flow hedges	(14)	(27)
Unrealized gains on marketable securities	41	10
Minimum pension liability adjustment	(888)	(901)
Accumulated other comprehensive loss	$ (1,516)	$ (1,783)

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9. Earnings Per Share

The following table is a reconciliation of the share amounts used in computing earnings per share.

(Dollars and Shares in Millions, Except Per Share Amounts)	Three Months Ended September 30, 2006	2005	Nine Months Ended September 30, 2006	2005
Net Income Used For Basic Earnings Per Common Share				
Income before discontinued operations and cumulative effect of accounting change	$ 1,798	$ 1,792	$ 4,826	$ 5,547
Income from discontinued operations, net of tax	124	77	381	192
Cumulative effect of accounting change, net of tax			(42)	
Net income	$ 1,922	$ 1,869	$ 5,165	$ 5,739
Net Income Used For Diluted Earnings Per Common Share				
Income before discontinued operations and cumulative effect of accounting change	$ 1,798	$ 1,792	$ 4,826	$ 5,547
After-tax minority interest expense related to exchangeable equity interest	4	9	20	23
After-tax interest expense related to zero-coupon convertible notes		6	11	20
Income before discontinued operations and cumulative effect of accounting change after assumed conversion of dilutive securities	1,802	1,807	4,857	5,590
Income from discontinued operations, net of tax	124	77	381	192
Cumulative effect of accounting change, net of tax			(42)	
Net income after assumed conversion of dilutive securities	$ 1,926	$ 1,884	$ 5,196	$ 5,782
Basic Earnings Per Common Share[(1)]				
Weighted-average shares outstanding basic	2,907	2,765	2,911	2,767
Income before discontinued operations and cumulative effect of accounting change	$ .62	$ .65	$ 1.66	$ 2.00
Income from discontinued operations, net of tax	.04	.03	.13	.07
Cumulative effect of accounting change, net of tax			(.01)	
Net income	$ .66	$ .68	$ 1.77	$ 2.07
Diluted Earnings Per Common Share[(1)]				
Weighted-average shares outstanding basic	2,907	2,765	2,911	2,767
Effect of dilutive securities:				
Stock options	1	6	1	5
Exchangeable equity interest	15	29	25	29
Zero-coupon convertible notes		17	8	17
Weighted-average shares outstanding diluted	2,923	2,817	2,945	2,818
Income before discontinued operations and cumulative effect of accounting change	$ .62	$ .64	$ 1.65	$ 1.98
Income from discontinued operations, net of tax	.04	.03	.13	.07
Cumulative effect of accounting change, net of tax			(.01)	
Net income	$ .66	$ .67	$ 1.76	$ 2.05

(1) Total per share amounts may not add due to rounding.

Stock options for 227 million shares and 233 million shares for the three and nine months ended September 30, 2006, respectively were not included in the computation of diluted earnings per share because the exercise price of the stock options was greater than the average market price of the common stock. For the three and nine months ended September 30, 2005, the number of shares not included in the computation of diluted earnings per share were 247 million and 246 million, respectively.

The zero coupon convertible notes were retired on May 15, 2006.

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The exchangeable equity interest was converted on August 15, 2006 by issuing 29.5 million Verizon shares (see Note 2, Acquisitions Other Acquisitions).

10. Segment Information

As a result of reaching definitive agreements to sell our interests in Verizon Dominicana, TELPRI and CANTV, which were included in the International segment, the operations of Verizon Dominicana and TELPRI are reported as discontinued operations and assets held for sale, while CANTV continues to be accounted for as an equity method investment. Accordingly, we now have three reportable segments, which we operate and manage as strategic business units and organize by products and services. Our segments include: Wireline including the operations of the former MCI, consists of Verizon Telecom, a provider of telephone services, including voice, broadband, data, network access, long distance, video, and other services to consumer and small business customers and carriers and Verizon Business, which provides a broad range of telecommunications and next-generation IP network services globally to medium and large businesses and government customers; Domestic Wireless primarily representing the operations of the Verizon Wireless joint venture with Vodafone Group Plc (Vodafone), that provides domestic wireless products and services, including wireless voice and data services and equipment sales across the United States; and Information Services - representing our directory publishing businesses and electronic commerce services.

We measure and evaluate our reportable segments based on segment income. This segment income excludes unallocated corporate expenses and other adjustments arising during each period. The other adjustments include transactions that the chief operating decision makers exclude in assessing business unit performance due primarily to their non-recurring and/or non-operational nature. Although such transactions are excluded from the business segment results, they are included in reported consolidated earnings. Gains and losses that are not individually significant are included in all segment results, since these items are included in the chief operating decision makers assessment of unit performance.

The following table provides operating financial information for our three reportable segments and a reconciliation of segment results to consolidated results. Prior period amounts are revised to reflect the change in reportable segments as discussed above.

	Three Months Ended September 30,		Nine Months Ended September 30,	
(Dollars in Millions)	2006	2005	2006	2005
External Operating Revenues				
Wireline	$ 12,477	$ 9,183	$ 37,221	$ 27,521
Domestic Wireless	9,835	8,332	27,858	23,556
Information Services	804	857	2,443	2,608
Total segments	23,116	18,372	67,522	53,685
Reconciling items	138	114	468	536
Total consolidated reported	$ 23,254	$ 18,486	$ 67,990	$ 54,221
Intersegment Revenues				
Wireline	$ 320	$ 262	$ 840	$ 736
Domestic Wireless	34	19	86	59
Information Services				
Total segments	354	281	926	795
Reconciling items	(354)	(281)	(926)	(795)
Total consolidated reported	$	$	$	$
Total Operating Revenues				
Wireline	$ 12,797	$ 9,445	$ 38,061	$ 28,257
Domestic Wireless	9,869	8,351	27,944	23,615
Information Services	804	857	2,443	2,608
Total segments	23,470	18,653	68,448	54,480

Reconciling items	(216)	(167)	(458)	(259)
Total consolidated reported	$ 23,254	$ 18,486	$ 67,990	$ 54,221
Operating Income				
Wireline	$ 1,123	$ 1,300	$ 3,429	$ 3,754
Domestic Wireless	2,587	1,819	7,076	5,141
Information Services	373	441	1,144	1,269
Total segments	4,083	3,560	11,649	10,164
Reconciling items	(159)	(63)	(542)	596
Total consolidated reported	$ 3,924	$ 3,497	$ 11,107	$ 10,760

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(Dollars in Millions)	Three Months Ended September 30, 2006	2005	Nine Months Ended September 30, 2006	2005
Segment Income				
Wireline	$ 393	$ 537	$ 1,200	$ 1,500
Domestic Wireless	804	574	2,164	1,524
Information Services	249	279	728	798
Total segment income	1,446	1,390	4,092	3,822
Reconciling items	476	479	1,073	1,917
Total consolidated net income reported	$ 1,922	$ 1,869	$ 5,165	$ 5,739

(Dollars in Millions)	At September 30, 2006	At December 31, 2005
Assets		
Wireline	$ 90,519	$ 75,188
Domestic Wireless	79,094	76,729
Information Services	1,505	1,525
Total segments	171,118	153,442
Reconciling items	14,561	14,688
Total consolidated	$ 185,679	$ 168,130

Major reconciling items between the segments and the consolidated results are as follows:

(Dollars in Millions)	Three Months Ended September 30, 2006	2005	Nine Months Ended September 30, 2006	2005
Total Operating Revenues				
Hawaii operations	$	$	$	$ 202
Corporate, eliminations and other	(216)	(167)	(458)	(461)
	$ (216)	$ (167)	$ (458)	$ (259)
Operating Income				
Severance, pension and benefit charges (see Note 4)	$ (29)	$	$ (329)	$
Verizon Center relocation costs (see Note 4)	(48)	64	(138)	64
Merger integration costs (see Note 4)	(25)		(157)	
Hawaii operations				78
Sales of businesses, net (see Note 5)				530
Other special items (see Note 4)		(125)		(125)
Corporate and other	(57)	(2)	82	49
	$ (159)	$ (63)	$ (542)	$ 596
Net Income				
Debt extinguishment costs (see Note 7)	$	$ (6)	$ (16)	$ (6)
Severance, pension and benefit charges (see Note 4)	(17)		(203)	
Verizon Center relocation costs (see Note 4)	(31)	37	(88)	37
Merger integration costs (see Note 4)	(16)		(99)	
Cumulative effect of accounting change (see Note 3)			(42)	
Sales of businesses, net (see Note 5)				336

Tax benefits (see Note 4)		94		336
Tax benefit (provision) on repatriated earnings (see Note 4)		21		(211)
Other special items (see Note 4)		(125)		(125)
Income from discontinued operations, net of tax (see Note 5)	124	77	381	192
Corporate and other	416	381	1,140	1,358
	$ 476	$ 479	$ 1,073	$ 1,917

Financial information for Wireline and Information Services excludes the effects of Hawaii access lines and directory operations sold in the second quarter of 2005.

Corporate, eliminations and other includes unallocated corporate expenses, intersegment eliminations recorded in consolidation, the results of other businesses such as our investments in unconsolidated businesses, primarily Omnitel and CANTV, lease financing, and asset impairments and expenses that are not allocated in assessing segment performance due to their non-recurring nature.

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We generally account for intersegment sales of products and services and asset transfers at current market prices. We are not dependent on any single customer.

11. Employee Benefits

We maintain noncontributory defined benefit pension plans for the majority of our employees. In addition, we maintain postretirement health care and life insurance plans for our retirees and their dependents, which are both contributory and non-contributory and include a limit on the company s share of cost for certain recent and future retirees.

In December 2005, we announced that Verizon management employees will no longer earn pension benefits or earn service towards the company retiree medical subsidy after June 30, 2006, after receiving an 18-month enhancement of the value of their pension and retiree medical subsidy. In addition, new management employees hired after December 31, 2005, are not eligible for pension benefits and managers with less than 13.5 years of service as of June 30, 2006, are not eligible for company-subsidized retiree healthcare or retiree life insurance benefits. Beginning July 1, 2006, management employees receive an increased company match on their savings plan contributions.

Net Periodic Cost

The following tables summarize the benefit costs related to our pension and postretirement health care and life insurance plans:

				(Dollars in Millions)
		Pension		**Health Care and Life**
Three Months Ended September 30,	**2006**	**2005**	**2006**	**2005**
Service cost	$ 116	$ 173	$ 90	$ 91
Interest cost	508	498	380	372
Expected return on plan assets	(803)	(817)	(83)	(88)
Amortization of prior service cost	12	10	91	74
Actuarial loss, net	46	32	74	67
Net periodic benefit (income) cost	(121)	(104)	552	516
Termination benefits		3		1
Settlement loss	29			
Total (income) cost	$ (92)	$ (101)	$ 552	$ 517

				(Dollars in Millions)
		Pension		**Health Care and Life**
Nine Months Ended September 30,	**2006**	**2005**	**2006**	**2005**
Service cost	$ 480	$ 524	$ 272	$ 273
Interest cost	1,525	1,498	1,140	1,114
Expected return on plan assets	(2,409)	(2,456)	(249)	(264)
Amortization of prior service cost	34	31	271	218
Actuarial loss, net	136	94	222	195
Net periodic benefit (income) cost	(234)	(309)	1,656	1,536
Termination benefits	38	3	11	1
Termination benefits Hawaii operations sold		8		
Settlement loss Hawaii operations sold		80		
Curtailment loss Hawaii operations sold		6		
Settlement loss	29			

Total (income) cost	$ (167)	$ (212)	$ 1,667	$ 1,537

The termination benefits, settlement loss and curtailment loss amounts pertaining to the Hawaii operations sold were recorded in Sales of Businesses, Net.

Employer Contributions

In 2006, based on the funded status of the plans at December 31, 2005, we anticipate contributions of $1 million to our qualified pension trust, $144 million to our nonqualified pension plans and $1,154 million to our other postretirement benefit plans. During the three months ended September 30, 2006, we made no contributions to our qualified pension trusts, and contributed $24 million to our nonqualified pension plans and $289 million to our other postretirement benefit plans. During the nine months ended September 30, 2006, we made no contributions to our qualified pension trusts, and contributed $94 million to our nonqualified pension plans and $958 million to our other

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postretirement benefit plans. Our estimate of the amount and timing of required qualified pension trust contributions for 2006 is based on current regulations, including continued pension funding relief. The anticipated required qualified pension trust contributions disclosed in Verizon s Annual Report on Form 10-K for the year ended December 31, 2005 continue to be accurate.

Severance Benefits

During the three and nine months ended September 30, 2006, we paid severance benefits of $154 million and $308 million, respectively. At September 30, 2006, we had a remaining severance liability of $711 million, which includes future contractual payments to employees separated, or to be separated within 12 months, as of September 30, 2006.

12. Guarantees of Operating Subsidiary Debt

Verizon has guaranteed the obligations of the following two wholly-owned operating subsidiaries: $480 million 7% debentures series B, due 2042 issued by Verizon New England Inc. and $300 million 7% debentures series F issued by Verizon South Inc. due 2041. These guarantees are full and unconditional and would require Verizon to make scheduled payments immediately if either of the two subsidiaries failed to do so. Both of these securities were issued in denominations of $25 and were sold primarily to retail investors and are listed on the New York Stock Exchange. SEC rules permit us to include condensed consolidating financial information for these two subsidiaries in our periodic SEC reports rather than filing separate subsidiary periodic SEC reports.

Below is the condensed consolidating financial information. Verizon New England and Verizon South are presented in separate columns. The column labeled Parent represents Verizon s investments in all of its subsidiaries under the equity method and the Other column represents all other subsidiaries of Verizon on a combined basis. The Adjustments column reflects intercompany eliminations.

Condensed Consolidating Statements of Income

Three Months Ended September 30, 2006

(Dollars in Millions)	Parent	Verizon New England	Verizon South	Other	Adjustments	Total
Operating revenues	$	$ 957	$ 212	$ 22,284	$ (199)	$ 23,254
Operating expenses	39	960	171	18,359	(199)	19,330
Operating income (loss)	(39)	(3)	41	3,925		3,924
Equity in earnings of unconsolidated businesses	1,836	3		(99)	(1,452)	288
Other income and (expense), net	391	5	1	94	(390)	101
Interest expense	(331)	(43)	(12)	(192)	6	(572)
Minority interest				(1,088)		(1,088)
Income (loss) before provision for income taxes and discontinued operations	1,857	(38)	30	2,640	(1,836)	2,653
Income tax benefit (provision)	65	19	(11)	(928)		(855)
Income (loss) before discontinued operations	1,922	(19)	19	1,712	(1,836)	1,798
Income from discontinued operations, net of tax				124		124
Net income (loss)	$ 1,922	$ (19)	$ 19	$ 1,836	$ (1,836)	$ 1,922

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Condensed Consolidating Statements of Income

Nine Months Ended September 30, 2006

(Dollars in Millions)	Parent	Verizon New England	Verizon South	Other	Adjustments	Total
Operating revenues	$	$ 2,908	$ 640	$ 65,015	$ (573)	$ 67,990
Operating expenses	131	2,766	491	54,068	(573)	56,883
Operating income (loss)	(131)	142	149	10,947		11,107
Equity in earnings of unconsolidated businesses	4,969	10		(444)	(3,919)	616
Other income and (expense), net	1,122	9	14	189	(1,070)	264
Interest expense	(883)	(134)	(43)	(758)	20	(1,798)
Minority interest				(2,942)		(2,942)
Income before provision for income taxes, discontinued operations and cumulative effect of accounting change	5,077	27	120	6,992	(4,969)	7,247
Income tax benefit (provision)	88	(1)	(45)	(2,463)		(2,421)
Income before discontinued operations and cumulative effect of accounting change	5,165	26	75	4,529	(4,969)	4,826
Income from discontinued operations, net of tax				381		381
Cumulative effect of accounting change, net of tax				(42)		(42)
Net income	$ 5,165	$ 26	$ 75	$ 4,868	$ (4,969)	$ 5,165

Condensed Consolidating Statements of Income

Three Months Ended September 30, 2005

(Dollars in Millions)	Parent	Verizon New England	Verizon South	Other	Adjustments	Total
Operating revenues	$	$ 993	$ 227	$ 17,386	$ (120)	$ 18,486
Operating expenses	32	924	174	13,979	(120)	14,989
Operating income (loss)	(32)	69	53	3,407		3,497
Equity in earnings of unconsolidated businesses	1,747	3		88	(1,656)	182
Other income and (expense), net	137	(8)	2	53	(96)	88
Interest expense	(21)	(43)	(16)	(450)	5	(525)
Minority interest				(748)		(748)
Income before provision for income taxes and discontinued operations	1,831	21	39	2,350	(1,747)	2,494
Income tax benefit (provision)	38	(5)	(15)	(720)		(702)

Income before discontinued operations	1,869	16	24	1,630	(1,747)	1,792
Income from discontinued operations, net of tax				77		77
Net income	$ 1,869	$ 16	$ 24	$ 1,707	$ (1,747)	$ 1,869

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Condensed Consolidating Statements of Income

Nine Months Ended September 30, 2005

(Dollars in Millions)	Parent	Verizon New England	Verizon South	Other	Adjustments	Total
Operating revenues	$	$ 2,945	$ 683	$ 50,934	$ (341)	$ 54,221
Operating expenses	30	2,682	512	40,578	(341)	43,461
Operating income (loss)	(30)	263	171	10,356		10,760
Equity in earnings of unconsolidated businesses	5,233	18		244	(4,942)	553
Other income and (expense), net	372	(6)	4	223	(303)	290
Interest expense	(39)	(128)	(48)	(1,398)	12	(1,601)
Minority interest				(2,069)		(2,069)
Income before provision for income taxes and discontinued operations	5,536	147	127	7,356	(5,233)	7,933
Income tax benefit (provision)	203	(45)	(49)	(2,495)		(2,386)
Income before discontinued operations	5,739	102	78	4,861	(5,233)	5,547
Income from discontinued operations, net of tax				192		192
Net income	$ 5,739	$ 102	$ 78	$ 5,053	$ (5,233)	$ 5,739

Condensed Consolidating Balance Sheets

At September 30, 2006

(Dollars in Millions)	Parent	Verizon New England	Verizon South	Other	Adjustments	Total
Cash	$	$	$	$ 1,846	$	$ 1,846
Short-term investments		71	11	1,507		1,589
Accounts receivable, net	10	706	114	10,836	(832)	10,834
Other current assets	27,021	150	29	7,157	(27,011)	7,346
Total current assets	27,031	927	154	21,346	(27,843)	21,615
Plant, property and equipment, net	1	6,148	1,137	74,116		81,402
Investments in unconsolidated businesses	42,938	116		6,129	(44,705)	4,478
Other assets	621	429	388	76,976	(230)	78,184
Total assets	$ 70,591	$ 7,620	$ 1,679	$ 178,567	$ (72,778)	$ 185,679
Debt maturing within one year	$ 8,041	$ 186	$ 273	$ 30,144	$ (27,115)	$ 11,529

Other current liabilities	2,803	993	167	20,549	(728)	23,784
Total current liabilities	10,844	1,179	440	50,693	(27,843)	35,313
Long-term debt	12,916	2,575	417	14,476	(230)	30,154
Employee benefit obligations	392	2,070	254	17,515		20,231
Deferred income taxes	153	444	208	21,100		21,905
Other liabilities	7	114	24	4,129		4,274
Minority interest				27,523		27,523
Total shareowners investment	46,279	1,238	336	43,131	(44,705)	46,279
Total liabilities and shareowners investment	$ 70,591	$ 7,620	$ 1,679	$ 178,567	$ (72,778)	$ 185,679

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Condensed Consolidating Balance Sheets

At December 31, 2005

(Dollars in Millions)	Parent	Verizon New England	Verizon South	Other	Adjustments	Total
Cash	$	$	$	$ 776	$	$ 776
Short-term investments		216	32	2,250		2,498
Accounts receivable, net	20	910	142	9,042	(1,330)	8,784
Other current assets	9,365	166	185	6,999	(9,497)	7,218
Total current assets	9,385	1,292	359	19,067	(10,827)	19,276
Plant, property and equipment, net	1	6,146	1,158	65,848		73,153
Investments in unconsolidated businesses	32,593	116		10,017	(38,122)	4,604
Other assets	532	472	390	69,933	(230)	71,097
Total assets	$ 42,511	$ 8,026	$ 1,907	$ 164,865	$ (49,179)	$ 168,130
Debt maturing within one year	$ 22	$ 471	$	$ 15,999	$ (9,804)	$ 6,688
Other current liabilities	2,511	1,049	176	16,769	(1,023)	19,482
Total current liabilities	2,533	1,520	176	32,768	(10,827)	26,170
Long-term debt	92	2,702	901	28,104	(230)	31,569
Employee benefit obligations	205	1,892	254	15,847		18,198
Deferred income taxes		537	220	21,958		22,715
Other liabilities	1	146	27	3,189		3,363
Minority interest				26,435		26,435
Total shareowners investment	39,680	1,229	329	36,564	(38,122)	39,680
Total liabilities and shareowners investment	$ 42,511	$ 8,026	$ 1,907	$ 164,865	$ (49,179)	$ 168,130

Condensed Consolidating Statements of Cash Flows

Nine Months Ended September 30, 2006

(Dollars in Millions)	Parent	Verizon New England	Verizon South	Other	Adjustments	Total
Net cash from operating activities	$ 2,733	$ 965	$ 202	$ 16,710	$ (2,359)	$ 18,251
Net cash from investing activities	(779)	(526)	68	(8,155)	70	(9,322)
Net cash from financing activities	(1,954)	(439)	(270)	(7,485)	2,289	(7,859)
Net increase in cash	$	$	$	$ 1,070	$	$ 1,070

Condensed Consolidating Statements of Cash Flows

Nine Months Ended September 30, 2005

(Dollars in Millions)	Parent	Verizon New England	Verizon South	Other	Adjustments	Total
Net cash from operating activities	$ 4,532	$ 537	$ 212	$ 14,098	$ (4,104)	$ 15,275
Net cash from investing activities	(1,121)	(413)	(167)	(11,820)	(104)	(13,625)
Net cash from financing activities	(3,411)	(124)	(45)	(3,952)	4,208	(3,324)
Net decrease in cash	$	$	$	$ (1,674)	$	$ (1,674)

13. Recent Accounting Pronouncements

Uncertainty in Income Taxes

In July 2006, the Financial Accounting Standards Board (FASB) issued Interpretation No. 48, Accounting for Uncertainty in Income Taxes (FIN 48). FIN 48 requires the use of a two-step approach for recognizing and measuring tax benefits taken or expected to be taken in a tax return and disclosures regarding uncertainties in income tax positions. We are required to adopt FIN 48 effective January 1, 2007. The cumulative effect of initially adopting FIN 48 will be recorded as an adjustment to opening retained earnings in the year of adoption and will be presented separately. Only tax positions that meet the more likely than not recognition threshold at the effective date may be

recognized upon adoption of FIN 48. We are currently evaluating the impact this new standard will have on our future results of operations and financial position.

Leveraged Leases

In July 2006, the FASB issued Staff Position No. FAS 13-2, Accounting for a Change or Projected Change in the Timing of Cash Flows Relating to Income Taxes Generated by a Leveraged Lease Transaction (FSP 13-2). FSP 13-2 requires that changes in the projected timing of income tax cash flows generated by a leveraged lease transaction be recognized as a gain or loss in the year in which change occurs. The pretax gain or loss is required to be included in the same line item in which the leveraged lease income is recognized, with the tax effect being included in the provision for income taxes. We are required to adopt FSP 13-2 effective January 1, 2007. The cumulative effect of initially adopting this FSP will be recorded as an adjustment to opening retained earnings in the year of adoption and will be presented separately. We are currently evaluating the impact this new standard will have on our future results of operations and financial position.

Effects of Prior Year Misstatements

In September 2006, the SEC issued Staff Accounting Bulletin No. 108, Considering the Effects of Prior Year Misstatements when Quantifying Misstatements in Current Year Financial Statements (SAB 108). SAB 108 requires the quantification of financial statement errors based on the effects on the current year income statement and the cumulative effects on the balance sheet. SAB 108 is effective December 31, 2006 and we expect that the adoption of SAB 108 will not affect our results of operations or financial position.

Fair Value Measurements

In September 2006, the FASB issued Statement of Financial Accounting Standards No. 157, *Fair Value Measurement* (SFAS No. 157). SFAS No. 157 expands disclosures about fair value measurements. SFAS No. 157 defines fair value, establishes a framework for measuring fair value in generally accepted accounting principles and establishes a hierarchy that categorizes and prioritizes the sources to be used to estimate fair value. We are required to adopt SFAS No. 157 effective January 1, 2008 on a prospective basis. We are currently evaluating the impact this new standard will have on our future results of operations and financial position.

Employers Accounting for Defined Benefit Pension and Other Postretirement Plans

In September 2006, the FASB issued Statement of Financial Accounting Standards No. 158, *Employers Accounting for Defined Benefit Pension and Other Postretirement Plans an amendment of FASB Statements No. 87, 88, 106, and 132(R)* (SFAS No. 158). SFAS No. 158 requires the recognition of a defined benefit postretirement plan s funded status as either an asset or liability on the balance sheet. SFAS No. 158 also requires the immediate recognition of the unrecognized actuarial gains and losses and prior service costs and credits that arise during the period as a component of other accumulated comprehensive income, net of applicable income taxes. Additionally, the fair value of plan assets must be determined as of the company s year-end. We are required to adopt SFAS No. 158 effective December 31, 2006. We expect that the impact of adopting SFAS No. 158 will result in a net decrease to shareowners investment of approximately $10 billion. However, the impact of adopting SFAS No. 158 is dependent on plan asset performance through the end of 2006, as well as interest rates and other factors that will be applicable as of December 31, 2006.

14. Commitments and Contingencies

Several state and federal regulatory proceedings may require our telephone operations to pay penalties or to refund to customers a portion of the revenues collected in the current and prior periods. There are also various legal actions pending to which we are a party and claims which, if asserted, may lead to other legal actions. We have established reserves for specific liabilities in connection with regulatory and legal actions, including environmental matters, that we currently deem to be probable and estimable. We do not expect that the ultimate resolution of pending regulatory and legal matters in future periods, including the Hicksville matters described below, will have a material effect on our financial condition, but it could have a material effect on our results of operations.

During 2003, under a government-approved plan, remediation commenced at the site of a former Sylvania facility in Hicksville, New York that processed nuclear fuel rods in the 1950s and 1960s. Remediation beyond original expectations proved to be necessary and a reassessment of the anticipated remediation costs was conducted. A reassessment of costs related to remediation efforts at several other former facilities was also undertaken. As a result, an additional environmental remediation expense of $240 million was recorded in Selling, General and Administrative Expense in the consolidated statements of income in 2003, for remedial activities likely to take place

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over the next several years. In September 2005, the Army Corps of Engineers (ACE) accepted the Hicksville site into the Formerly Utilized Sites Remedial Action Program. This may result in the ACE performing some or all of the remaining remediation effort for the Hicksville site with a corresponding decrease in costs to Verizon. To the extent that the ACE assumes responsibility for some or all of the remaining remedial work at the Hicksville site, an adjustment to the remaining reserve may be necessary. Adjustments may also be made based upon actual conditions discovered during the remediation at any of the other sites requiring remediation.

There are also litigation matters associated with the Hicksville site primarily involving personal injury claims in connection with alleged emissions arising from operations in the 1950s and 1960s at the Hicksville site. These matters are in various stages, and no trial date has been set.

In connection with the execution of agreements for the sales of businesses and investments, Verizon ordinarily provides representations and warranties to the purchasers pertaining to a variety of nonfinancial matters, such as ownership of the securities being sold, as well as financial losses.

Under the terms of an investment agreement, Vodafone had the right to require Verizon Wireless to purchase up to an aggregate of $20 billion worth of Vodafone s interest in Verizon Wireless at designated times (put windows) at its then fair market value, not to exceed $10 billion in any one put window. In the event Vodafone exercised its put rights, we (instead of Verizon Wireless) had the right, exercisable at our sole discretion, to purchase up to $12.5 billion of Vodafone s interest for cash or Verizon stock at our option. Vodafone had the right to require the purchase of up to $10 billion during a 61-day period which opened on June 10 and closed on August 9 in 2006, and did not exercise that right. As a result, Vodafone only has the right to require the purchase of up to $10 billion worth of its interest, during a 61-day period opening on June 10 and closing on August 9 in 2007, under its one remaining put window. Vodafone also may require that Verizon Wireless pay for up to $7.5 billion of the required repurchase through the assumption or incurrence of debt.

15. Subsequent Event

Spectrum Purchase

On July 7, 2006, the FCC accepted an application that Verizon Wireless filed in June 2006 seeking to qualify to bid on any of the licenses being sold in the Advanced Wireless Services spectrum auction (AWS auction) that commenced on August 9, 2006. On July 17, 2006, Verizon Wireless paid to the FCC a $383 million deposit, which is included in Other Assets in the accompanying condensed consolidated balance sheets, in order to obtain 256 million bidding eligibility units for participation in the AWS auction. On September 18, 2006 the FCC completed the AWS auction and Verizon Wireless was the high bidder on thirteen 20 MHz licenses with bids totaling $2,809 million. An additional $178 million was remitted to the FCC on October 4, 2006. The remaining balance was paid to the FCC on October 19, 2006 and we expect the FCC will grant the licenses in the fourth quarter of 2006 or in the first quarter of 2007.

Disposition of Information Services

In December 2005, we announced that we were reviewing strategic alternatives for the disposition of Information Services. On July 7, 2006 we filed a Form 10 registration statement with the SEC for Verizon Directories Disposition Corporation (VDDC) in a step toward a proposed spin-off of Information Services domestic print and Internet yellow pages directories to our stockholders. On October 18, 2006 the Verizon Board of Directors approved the proposed spin-off of our U.S. print and Internet yellow pages directories business to our shareholders. The spin-off will result in a new public company, named Idearc Inc., formerly VDDC (Idearc), that will be separate from Verizon. Subject to the satisfaction of certain conditions, the distribution is expected to occur on or about November 17, 2006 and is expected to qualify as a tax-free distribution to our shareholders.

It is expected that the spin-off will result in each shareowner receiving one share of Idearc stock for 20 shares of Verizon for shareowners of record as of November 1, 2006. As a result of the spin-off transaction, Verizon expects to reduce its debt by approximately $7 billion through a debt-for-debt exchange mechanism and receive approximately $2 billion in cash. We also expect that the spin-off transaction will result in an after tax charge of $100 million to $125 million to our consolidated results, primarily related to costs associated with the transaction. The U.S. print and Internet yellow pages directories results of operations, financial position and cash flows remain in continuing operations in our financial statements until the completion of the spin-off at which time the business will be reported as discontinued operations.

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

Overview

Verizon Communications Inc. (Verizon) is one of the world s leading providers of communications services. Verizon s Wireline telecommunications business provides local telephone services, including broadband, nationwide long-distance and other communications products and services. As a result of the MCI merger, which closed on January 6, 2006, we also own and operate one of the most expansive end-to-end global Internet Protocol (IP) networks providing access to over 140 countries worldwide and next-generation IP network services to medium and large businesses and government customers. Verizon s domestic wireless business, operating as Verizon Wireless, provides wireless voice and data products and services across the United States using one of the most extensive wireless networks. Information Services operates directory publishing businesses and provides electronic commerce services. Stressing diversity and commitment to the communities in which we operate, Verizon has a highly diverse workforce of 250,000 employees.

The sections that follow provide information about the important aspects of our operations and investments, both at the consolidated and segment levels, and include discussions of our results of operations, financial position and sources and uses of cash. In addition, we have highlighted key trends and uncertainties to the extent practicable. The content and organization of the financial and non-financial data presented in these sections are consistent with information used by our chief operating decision makers for, among other purposes, evaluating performance and allocating resources. We also monitor several key economic indicators as well as the state of the economy in general, primarily in the United States where the majority of our operations are located, in evaluating our operating results and analyzing and understanding business trends. While most key economic indicators, including gross domestic product, impact our operations to some degree, we have noted higher correlations to housing starts, non-farm employment, personal consumption expenditures and capital spending, as well as more general economic indicators such as inflation and unemployment rates.

Our results of operations, financial position and sources and uses of cash in the current and future periods reflect Verizon management s focus on the following four key areas:

Revenue Growth Our emphasis is on revenue transformation, devoting more resources to higher growth markets such as wireless, long distance, wireline broadband connections, including digital subscriber lines (DSL) and fiber optics to the home (Verizon s FiOS data and TV services) and other data services, as well as expanded services to business markets, rather than to traditional wireline voice services, where we have been experiencing access line losses. In the third quarter of 2006, revenues from these growth areas were more than 50% of total revenue. Verizon reported consolidated revenue growth of 25.8% in the third quarter of 2006 compared to the similar period in 2005. This revenue growth was primarily driven by the merger with MCI, as well as higher revenue at Domestic Wireless. Verizon added 1,912,000 wireless customers and 448,000 broadband connections in the third quarter of 2006.

Operational Efficiency While focusing resources on growth markets, we are continually challenging our management team to lower expenses, particularly through technology-assisted productivity improvements including self-service initiatives. The effect of these and other efforts, such as real estate consolidations and call center routing improvements, has been to significantly change the company s cost structure and maintain stable operating income margins. Real estate consolidations include our decision to establish Verizon Center for the leadership team. With our deployment of the FiOS network, we expect to realize savings in annual, ongoing operating expenses as a result of efficiencies gained from fiber network facilities. In 2005, Verizon restructured its management retirement benefit plans such that management employees no longer earn pension benefits or earn service towards the company retiree medical subsidy after June 30, 2006, after being provided an 18-month enhancement of the value of their pension and retiree medical benefits, but will receive higher savings plan matching contributions. The net effect of these management benefit plan changes is expected to be a reduction in pretax benefit expenses of approximately $3 billion over 10 years.

Capital Allocation Our capital spending continues to be directed toward growth markets. High-speed wireless data (EV-DO) services, replacement of copper access lines with fiber optics to the home, as well as expanded services to business markets are examples of areas of capital spending in support of these growth markets. In the nine months ended September 30, 2006, capital expenditures were $12,318 million compared to $11,363 million in the nine months ended September 30, 2005. In 2006, Verizon management expects capital expenditures to be in the range of $17.0 billion to $17.4 billion. In addition to capital expenditures, Domestic Wireless continues to participate in the FCC s wireless spectrum auctions and continues to evaluate spectrum acquisitions in support of

expanding data applications and its growing customer base. On September 18, 2006, the FCC completed the Advanced Wireless Services spectrum auction (AWS auction) and Verizon Wireless was the high bidder on thirteen 20 MHz licenses covering a population of nearly 200 million, with bids totaling $2,809 million.

- Cash Flow Generation The financial statements reflect the emphasis of management on not only directing resources to growth markets, but also using cash provided by our operating and investing activities for the repayment of debt in addition to providing a stable dividend to our shareowners. Verizon s total debt increased to $41,683 million as of September 30, 2006 from $38,257 million as of December 31, 2005, primarily as a result of debt acquired in connection with the MCI merger. However, Verizon s ratio of debt to debt combined with shareowners equity was 47.4% as of September 30, 2006 compared with 49.1% as of December 31, 2005 and 49.7% as of September 30, 2005. Verizon repurchased $1,348 million of its common stock as part of its previously announced program during the nine months ended September 30, 2006. Additionally, Verizon s balance of cash and cash equivalents at September 30, 2006 was $1,846 million.

Supporting these key focus areas are continuing initiatives to effectively package and enhance the value of our products and services. In 2004, Verizon announced a deployment expansion of FiOS in several states in our service territory. As of the end of 2005, we met our goal of passing three million premises and are on target to pass a total of 6 million premises by year-end 2006. Our FiOS Internet service continues to gain market share against competitive services in a growing broadband market by offering unsurpassed Internet-access speeds, with upstream speeds of up to 10 Mbps (megabits per second) and with plans to offer downstream speeds of up to 100 Mbps. We have achieved a data penetration rate of 14% across all markets where we have been selling FiOS data, with 3.8 million premises open for sale as of the end of the third quarter of 2006. As of September 30, 2006, FiOS data services are available in 16 states. In 2005, Verizon began offering video on the FiOS network in three markets and now video service is available in 7 states and we continue our efforts to acquire franchises to offer video services. As of September 30, 2006, Verizon obtained 165 video franchises covering 3.4 million households with service available for sale to 1.2 million premises. We have set a target of 175,000 FiOS TV customers by year-end 2006, making the service available to 1.8 million households. As of the September 30, 2006, Verizon had 118,000 FIOS TV customers, which is a video service penetration rate of 10% across all markets. FiOS TV includes a collection of all-digital programming with as many as 395 channels, 47 music channels and 27 high-definition television channels. Innovative product bundles include local wireline, long distance, wireless and broadband services for consumer and general business retail customers. These efforts will also help counter the effects of competition and technology substitution that have resulted in access line losses.

Our integration activities in connection with the MCI merger are continuing on plan. During this period, we have trained our salesforce regarding the products and services available, including new products and bundled product offerings, to the customers of the Verizon Business product line. In 2006, we expect to achieve at least $550 million of merger synergies, and incur integration expenses of approximately $250 million. These synergies include, in part, workforce reductions and data traffic migration onto Verizon s networks rather than utilizing third party access providers.

At Domestic Wireless, we continue to execute on the fundamentals of our network superiority and value proposition to deliver growth for the business and provide new and innovative products and services for our customers such as Broadband Access, our Evolution Data Optimized (EV-DO) service. To accomplish our goal of being the acknowledged market leader in providing wireless voice and data communication services in the U.S, we will continue to implement the following key elements of our business strategy:

- Provide the highest network quality through our code division multiple access (CDMA) 1XRTT technology and EV-DO technology, which significantly increases data transmission rates.

- Profitably acquire, satisfy and retain our customers and increase the value of our service offerings to customers while achieving revenue and net income growth.

- Continue to expand our wireless data, messaging and multi-media offerings for both consumer and business customers and take advantage of the growing demand for wireless data services.

- Focus on operating margins and capital efficiency by driving down costs and leveraging our scale.

On April 3, 2006, we reached definitive agreements to sell our interests in Verizon Dominicana, C. por A. (Verizon Dominicana), Telecomunicaciones de Puerto Rico, Inc. (TELPRI) and Compañía Anónima Nacional Teléfonos de Venezuela (CANTV) in three separate transactions to América Móvil, S.A. de C.V. (América Móvil), a wireless

service provider throughout Latin America, and a company owned jointly by Teléfonos de México, S.A. de C.V. (Telmex) and América Móvil.

On October 18, 2006, the Verizon Board of Directors approved the proposed spin-off of our U.S. print and Internet yellow pages directories business to our shareholders. Additional information related to this transaction is included in the Recent Developments section herein.

Consolidated Results of Operations

In this section, we discuss our overall results of operations and highlight special and non-recurring items. As a result of reaching definitive agreements to sell our interests in Verizon Dominicana, TELPRI and CANTV, which were included in the International segment, the operations of Verizon Dominicana and TELPRI are reported as discontinued operations and assets held for sale, while CANTV continues to be accounted for as an equity method investment. Accordingly, we now have three reportable segments. Prior period amounts and discussions are revised to reflect this change. We include in our results of operations the results of the former MCI business subsequent to the close of the merger on January 6, 2006. We exclude the effects of the special and non-recurring items from the segments results of operations since management does not consider them in assessing segment performance, due primarily to their non-recurring and/or non-operational nature. We believe that this presentation will assist readers in better understanding our results of operations and trends from period to period. This section on consolidated results of operations carries forward the segment results, which exclude the special and non-recurring items, and highlights and describes those items separately to ensure consistency of presentation in this section and the Segment Results of Operations section.

Consolidated Revenues

	Three Months Ended September 30,			Nine Months Ended September 30,		
(Dollars in Millions)	2006	2005	% Change	2006	2005	% Change
Wireline						
Verizon Telecom	$ 8,325	$ 8,056		$ 25,104	$ 24,068	
Verizon Business	5,201	1,852		15,171	5,550	
Intrasegment eliminations	(729)	(463)		(2,214)	(1,361)	
	12,797	9,445	35.5%	38,061	28,257	34.7%
Domestic Wireless	9,869	8,351	18.2	27,944	23,615	18.3
Information Services	804	857	(6.2)	2,443	2,608	(6.3)
Corporate & Other	(216)	(167)	29.3	(458)	(461)	(0.7)
Revenues of Hawaii operations sold					202	(100.0)
Consolidated Revenues	$ 23,254	$ 18,486	25.8	$ 67,990	$ 54,221	25.4

Consolidated revenues in the third quarter of 2006 were higher by $4,768 million, or 25.8%, and $13,769 million, or 25.4%, for the nine months ended September 30, 2006 compared to the similar periods in 2005. These increases were primarily the result of significantly higher revenues at Wireline and Domestic Wireless, partially offset by the sale of Hawaii operations in the second quarter of 2005.

Revenues at the Wireline segment increased during the third quarter of 2006 by $3,352 million, or 35.5% and $9,804 million, or 34.7% for the nine months ended September 30, 2006 compared to the similar periods in 2005. The increase is primarily attributable to the acquisition of MCI and, to a lesser extent, growth from broadband and long distance services. Broadband connections increased to 6.6 million lines at September 30, 2006, an increase of 45.1% from September 30, 2005. The number of Freedom service plans continue to stimulate growth in long distance services, as the number of packages reached 7.5 million as of September 30, 2006, representing a 48.9% increase from September 30, 2005. These increases were partially offset by declines in wholesale revenues at Verizon Telecom and continued downward pressure due to subscriber losses resulting from technology substitution, including Wireless and Voice over Internet Protocol (VoIP). Wholesale revenues at Verizon

Telecom declined by $180 million, or 7.9% for the third quarter of 2006 and by $545 million, or 8.0% for the nine months ended September 30, 2006 compared to similar periods in 2005 primarily due to the exclusion of affiliated access revenues billed to the former MCI mass market entities in the current quarter and year-to-date periods. Revenues at Verizon Business increased primarily due to the acquisition of MCI.

Domestic Wireless s revenues increased during the third quarter of 2006 by $1,518 million, or 18.2% and $4,329 million, or 18.3% for the nine months ended September 30, 2006 compared to the similar periods in 2005 due to increases in service revenues, including data revenues, and equipment and other revenues. Data revenues were $1,197 million in the third quarter of 2006 and $3,104 million for the nine months ended September 30, 2006,

compared to $613 million and $1,512 million in the third quarter of 2005 and the nine months ended September 30, 2005, respectively. Domestic Wireless ended the third quarter of 2006 with 56.7 million customers, an increase of 15.1% over the third quarter of 2005. Domestic Wireless s retail customer base as of September 30, 2006 was approximately 54.6 million, a 15.6% increase over the third quarter of 2005, and comprised approximately 96.2% of our total customer base. Average service revenue per customer (ARPU) increased by 0.9% to $50.59 in the third quarter of 2006 compared to the similar period in 2005, primarily attributable to increases in data revenue per customer driven by increased use of our messaging and other data services. ARPU increased by 0.3% to $49.68 for the nine months ended September 30, 2006 compared to the similar period in 2005. ARPU per retail customer of $51.21 for the quarter ended September 30, 2006 also grew compared to the similar period in 2005. Increases in wireless devices sold and revenue per unit sold drove increases in equipment and other revenue in the third quarter of 2006 and for the nine months ended September 30, 2006 compared to the similar periods in 2005.

Consolidated Operating Expenses

(Dollars in Millions)	Three Months Ended September 30, 2006	2005	% Change	Nine Months Ended September 30, 2006	2005	% Change
Cost of services and sales	$ 8,982	$ 6,361	41.2%	$ 26,349	$ 18,390	43.3%
Selling, general and administrative expense	6,720	5,195	29.4	19,587	15,382	27.3
Depreciation and amortization expense	3,628	3,433	5.7	10,947	10,219	7.1
Sale of businesses, net			nm		(530)	(100.0)
Total Operating Expenses	$ 19,330	$ 14,989	29.0	$ 56,883	$ 43,461	30.9

nm Not meaningful

Cost of Services and Sales

Consolidated cost of services and sales in the third quarter of 2006 increased $2,621 million, or 41.2% and $7,959 million, or 43.3% for the nine months ended September 30, 2006 compared to the similar periods in 2005. These increases were primarily driven by higher costs attributable to the inclusion of the former MCI operations in the Wireline segment subsequent to the completion of the merger, higher wireless network costs, increases in wireless equipment costs and increases in pension and other postretirement benefit costs, partially offset by the net impact of productivity improvement initiatives.

The higher wireless network costs were caused by increased network usage relating to both voice and data services in the third quarter of 2006 and for the nine months ended September 30, 2006 compared to the similar periods in 2005, partially offset by decreased roaming, local interconnection and long distance rates. Cost of wireless equipment sales increased in the third quarter of 2006 and for the nine months ended September 30, 2006 compared to the similar periods in 2005 primarily as a result of an increase in wireless devices sold due to an increase in gross activations and equipment upgrades, together with an increase in cost per unit.

Costs in these periods were also impacted by increased pension and other postretirement benefit costs. As of December 31, 2005, we evaluated key employee benefit plan assumptions in response to current conditions in the securities markets. The overall impact of the 2006 assumptions, combined with the impact of lower than expected actual asset returns over the past several years, resulted in pension and other postretirement benefit expense of approximately $332 million in the third quarter of 2006 and $1,100 million for the nine months ended September 30, 2006, compared to net pension and postretirement benefit expense of $319 million and $954 million in the third quarter of 2005 and nine months ended September 30, 2005, respectively. Special and non-recurring items recorded during the third quarter of 2006 included $6 million of merger integration costs.

Selling, General and Administrative Expense

Consolidated selling, general and administrative expense in the third quarter of 2006 increased $1,525 million, or 29.4% and $4,205 million, or 27.3% for the nine months ended September 30, 2006 compared to the similar periods in 2005. These increases were primarily attributable to the

inclusion of the former MCI operations in the Wireline segment subsequent to the completion of the merger, increases in the Domestic Wireless segment primarily related to increased salary and benefits expenses, and special and non-recurring charges.

Special and non-recurring items recorded during the third quarter of 2006 include $29 million related to pension settlement losses incurred in connection with our benefit plans. For the nine months ended September 30, 2006, special and non-recurring charges also included $300 million for employee severance and severance-related activities

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in connection with the involuntary separation of approximately 3,200 employees, the majority of whom were separated in the second and third quarters of 2006. The remaining employees will be separated during the fourth quarter of 2006. Special and non-recurring charges also included $19 million and $151 million in the third quarter of 2006 and nine months ended September 30, 2006 respectively, of merger integration costs, primarily for advertising and other costs related to re-branding initiatives and systems integration activities. Additionally, the third quarter of 2006 and nine months ended September 30, 2006 included $48 million and $138 million, respectively, of special and non-recurring charges for Verizon Center relocation costs. Special and non-recurring items in the third quarter of 2005 and the nine months ended September 30, 2005 included a pretax impairment charge of $125 million pertaining to our leasing operations for airplanes leased to airlines experiencing financial difficulties, partially offset by net pretax gain of $64 million in connection with the relocation of several functions to Verizon Center.

Depreciation and Amortization Expense

Consolidated depreciation and amortization expense in the third quarter of 2006 increased $195 million, or 5.7% and $728 million, or 7.1% for the nine months ended September 30, 2006 compared to the similar periods in 2005 primarily due to higher depreciable and amortizable asset bases as a result of the MCI merger and, to a lesser extent, increased capital expenditures.

Sales of Businesses, Net

During the second quarter of 2005, we sold our wireline and directory businesses in Hawaii and recorded a pretax gain of $530 million.

Other Consolidated Results

Equity in Earnings of Unconsolidated Businesses

Equity in earnings of unconsolidated businesses increased by $106 million, or 58.2% in the third quarter of 2006 and by $63 million, or 11.4% for the nine months ended September 30, 2006 compared to the similar periods in 2005. The increase for the third quarter of 2006 compared to the similar period of 2005 is primarily driven by additional pension liabilities at CANTV recorded in the prior year quarter as well as higher tax benefits at CANTV and improved operational results. In addition, the increase reflects our proportionate share, or $85 million, of a tax benefit booked at Vodafone Omnitel, partially offset by a similar benefit recorded in the three months ended September 30, 2005 of $76 million. The increase for the nine months ended September 30, 2006 compared to the similar period of 2005 is primarily driven by the aforementioned items described above, partially offset by lower operational results, lower tax benefits and unfavorable foreign exchange fluctuations at Vodafone Omnitel compared with the similar period in 2005.

Other Income and (Expense), Net

(Dollars in Millions)	Three Months Ended September 30, 2006	2005	% Change	Nine Months Ended September 30, 2006	2005	% Change
Interest income	$ 40	$ 24	66.7%	$ 143	$ 87	64.4%
Foreign exchange gains, net	2	12	(83.3)	5	11	(54.5)
Other, net	59	52	13.5	116	192	(39.6)
Total	$ 101	$ 88	14.8	$ 264	$ 290	(9.0)

The increase in other income and expense, net in the third quarter of 2006 compared to the similar period of 2005 is primarily due to higher interest income as well as higher Other, net income, partially offset by lower foreign exchange gains. Other, net income in the third quarter of 2006 includes leased asset gains compared to leased asset losses in the similar period of 2005. Other, net income in the third quarter of 2006 also includes a pretax gain on the sale of a small domestic investment, while the third quarter of 2005 includes a pretax gain on the sale of a small international business and other investment gains. Additionally, Other, net income in the third quarter of 2005 includes costs of $10 million recorded in connection with the early extinguishment of debt.

The decrease in other income and expense, net for the nine months ended September 30, 2006 compared to the similar period of 2005 is primarily due to lower Other, net income, partially offset by higher interest income. Lower Other, net income in the nine months ended September 30, 2006 was primarily driven by leased asset losses

compared to leased asset gains in the similar period of 2005, as well as by higher gains on the sales of businesses and investments in the nine months ended September 30, 2005.

Interest Expense

(Dollars in Millions)	Three Months Ended September 30, 2006	2005	% Change	Nine Months Ended September 30, 2006	2005	% Change
Interest expense	$ 572	$ 525	9.0%	$ 1,798	$ 1,601	12.3%
Capitalized interest costs	125	100	25.0	350	263	33.1
Total interest costs on debt balances	$ 697	$ 625	11.5	$ 2,148	$ 1,864	15.2
Average debt outstanding	$ 41,979	$ 39,808		$ 42,441	$ 39,511	
Effective interest rate	6.64%	6.28%		6.75%	6.29%	

The increase in interest costs for the third quarter of 2006 and for the nine months ended September 30, 2006 compared to the similar periods in 2005 were due to higher average debt levels of $2,171 million and $2,930 million, respectively, as a result of the debt acquired in connection with the merger with MCI, and higher average interest rates, partially offset by a higher level of interest capitalized in connection with the build-out of our FiOS network.

Minority Interest

(Dollars in Millions)	Three Months Ended September 30, 2006	2005	% Change	Nine Months Ended September 30, 2006	2005	% Change
Minority interest	$ 1,088	$ 748	45.5%	$ 2,942	$ 2,069	42.2%

The increase in minority interest expense in the third quarter of 2006 and for the nine months ended September 30, 2006 compared to the similar periods in 2005 is primarily due to the higher earnings at Domestic Wireless, which has a significant minority interest attributable to Vodafone Group Plc (Vodafone).

Provision for Income Taxes

(Dollars in Millions)	Three Months Ended September 30, 2006	2005	% Change	Nine Months Ended September 30, 2006	2005	% Change
Provision for income taxes	$ 855	$ 702	21.8%	$ 2,421	$ 2,386	1.5%
Effective income tax rate	32.2%	28.1%		33.4%	30.1%	

The effective income tax rate is the provision for income taxes as a percentage of income before the provision for income taxes, discontinued operations and cumulative effect of accounting change. The effective tax rate for the third quarter of 2006 compared to the similar period of 2005 was higher due to tax benefits recorded in 2005 related to prior year investment losses, the impact of favorable tax benefits resulting from tax reserve adjustments, including audit settlements and other activity in 2005 compared to 2006 and higher state taxes in 2006 due to a favorable legislative change which decreased state taxes in 2005. This increase in the 2006 rate compared to the 2005 rate was partially offset by higher foreign related tax benefits as well as by benefits provided by the American Jobs Creation Act of 2004. The effective tax rate for the nine months ended September 30, 2006 compared to the similar period of 2005 was higher as a result of those items described above, with the exception of lower state taxes benefiting the 2006 period compared to the similar period of 2005. In addition, principally as a result of the capital gain realized in the second quarter of 2005 in connection with the sale of our Hawaii businesses, we recorded tax benefits of $336 million in 2005 primarily related to previous investment losses, which was largely offset by a net tax provision of $211 million related to the repatriation of foreign earnings under the provisions of the American Jobs Creation Act of 2004.

Cumulative Effect of Accounting Change

In December 2004, the Financial Accounting Standards Board (FASB) issued SFAS No. 123(R), *Share-Based Payment*, which revises SFAS No. 123, *Accounting for Stock-Based Compensation*. SFAS No. 123(R) requires all share-based payments to employees, including grants of employee stock options, to be recognized as compensation expense based on their fair value. Effective January 1, 2003, we adopted the fair value recognition provisions of SFAS No. 123, using the prospective

method (as permitted under SFAS No. 148, *Accounting for Stock-Based Compensation Transition and Disclosure*) for all new awards granted, modified or settled after January 1, 2003. Under the prospective method, employee compensation expense in the first year is recognized for new awards granted, modified, or settled. The options generally vest over a term of three years, therefore the expenses related to stock-based employee compensation included in the determination of net income for 2006, 2005 and 2004 are less than what would have been recorded if the fair value method had been applied to previously issued awards.

Effective January 1, 2006, we adopted SFAS No. 123(R) utilizing the modified prospective method. SFAS No. 123(R) requires the measurement of stock-based compensation expense based on the fair value of the award on the date of grant. Under the modified prospective method, the provisions of SFAS No. 123(R) apply to all awards granted or modified after the date of adoption. SFAS No. 123(R) is supplemented by Staff Accounting Bulletin (SAB) No. 107, Share-Based Payments (SAB No. 107). This SAB, which was issued by the SEC in March 2005, expresses the views of the SEC staff regarding the relationship between SFAS No. 123(R) and certain SEC rules and regulations. In particular, this SAB provides guidance related to valuation methods, the classification of compensation expense, non-GAAP financial measures, the accounting for income tax effects of share-based payment arrangements, disclosures in Management s Discussion and Analysis subsequent to adoption of SFAS No. 123(R), and interpretations of other share-based payment arrangements. We also adopted SAB No. 107 on January 1, 2006.

We recorded a $42 million cumulative effect of accounting change as of January 1, 2006, net of taxes and after minority interest, to recognize the effect of initially measuring the outstanding liability awards (VARs) of the Verizon Wireless joint venture at fair value utilizing a Black-Scholes model. Although we recorded a cumulative effect of adoption as of January 1, 2006, we do not expect SFAS No. 123(R) to have a material effect on our consolidated financial statements in future periods (see Note 3).

Discontinued Operations

Verizon Dominicana and Telecomunicaciones de Puerto Rico, Inc.

During the second quarter of 2006, we reached definitive agreements to sell our interests in our Caribbean and Latin American telecommunications operations in three separate transactions to América Móvil, a wireless service provider throughout Latin America, and a company owned jointly by Telmex and América Móvil. We agreed to sell our 100 percent indirect interest in Verizon Dominicana and our 52 percent interest in TELPRI to América Móvil. An entity jointly owned by América Móvil and Telmex has agreed to purchase our indirect 28.5 percent interest in CANTV.

Upon closing, the transactions are expected to result in pretax proceeds of approximately $3,700 million, prior to purchase price adjustments as defined in the sale agreements. Each transaction is subject to separate regulatory approvals and none of the sales is contingent on the closing of any of the other transactions. We expect to close the sale of our interest in TELPRI in 2006 or 2007. In September 2006, we extended the expiration date of the Verizon Dominicana and CANTV transactions until December 29, 2006. The transactions are expected to close subject to the receipt of regulatory approvals. Although we anticipate pretax gains on the transactions, in the case of Verizon Dominicana, the U.S. taxes that will become payable and be recorded at the time the transaction closes will significantly exceed the amount of the pretax gain. In addition, the government tax authority in the Dominican Republic has issued an assessment of capital gains tax in connection with the proposed transaction. We believe that the assessment is without merit, have filed an appeal and are contesting it vigorously. We are unable to predict the ultimate outcome of this proceeding or its effect on the transaction.

Income from discontinued operations, net of tax increased by $47 million, or 61.0% in the third quarter of 2006 and $189 million, or 98.4% for the nine months ended September 30, 2006 compared to the similar periods in 2005. These increases were primarily due to the cessation of depreciation on fixed assets in the third quarter of 2006, consistent with the accounting requirements for discontinued operations, and the sale of directory publication rights of TELPRI, as well as the cessation of depreciation during the nine months ended September 30, 2006.

Segment Results of Operations

As a result of reaching definitive agreements to sell our interests in Verizon Dominicana, TELPRI and CANTV, which were included in the International segment, the operations of Verizon Dominicana and TELPRI are reported as discontinued operations and assets held for sale, while CANTV continues to be accounted for as an equity method investment. Accordingly, we now have three reportable segments and prior period amounts and discussions are revised to reflect this change. Our segments are Wireline, Domestic Wireless, and Information Services. You can find additional information about our segments in Note 10 to the unaudited condensed consolidated financial statements.

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We measure and evaluate our reportable segments based on segment income, which excludes unallocated corporate expenses and other adjustments arising during each period. The other adjustments include transactions that the chief operating decision makers exclude in assessing business unit performance due primarily to their non-recurring and/or non-operational nature. Although such transactions are excluded from business segment results, they are included in reported consolidated earnings. We previously highlighted the more significant of these transactions in the Consolidated Results of Operations section. Gains and losses that are not individually significant are included in all segment results, since these items are included in the chief operating decision makers assessment of unit performance.

Wireline

The Wireline segment, which includes the operations of the former MCI, consists of the operations of Verizon Telecom, a provider of telephone services, including voice, broadband, data, network access, long distance, video, and other services to consumer and small business customers and carriers, and Verizon Business, a provider of next-generation IP network services globally to medium and large businesses and government customers. As discussed earlier under Consolidated Results of Operations, in the second quarter of 2005, we sold wireline properties in Hawaii representing approximately 700,000 access lines or 1% of the total Verizon Telecom switched access lines in service. For comparability purposes, the results of operations shown in the tables below exclude the Hawaii properties that have been sold.

Operating Revenues

(Dollars in Millions)	Three Months Ended September 30, 2006	2005	% Change	Nine Months Ended September 30, 2006	2005	% Change
Verizon Telecom						
Mass Markets	$ 5,640	$ 5,145	9.6%	$ 17,014	$ 15,376	10.7%
Wholesale	2,104	2,284	(7.9)	6,262	6,807	(8.0)
Other	581	627	(7.3)	1,828	1,885	(3.0)
Verizon Business						
Enterprise Business	3,562	1,501	137.3	10,338	4,521	128.7
Wholesale	844	351	140.5	2,515	1,029	144.4
International and Other	795		nm	2,318		nm
Intrasegment Eliminations	(729)	(463)	57.5	(2,214)	(1,361)	62.7
Total Wireline Operating Revenues	$ 12,797	$ 9,445	35.5	$ 38,061	$ 28,257	34.7

nm Not meaningful

In connection with the completion of the MCI merger, our product lines were realigned to be reflective of the Line of Business structure in which the product lines are currently being managed. Prior period amounts and discussions were reclassified to conform to the current presentation.

Verizon Telecom

Mass Markets

Verizon Telecom s Mass Markets revenue includes local exchange (basic service and end-user access), value-added services, long distance, broadband services for residential and certain small business accounts and FiOS TV services. Value-added services are a family of services that expand the utilization of the network, including products such as Caller ID, Call Waiting, Home Voicemail and Return Call. Long distance includes both intraLATA toll services and interLATA long distance services. Broadband services include DSL and FiOS. In addition to subscriber services, Mass Markets offers non-subscriber services that include dial around long distance products.

The increase in mass market revenue of $495 million, or 9.6% in the third quarter of 2006 and $1,638 million, or 10.7% for the nine months ended September 30, 2006 compared to the similar periods in 2005 was due to the inclusion of revenues from the former MCI in the current year and growth from broadband and long distance, offset by lower demand and usage of our basic local exchange and accompanying services attributable to subscriber losses due to technology substitution, including wireless and VoIP.

We added 1,429,000 new broadband connections, including 352,000 for FiOS in the nine months ended September 30, 2006. For the third quarter 2006, we added 448,000 broadband connections, including 147,000 for FiOS, for a total of 6,573,000 lines at September 30, 2006, representing a 45.1% increase from September 30, 2005. Our Freedom service plans continue to stimulate growth in long distance services, as the number of packages reached 7.5 million as of September 30, 2006, representing a 48.9% increase from September 30, 2005. As of September 30, 2006, approximately 57% of our legacy Verizon wireline customers have chosen Verizon as their long distance carrier.

A 7.5% decline in switched access lines in service from third quarter 2005 to third quarter 2006 was mainly driven by the effects of competition and technology substitution. Demand for legacy Verizon residential access lines declined 6.8% at September 30, 2006 compared to September 30, 2005, as customers substituted wireless, broadband and cable services for traditional landline services. At the same time, legacy Verizon business access lines declined 3.2% at September 30, 2006 compared to September 30, 2005, primarily reflecting competition and a shift to high-speed, high-volume special access lines.

We continue to seek opportunities to retain and win back customers. Our Freedom service plans offer local services with various combinations of long distance and Internet access services in a discounted bundle available on one bill. We have introduced our Freedom service plans in nearly all of our key markets.

Wholesale

Wholesale revenues are earned from long distance and other competing carriers who use our local exchange facilities to provide usage services to their customers. Switched access revenues are derived from fixed and usage-based charges paid by carriers for access to our local network. Special access revenues originate from carriers that buy dedicated local exchange capacity to support their private networks. Wholesale services also include local wholesale revenues from unbundled network elements (UNEs), interconnection revenues from competitive local exchange carriers (CLECs) and wireless carriers, and some data transport revenues.

Wholesale revenues decreased by $180 million, or 7.9% in the third quarter of 2006 and by $545 million, or 8.0% for the nine months ended September 30, 2006 compared to the similar periods in 2005, due to the exclusion of affiliated access revenues billed to the former MCI mass market entities in the current quarter and year-to-date periods, and declines in legacy Verizon switched access revenues and local wholesale revenues, offset by increases in special access revenues.

Switched minutes of use (MOUs) declined in the third quarter of 2006 and for the nine months ended September 30, 2006 compared to the similar periods in 2005, reflecting the impact of access line loss and technology substitution. Wholesale lines decreased by 18.2% due to the impact of a decision by a major competitor to deemphasize their local market initiatives in 2005. Special access revenue growth reflects continuing demand in the business market for high-capacity, high-speed digital services, partially offset by lessening demand for older, low-speed data products and services. As of September 30, 2006, customer demand for high capacity and digital data services increased 9.3% compared to the similar period in 2005.

The FCC regulates the rates that we charge customers for interstate access services. See Other Factors That May Affect Future Results Regulatory and Competitive Trends FCC Regulation for additional information on FCC rulemaking concerning federal access rates, universal service and certain broadband services.

Other

Other revenues include services such as operator services (including deaf relay services), public (coin) telephone, card services and supply sales, as well as former MCI dial around services including 10-10-987, 10-10-220, 1-800-COLLECT and Prepaid Cards.

Verizon Telecom s revenues from other services decreased by $46 million, or 7.3% in the third quarter, and by $57 million, or 3.0% for the nine months ended September 30, 2006 compared to the similar periods in 2005. Revenue increases, due to the inclusion of revenues from the former MCI in the current year, were more than offset by decreases due to the dissolution of non-strategic businesses, including the termination of a large commercial inventory management contract in 2005, and reduced business volumes.

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Verizon Business

Enterprise Business

Our Enterprise Business market provides voice, data and internet communications services to medium and large business customers, multi-national corporations, and state and federal government customers. In addition, the Enterprise Business market also provides value-added services that make communications more secure, reliable and efficient, and managed network services for customers that outsource all or portions of their communications and information processing operations. Traditional local and long distance services comprise $1,655 million, or 46.5% of revenue in the quarter ended September 30, 2006, and $4,872 million or 47.1% of revenue for the nine months ended September 30, 2006. Enterprise Business also provides data services such as Private Line, Frame Relay and ATM services, both domestically and internationally, as well as managed network services to its customers.

Enterprise Business revenues increased by $2,061 million, or 137.3% in the third quarter of 2006 and by $5,817 million or 128.7% for the nine months ended September 30, 2006 compared to the similar periods in 2005 primarily due to the acquisition of MCI. Data services revenue represented $1,389 million, or 39.0% of Enterprise Business s revenue stream in the third quarter of 2006 and $4,010 million or 38.8% for the nine months ended September 30, 2006. Internet services revenue was $518 million for the third quarter of 2006, or 14.5% of Enterprise Business s revenues and $1,456 million or 14.1% for the nine months ended September 30, 2006. The Internet suite of products is Enterprise Business s fastest growing product line and includes Private IP, IP VPN, Web Hosting and VoIP.

Wholesale

Wholesale revenues relate to domestic wholesale services, which include all wholesale traffic sold in the United States, as well as traffic that originates in the United States and terminates in a different country.

Verizon Business wholesale revenues increased by $493 million, or 140.5%, in the third quarter of 2006 and by $1,486 million, or 144.4% for the nine months ended September 30, 2006 compared to the similar period in 2005, primarily due to the MCI acquisition. Local and long distance voice products, including transport, represented $596 million or 70.6% of the market s total revenue in the third quarter of 2006, and $1,751 million or 69.6% for the nine months ended September 30, 2006. Wholesale revenue is influenced by aggressive competitive pricing, in particular long distance voice services. Wholesale data and Internet revenues were $248 million or 29.4% of total Wholesale revenue in the third quarter of 2006 and $764 million or 30.4% of total Wholesale revenue for the nine months ended September 30, 2006.

International and Other

International operations serve businesses, government entities and telecommunication carriers outside of the United States. Other operations include our Skytel paging business.

Our revenues from International and Other were $795 million in the third quarter of 2006 and $2,318 million in the nine months ended September 30, 2006. This market represents a new revenue stream to Verizon resulting from the MCI acquisition. International and Other had voice revenue of $472 which comprised 59.4% of the total International and Other revenues in the third quarter of 2006, and $1,371 million or 59.1% of the total International and Other revenues for the nine months ended September 30, 2006. Internet revenues in the third quarter of 2006 represented $228 million, or 28.7%, of total International and Other revenues and $655 million or 28.3% of total International and Other revenues for the nine months ended September 30, 2006. Data revenues were $95 million, or 11.9% of total International and Other revenues in the third quarter of 2006 and $292 million or 12.6% of total International and Other revenues for the nine months ended September 30, 2006.

Operating Expenses

(Dollars in Millions)	Three Months Ended September 30, 2006	2005	% Change	Nine Months Ended September 30, 2006	2005	% Change
Cost of services and sales	$ 6,205	$ 3,932	57.8%	$ 18,326	$ 11,633	57.5%
Selling, general and administrative expense	3,093	2,016	53.4	9,142	6,288	45.4
Depreciation and amortization expense	2,376	2,197	8.1	7,164	6,582	8.8

$ 11,674	$ 8,145	43.3	$ 34,632	$ 24,503	41.3

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Cost of Services and Sales

Cost of services and sales includes the following costs directly attributable to a service or product: salaries and wages, benefits, materials and supplies, contracted services, network access and transport costs, customer provisioning costs, computer systems support, costs to support our outsourcing contracts and technical facilities, contributions to the universal service fund, customer provisioning costs and cost of products sold. Aggregate customer care costs, which include billing and service provisioning, are allocated between cost of services and sales and selling, general and administrative expense.

Cost of services and sales increased by $2,273 million, or 57.8% in the third quarter of 2006 and $6,693 million, or 57.5% for the nine months ended September 30, 2006 compared to the similar periods in 2005. This increase was primarily due to the MCI merger partially offset by the net impact of other cost changes. Higher costs associated with our growth businesses and annual wage increases were partially offset by productivity improvement initiatives, which reduced cost of services and sales expenses in the current periods. Both periods in 2006 were also impacted by increased net pension and other postretirement benefit costs. As of December 31, 2005, we evaluated key employee benefit plan assumptions in response to current conditions in the securities markets. The overall impact of the 2006 assumptions, combined with the impact of lower than expected actual asset returns over the past several years, resulted in pension and other postretirement benefit expense of $331 million (primarily in cost of services and sales) in the third quarter of 2006 and $1,081 million for the nine months ended September 30, 2006, compared to net pension and postretirement benefit expense of $312 million and $931 million in the third quarter of 2005 and nine months ended September 30, 2005, respectively. Further, expenses decreased in both periods due to the dissolution of non-strategic businesses, including the termination of a large commercial inventory management contract in 2005.

Selling, General and Administrative Expense

Selling, general and administrative expense includes salaries and wages and benefits not directly attributable to a service or product, bad debt charges, taxes other than income, advertising and sales commission costs, customer billing, call center and information technology costs, professional service fees and rent for administrative space.

Selling, general and administrative expenses in the third quarter of 2006 increased by $1,077 million or 53.4% and $2,854 million or 45.4% for the nine months ended September 30, 2006 compared to the similar periods in 2005. This increase was primarily due to the inclusion of expenses from the former MCI in the current year and gains on the sale of real estate in the third quarter of 2005, partially offset by the impact of other cost changes. Additionally, there were charges related to miscellaneous adjustments at Verizon New England, partially offset by similar items at other Wireline companies. Expense reductions were attributable to cost reduction initiatives and lower bad debt costs.

Depreciation and Amortization Expense

The increase in depreciation and amortization expense of $179 million, or 8.1% in the third quarter of 2006 and $582 million, or 8.8% for the nine months ended September 30, 2006 compared to the similar periods in 2005 was mainly driven by the acquisition of MCI s depreciable property and equipment and finite-lived intangibles, including its customer lists and capitalized non-network software, measured at fair value and by growth in depreciable telephone plant, partially offset by lower rates of depreciation. Amortization expense increased by $69 million in the third quarter of 2006 and $218 million for the nine months ended September 30, 2006 compared to the similar periods in 2005, primarily due to a higher level of capitalized non-network software and amortization of the acquired MCI intangibles.

Segment Income

(Dollars in Millions)	Three Months Ended September 30, 2006	2005	% Change	Nine Months Ended September 30, 2006	2005	% Change
Segment Income	$ 393	$ 537	(26.8)%	$ 1,200	$ 1,500	(20.0)%

Segment income decreased by $144 million, or 26.8% in the third quarter of 2006 and by $300 million, or 20.0% for the nine months ended September 30, 2006 compared to the similar periods in 2005, due to the after-tax impact of operating revenues and operating expenses described above partially offset by favorable income tax adjustments.

Special and non-recurring items not included in Verizon Wireline s segment income totaled $44 million and $(64) million in the third quarter of 2006 and 2005, respectively. Special and non-recurring items in the third quarter

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of 2006 included costs associated with pension settlement losses, merger integration costs as well as Verizon Center relocation-related costs. Special and non-recurring items in the third quarter of 2005 included a net gain on the sale of a New York City office building and Verizon Center relocation-related costs. Special and non-recurring items during the nine months ended September 30, 2006 of $300 million included costs associated with severance activity, pension settlement losses, Verizon Center relocation-related costs, merger integration costs and costs associated with the redemption and refinancing of debt acquired from MCI. Special and non-recurring items totaling $(287) million for the nine months ended September 30, 2005 related to the Hawaii results of operations and gain on the sale of the Hawaii wireline operations, the net gain on the sale of a New York City office building and Verizon Center relocation-related costs.

Domestic Wireless

Our Domestic Wireless segment provides wireless voice and data services and equipment sales across the United States. This segment primarily represents the operations of the Verizon Wireless joint venture.

Operating Revenues

Three Months Ended September&nb>	(3.6)%	(3.5)%

(1) In 2011, this charge includes severance, impairment and other charges associated with the combination of our FedEx Freight and FedEx National LTL operations, effective January 30, 2011. In 2010, this charge represents impairment charges associated with goodwill related to the FedEx National LTL acquisition.

FedEx Freight Segment Revenues

During 2012, FedEx Freight revenues increased 8% due to increased LTL yield and weight per LTL shipment, partially offset by lower average daily LTL shipments. LTL yield increased 7% during 2012 due to higher fuel surcharges and base yield improvement. Average daily LTL shipments decreased 1% in 2012; however, during the second half of 2012, LTL shipment year-over-year comparisons improved sequentially (2% in the third quarter and 4% in the fourth quarter) due to enhanced service levels, strong customer satisfaction from our service offerings and the impact of severe weather in the prior year.

FedEx Freight segment revenues increased 14% in 2011 due to higher LTL yield and average daily LTL shipments. LTL yields increased 7% in 2011 due to our yield management programs and higher fuel surcharges. Under these programs, LTL yields increased sequentially in each of the previous four quarters, while average daily LTL shipments fell during the second half of 2011. For the full year, average daily LTL shipments increased 4% in 2011 primarily due to volume increases during the first half of 2011 resulting from the impact of discounted pricing in contracts signed during 2010.

The indexed LTL fuel surcharge is based on the average of the national U.S. on-highway average price for a gallon of diesel fuel, as published by the Department of Energy. The indexed LTL fuel surcharge ranged as follows for the years ended May 31:

	2012	2011	2010
Low	19.80%	15.10%	10.80%
High	24.30	20.70	16.10
Weighted-average	22.90	17.00	14.00

On June 8, 2012, FedEx Freight announced a general rate increase of 6.9% for LTL shipments to be effective on July 9, 2012. In June 2011, FedEx Freight increased the fuel surcharge rate to a maximum of 3.6 percentage points above previous levels. In September 2011, we implemented a general rate increase of 6.75% for LTL shipments. In November 2010, we implemented a 6.9% general rate increase for LTL shipments.

FedEx Freight Segment Operating Income (Loss)

In 2012, the FedEx Freight segment operating income increased significantly as a result of higher fuel surcharges, yield growth and ongoing improvements in operational efficiencies due to the combination of our FedEx Freight and FedEx National LTL operations in 2011 (see below). Additionally, the FedEx Freight segment s 2012 results benefited from milder winter weather, while our 2011 results were negatively impacted by unusually severe winter weather.

Purchased transportation costs increased 9% in 2012 due to higher rates and the increased utilization of rail, partially offset by a lower cost per mile due to our ability to optimize mode of transportation while meeting service standards. Fuel costs increased 9% in 2012 due to a higher average price per gallon of diesel fuel partially offset by the increased utilization of rail. Based on a static analysis of the net impact of year-over-year changes in fuel prices compared to year-over-year changes in fuel surcharges, fuel had a positive impact to operating income in 2012. Depreciation and amortization expense decreased 10% in 2012 primarily due to accelerated depreciation in 2011 associated with the combination of our LTL operations.

The FedEx Freight segment operating loss in 2011 included costs associated with the combination of our FedEx Freight and FedEx National LTL operations and the significant impact from severe weather in the second half of the year. We incurred costs associated with the combination of $133 million in 2011, including $89 million recorded in the Impairment and other charges caption of the consolidated income statement.

Salaries and employee benefits increased 8% in 2011 primarily due to volume-related increases in labor, wage increases, higher healthcare and pension costs, and the reinstatement of full 401(k) company-matching contributions. Purchased transportation costs increased 13% in 2011 due to higher shipment volumes and higher rates. Fuel costs increased 31% in 2011 due to a higher average price per gallon of diesel fuel and increased fuel consumption as a result of higher shipment volumes. Based on a static analysis of the net impact of year-over-year changes in fuel prices compared to year-over-year changes in fuel surcharges, fuel had a slightly

favorable impact to operating income in 2011. Maintenance and repairs expense increased 23% in 2011 due to higher volumes and the aging of our fleet. Also, higher intercompany charges in 2011 reflect the transfer of sales and customer service employees from the FedEx Freight segment entities in the first quarter of 2010.

FedEx Freight Segment Outlook

We expect revenue growth at the FedEx Freight segment in 2013 as customers increase their utilization of our integrated network. In addition, we expect yield and volume improvement driven by the unique value proposition of our differentiated LTL services.

FedEx Freight operating income is expected to increase significantly in 2013 driven by improvements in yields and the continued improvement in productivity and efficiency across our integrated network. We will continue to use investments in technology, focused on network and equipment planning and customer automation, to further enhance customer service levels throughout 2013.

Capital expenditures in 2013 are expected to be comparable to 2012, with the majority of our spending for replacement of vehicles and freight handling equipment.

FINANCIAL CONDITION

LIQUIDITY

Cash and cash equivalents totaled $2.8 billion at May 31, 2012, compared to $2.3 billion at May 31, 2011. The following table provides a summary of our cash flows for the periods ended May 31 (in millions):

	2012	2011	2010
Operating activities:			
Net income	$ 2,032	$ 1,452	$ 1,184
Impairment and other charges	134	29	18
Other noncash charges and credits	3,504	2,892	2,514
Changes in assets and liabilities	(835)	(332)	(578)
Cash provided by operating activities	4,835	4,041	3,138
Investing activities:			
Capital expenditures	(4,007)	(3,434)	(2,816)
Business acquisitions, net of cash acquired	(116)	(96)	
Proceeds from asset dispositions and other	74	111	35
Cash used in investing activities	(4,049)	(3,419)	(2,781)
Financing activities:			
Purchase of treasury stock	(197)		
Principal payments on debt	(29)	(262)	(653)
Dividends paid	(164)	(151)	(138)
Other	146	126	99
Cash used in financing activities	(244)	(287)	(692)
Effect of exchange rate changes on cash	(27)	41	(5)
Net increase (decrease) in cash and cash equivalents	$ 515	$ 376	$ (340)

Cash Provided by Operating Activities. Cash flows from operating activities increased $794 million in 2012 primarily due to increased earnings, partially offset by higher pension contributions. Cash flows from operating activities increased $903 million in 2011 primarily due to increased earnings and lower pension contributions.

We made contributions of $722 million to our tax-qualified U.S. domestic pension plans (U.S. Pension Plans) during 2012, including $226 million in voluntary contributions, and contributions of $480 million to our U.S. Pension Plans during 2011, including $121 million in voluntary contributions. We made contributions of $848 million to our U.S. Pension Plans during 2010, including $495 million in voluntary contributions.

Cash Used in Investing Activities. Capital expenditures were 17% higher in 2012 largely due to increased spending at FedEx Express and FedEx Freight and 22% higher in 2011 primarily due to increased spending at FedEx Express. See Capital Resources for a discussion of capital expenditures during 2012 and 2011.

Financing Activities. During the second quarter of 2012, we repurchased 2.8 million FedEx common shares at an average price of $70 per share for a total of $197 million. As of May 31, 2012, 2.9 million shares remained under existing share repurchase authorizations.

During 2011, we repaid our $250 million 7.25% notes that matured on February 15, 2011.

CAPITAL RESOURCES

Our operations are capital intensive, characterized by significant investments in aircraft, vehicles, technology, facilities, and package-handling and sort equipment. The amount and timing of capital additions depend on various factors, including pre-existing contractual commitments, anticipated volume growth, domestic and international economic conditions, new or enhanced services, geographical expansion of services, availability of satisfactory financing and actions of regulatory authorities.

The following table compares capital expenditures by asset category and reportable segment for the years ended May 31 (in millions):

	2012	2011	2010	Percent Change 2012/2011	Percent Change 2011/2010
Aircraft and related equipment	$ 1,875	$ 1,988	$ 1,537	(6)	29
Facilities and sort equipment	638	555	630	15	(12)
Vehicles	723	282	220	156	28
Information and technology investments	541	455	289	19	57
Other equipment	230	154	140	49	10
Total capital expenditures	$ 4,007	$ 3,434	$ 2,816	17	22
FedEx Express segment	$ 2,689	$ 2,467	$ 1,864	9	32
FedEx Ground segment	536	426	400	26	7
FedEx Freight segment	340	153	212	122	(28)
FedEx Services segment	437	387	340	13	14
Other	5	1		NM	NM
Total capital expenditures	$ 4,007	$ 3,434	$ 2,816	17	22

Capital expenditures during 2012 were higher than the prior year primarily due to increased spending for vehicles at FedEx Express, FedEx Freight and FedEx Ground, although spending for aircraft and related equipment at FedEx Express decreased. Aircraft and aircraft-related equipment purchases at FedEx Express during 2012 included the delivery of seven B777Fs and 15 B757s. Capital expenditures during 2011 were higher than the prior year primarily due to increased spending at FedEx Express for aircraft and aircraft-related equipment and at FedEx Services for information technology investments. Aircraft and aircraft-related equipment purchases at FedEx Express during 2011 included six new B777Fs and 22 B757s.

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LIQUIDITY OUTLOOK

We believe that our existing cash and cash equivalents, cash flow from operations, and available financing sources will be adequate to meet our liquidity needs, including working capital, capital expenditure requirements and debt payment obligations. Our cash and cash equivalents balance at May 31, 2012 includes $410 million of cash in offshore jurisdictions associated with our permanent reinvestment strategy. We do not believe that the indefinite reinvestment of these funds offshore impairs our ability to meet our domestic debt or working capital obligations.

We have a shelf registration statement filed with the Securities and Exchange Commission (SEC) that allows us to sell, in one or more future offerings, any combination of our unsecured debt securities and common stock. Historically, we have been successful in obtaining unsecured financing, from both domestic and international sources, although the marketplace for such investment capital can become restricted depending on a variety of economic factors.

A $1 billion revolving credit facility is available to finance our operations and other cash flow needs and to provide support for the issuance of commercial paper. The revolving credit agreement expires in April 2016. The agreement contains a financial covenant, which requires us to maintain a leverage ratio of adjusted debt (long-term debt, including the current portion of such debt, plus six times our last four fiscal quarters rentals and landing fees) to capital (adjusted debt plus total common stockholders investment) that does not exceed 70%. Our leverage ratio of adjusted debt to capital was 53% at May 31, 2012. We believe the leverage ratio covenant is our only significant restrictive covenant in our revolving credit agreement. Our revolving credit agreement contains other customary covenants that do not, individually or in the aggregate, materially restrict the conduct of our business. We are in compliance with the leverage ratio covenant and all other covenants of our revolving credit agreement and do not expect the covenants to affect our operations, including our liquidity or expected funding needs. As of May 31, 2012, no commercial paper was outstanding, and the entire $1 billion under the revolving credit facility was available for future borrowings.

Standard & Poor s has assigned us a senior unsecured debt credit rating of BBB, commercial paper rating of A-2 and a ratings outlook of stable. During 2012, Moody s Investors Service raised our senior unsecured debt credit rating to Baa1 from Baa2 and affirmed a commercial paper rating of P-2 and a ratings outlook of stable. If our credit ratings drop, our interest expense may increase. If our commercial paper ratings drop below current levels, we may have difficulty utilizing the commercial paper market. If our senior unsecured debt credit ratings drop below investment grade, our access to financing may become limited.

Subsequent to year-end, we completed acquisitions in Poland, Brazil and France for approximately $500 million (see Business Acquisitions for additional information), and on June 15, 2012, we repaid our $300 million 9.65% unsecured notes when they matured.

Our capital expenditures are expected to be $3.9 billion in 2013. We anticipate that our cash flow from operations will be sufficient to fund our capital expenditures in 2013, which will include spending for aircraft and aircraft-related equipment at FedEx Express, sort facility expansion at FedEx Express and FedEx Ground and vehicle replacement at all our transportation segments. We expect approximately 46% of capital expenditures in 2013 will be designated for growth initiatives and 54% dedicated to maintaining our existing operations. Our capital expenditures are expected to decrease in 2013 due to delayed delivery of two B777F aircraft (see below) partially offset by increased spending on facility investment. Our expected capital expenditures for 2013 include $1.3 billion in investments for delivery of aircraft as well as progress payments toward future aircraft deliveries at FedEx Express. For 2013, we anticipate making required contributions to our U.S. Pension Plans totaling approximately $550 million. Our U.S. Pension Plans have ample funds to meet expected benefit payments.

We have several aircraft modernization programs underway which are supported by the purchase of B777F, B767F and B757 aircraft. These aircraft are significantly more fuel-efficient per unit than the aircraft type previously utilized, and these expenditures are necessary to achieve significant long-term operating savings and to support projected long-term international volume growth. Our ability to delay the timing of these aircraft-related expenditures is limited without incurring significant costs to modify existing purchase agreements. We will have a benefit from the tax expensing and accelerated depreciation provisions of the Tax Relief Act of 2010 on qualifying capital investments we make until December 31, 2012.

B777F Aircraft. We have agreed to purchase a total of 43 B777F aircraft (19 of which were in service at May 31, 2012, and an additional four to be delivered in 2013). During the second quarter of 2012, FedEx Express delayed the delivery of two B777F aircraft from 2013, and in conjunction with the execution of the December 2011 B767F aircraft purchase agreement (described below), also delayed the delivery of nine B777F aircraft, five of which were deferred from 2014 and one per year from 2015 to 2018, to better align air network capacity to demand. FedEx Express also exercised two B777F options for aircraft to be delivered at the end of the delivery schedule.

In conjunction with the June 29, 2012 supplemental agreement to purchase B767F aircraft (described below), we agreed to convert four contracted B777F aircraft deliveries that were subject to the Railway Labor Act of 1926, as amended (RLA) (two scheduled for delivery in fiscal 2016 and two scheduled for delivery in fiscal 2017) to equivalent purchase value for B767F aircraft acquired under the supplemental agreement referenced below.

With consideration of the supplemental agreement, our obligation to purchase 9 of these B777F aircraft is conditioned upon there being no event that causes FedEx Express or its employees not to be covered by the RLA.

B767F Aircraft. We have agreed to purchase a total of 46 B767F aircraft (the first three to be delivered in 2014). In December 2011, FedEx Express entered into an agreement to acquire 27 new B767F aircraft, with the first three arriving in 2014 followed by six per year from 2015 to 2018. The B767F was selected as the best choice to begin replacing FedEx Express s MD10 aircraft, some of which are more than 40 years old. The B767Fs will provide similar capacity as the MD10s, with improved reliability, an approximate 30% increase in fuel efficiency and a minimum of a 20% reduction in unit operating costs.

On June 29, 2012, FedEx Express entered into a supplemental agreement to purchase nine additional B767F aircraft. Additionally, FedEx Express exercised ten B767F options available under the December 2011 agreement and purchased the right to 15 additional options. Four of these 19 additional B767F aircraft purchases are subject to the RLA condition. These 19 additional B767F aircraft are expected to be delivered from fiscal 2015 to 2019 and will replace current MD10-10 and A310-200 aircraft.

B757 Aircraft. Our B757 aircraft are replacing our B727 aircraft, and we expect to be completely transitioned out of the B727 aircraft by 2015.

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CONTRACTUAL CASH OBLIGATIONS AND OFF-BALANCE SHEET ARRANGEMENTS

The following table sets forth a summary of our contractual cash obligations as of May 31, 2012. Certain of these contractual obligations are reflected in our balance sheet, while others are disclosed as future obligations under accounting principles generally accepted in the United States. Except for the current portion of long-term debt and capital lease obligations, this table does not include amounts already recorded in our balance sheet as current liabilities at May 31, 2012. We have certain contingent liabilities that are not accrued in our balance sheet in accordance with accounting principles generally accepted in the United States. These contingent liabilities are not included in the table below. We have other long-term liabilities reflected in our balance sheet, including deferred income taxes, qualified and nonqualified pension and postretirement healthcare plan liabilities and other self-insurance accruals. The payment obligations associated with these liabilities are not reflected in the table below due to the absence of scheduled maturities. Accordingly, this table is not meant to represent a forecast of our total cash expenditures for any of the periods presented.

	Payments Due by Fiscal Year (Undiscounted) (in millions)						
	2013	2014	2015	2016	2017	Thereafter	Total
Operating activities:							
Operating leases	$ 1,872	$ 1,725	$ 1,572	$ 1,391	$ 1,433	$ 5,993	$ 13,986
Non-capital purchase obligations and other	173	191	139	78	52	134	767
Interest on long-term debt	98	97	78	78	78	1,581	2,010
Quarterly contributions to our U.S. Pension Plans	550						550
Investing activities:							
Aircraft and aircraft-related capital commitments	965	558	824	912	1,009	5,166	9,434
Other capital purchase obligations	127						127
Financing activities:							
Debt	300	250				989	1,539
Capital lease obligations	120	2	2	1	1	11	137
Total	$ 4,205	$ 2,823	$ 2,615	$ 2,460	$ 2,573	$ 13,874	$ 28,550

Open purchase orders that are cancelable are not considered unconditional purchase obligations for financial reporting purposes and are not included in the table above. Such purchase orders often represent authorizations to purchase rather than binding agreements. See Note 16 of the accompanying consolidated financial statements for more information.

Operating Activities

In accordance with accounting principles generally accepted in the United States, future contractual payments under our operating leases (totaling $14 billion on an undiscounted basis) are not recorded in our balance sheet. Credit rating agencies routinely use information concerning minimum lease payments required for our operating leases to calculate our debt capacity. The amounts reflected in the table above for operating leases represent future minimum lease payments under noncancelable operating leases (principally aircraft and facilities) with an initial or remaining term in excess of one year at May 31, 2012. In the past, we financed a significant portion of our aircraft needs (and certain other equipment needs) using operating leases (a type of off-balance sheet financing). At the time that the decision to lease was made, we determined that these operating leases would provide economic benefits favorable to ownership with respect to market values, liquidity or after-tax cash flows.

The amounts reflected for purchase obligations represent noncancelable agreements to purchase goods or services that are not capital-related. Such contracts include those for printing and advertising and promotions contracts.

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Included in the table above within the caption entitled Non-capital purchase obligations and other is our estimate of the current portion of the liability ($1 million) for uncertain tax positions. We cannot reasonably estimate the timing of the long-term payments or the amount by which the liability will increase or decrease over time; therefore, the long-term portion of the liability ($50 million) is excluded from the table. See Note 11 of the accompanying consolidated financial statements for further information.

The amounts reflected in the table above for interest on long-term debt represent future interest payments due on our long-term debt, all of which are fixed rate.

Investing Activities

The amounts reflected in the table above for capital purchase obligations represent noncancelable agreements to purchase capital-related equipment. Such contracts include those for certain purchases of aircraft, aircraft modifications, vehicles, facilities, computers and other equipment. Commitments to purchase aircraft in passenger configuration do not include the attendant costs to modify these aircraft for cargo transport unless we have entered into noncancelable commitments to modify such aircraft.

Financing Activities

We have certain financial instruments representing potential commitments, not reflected in the table above, that were incurred in the normal course of business to support our operations, including standby letters of credit and surety bonds. These instruments are required under certain U.S. self-insurance programs and are also used in the normal course of international operations. The underlying liabilities insured by these instruments are reflected in our balance sheets, where applicable. Therefore, no additional liability is reflected for the letters of credit and surety bonds themselves.

The amounts reflected in the table above for long-term debt represent future scheduled payments on our long-term debt. In 2013, we have scheduled debt payments of $420 million, which includes $300 million for principal payments on our 9.65% unsecured notes that matured in June 2012, and principal and interest payments on capital leases.

CRITICAL ACCOUNTING ESTIMATES

The preparation of financial statements in accordance with accounting principles generally accepted in the United States requires management to make significant judgments and estimates to develop amounts reflected and disclosed in the financial statements. In many cases, there are alternative policies or estimation techniques that could be used. We maintain a thorough process to review the application of our accounting policies and to evaluate the appropriateness of the many estimates that are required to prepare the financial statements of a complex, global corporation. However, even under optimal circumstances, estimates routinely require adjustment based on changing circumstances and new or better information.

The estimates discussed below include the financial statement elements that are either the most judgmental or involve the selection or application of alternative accounting policies and are material to our financial statements. Management has discussed the development and selection of these critical accounting estimates with the Audit Committee of our Board of Directors and with our independent registered public accounting firm.

RETIREMENT PLANS

OVERVIEW. We sponsor programs that provide retirement benefits to most of our employees. These programs include defined benefit pension plans, defined contribution plans and postretirement healthcare plans.

Pension benefits for most employees are accrued under a cash balance formula we call the Portable Pension Account. Under the Portable Pension Account, the retirement benefit is expressed as a dollar amount in a notional account that grows with annual credits based on pay, age and years of credited service, and interest on the notional account balance. The Portable Pension Account benefit

is payable as a lump sum or an annuity at retirement at the election of the employee. The plan interest credit rate varies from year to year based on a U.S. Treasury index and corporate bond rates. Prior to 2009, certain employees earned benefits using a traditional pension formula (based on average earnings and years of service). Benefits under this formula were capped on May 31, 2008 for most employees.

The current rules for pension accounting are complex and can produce tremendous volatility in our results, financial condition and liquidity. Our pension expense is primarily a function of the value of our plan assets and the discount rate used to measure our pension liabilities at a single point in time at the end of our fiscal year (the measurement date). Both of these factors are significantly influenced by the stock and bond markets, which in recent years have experienced substantial volatility.

In addition to expense volatility, we are required to record year-end adjustments to our balance sheet on an annual basis for the net funded status of our pension and postretirement healthcare plans. These adjustments have fluctuated significantly over the past several years and like our pension expense, are a result of the discount rate and value of our plan assets at the measurement date. The funded status of our plans also impacts our liquidity, as current funding laws require increasingly aggressive funding levels for our pension plans. However, the cash funding rules operate under a completely different set of assumptions and standards than those used for financial reporting purposes, so our actual cash funding requirements can differ materially from our reported funded status.

Our retirement plans cost is included in the Salaries and Employee Benefits caption in our consolidated income statements. A summary of our retirement plans costs over the past three years is as follows (in millions):

	2012	2011	2010
U.S. domestic and international pension plans	$ 524	$ 543	$ 308
U.S. domestic and international defined contribution plans	338	257	136
Postretirement healthcare plans	70	60	42
	$ 932	$ 860	$ 486

Total retirement plans cost increased $72 million in 2012 primarily due to higher expenses for our 401(k) plans due to the full restoration of company matching contributions on January 1, 2011. Total retirement plans cost increased $374 million in 2011 driven by lower discount rates used to measure our benefit obligations at our May 31, 2010 measurement date. Additionally, we incurred higher expenses for our 401(k) plans in 2011 due to the partial reinstatement of company-matching contributions on January 1, 2010 (previously suspended in February 2009).

Our retirement plans costs are expected to increase significantly in 2013, as historically low discount rates at May 31, 2012 will increase our expenses by over $165 million, of which $150 million is attributable to U.S. Pension Plan expense.

PENSION COST. The accounting for pension and postretirement healthcare plans includes numerous assumptions, including the discount rate and expected long-term investment returns on plan assets. These assumptions most significantly impact our U.S. Pension Plans. The components of pension cost for all pension plans are as follows (in millions):

	2012	2011	2010
Service cost	$ 593	$ 521	$ 417
Interest cost	976	900	823
Expected return on plan assets	(1,240)	(1,062)	(955)
Recognized actuarial losses (gains) and other	195	184	23
Net periodic benefit cost	$ 524	$ 543	$ 308

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Following is a discussion of the key estimates we consider in determining our pension cost:

DISCOUNT RATE. This is the interest rate used to discount the estimated future benefit payments that have been accrued to date (the projected benefit obligation, or PBO) to their net present value and to determine the succeeding year s pension expense. The discount rate is determined each year at the plan measurement date. A decrease in the discount rate increases pension expense. The discount rate affects the PBO and pension expense based on the measurement dates, as described below.

Measurement Date	Discount Rate	Amounts Determined by Measurement Date and Discount Rate
5/31/2012	4.44%	2012 PBO and 2013 expense
5/31/2011	5.76	2011 PBO and 2012 expense
5/31/2010	6.37	2010 PBO and 2011 expense
5/31/2009	7.68	2009 PBO and 2010 expense

We determine the discount rate with the assistance of actuaries, who calculate the yield on a theoretical portfolio of high-grade corporate bonds (rated Aa or better) with cash flows designed to match our expected benefit payments in future years. In developing this theoretical portfolio, we select bonds that match cash flows to benefit payments, limit our concentration by industry and issuer, and apply screening criteria to ensure bonds with a call feature have a low probability of being called. To the extent scheduled bond proceeds exceed the estimated benefit payments in a given period, the calculation assumes those excess proceeds are reinvested at one-year forward rates.

The discount rate assumption is highly sensitive, as the following table illustrates for our largest tax-qualified U.S. domestic pension plan:

	Sensitivity (in millions)	
	Effect on 2013 Pension Expense	Effect on 2012 Pension Expense
One-basis-point change in discount rate	$ 2.3	$ 1.9

At our May 31, 2012 measurement date, a 50-basis-point increase in the discount rate would have decreased our 2012 PBO by approximately $1.5 billion and a 50-basis-point decrease in the discount rate would have increased our 2012 PBO by approximately $1.7 billion. From 2009 to 2012, the discount rate used to value our liabilities has declined by over 300 basis points, which increased the valuation of our liabilities by over $7 billion.

PLAN ASSETS. The estimated average rate of return on plan assets is a long-term, forward-looking assumption that also materially affects our pension cost. It is required to be the expected future long-term rate of earnings on plan assets. Our pension plan assets are invested primarily in listed securities, and our pension plans hold only a minimal investment in FedEx common stock that is entirely at the discretion of third-party pension fund investment managers. As part of our strategy to manage future pension costs and net funded status volatility, we have transitioned to a liability-driven investment strategy with a greater concentration of fixed-income securities to better align plan assets with liabilities.

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Establishing the expected future rate of investment return on our pension assets is a judgmental matter, which we review on an annual basis and revise as appropriate. Management considers the following factors in determining this assumption:

- the duration of our pension plan liabilities, which drives the investment strategy we can employ with our pension plan assets;
- the types of investment classes in which we invest our pension plan assets and the expected compound geometric return we can reasonably expect those investment classes to earn over time; and
- the investment returns we can reasonably expect our investment management program to achieve in excess of the returns we could expect if investments were made strictly in indexed funds.

The following table summarizes our current asset allocation strategy (dollars in millions):

	Plan Assets at Measurement Date					
	2012			2011		
Asset Class	Actual	Actual %	Target %	Actual	Actual %	Target %
Domestic equities	$ 5,616	33%	33%	$ 5,761	37%	33%
International equities	1,657	10	12	2,013	13	12
Private equities	402	2	5	403	3	5
Total equities	7,675	45	50	8,177	53	50
Fixed-income securities	8,799	52	49	6,995	45	49
Cash and other	539	3	1	346	2	1
	$ 17,013	100%	100%	$ 15,518	100%	100%

We have assumed an 8.0% compound geometric long-term rate of return on our U.S. Pension Plan assets for 2013, 2012 and 2011. The actual returns during each of the last three fiscal years have exceeded that long-term assumption. The actual historical return on our U.S. Pension Plan assets, calculated on a compound geometric basis, was approximately 7.4%, net of investment manager fees, for the 15-year period ended May 31, 2012 and 7.8%, net of investment manager fees, for the 15-year period ended May 31, 2011. A one-basis-point change in our expected return on plan assets impacts our pension expense by $1.7 million.

Pension expense is also affected by the accounting policy used to determine the value of plan assets at the measurement date. We use a calculated-value method to determine the value of plan assets, which helps mitigate short-term volatility in market performance (both increases and decreases) by amortizing certain actuarial gains or losses over a period no longer than four years. Another method used in practice applies the market value of plan assets at the measurement date. For purposes of valuing plan assets for determining 2013 pension expense, the calculated value method resulted in the same value as the market value.

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FUNDED STATUS. Following is information concerning the funded status of our pension plans as of May 31 (in millions):

	2012	2011
Funded Status of Plans:		
Projected benefit obligation (PBO)	$ 22,187	$ 17,372
Fair value of plan assets	17,334	15,841
Funded status of the plans	$ (4,853)	$ (1,531)
Components of Funded Status by Plans:		
U.S. qualified plans	$ (4,179)	$ (927)
U.S. nonqualified plans	(355)	(339)
International plans	(319)	(265)
Net funded status	$ (4,853)	$ (1,531)
Components of Amounts Included in Balance Sheets:		
Current pension and other benefit obligations	$ (35)	$ (33)
Noncurrent pension and other benefit obligations	(4,818)	(1,498)
Net amount recognized	$ (4,853)	$ (1,531)
Cash Amounts:		
Cash contributions during the year	$ 780	$ 557
Benefit payments during the year	$ 502	$ 468

The amounts recognized in the balance sheet reflect a snapshot of the state of our long-term pension liabilities at the plan measurement date and the effect of year-end accounting on plan assets. At May 31, 2012, we recorded a decrease to equity through OCI of $2.4 billion (net of tax) to reflect unrealized actuarial losses during 2012 related to a decline in the discount rate. Those losses are subject to amortization over future years and may be reflected in future income statements unless they are recovered. At May 31, 2011, we recorded a decrease to equity through OCI of $350 million (net of tax) to reflect unrealized actuarial losses during 2011 related to a decline in the discount rate.

The funding requirements for our U.S. Pension Plans are governed by the Pension Protection Act of 2006, which has aggressive funding requirements in order to avoid benefit payment restrictions that become effective if the funded status determined under Internal Revenue Service rules falls below 80% at the beginning of a plan year. All of our U.S. Pension Plans have funded status levels in excess of 80% and our plans remain adequately funded to provide benefits to our employees as they come due. Additionally, current benefit payments are nominal compared to our total plan assets (benefit payments for our U.S. Pension Plans for 2012 were approximately $465 million or 3% of plan assets).

During 2012, we made $722 million in contributions to our U.S. Pension Plans, including $226 million in voluntary contributions. Over the past several years, we have made voluntary contributions to our U.S. Pension Plans in excess of the minimum required contributions. Amounts contributed in excess of the minimum required result in a credit balance for funding purposes that can be used to meet minimum contribution requirements in future years. For 2013, we anticipate making required contributions to our U.S. Pension Plans totaling approximately $550 million.

Cumulative unrecognized actuarial losses were $8.9 billion through May 31, 2012, compared to $5.4 billion through May 31, 2011. These unrecognized losses reflect changes in the discount rates and differences between expected and actual asset returns, which are being amortized over future periods. These unrecognized losses may be recovered in future periods through actuarial gains. However, unless they are below a corridor amount, these unrecognized actuarial losses are required to be amortized and recognized in future periods. Our pension expense includes amortization of these actuarial losses of $302 million in 2012, $276 million in 2011 and $125 million in 2010.

SELF-INSURANCE ACCRUALS

We are self-insured up to certain limits for costs associated with workers compensation claims, vehicle accidents and general business liabilities, and benefits paid under employee healthcare and long-term disability programs. Our reserves are established for estimates of loss on reported claims, including incurred-but-not-reported claims. Self-insurances accruals reflected in our balance sheet were $1.6 billion at May 31, 2012, and May 31, 2011. Approximately 40% of these accruals were classified as current liabilities.

Our self-insurance accruals are primarily based on the actuarially estimated, undiscounted cost of claims incurred as of the balance sheet date. These estimates include consideration of factors such as severity of claims, frequency of claims and future healthcare costs. Cost trends on material accruals are updated each quarter. We self-insure up to certain limits that vary by operating company and type of risk. Periodically, we evaluate the level of insurance coverage and adjust insurance levels based on risk tolerance and premium expense. Historically, it has been infrequent that incurred claims exceeded our self-insured limits.

We believe the use of actuarial methods to account for these liabilities provides a consistent and effective way to measure these highly judgmental accruals. However, the use of any estimation technique in this area is inherently sensitive given the magnitude of claims involved and the length of time until the ultimate cost is known. We believe our recorded obligations for these expenses are consistently measured on a conservative basis. Nevertheless, changes in healthcare costs, accident frequency and severity, insurance retention levels and other factors can materially affect the estimates for these liabilities.

LONG-LIVED ASSETS

PROPERTY AND EQUIPMENT. Our key businesses are capital intensive, with approximately 58% of our total assets invested in our transportation and information systems infrastructures. We capitalize only those costs that meet the definition of capital assets under accounting standards. Accordingly, repair and maintenance costs that do not extend the useful life of an asset or are not part of the cost of acquiring the asset are expensed as incurred.

The depreciation or amortization of our capital assets over their estimated useful lives, and the determination of any salvage values, requires management to make judgments about future events. Because we utilize many of our capital assets over relatively long periods (the majority of aircraft costs are depreciated over 15 to 30 years), we periodically evaluate whether adjustments to our estimated service lives or salvage values are necessary to ensure these estimates properly match the economic use of the asset. This evaluation may result in changes in the estimated lives and residual values used to depreciate our aircraft and other equipment. In May 2012, we made the decision to shorten the depreciable lives for 54 aircraft and related engines to accelerate the retirement of these aircraft to better align the U.S. domestic air network capacity to match current and anticipated shipment volumes in light of the delivery schedule for replacement aircraft. Due to our decision to accelerate retirement of certain aircraft and related engines, our depreciation expense will increase over the next three years, partially offset from the avoidance of depreciation related to aircraft retirements. (See the Outlook section for additional information). For our aircraft, we typically assign no residual value due to the utilization of these assets in cargo configuration, which results in little to no value at the end of their useful life. These estimates affect the amount of depreciation expense recognized in a period and, ultimately, the gain or loss on the disposal of the asset. Changes in the estimated lives of assets will result in an increase or decrease in the amount of depreciation recognized in future periods and could have a material impact on our results of operations. Historically, gains and losses on disposals of operating equipment have not been material. However, such amounts may differ materially in the future due to changes in business levels, technological obsolescence, accident frequency, regulatory changes and other factors beyond our control.

Because of the lengthy lead times for aircraft manufacture and modifications, we must anticipate volume levels and plan our fleet requirements years in advance, and make commitments for aircraft based on those projections. Furthermore, the timing and availability of certain used aircraft types (particularly those with better fuel efficiency) may create limited opportunities to acquire these aircraft at favorable prices in advance of our capacity needs. These activities create risks that asset capacity may exceed demand and that an impairment of our assets may occur. Aircraft purchases (primarily aircraft in passenger configuration) that have not been placed in service totaled $127 million at May 31, 2012 and $173 million at May 31, 2011. We plan to modify these assets in the future and place them into operations.

The accounting test for whether an asset held for use is impaired involves first comparing the carrying value of the asset with its estimated future undiscounted cash flows. If the cash flows do not exceed the carrying value, the asset must be adjusted to its current fair value. We operate integrated transportation networks and, accordingly, cash flows for most of our operating assets are assessed at a network level, not at an individual asset level for our analysis of impairment. Further, decisions about capital investments are evaluated based on the impact to the overall network rather than the return on an individual asset. We make decisions to remove certain long-lived assets from service based on projections of reduced capacity needs or lower operating costs of newer aircraft types, and those decisions may result in an impairment charge. Assets held for disposal must be adjusted to their estimated fair values less costs to sell when the decision is made to dispose of the asset and certain other criteria are met. The fair value determinations for such aircraft may require management estimates, as there may not be active markets for some of these aircraft. Such estimates are subject to revision from period to period.

During the fourth quarter of 2012, we incurred a noncash impairment charge of $134 million. This charge related to our May 2012 decision to permanently retire 18 Airbus A310-200 aircraft and 26 related engines as well as six Boeing MD10-10 aircraft and 17 related engines to better align the U.S. domestic air network capacity of FedEx Express to match current and anticipated shipment volumes. The majority of these aircraft were temporarily idled and not in revenue service.

In 2011, we incurred asset impairment charges of $29 million related to the combination of our LTL operations at FedEx Freight. There were no material property and equipment impairment charges recognized in 2010.

LEASES. We utilize operating leases to finance certain of our aircraft, facilities and equipment. Such arrangements typically shift the risk of loss on the residual value of the assets at the end of the lease period to the lessor. As disclosed in Contractual Cash Obligations and Note 7 of the accompanying consolidated financial statements, at May 31, 2012 we had approximately $14 billion (on an undiscounted basis) of future commitments for payments under operating leases. The weighted-average remaining lease term of all operating leases outstanding at May 31, 2012 was approximately six years. The future commitments for operating leases are not reflected as a liability in our balance sheet under current U.S. accounting rules.

The determination of whether a lease is accounted for as a capital lease or an operating lease requires management to make estimates primarily about the fair value of the asset and its estimated economic useful life. In addition, our evaluation includes ensuring we properly account for build-to-suit lease arrangements and making judgments about whether various forms of lessee involvement during the construction period make the lessee an agent for the owner-lessor or, in substance, the owner of the asset during the construction period. We believe we have well-defined and controlled processes for making these evaluations, including obtaining third-party appraisals for material transactions to assist us in making these evaluations.

Under a proposed revision to the accounting standards for leases, we would be required to record an asset and a liability for our outstanding operating leases similar to the current accounting for capital leases. Notably, the amount we record in the future would be the net present value of our future lease commitments at the date of adoption. This proposed guidance has not been issued and has been subjected to numerous revisions since the proposal was issued. Accordingly, we cannot make any judgments about the specific impact of the new proposed standard to us. However, our existing financing agreements and the rating agencies that evaluate our credit worthiness already take our operating leases into account.

GOODWILL. As of May 31, 2012, we had $2.4 billion of recorded goodwill from our acquisitions, representing the excess of the purchase price over the fair value of the net assets we have acquired. Several factors give rise to goodwill in our acquisitions, such as the expected benefit from synergies of the combination and the existing workforce of the acquired entity.

In our evaluation of goodwill impairment, we perform a qualitative assessment which requires management judgment and the use of estimates to determine if it is more likely than not that the fair value of a reporting unit is less than its carrying amount. If the qualitative assessment is not conclusive, we would proceed to a two-step process to test goodwill for impairment, including comparing the fair value of each reporting unit with its carrying value (including attributable goodwill). Fair value is estimated using standard valuation methodologies (principally the income or market approach) incorporating market participant considerations and management s assumptions on revenue growth rates, operating margins, discount rates and expected capital expenditures. Estimates used by management can significantly affect the outcome of the impairment test. Changes in forecasted operating results and other assumptions could materially affect these estimates. We perform our annual impairment tests in the fourth quarter unless circumstances indicate the need to accelerate the timing of the test.

Our reporting units with significant recorded goodwill include our FedEx Express, FedEx Freight and FedEx Office (reported in the FedEx Services segment) reporting units. We evaluated these reporting units during the fourth quarters of 2012 and 2011. The estimated fair value of each of these reporting units exceeded their carrying values in 2012 and 2011, and we do not believe that any of these reporting units were at risk as of May 31, 2012. We have recorded goodwill impairment charges associated with our FedEx Office reporting unit in recent years. While the performance of this business has improved, the realization of the value of the remaining attributable goodwill ($351 million) is dependent upon execution of our growth strategies and initiatives in the future.

In connection with our annual impairment testing of goodwill conducted in the fourth quarter of 2010, we recorded a charge of $18 million for impairment of the value of the remaining goodwill at our FedEx National LTL reporting unit. The impairment charge resulted from the significant negative impact of the U.S. recession on the LTL industry, which resulted in volume and yield declines and operating losses. In connection with the combination of our LTL networks in 2011, this unit was merged into the FedEx Freight reporting unit.

CONTINGENCIES

We are subject to various loss contingencies, including tax proceedings and litigation, in connection with our operations. Contingent liabilities are difficult to measure, as their measurement is subject to multiple factors that are not easily predicted or projected. Further, additional complexity in measuring these liabilities arises due to the various jurisdictions in which these matters occur, which makes our ability to predict their outcome highly uncertain. Moreover, different accounting rules must be employed to account for these items based on the nature of the contingency. Accordingly, significant management judgment is required to assess these matters and to make determinations about the measurement of a liability, if any. Our material pending loss contingencies are described in Note 17 of the accompanying consolidated financial statements. In the opinion of management, the aggregate liability, if any, of individual matters or groups of matters not specifically described in Note 17 is not expected to be material to our financial position, results of operations or cash flows. The following describes our methods and associated processes for evaluating these matters.

TAX CONTINGENCIES. We are subject to income and operating tax rules of the U.S., its states and municipalities, and of the foreign jurisdictions in which we operate. Significant judgment is required in determining income tax provisions, as well as deferred tax asset and liability balances and related deferred tax valuation allowances, if necessary, due to the complexity of these rules and their interaction with one another. We account for income taxes by recording both current taxes payable and deferred tax assets and liabilities. Our provision for income taxes is based on domestic and international statutory income tax rates in the jurisdictions in which we operate, applied to taxable income, reduced by applicable tax credits.

Tax contingencies arise from uncertainty in the application of tax rules throughout the many jurisdictions in which we operate and are impacted by several factors, including tax audits, appeals, litigation, changes in tax laws and other rules and their interpretations, and

changes in our business. We regularly assess the potential impact of these factors for the current and prior years to determine the adequacy of our tax provisions. We continually evaluate the likelihood and amount of potential adjustments and adjust our tax positions, including the current and deferred tax liabilities, in the period in which the facts that give rise to a revision become known. In addition, management considers the advice of third parties in making conclusions regarding tax consequences.

We recognize liabilities for uncertain income tax positions based on a two-step process. The first step is to evaluate the tax position for recognition by determining if the weight of available evidence indicates that it is more likely than not that the position will be sustained on audit, including resolution of related appeals or litigation processes, if any. The second step requires us to estimate and measure the tax benefit as the largest amount that is more than 50% likely to be realized upon ultimate settlement. It is inherently difficult and subjective to estimate such amounts, as we must determine the probability of various possible outcomes. We reevaluate these uncertain tax positions on a quarterly basis or when new information becomes available to management. These reevaluations are based on factors including, but not limited to, changes in facts or circumstances, changes in tax law, successfully settled issues under audit and new audit activity. Such a change in recognition or measurement could result in the recognition of a tax benefit or an increase to the related provision.

We classify interest related to income tax liabilities as interest expense, and if applicable, penalties are recognized as a component of income tax expense. The income tax liabilities and accrued interest and penalties that are due within one year of the balance sheet date are presented as current liabilities. The remaining portion of our income tax liabilities and accrued interest and penalties are presented as noncurrent liabilities because payment of cash is not anticipated within one year of the balance sheet date. These noncurrent income tax liabilities are recorded in the caption Other liabilities in the accompanying consolidated balance sheets.

We account for operating taxes based on multi-state, local and foreign taxing jurisdiction rules in those areas in which we operate. Provisions for operating taxes are estimated based upon these rules, asset acquisitions and disposals, historical spend and other variables. These provisions are consistently evaluated for reasonableness against compliance and risk factors.

We measure and record operating tax contingency accruals in accordance with accounting guidance for contingencies. As discussed below, this guidance requires an accrual of estimated loss from a contingency, such as a tax or other legal proceeding or claim, when it is probable that a loss will be incurred and the amount of the loss can be reasonably estimated.

OTHER CONTINGENCIES. Because of the complex environment in which we operate, we are subject to other legal proceedings and claims, including those relating to general commercial matters, employment-related claims and FedEx Ground s owner-operators. Accounting guidance for contingencies requires an accrual of estimated loss from a contingency, such as a tax or other legal proceeding or claim, when it is probable (i.e., the future event or events are likely to occur) that a loss will be incurred and the amount of the loss can be reasonably estimated. This guidance also requires disclosure of a loss contingency matter when, in management s judgment, a material loss is reasonably possible or probable.

During the preparation of our financial statements, we evaluate our contingencies to determine whether it is probable, reasonably possible or remote that a liability has been incurred. A loss is recognized for all contingencies deemed probable and estimable, regardless of amount. For unresolved contingencies with potentially material exposure that are deemed reasonably possible, we evaluate whether a potential loss or range of loss can be reasonably estimated.

Our evaluation of these matters is the result of a comprehensive process designed to ensure that accounting recognition of a loss or disclosure of these contingencies is made in a timely manner and involves our legal and accounting personnel, as well as external counsel where applicable. The process includes regular communications during each quarter and scheduled meetings shortly before the completion of our financial statements to evaluate any new legal proceedings and the status of any existing matters.

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In determining whether a loss should be accrued or a loss contingency disclosed, we evaluate, among other factors:

- the current status of each matter within the scope and context of the entire lawsuit (i.e., the lengthy and complex nature of class-action matters);
- the procedural status of each lawsuit;
- any opportunities to dispose of the lawsuit on its merits before trial (i.e., motion to dismiss or for summary judgment);
- the amount of time remaining before the trial date;
- the status of discovery;
- the status of settlement, arbitration or mediation proceedings, and;
- our judgment regarding the likelihood of success prior to or at trial.

In reaching our conclusions with respect to accrual of a loss or loss contingency disclosure, we take a holistic view of each matter based on these factors and the information available prior to the issuance of our financial statements. Uncertainty with respect to an individual factor or combination of these factors may impact our decisions related to accrual or disclosure of a loss contingency, including a conclusion that we are unable to establish an estimate of possible loss or a meaningful range of possible loss. We update our disclosures to reflect our most current understanding of the contingencies at the time we issue our financial statements. However, events may arise that were not anticipated and the outcome of a contingency may result in a loss to us that differs materially from our previously estimated liability or range of possible loss.

Despite the inherent complexity in the accounting and disclosure of contingencies, we believe that our processes are robust and thorough and provide a consistent framework for management in evaluating the potential outcome of contingencies for proper accounting recognition and disclosure.

RISK FACTORS

Our financial and operating results are subject to many risks and uncertainties, as described below.

We are directly affected by the state of the economy. While macro-economic risks apply to most companies, we are particularly vulnerable. The transportation industry is highly cyclical and especially susceptible to trends in economic activity, such as the recent global recession. Our primary business is to transport goods, so our business levels are directly tied to the purchase and production of goods key macro-economic measurements. When individuals and companies purchase and produce fewer goods, we transport fewer goods. In addition, we have a relatively high fixed-cost structure, which is difficult to quickly adjust to match shifting volume levels. Moreover, as we continue to grow our international business, we are increasingly affected by the health of the global economy. In 2012, global economic conditions resulted in decreased demand for our U.S. domestic and International Priority package services at FedEx Express, as customers utilized lower priced deferred services.

Our businesses depend on our strong reputation and the value of the FedEx brand. The FedEx brand name symbolizes high-quality service, reliability and speed. FedEx is one of the most widely recognized, trusted and respected brands in the world, and the FedEx brand is one of our most important and valuable assets. In addition, we have a strong reputation among customers and the general public for high standards of social and environmental responsibility and corporate governance and ethics. The FedEx brand name and our corporate reputation are powerful sales and marketing tools, and we devote significant resources to promoting and protecting them. Adverse publicity (whether or not justified) relating to activities by our employees, contractors or agents, such as customer service mishaps or noncompliance with anti-corruption laws, could tarnish our reputation and reduce the value of our brand. With the increase in the use of social media outlets such as YouTube and Twitter,

adverse publicity can be disseminated quickly and broadly, making it increasingly difficult for us to defend against. Damage to our reputation and loss of brand equity could reduce demand for our services and thus have an adverse effect on our financial condition, liquidity and results of operations, as well as require additional resources to rebuild our reputation and restore the value of our brand.

We rely heavily on information and technology to operate our transportation and business networks, and any disruption to our technology infrastructure or the Internet could harm our operations and our reputation among customers. Our ability to attract and retain customers and to compete effectively depends in part upon the sophistication and reliability of our technology network, including our ability to provide features of service that are important to our customers. External and internal risks, such as malware, code anomalies, Acts of God, attempts to penetrate our networks, data leakage and human error, pose a direct threat to our products, services and data. Any disruption to the Internet or our complex, global technology infrastructure, including those impacting our computer systems and customer Web sites, could adversely impact our customer service, volumes, and revenues and result in increased costs. These types of adverse impacts could also occur in the event the confidentiality, integrity, or availability of company and customer information was compromised due to a data loss by FedEx or a trusted third party. While we have invested and continue to invest in technology security initiatives, information technology risk management and disaster recovery plans, these measures cannot fully insulate us from technology disruptions or data loss and the resulting adverse effect on our operations and financial results.

Our transportation businesses may be impacted by the price and availability of fuel. We must purchase large quantities of fuel to operate our aircraft and vehicles, and the price and availability of fuel can be unpredictable and beyond our control. To date, we have been mostly successful in mitigating over time the expense impact of higher fuel costs through our indexed fuel surcharges, as the amount of the surcharges is closely linked to the market prices for fuel. If we are unable to maintain or increase our fuel surcharges because of competitive pricing pressures or some other reason, fuel costs could adversely impact our operating results. Even if we are able to offset the cost of fuel with our surcharges, high fuel surcharges could move our customers, especially in the U.S. domestic market, away from our higher-yielding express services to our lower-yielding ground services or even reduce customer demand for our services altogether. In addition, disruptions in the supply of fuel could have a negative impact on our ability to operate our transportation networks.

Our businesses are capital intensive, and we must make capital decisions based upon projected volume levels. We make significant investments in aircraft, vehicles, technology, package handling facilities, sort equipment, copy equipment and other assets to support our transportation and business networks. We also make significant investments to rebrand, integrate and grow the companies that we acquire. The amount and timing of capital investments depend on various factors, including our anticipated volume growth. We must make commitments to purchase or modify aircraft years before the aircraft are actually needed. We must predict volume levels and fleet requirements and make commitments for aircraft based on those projections. Missing our projections could result in too much or too little capacity relative to our shipping volumes. Overcapacity could lead to asset dispositions or write-downs and undercapacity could negatively impact service levels. For example, in the fourth quarter of 2012, in order to better align the U.S. domestic air network capacity of FedEx Express to match current and anticipated shipment volumes, we made a decision to retire from service certain aircraft and certain excess aircraft engines and thus recorded a noncash impairment charge of $134 million. We are also developing operating and cost structure plans to further improve our efficiency at FedEx Express.

We face intense competition. The transportation and business services markets are both highly competitive and sensitive to price and service, especially in periods of little or no macro-economic growth. Some of our competitors have more financial resources than we do, or they are controlled or subsidized by foreign governments, which enables them to raise capital more easily. We believe we compete effectively with these companies for example, by providing more reliable service at compensatory prices. However, an irrational pricing environment can limit our ability not only to maintain or increase our prices (including our fuel surcharges in response to rising fuel costs), but also to maintain or grow our market share. In addition, high volume package shippers could develop in-house ground delivery capabilities, which would in turn reduce our revenues and market share. While we believe we compete effectively through our current service offerings, if our current competitors or potential future competitors offer a broader range of services or more effectively bundle their services or our current customers become competitors, it could impede our ability to maintain or grow our market share.

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If we do not effectively operate, integrate, leverage and grow acquired businesses, our financial results and reputation may suffer. Our strategy for long-term growth, productivity and profitability depends in part on our ability to make prudent strategic acquisitions and to realize the benefits we expect when we make those acquisitions. In furtherance of this strategy, we recently made strategic acquisitions in Mexico, Poland, France and Brazil. While we expect our past and future acquisitions to enhance our value proposition to customers and improve our long-term profitability, there can be no assurance that we will realize our expectations within the time frame we have established, if at all, or that we can continue to support the value we allocate to these acquired businesses, including their goodwill or other intangible assets.

Labor organizations attempt to organize groups of our employees from time to time, and potential changes in labor laws could make it easier for them to do so. If we are unable to continue to maintain good relationships with our employees and prevent labor organizations from organizing groups of our employees, our operating costs could significantly increase and our operational flexibility could be significantly reduced. Despite continual organizing attempts by labor unions, other than the pilots of FedEx Express, all of our U.S. employees have thus far chosen not to unionize. The U.S. Congress has, in the past, considered adopting changes in labor laws, however, that would make it easier for unions to organize units of our employees. For example, there is always a possibility that Congress could remove most FedEx Express employees from the purview of the RLA. For additional discussion of the RLA, see Part I, Item 1 of this Annual Report under the caption Regulation. Such legislation could expose our customers to the type of service disruptions that the RLA was designed to prevent local work stoppages in key areas that interrupt the timely flow of shipments of time-sensitive, high-value goods throughout our global network. Such disruptions could threaten our ability to provide competitively priced shipping options and ready access to global markets. There is also the possibility that Congress could pass other labor legislation that could adversely affect our companies, such as FedEx Ground and FedEx Freight, whose employees are governed by the National Labor Relations Act of 1935, as amended (the NLRA). In addition, federal and state governmental agencies, such as the National Labor Relations Board, have and may continue to take actions that could make it easier for our employees to organize under the RLA or NLRA. Finally, changes to federal or state laws governing employee classification could impact the status of FedEx Ground s owner-operators as independent contractors.

FedEx Ground relies on owner-operators to conduct its linehaul and pickup-and-delivery operations, and the status of these owner-operators as independent contractors, rather than employees, is being challenged. FedEx Ground s use of independent contractors is well suited to the needs of the ground delivery business and its customers, as evidenced by the strong growth of this business segment. We are involved in numerous lawsuits and state tax and other administrative proceedings that claim that the company s owner-operators or their drivers should be treated as our employees, rather than independent contractors. We incur certain costs, including legal fees, in defending the status of FedEx Ground s owner-operators as independent contractors. We believe that FedEx Ground s owner-operators are properly classified as independent contractors and that FedEx Ground is not an employer of the drivers of the company s independent contractors. However, adverse determinations in these matters could, among other things, entitle certain of our contractors and their drivers to the reimbursement of certain expenses and to the benefit of wage-and-hour laws and result in employment and withholding tax and benefit liability for FedEx Ground, and could result in changes to the independent contractor status of FedEx Ground s owner-operators. If FedEx Ground is compelled to convert its independent contractors to employees, labor organizations could more easily organize these individuals, our operating costs could increase materially and we could incur significant capital outlays.

The transportation infrastructure continues to be a target of terrorist activities. Because transportation assets continue to be a target of terrorist activities, governments around the world are adopting or are considering adopting stricter security requirements that will increase operating costs and potentially slow service for businesses, including those in the transportation industry. For example, the U.S. Transportation Security Administration continues to require FedEx Express to comply with a Full All-Cargo Aircraft Operator Standard Security Plan, which contains evolving and strict security requirements. These requirements are not static, but change periodically as the result of regulatory and legislative requirements, imposing additional security costs and creating a level of uncertainty for our operations. Thus, it is reasonably possible that these rules or other future security requirements could impose material costs on us. Moreover, a terrorist attack directed at FedEx or other aspects of the transportation infrastructure could disrupt our operations and adversely impact demand for our services.

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Increased pilot safety requirements could impose substantial costs on us. The FAA, in September 2010, proposed rules that would significantly reduce the maximum number of hours on duty and increase the minimum amount of rest time for our pilots, and thus require us to hire additional pilots and modify certain of our aircraft. When the FAA issued final regulations in December 2011, all-cargo carriers, including FedEx Express, were exempt from these new pilot fatigue requirements, and instead required to continue complying with previously enacted flight and duty time rules. In May 2012, however, the FAA indicated that it would reconsider the exclusion of cargo pilots from these new pilot fatigue requirements. Thus, it is reasonably possible that these rules or other future flight safety requirements could impose material costs on us.

The regulatory environment for global aviation or other transportation rights may impact our operations. Our extensive air network is critical to our success. Our right to serve foreign points is subject to the approval of the Department of Transportation and generally requires a bilateral agreement between the United States and foreign governments. In addition, we must obtain the permission of foreign governments to provide specific flights and services. Our operations outside of the United States, such as FedEx Express s growing international domestic operations, are also subject to current and potential regulations, including certain postal regulations and licensing requirements, that restrict, make difficult and sometimes prohibit, the ability of foreign-owned companies such as FedEx Express to compete effectively in parts of the international domestic transportation and logistics market. Regulatory actions affecting global aviation or transportation rights or a failure to obtain or maintain aviation or other transportation rights in important international markets could impair our ability to operate our networks.

We may be affected by global climate change or by legal, regulatory or market responses to such change. Concern over climate change, including the impact of global warming, has led to significant U.S. and international legislative and regulatory efforts to limit greenhouse gas (GHG) emissions, including our aircraft and diesel engine emissions. For example, during 2009, the European Commission approved the extension of the European Union Emissions Trading Scheme (ETS) for GHG emissions, to the airline industry. Under this decision, all FedEx Express flights to and from any airport in any member state of the European Union are now covered by the ETS requirements, and each year we are required to submit emission allowances in an amount equal to the carbon dioxide emissions from such flights. In addition, the U.S. Congress has, in the past, considered bills that would regulate GHG emissions, and some form of federal climate change legislation is possible in the future. Increased regulation regarding GHG emissions, especially aircraft or diesel engine emissions, could impose substantial costs on us, especially at FedEx Express. These costs include an increase in the cost of the fuel and other energy we purchase and capital costs associated with updating or replacing our aircraft or vehicles prematurely. Until the timing, scope and extent of such regulation becomes known, we cannot predict its effect on our cost structure or our operating results. It is reasonably possible, however, that it could impose material costs on us. Moreover, even without such regulation, increased awareness and any adverse publicity in the global marketplace about the GHGs emitted by companies in the airline and transportation industries could harm our reputation and reduce customer demand for our services, especially our air express services. Finally, given the broad and global scope of our operations and our susceptibility to global macro-economic trends, we are particularly vulnerable to the physical risks of climate change that could affect all of humankind, such as shifts in weather patterns and world ecosystems.

A localized disaster in a key geography could adversely impact our business. While we operate several integrated networks with assets distributed throughout the world, there are concentrations of key assets within our networks that are exposed to localized risks from natural or manmade disasters such as tornados, floods, earthquakes or terrorist attacks. The loss of a key location such as our Memphis super hub or one of our information technology centers could cause a significant disruption to our operations and cause us to incur significant costs to reestablish or relocate these functions. Moreover, resulting economic dislocations, including supply chain and fuel disruptions, could adversely impact demand for our services.

Our business may be adversely impacted by disruptions or modifications in service by the USPS. The USPS is a significant customer and vendor of FedEx, and thus, disruptions or modifications in services by the USPS as a consequence of the USPS s current financial difficulties or any resulting structural changes to its operations, network, service offerings or pricing could have an

adverse effect on our operations and financial results. For instance, because FedEx SmartPost uses the USPS for final delivery to residences, any changes in USPS services (such as the cessation of Saturday delivery) could impact the terms and cost of our FedEx SmartPost service.

In addition, the USPS has informed us that it intends to solicit proposals for the provision of air transportation services currently provided by FedEx Express upon the expiration of the current agreement in September 2013. Accordingly, upon the expiration of the current agreement, the transportation services we provide to the USPS could be transitioned, in whole or in part, to another provider. This would have a negative impact on our asset utilization and profitability. Moreover, to the extent that any such services are retained by us, the terms and conditions of the new arrangement may be less favorable than those currently in place.

We are also subject to other risks and uncertainties that affect many other businesses, including:

increasing costs, the volatility of costs and funding requirements and other legal mandates for employee benefits, especially pension and healthcare benefits;

the increasing costs of compliance with federal and state governmental agency mandates and defending against inappropriate or unjustified enforcement or other actions by such agencies;

the impact of any international conflicts on the United States and global economies in general, the transportation industry or us in particular, and what effects these events will have on our costs or the demand for our services;

any impacts on our businesses resulting from new domestic or international government laws and regulation;

changes in foreign currency exchange rates, especially in the British pound, Canadian dollar, Chinese yuan, euro, Hong Kong dollar and Japanese yen, which can affect our sales levels and foreign currency sales prices;

market acceptance of our new service and growth initiatives;

any liability resulting from and the costs of defending against class-action litigation, such as wage-and-hour and discrimination and retaliation claims, and any other legal or governmental proceedings;

the outcome of future negotiations to reach new collective bargaining agreements including with the union that represents the pilots of FedEx Express (the current pilot contract is scheduled to become amendable in March 2013);

the impact of technology developments on our operations and on demand for our services, and our ability to continue to identify and eliminate unnecessary information technology redundancy and complexity throughout the organization;

widespread outbreak of an illness or any other communicable disease, or any other public health crisis; and

availability of financing on terms acceptable to us and our ability to maintain our current credit ratings, especially given the capital intensity of our operations.

FORWARD-LOOKING STATEMENTS

Certain statements in this report, including (but not limited to) those contained in Outlook (including segment outlooks), Liquidity, Capital Resources, Liquidity Outlook, Contractual Cash Obligations and Critical Accounting Estimates, and the Retirement Plans and Contingencies notes to the consolidated financial statements, are forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995 with respect to our financial condition, results of operations, cash flows, plans, objectives, future performance and business. Forward-looking statements include those preceded by, followed by or that

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include the words may, could, would, should, believes, expects, anticipates, plans, estimates, targets, projects, intends o These forward-looking statements involve risks and uncertainties. Actual results may differ materially from those contemplated (expressed or implied) by such forward-looking statements, because of, among other things, the risk factors identified above and the other risks and uncertainties you can find in our press releases and other SEC filings.

As a result of these and other factors, no assurance can be given as to our future results and achievements. Accordingly, a forward-looking statement is neither a prediction nor a guarantee of future events or circumstances and those future events or circumstances may not occur. You should not place undue reliance on the forward-looking statements, which speak only as of the date of this report. We are under no obligation, and we expressly disclaim any obligation, to update or alter any forward-looking statements, whether as a result of new information, future events or otherwise.

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MANAGEMENT S REPORT ON INTERNAL

CONTROL OVER FINANCIAL REPORTING

Our management is responsible for establishing and maintaining adequate internal control over financial reporting (as defined in Rules 13a-15(f) and 15d-15(f) under the Securities Exchange Act of 1934, as amended). Our internal control over financial reporting includes, among other things, defined policies and procedures for conducting and governing our business, sophisticated information systems for processing transactions and a properly staffed, professional internal audit department. Mechanisms are in place to monitor the effectiveness of our internal control over financial reporting and actions are taken to correct all identified deficiencies. Our procedures for financial reporting include the active involvement of senior management, our Audit Committee and our staff of highly qualified financial and legal professionals.

Management, with the participation of our principal executive and financial officers, assessed our internal control over financial reporting as of May 31, 2012, the end of our fiscal year. Management based its assessment on criteria established in Internal Control Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (the COSO criteria).

Based on this assessment, management has concluded that our internal control over financial reporting was effective as of May 31, 2012.

The effectiveness of our internal control over financial reporting as of May 31, 2012, has been audited by Ernst & Young LLP, the independent registered public accounting firm who also audited the Company s consolidated financial statements included in this Annual Report on Form 10-K. Ernst & Young LLP s report on the Company s internal control over financial reporting is included in this Annual Report on Form 10-K.

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REPORT OF INDEPENDENT REGISTERED

PUBLIC ACCOUNTING FIRM

The Board of Directors and Stockholders

FedEx Corporation

We have audited FedEx Corporation s internal control over financial reporting as of May 31, 2012, based on criteria established in Internal Control Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (the COSO criteria). FedEx Corporation s management is responsible for maintaining effective internal control over financial reporting, and for its assessment of the effectiveness of internal control over financial reporting included in the accompanying Management s Report on Internal Control over Financial Reporting. Our responsibility is to express an opinion on the company s internal control over financial reporting based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, testing and evaluating the design and operating effectiveness of internal control based on the assessed risk, and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

A company s internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company s internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company s assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, FedEx Corporation maintained, in all material respects, effective internal control over financial reporting as of May 31, 2012, based on the COSO criteria.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheets of FedEx Corporation as of May 31, 2012 and 2011, and the related consolidated statements of income, changes in stockholders investment and comprehensive income (loss), and cash flows for each of the three years in the period ended May 31, 2012 of FedEx Corporation and our report dated July 16, 2012 expressed an unqualified opinion thereon.

/s/ Ernst & Young LLP

Memphis, Tennessee

July 16, 2012

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REPORT OF INDEPENDENT REGISTERED

PUBLIC ACCOUNTING FIRM

The Board of Directors and Stockholders

FedEx Corporation

We have audited the accompanying consolidated balance sheets of FedEx Corporation as of May 31, 2012 and 2011, and the related consolidated statements of income, changes in stockholders investment and comprehensive income (loss), and cash flows for each of the three years in the period ended May 31, 2012. These financial statements are the responsibility of the Company s management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of FedEx Corporation at May 31, 2012 and 2011, and the consolidated results of its operations and its cash flows for each of the three years in the period ended May 31, 2012, in conformity with U.S. generally accepted accounting principles.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), FedEx Corporation s internal control over financial reporting as of May 31, 2012, based on criteria established in Internal Control-Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission and our report dated July 16, 2012 expressed an unqualified opinion thereon.

/s/ Ernst & Young LLP

Memphis, Tennessee

July 16, 2012

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FEDEX CORPORATION

CONSOLIDATED BALANCE SHEETS

(IN MILLIONS)

	May 31, 2012	May 31, 2011
ASSETS		
CURRENT ASSETS		
Cash and cash equivalents	$ 2,843	$ 2,328
Receivables, less allowances of $178 and $182	4,704	4,581
Spare parts, supplies and fuel, less allowances of $184 and $169	440	437
Deferred income taxes	533	610
Prepaid expenses and other	536	329
Total current assets	9,056	8,285
PROPERTY AND EQUIPMENT, AT COST		
Aircraft and related equipment	14,360	13,146
Package handling and ground support equipment	5,912	5,591
Computer and electronic equipment	4,646	4,408
Vehicles	3,654	3,294
Facilities and other	7,592	7,247
	36,164	33,686
Less accumulated depreciation and amortization	18,916	18,143
Net property and equipment	17,248	15,543
OTHER LONG-TERM ASSETS		
Goodwill	2,387	2,326
Other assets	1,212	1,231
Total other long-term assets	3,599	3,557
	$ 29,903	$ 27,385

The accompanying notes are an integral part of these consolidated financial statements.

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FEDEX CORPORATION

CONSOLIDATED BALANCE SHEETS

(IN MILLIONS, EXCEPT SHARE DATA)

	May 31,	
	2012	2011
LIABILITIES AND STOCKHOLDERS INVESTMENT		
CURRENT LIABILITIES		
Current portion of long-term debt	$ 417	$ 18
Accrued salaries and employee benefits	1,635	1,268
Accounts payable	1,613	1,702
Accrued expenses	1,709	1,894
Total current liabilities	5,374	4,882
LONG-TERM DEBT, LESS CURRENT PORTION	1,250	1,667
OTHER LONG-TERM LIABILITIES		
Deferred income taxes	836	1,336
Pension, postretirement healthcare and other benefit obligations	5,582	2,124
Self-insurance accruals	963	977
Deferred lease obligations	784	779
Deferred gains, principally related to aircraft transactions	251	246
Other liabilities	136	154
Total other long-term liabilities	8,552	5,616
COMMITMENTS AND CONTINGENCIES		
COMMON STOCKHOLDERS INVESTMENT		
Common stock, $0.10 par value; 800 million shares authorized; 317 million shares issued as of May 31, 2012 and May 31, 2011	32	32
Additional paid-in capital	2,595	2,484
Retained earnings	17,134	15,266
Accumulated other comprehensive loss	(4,953)	(2,550)
Treasury stock, at cost	(81)	(12)
Total common stockholders investment	14,727	15,220
	$ 29,903	$ 27,385

The accompanying notes are an integral part of these consolidated financial statements.

FEDEX CORPORATION

CONSOLIDATED STATEMENTS OF INCOME

(IN MILLIONS, EXCEPT PER SHARE AMOUNTS)

	Years ended May 31,		
	2012	2011	2010
REVENUES	$ 42,680	$ 39,304	$ 34,734
OPERATING EXPENSES:			
Salaries and employee benefits	16,099	15,276	14,027
Purchased transportation	6,335	5,674	4,728
Rentals and landing fees	2,487	2,462	2,359
Depreciation and amortization	2,113	1,973	1,958
Fuel	4,956	4,151	3,106
Maintenance and repairs	1,980	1,979	1,715
Impairment and other charges	134	89	18
Other	5,390	5,322	4,825
	39,494	36,926	32,736
OPERATING INCOME	3,186	2,378	1,998
OTHER INCOME (EXPENSE):			
Interest expense	(52)	(86)	(79)
Interest income	13	9	8
Other, net	(6)	(36)	(33)
	(45)	(113)	(104)
INCOME BEFORE INCOME TAXES	3,141	2,265	1,894
PROVISION FOR INCOME TAXES	1,109	813	710
NET INCOME	$ 2,032	$ 1,452	$ 1,184
BASIC EARNINGS PER COMMON SHARE	$ 6.44	$ 4.61	$ 3.78
DILUTED EARNINGS PER COMMON SHARE	$ 6.41	$ 4.57	$ 3.76

The accompanying notes are an integral part of these consolidated financial statements.

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FEDEX CORPORATION

CONSOLIDATED STATEMENTS OF CASH FLOWS

(IN MILLIONS)

	Years ended May 31,		
	2012	2011	2010
OPERATING ACTIVITIES			
Net income	$ 2,032	$ 1,452	$ 1,184
Adjustments to reconcile net income to cash provided by operating activities:			
Depreciation and amortization	2,113	1,973	1,958
Provision for uncollectible accounts	160	152	124
Deferred income taxes and other noncash items	1,126	669	331
Impairment and other charges	134	29	18
Stock-based compensation	105	98	101
Changes in assets and liabilities:			
Receivables	(254)	(400)	(906)
Other current assets	(231)	(114)	276
Pension assets and liabilities, net	(453)	(169)	(611)
Accounts payable and other liabilities	144	370	710
Other, net	(41)	(19)	(47)
Cash provided by operating activities	4,835	4,041	3,138
INVESTING ACTIVITIES			
Capital expenditures	(4,007)	(3,434)	(2,816)
Business acquisitions, net of cash acquired	(116)	(96)	
Proceeds from asset dispositions and other	74	111	35
Cash used in investing activities	(4,049)	(3,419)	(2,781)
FINANCING ACTIVITIES			
Principal payments on debt	(29)	(262)	(653)
Proceeds from stock issuances	128	108	94
Excess tax benefit on the exercise of stock options	18	23	25
Dividends paid	(164)	(151)	(138)
Purchase of treasury stock	(197)		
Other, net		(5)	(20)
Cash used in financing activities	(244)	(287)	(692)
Effect of exchange rate changes on cash	(27)	41	(5)
Net increase (decrease) in cash and cash equivalents	515	376	(340)
Cash and cash equivalents at beginning of period	2,328	1,952	2,292
Cash and cash equivalents at end of period	$ 2,843	$ 2,328	$ 1,952

The accompanying notes are an integral part of these consolidated financial statements.

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FEDEX CORPORATION

CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS

INVESTMENT AND COMPREHENSIVE INCOME (LOSS)

(IN MILLIONS, EXCEPT SHARE DATA)

	Common Stock	Additional Paid-in Capital	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Treasury Stock	Total
Balance at May 31, 2009	**$ 31**	**$ 2,053**	**$ 12,919**	**$ (1,373)**	**$ (4)**	**$ 13,626**
Net income			1,184			1,184
Foreign currency translation adjustment, net of tax of $2				(25)		(25)
Retirement plans adjustments, net of tax of $617				(1,042)		(1,042)
Total comprehensive income						117
Purchase of treasury stock					(3)	(3)
Cash dividends declared ($0.44 per share)			(137)			(137)
Employee incentive plans and other (2,375,753 shares issued)		208				208
Balance at May 31, 2010	**31**	**2,261**	**13,966**	**(2,440)**	**(7)**	**13,811**
Net income			1,452			1,452
Foreign currency translation adjustment, net of tax of $27				125		125
Retirement plans adjustments, net of tax of $141				(235)		(235)
Total comprehensive income						1,342
Purchase of treasury stock					(5)	(5)
Cash dividends declared ($0.48 per share)			(152)			(152)
Employee incentive plans and other (2,229,051 shares issued)	1	223				224
Balance at May 31, 2011	**32**	**2,484**	**15,266**	**(2,550)**	**(12)**	**15,220**
Net income			2,032			2,032
Foreign currency translation adjustment, net of tax of $26				(95)		(95)
Retirement plans adjustments, net of tax of $1,369				(2,308)		(2,308)
Total comprehensive loss						(371)
Purchase of treasury stock					(197)	(197)
Cash dividends declared ($0.52 per share)			(164)			(164)
Employee incentive plans and other (2,359,659 shares issued)		111			128	239

Balance at May 31, 2012	**$**	**32**	**$**	**2,595**	**$ 17,134**	**$**	**(4,953)**	**$**	**(81)**	**$ 14,727**

The accompanying notes are an integral part of these consolidated financial statements.

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FEDEX CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 1: DESCRIPTION OF BUSINESS AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

DESCRIPTION OF BUSINESS. FedEx Corporation (FedEx) provides a broad portfolio of transportation, e-commerce and business services through companies competing collectively, operating independently and managed collaboratively, under the respected FedEx brand. Our primary operating companies are Federal Express Corporation (FedEx Express), the world s largest express transportation company; FedEx Ground Package System, Inc. (FedEx Ground), a leading North American provider of small-package ground delivery services; and FedEx Freight, Inc. (FedEx Freight), a leading North American provider of less-than-truckload (LTL) freight services. These companies represent our major service lines and, along with FedEx Corporate Services, Inc. (FedEx Services), form the core of our reportable segments. Our FedEx Services segment provides sales, marketing, information technology, communications and back-office support to our transportation segments. In addition, the FedEx Services segment provides customers with retail access to FedEx Express and FedEx Ground shipping services through FedEx Office and Print Services, Inc. (FedEx Office) and provides customer service, technical support and billing and collection services through FedEx TechConnect, Inc. (FedEx TechConnect).

FISCAL YEARS. Except as otherwise specified, references to years indicate our fiscal year ended May 31, 2012 or ended May 31 of the year referenced.

PRINCIPLES OF CONSOLIDATION. The consolidated financial statements include the accounts of FedEx and its subsidiaries, substantially all of which are wholly owned. All significant intercompany accounts and transactions have been eliminated in consolidation.

REVENUE RECOGNITION. We recognize revenue upon delivery of shipments for our transportation businesses and upon completion of services for our business services, logistics and trade services businesses. Transportation services are provided with the use of employees and independent contractors. FedEx is the principal to the transaction for these services and revenue from these transactions is recognized on a gross basis (with the exception of FedEx SmartPost as described below). Costs associated with independent contractor settlements are recognized as incurred and included in the caption Purchased transportation in the accompanying consolidated statements of income. For shipments in transit, revenue is recorded based on the percentage of service completed at the balance sheet date. Estimates for future billing adjustments to revenue and accounts receivable are recognized at the time of shipment for money-back service guarantees and billing corrections. Delivery costs are accrued as incurred.

Our contract logistics, global trade services and certain transportation businesses, such as FedEx SmartPost, engage in some transactions wherein they act as agents. Revenue from these transactions is recorded on a net basis. Net revenue includes billings to customers less third-party charges, including transportation or handling costs, fees, commissions, and taxes and duties.

Certain of our revenue-producing transactions are subject to taxes, such as sales tax, assessed by governmental authorities. We present these revenues net of tax.

CREDIT RISK. We routinely grant credit to many of our customers for transportation and business services without collateral. The risk of credit loss in our trade receivables is substantially mitigated by our credit evaluation process, short collection terms and sales to a large number of customers, as well as the low revenue per transaction for most of our services. Allowances for potential credit losses are determined based on historical experience and the impact of current economic factors on the composition of accounts receivable. Historically, credit losses have been within management s expectations.

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ADVERTISING. Advertising and promotion costs are expensed as incurred and are classified in other operating expenses. Advertising and promotion expenses were $421 million in 2012, $375 million in 2011 and $374 million in 2010.

CASH EQUIVALENTS. Cash in excess of current operating requirements is invested in short-term, interest-bearing instruments with maturities of three months or less at the date of purchase and is stated at cost, which approximates market value.

SPARE PARTS, SUPPLIES AND FUEL. Spare parts (principally aircraft-related) are reported at weighted-average cost. Allowances for obsolescence are provided for spare parts expected to be on hand at the date the aircraft are retired from service. These allowances are provided over the estimated useful life of the related aircraft and engines. Additionally, allowances for obsolescence are provided for spare parts currently identified as excess or obsolete. These allowances are based on management estimates, which are subject to change. Supplies and fuel are reported at weighted average cost.

PROPERTY AND EQUIPMENT. Expenditures for major additions, improvements and flight equipment modifications are capitalized when such costs are determined to extend the useful life of the asset or are part of the cost of acquiring the asset. Expenditures for equipment overhaul costs of engines or airframes prior to their operational use are capitalized as part of the cost of such assets as they are costs required to ready the asset for its intended use. Maintenance and repairs are charged to expense as incurred. We capitalize certain direct internal and external costs associated with the development of internal-use software. Gains and losses on sales of property used in operations are classified within operating expenses.

For financial reporting purposes, we record depreciation and amortization of property and equipment on a straight-line basis over the asset s service life or related lease term, if shorter. For income tax purposes, depreciation is computed using accelerated methods when applicable. The depreciable lives and net book value of our property and equipment are as follows (dollars in millions):

		Net Book Value at May 31,	
	Range	2012	2011
Wide-body aircraft and related equipment	15 to 30 years	$ 7,161	$ 6,536
Narrow-body and feeder aircraft and related equipment	5 to 18 years	1,881	1,517
Package handling and ground support equipment	3 to 30 years	2,101	1,985
Vehicles	3 to 15 years	1,411	1,076
Computer and electronic equipment	2 to 10 years	930	776
Facilities and other	2 to 40 years	3,764	3,653

Substantially all property and equipment have no material residual values. The majority of aircraft costs are depreciated on a straight-line basis over 15 to 30 years. We periodically evaluate the estimated service lives and residual values used to depreciate our property and equipment. This evaluation may result in changes in the estimated lives and residual values as it did in 2012 with certain aircraft. Such changes did not materially affect depreciation expense in any period presented; however, changes to the estimated lives of certain aircraft will impact 2013 depreciation expense. In May 2012, FedEx Express made the decision to accelerate the retirement of 54 aircraft and related engines to better align with the delivery schedule for replacement aircraft, and we expect an additional $69 million in accelerated depreciation expense in 2013, with a partial offset from the avoidance of depreciation related to the aircraft retirements (described in the Impairment of Long-Lived Assets section below).

Depreciation expense, excluding gains and losses on sales of property and equipment used in operations, was $2.1 billion in 2012 and $1.9 billion in 2011 and 2010. Depreciation and amortization expense includes amortization of assets under capital lease.

CAPITALIZED INTEREST. Interest on funds used to finance the acquisition and modification of aircraft, including purchase deposits, construction of certain facilities, and development of certain software up to the date the asset is ready for its intended use is capitalized and included in the cost of the asset if the asset is actively under construction. Capitalized interest was $85 million in 2012, $71 million in 2011 and $80 million in 2010.

IMPAIRMENT OF LONG-LIVED ASSETS. Long-lived assets are reviewed for impairment when circumstances indicate the carrying value of an asset may not be recoverable. For assets that are to be held and used, an impairment is recognized when the estimated undiscounted cash flows associated with the asset or group of assets is less than their carrying value. If impairment exists, an adjustment is made to write the asset down to its fair value, and a loss is recorded as the difference between the carrying value and fair value. Fair values are determined based on quoted market values, discounted cash flows or internal and external appraisals, as applicable. Assets to be disposed of are carried at the lower of carrying value or estimated net realizable value.

We operate integrated transportation networks, and accordingly, cash flows for most of our operating assets are assessed at a network level, not at an individual asset level, for our analysis of impairment.

In May 2012, we made the decision to retire from service 18 Airbus A310-200 aircraft and 26 related engines, as well as six Boeing MD10-10 aircraft and 17 related engines. As a consequence of this decision, a noncash impairment charge of $134 million ($84 million, net of tax, or $0.26 per diluted share) was recorded in the fourth quarter. The decision to retire these aircraft, the majority of which were temporarily idled and not in revenue service, will better align the U.S. domestic air network capacity of FedEx Express to match current and anticipated shipment volumes.

In 2011, we incurred asset impairment charges of $29 million related to the combination of our LTL operations at FedEx Freight (see FedEx Freight Network Combination below for additional information). There were no material property and equipment impairment charges recognized in 2010.

GOODWILL. Goodwill is recognized for the excess of the purchase price over the fair value of tangible and identifiable intangible net assets of businesses acquired. Several factors give rise to goodwill in our acquisitions, such as the expected benefit from synergies of the combination and the existing workforce of the acquired entity. Goodwill is reviewed at least annually for impairment. In our evaluation of goodwill impairment, we perform a qualitative assessment to determine if it is more likely than not that the fair value of a reporting unit is less than its carrying amount. If the qualitative assessment is not conclusive, we would proceed to a two-step process to test goodwill for impairment including comparing the fair value of each reporting unit with its carrying value (including attributable goodwill). Fair value for our reporting units is determined using an income or market approach incorporating market participant considerations and management s assumptions on revenue growth rates, operating margins, discount rates and expected capital expenditures. Fair value determinations may include both internal and third-party valuations. Unless circumstances otherwise dictate, we perform our annual impairment testing in the fourth quarter.

PENSION AND POSTRETIREMENT HEALTHCARE PLANS. Our defined benefit plans are measured using actuarial techniques that reflect management s assumptions for discount rate, expected long-term investment returns on plan assets, salary increases, expected retirement, mortality, employee turnover and future increases in healthcare costs. We determine the discount rate (which is required to be the rate at which the projected benefit obligation could be effectively settled as of the measurement date) with the assistance of actuaries, who calculate the yield on a theoretical portfolio of high-grade corporate bonds (rated Aa or better) with cash flows that are designed to match our expected benefit payments in future years. A calculated-value method is employed for purposes of determining the asset values for our tax-qualified U.S. domestic pension plans (U.S. Pension Plans). Our expected rate of return is a judgmental matter which is reviewed on an annual basis and revised as appropriate.

The accounting guidance related to employers accounting for defined benefit pension and other postretirement plans requires recognition in the balance sheet of the funded status of defined benefit pension and other postretirement benefit plans, and the recognition in other comprehensive income (OCI) of unrecognized gains or losses and prior service costs or credits. Additionally, the guidance requires the measurement date for plan assets and liabilities to coincide with the plan sponsor s year end.

At May 31, 2012, we recorded a decrease to equity through OCI of $2.4 billion (net of tax) based primarily on year-end adjustments related to increases in our projected benefit obligation due to a decrease in the discount rate used to measure the liability at May 31, 2012. At May 31, 2011, we recorded a decrease to equity through OCI of $350 million (net of tax) based primarily on year-end adjustments related to increases in our projected benefit obligation due to a decrease in the discount rate used to measure the liability at May 31, 2011.

INCOME TAXES. Deferred income taxes are provided for the tax effect of temporary differences between the tax basis of assets and liabilities and their reported amounts in the financial statements. The liability method is used to account for income taxes, which requires deferred taxes to be recorded at the statutory rate expected to be in effect when the taxes are paid.

We recognize liabilities for uncertain income tax positions based on a two-step process. The first step is to evaluate the tax position for recognition by determining if the weight of available evidence indicates that it is more likely than not that the position will be sustained on audit, including resolution of related appeals or litigation processes, if any. The second step requires us to estimate and measure the tax benefit as the largest amount that is more than 50% likely to be realized upon ultimate settlement. It is inherently difficult and subjective to estimate such amounts, as we must determine the probability of various possible outcomes. We reevaluate these uncertain tax positions on a quarterly basis or when new information becomes available to management. These reevaluations are based on factors including, but not limited to, changes in facts or circumstances, changes in tax law, successfully settled issues under audit and new audit activity. Such a change in recognition or measurement could result in the recognition of a tax benefit or an increase to the related provision.

We classify interest related to income tax liabilities as interest expense, and if applicable, penalties are recognized as a component of income tax expense. The income tax liabilities and accrued interest and penalties that are due within one year of the balance sheet date are presented as current liabilities. The remaining portion of our income tax liabilities and accrued interest and penalties are presented as noncurrent liabilities because payment of cash is not anticipated within one year of the balance sheet date. These noncurrent income tax liabilities are recorded in the caption Other liabilities in the accompanying consolidated balance sheets.

SELF-INSURANCE ACCRUALS. We are self-insured for costs associated with workers compensation claims, vehicle accidents and general business liabilities, and benefits paid under employee healthcare and long-term disability programs. Accruals are primarily based on the actuarially estimated, undiscounted cost of claims, which includes incurred-but-not-reported claims. Current workers compensation claims, vehicle and general liability, employee healthcare claims and long-term disability are included in accrued expenses. We self-insure up to certain limits that vary by operating company and type of risk. Periodically, we evaluate the level of insurance coverage and adjust insurance levels based on risk tolerance and premium expense.

LEASES. We lease certain aircraft, facilities, equipment and vehicles under capital and operating leases. The commencement date of all leases is the earlier of the date we become legally obligated to make rent payments or the date we may exercise control over the use of the property. In addition to minimum rental payments, certain leases provide for contingent rentals based on equipment usage principally related to aircraft leases at FedEx Express and copier usage at FedEx Office. Rent expense associated with contingent rentals is recorded as incurred. Certain of our leases contain fluctuating or escalating payments and rent holiday periods. The related rent expense is recorded on a straight-line basis over the lease term. The cumulative excess of rent payments over rent expense is accounted for as a deferred lease asset and recorded in Other assets in the accompanying consolidated balance sheets. The cumulative excess of rent expense over rent payments is accounted for as a deferred lease obligation. Leasehold improvements associated with assets utilized under capital or operating leases are amortized over the shorter of the asset s useful life or the lease term.

DEFERRED GAINS. Gains on the sale and leaseback of aircraft and other property and equipment are deferred and amortized ratably over the life of the lease as a reduction of rent expense. Substantially all of these deferred gains are related to aircraft transactions.

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FOREIGN CURRENCY TRANSLATION. Translation gains and losses of foreign operations that use local currencies as the functional currency are accumulated and reported, net of applicable deferred income taxes, as a component of accumulated other comprehensive income within common stockholders investment. Transaction gains and losses that arise from exchange rate fluctuations on transactions denominated in a currency other than the local currency are included in the caption Other, net in the accompanying consolidated statements of income and were immaterial for each period presented. Cumulative net foreign currency translation gains in accumulated other comprehensive income were $60 million at May 31, 2012, $156 million at May 31, 2011 and $30 million at May 31, 2010.

EMPLOYEES UNDER COLLECTIVE BARGAINING ARRANGEMENTS. The pilots of FedEx Express, which represent a small number of FedEx Express s total employees, are employed under a collective bargaining agreement. In 2011, the pilots ratified a new labor contract that includes safety initiatives, increases in hourly pay rates and travel per diem rates, and provisions for opening a European crew base. The new contract becomes amendable in March 2013. In addition to our pilots at FedEx Express, certain of FedEx s non-U.S. employees are unionized.

STOCK-BASED COMPENSATION. We recognize compensation expense for stock-based awards under the provisions of the accounting guidance related to share-based payments. This guidance requires recognition of compensation expense for stock-based awards using a fair value method.

TREASURY SHARES. During the second quarter of 2012, we repurchased 2.8 million FedEx common shares at an average price of $70 per share for a total of $197 million. As of May 31, 2012, 2.9 million shares remained under existing share repurchase authorizations.

DIVIDENDS DECLARED PER COMMON SHARE. On June 4, 2012, our Board of Directors declared a quarterly dividend of $0.14 per share of common stock. The dividend was paid on July 2, 2012 to stockholders of record as of the close of business on June 18, 2012. Each quarterly dividend payment is subject to review and approval by our Board of Directors, and we evaluate our dividend payment amount on an annual basis at the end of each fiscal year.

FEDEX FREIGHT NETWORK COMBINATION. The combination of our FedEx Freight and FedEx National LTL operations was completed on January 30, 2011. These actions resulted in total program costs of $133 million, which includes $89 million of impairment and other charges and $44 million of other program costs recorded during 2011.

USE OF ESTIMATES. The preparation of our consolidated financial statements requires the use of estimates and assumptions that affect the reported amounts of assets and liabilities, the reported amounts of revenues and expenses and the disclosure of contingent liabilities. Management makes its best estimate of the ultimate outcome for these items based on historical trends and other information available when the financial statements are prepared. Changes in estimates are recognized in accordance with the accounting rules for the estimate, which is typically in the period when new information becomes available to management. Areas where the nature of the estimate makes it reasonably possible that actual results could materially differ from amounts estimated include: self-insurance accruals; retirement plan obligations; long-term incentive accruals; tax liabilities; accounts receivable allowances; obsolescence of spare parts; contingent liabilities; loss contingencies, such as litigation and other claims; and impairment assessments on long-lived assets (including goodwill).

NOTE 2: RECENT ACCOUNTING GUIDANCE

New accounting rules and disclosure requirements can significantly impact our reported results and the comparability of our financial statements. We believe the following new accounting guidance is relevant to the readers of our financial statements.

During our fiscal year, the Financial Accounting Standards Board issued new guidance to make the presentation of items within OCI more prominent. The new standard will require companies to present items of net income, items of OCI and total comprehensive income in

one continuous statement or two separate consecutive statements, and companies will no longer be allowed to present items of OCI in the statement of stockholders equity. This new standard is effective for our fiscal year ending May 31, 2013.

We believe there is no additional new accounting guidance adopted but not yet effective that is relevant to the readers of our financial statements. However, there are numerous new proposals under development which, if and when enacted, may have a significant impact on our financial reporting.

NOTE 3: BUSINESS COMBINATIONS

During 2012, we continued to expand our FedEx Express international network. On July 25, 2011, we completed our acquisition of Servicios Nacionales Mupa, S.A. de C.V. (MultiPack), a Mexican domestic express package delivery company, for $128 million in cash from operations. Last year, FedEx Express completed the acquisition of the Indian logistics, distribution and express businesses of AFL Pvt. Ltd. and its affiliate Unifreight India Pvt. Ltd. for $96 million in cash on February 22, 2011. The financial results of these acquired businesses are included in the FedEx Express segment from the date of acquisition and were not material, individually or in the aggregate, to our results of operations or financial condition and therefore, pro forma financial information has not been presented. Substantially all of the purchase price was allocated to goodwill, which was entirely attributed to our FedEx Express reporting unit.

Subsequent to year-end, we completed the following acquisitions:

- Opek Sp. z o.o., a Polish domestic express package delivery company, for $54 million in cash from operations on June 13, 2012

- TATEX, a French express transportation company, for $55 million in cash from operations on July 3, 2012

- Rapidão Cometa Logística e Transportes S.A., a Brazilian transportation and logistics company, for $398 million in cash from operations on July 4, 2012

Based on the timing of the completion of these acquisitions in relation to the date of issuance of the financial statements, the initial purchase price accounting was not completed for these acquisitions. The financial results of these acquired businesses will be included in the FedEx Express segment from the date of acquisition and will be immaterial to our 2013 results. These acquisitions will give us more robust transportation networks within these countries and added capabilities in these important global markets.

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NOTE 4: GOODWILL AND OTHER INTANGIBLE ASSETS

GOODWILL. The carrying amount of goodwill attributable to each reportable operating segment and changes therein are as follows (in millions):

	xxxxxxxxxxxxxx FedEx Express Segment	xxxxxxxxxxxxxx FedEx Ground Segment	xxxxxxxxxxxxxx FedEx Freight Segment	xxxxxxxxxxxxxx FedEx Services Segment	xxxxxxxxxxxxxx Total
Goodwill at May 31, 2010	$ 1,145	$ 90	$ 736	$ 1,539	$ 3,510
Accumulated impairment charges			(133)	(1,177)	(1,310)
Balance as of May 31, 2010	1,145	90	603	362	2,200
Goodwill acquired[1]	89				89
Purchase adjustments and other[2]	38		(1)		37
Balance as of May 31, 2011	1,272	90	602	362	2,326
Goodwill acquired[3]	104				104
Purchase adjustments and other[2]	(32)			(11)	(43)
Balance as of May 31, 2012	$ 1,344	$ 90	$ 602	$ 351	$ 2,387
Accumulated goodwill impairment charges as of May 31, 2012	$	$	$ (133)	$ (1,177)	$ (1,310)

[1] Goodwill acquired in 2011 relates to the acquisition of the Indian logistics, distribution and express businesses of AFL Pvt. Ltd. and its affiliate Unifreight India Pvt. Ltd. See Note 3 for related disclosures.

[2] Primarily currency translation adjustments.

[3] Goodwill acquired in 2012 relates to the acquisition of the Mexican domestic express package delivery company, Multipack. See Note 3 for related disclosures.

Our reporting units with significant recorded goodwill include our FedEx Express, FedEx Freight and FedEx Office (reported in the FedEx Services segment) reporting units. We evaluated these reporting units during the fourth quarter of 2012. The estimated fair value of each of these reporting units exceeded their carrying values in 2012 and 2011, and we do not believe that any of these reporting units were at risk as of May 31, 2012.

In 2010, we recorded a charge of $18 million for impairment of the value of the remaining goodwill at our FedEx National LTL reporting unit. The impairment charge resulted from the significant negative impact of the U.S. recession on the LTL industry, which resulted in volume and yield declines and operating losses. In connection with the combination of our LTL networks in 2011, this unit was merged into the FedEx Freight reporting unit.

OTHER INTANGIBLE ASSETS. The net book value of our other intangible assets was $34 million at May 31, 2012 and $38 million at May 31, 2011. Amortization expense for intangible assets was $18 million in 2012, $32 million in 2011 and $51 million in 2010. Estimated amortization expense is expected to be immaterial in 2013.

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NOTE 5: SELECTED CURRENT LIABILITIES

The components of selected current liability captions were as follows (in millions):

	May 31, 2012	May 31, 2011
Accrued Salaries and Employee Benefits		
Salaries	$ 280	$ 256
Employee benefits, including variable compensation	803	468
Compensated absences	552	544
	$ 1,635	$ 1,268
Accrued Expenses		
Self-insurance accruals	$ 678	$ 696
Taxes other than income taxes	386	357
Other	645	841
	$ 1,709	$ 1,894

NOTE 6: LONG-TERM DEBT AND OTHER FINANCING ARRANGEMENTS

The components of long-term debt (net of discounts), along with maturity dates for the years subsequent to May 31, 2012, are as follows (in millions):

	May 31, 2012	May 31, 2011
Senior unsecured debt		
Interest rate of 9.65%, due in 2013	$ 300	$ 300
Interest rate of 7.38%, due in 2014	250	250
Interest rate of 8.00%, due in 2019	750	750
Interest rate of 7.60%, due in 2098	239	239
	1,539	1,539
Capital lease obligations	128	146
	1,667	1,685
Less current portion	417	18
	$ 1,250	$ 1,667

Interest on our fixed-rate notes is paid semi-annually. Long-term debt, exclusive of capital leases, had carrying values of $1.5 billion at May 31, 2012 and May 31, 2011 compared with estimated fair values of $2.0 billion at May 31, 2012 and $1.9 billion at May 31, 2011. The estimated fair values were determined based on quoted market prices or on the current rates offered for debt with similar terms and maturities.

We have a shelf registration statement filed with the Securities and Exchange Commission that allows us to sell, in one or more future offerings, any combination of our unsecured debt securities and common stock.

During 2012, we made principal payments in the amount of $29 million related to capital lease obligations. During 2011, we repaid our $250 million 7.25% unsecured notes that matured on February 15, 2011. During 2011, we made principal payments in the amount of $12 million related to capital lease obligations.

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A $1 billion revolving credit facility is available to finance our operations and other cash flow needs and to provide support for the issuance of commercial paper. The revolving credit agreement expires in April 2016. The agreement contains a financial covenant, which requires us to maintain a leverage ratio of adjusted debt (long-term debt, including the current portion of such debt, plus six times our last four fiscal quarters rentals and landing fees) to capital (adjusted debt plus total common stockholders investment) that does not exceed 70%. Our leverage ratio of adjusted debt to capital was 53% at May 31, 2012. We believe the leverage ratio covenant is our only significant restrictive covenant in our revolving credit agreement. Our revolving credit agreement contains other customary covenants that do not, individually or in the aggregate, materially restrict the conduct of our business. We are in compliance with the leverage ratio covenant and all other covenants of our revolving credit agreement and do not expect the covenants to affect our operations, including our liquidity or expected funding needs. As of May 31, 2012, no commercial paper was outstanding, and the entire $1 billion under the revolving credit facility was available for future borrowings.

We issue other financial instruments in the normal course of business to support our operations, including standby letters of credit and surety bonds. We had a total of $609 million in letters of credit outstanding at May 31, 2012, with $107 million unused under our primary $500 million letter of credit facility, and $458 million in outstanding surety bonds placed by third-party insurance providers. These instruments are required under certain U.S. self-insurance programs and are also used in the normal course of international operations. The underlying liabilities insured by these instruments are reflected in our balance sheets, where applicable. Therefore, no additional liability is reflected for the letters of credit and surety bonds themselves.

Our capital lease obligations include leases for aircraft and facilities. Our facility leases include leases that guarantee the repayment of certain special facility revenue bonds that have been issued by municipalities primarily to finance the acquisition and construction of various airport facilities and equipment. These bonds require interest payments at least annually, with principal payments due at the end of the related lease agreement.

NOTE 7: LEASES

We utilize certain aircraft, land, facilities, retail locations and equipment under capital and operating leases that expire at various dates through 2045. We leased 10% of our total aircraft fleet under capital or operating leases as of May 31, 2012 as compared to 11% as of May 31, 2011. A portion of our supplemental aircraft are leased by us under agreements that provide for cancellation upon 30 days notice. Our leased facilities include national, regional and metropolitan sorting facilities, retail facilities and administrative buildings.

The components of property and equipment recorded under capital leases were as follows (in millions):

	xx,xxx,x	xx,xxx,x
	May 31,	
	2012	2011
Aircraft	$ 7	$ 8
Package handling and ground support equipment	165	165
Vehicles	16	17
Other, principally facilities	147	145
	335	335
Less accumulated amortization	319	307
	$ 16	$ 28

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Rent expense under operating leases for the years ended May 31 was as follows (in millions):

	XX,XXX,X 2012	XX,XXX,X 2011	XX,XXX,X 2010
Minimum rentals	$ 2,018	$ 2,025	$ 2,001
Contingent rentals[1]	210	193	152
	$ 2,228	$ 2,218	$ 2,153

[1] Contingent rentals are based on equipment usage.

A summary of future minimum lease payments under capital leases and noncancelable operating leases with an initial or remaining term in excess of one year at May 31, 2012 is as follows (in millions):

	XX,XXX,X	XX,XXX,X	XX,XXX,X Operating Leases	XX,XXX,X
	Capital Leases	Aircraft and Related Equipment	Facilities and Other	Total Operating Leases
2013	$ 120	$ 486	$ 1,386	$ 1,872
2014	2	462	1,263	1,725
2015	2	448	1,124	1,572
2016	1	453	938	1,391
2017	1	391	1,042	1,433
Thereafter	11	1,150	4,843	5,993
Total	137	$ 3,390	$ 10,596	$ 13,986
Less amount representing interest	9			
Present value of net minimum lease payments	$ 128			

The weighted-average remaining lease term of all operating leases outstanding at May 31, 2012 was approximately six years. While certain of our lease agreements contain covenants governing the use of the leased assets or require us to maintain certain levels of insurance, none of our lease agreements include material financial covenants or limitations.

FedEx Express makes payments under certain leveraged operating leases that are sufficient to pay principal and interest on certain pass-through certificates. The pass-through certificates are not direct obligations of, or guaranteed by, FedEx or FedEx Express.

We are the lessee in a series of operating leases covering a portion of our leased aircraft. The lessors are trusts established specifically to purchase, finance and lease aircraft to us. These leasing entities meet the criteria for variable interest entities. We are not the primary beneficiary of the leasing entities, as the lease terms are consistent with market terms at the inception of the lease and do not include a residual value guarantee, fixed-price purchase option or similar feature that obligates us to absorb decreases in value or entitles us to participate in increases in the value of the aircraft. As such, we are not required to consolidate the entity as the primary beneficiary. Our maximum exposure under these leases is included in the summary of future minimum lease payments shown above.

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NOTE 8: PREFERRED STOCK

Our Certificate of Incorporation authorizes the Board of Directors, at its discretion, to issue up to 4,000,000 shares of preferred stock. The stock is issuable in series, which may vary as to certain rights and preferences, and has no par value. As of May 31, 2012, none of these shares had been issued.

NOTE 9: STOCK-BASED COMPENSATION

Our total stock-based compensation expense for the years ended May 31 was as follows (in millions):

	XXXXXX 2012	XXXXXX 2011	XXXXXX 2010
Stock-based compensation expense	$ 105	$ 98	$ 101

We have two types of equity-based compensation: stock options and restricted stock.

STOCK OPTIONS. Under the provisions of our incentive stock plans, key employees and non-employee directors may be granted options to purchase shares of our common stock at a price not less than its fair market value on the date of grant. Vesting requirements are determined at the discretion of the Compensation Committee of our Board of Directors. Option-vesting periods range from one to four years, with 83% of our options vesting ratably over four years. Compensation expense associated with these awards is recognized on a straight-line basis over the requisite service period of the award.

RESTRICTED STOCK. Under the terms of our incentive stock plans, restricted shares of our common stock are awarded to key employees. All restrictions on the shares expire ratably over a four-year period. Shares are valued at the market price on the date of award. The terms of our restricted stock provide for continued vesting subsequent to the employee s retirement. Compensation expense associated with these awards is recognized on a straight-line basis over the shorter of the remaining service or vesting period.

VALUATION AND ASSUMPTIONS. We use the Black-Scholes option pricing model to calculate the fair value of stock options. The value of restricted stock awards is based on the stock price of the award on the grant date. We record stock-based compensation expense in the Salaries and employee benefits caption in the accompanying consolidated statements of income.

The key assumptions for the Black-Scholes valuation method include the expected life of the option, stock price volatility, a risk-free interest rate, and dividend yield. Following is a table of the weighted-average Black-Scholes value of our stock option grants, the intrinsic value of options exercised (in millions), and the key weighted-average assumptions used in the valuation calculations for the options granted during the years ended May 31, and then a discussion of our methodology for developing each of the assumptions used in the valuation model:

	XXXXXX 2012	XXXXXX 2011	XXXXXX 2010
Weighted-average Black-Scholes value	$ 29.92	$ 28.12	$ 20.47
Intrinsic value of options exercised	$ 67	$ 80	$ 77
Black-Scholes Assumptions:			
Expected lives	6.0 years	5.9 years	5.7 years
Expected volatility	34%	34%	32%
Risk-free interest rate	1.79%	2.36%	3.24%
Dividend yield	0.563%	0.558%	0.742%

Expected Lives. This is the period of time over which the options granted are expected to remain outstanding. Options granted have a maximum term of 10 years. We examine actual stock option exercises to determine the expected life of the options. An increase in the expected term will increase compensation expense.

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Expected Volatility. Actual changes in the market value of our stock are used to calculate the volatility assumption. We calculate daily market value changes from the date of grant over a past period equal to the expected life of the options to determine volatility. An increase in the expected volatility will increase compensation expense.

Risk-Free Interest Rate. This is the U.S. Treasury Strip rate posted at the date of grant having a term equal to the expected life of the option. An increase in the risk-free interest rate will increase compensation expense.

Dividend Yield. This is the annual rate of dividends per share over the exercise price of the option. An increase in the dividend yield will decrease compensation expense.

The following table summarizes information about stock option activity for the year ended May 31, 2012:

	Stock Options			
	Shares	Weighted-Average Exercise Price	Weighted-Average Remaining Contractual Term	Aggregate Intrinsic Value (in millions)[1]
Outstanding at June 1, 2011	20,163,163	$ 81.20		
Granted	3,303,368	87.90		
Exercised	(2,142,410)	59.73		
Forfeited	(292,583)	84.70		
Outstanding at May 31, 2012	21,031,538	$ 84.39	5.6 years	$ 193
Exercisable	13,608,746	$ 87.59	4.2 years	$ 115
Expected to vest	6,977,189	$ 78.53	8.2 years	$ 73
Available for future grants	8,912,829			

(1) Only presented for options with market value at May 31, 2012 in excess of the exercise price of the option.

The options granted during the year ended May 31, 2012 are primarily related to our principal annual stock option grant in June 2011.

The following table summarizes information about vested and unvested restricted stock for the year ended May 31, 2012:

	Restricted Stock	
	Shares	Weighted-Average Grant Date Fair Value
Unvested at June 1, 2011	626,380	$ 73.20
Granted	214,435	88.95
Vested	(248,413)	78.25
Forfeited	(2,530)	74.98

Unvested at May 31, 2012	589,872	$ 76.79

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During the year ended May 31, 2011, there were 235,998 shares of restricted stock granted with a weighted-average fair value of $78.74. During the year ended May 31, 2010, there were 391,786 shares of restricted stock granted with a weighted-average fair value of $57.07.

The following table summarizes information about stock option vesting during the years ended May 31:

	Stock Options	
	Vested during the year	Fair value (in millions)
2010	2,296,211	$ 63
2011	2,721,602	67
2012	2,807,809	70

As of May 31, 2012, there was $150 million of total unrecognized compensation cost, net of estimated forfeitures, related to unvested share-based compensation arrangements. This compensation expense is expected to be recognized on a straight-line basis over the remaining weighted-average vesting period of approximately three years.

Total shares outstanding or available for grant related to equity compensation at May 31, 2012 represented 9% of the total outstanding common and equity compensation shares and equity compensation shares available for grant.

NOTE 10: COMPUTATION OF EARNINGS PER SHARE

The calculation of basic and diluted earnings per common share for the years ended May 31 was as follows (in millions, except per share amounts):

	xx,xxx,x	xx,xxx,x	xx,xxx,x
	2012	2011	2010
Basic earnings per common share:			
Net earnings allocable to common shares[1]	$ 2,029	$ 1,449	$ 1,182
Weighted-average common shares	315	315	312
Basic earnings per common share	$ 6.44	$ 4.61	$ 3.78
Diluted earnings per common share:			
Net earnings allocable to common shares[1]	$ 2,029	$ 1,449	$ 1,182
Weighted-average common shares	315	315	312
Dilutive effect of share-based awards	2	2	2
Weighted-average diluted shares	317	317	314
Diluted earnings per common share	$ 6.41	$ 4.57	$ 3.76
Anti-dilutive options excluded from diluted earnings per common share	12.6	9.3	11.5

(1) Net earnings available to participating securities were immaterial in all periods presented.

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NOTE 11: INCOME TAXES

The components of the provision for income taxes for the years ended May 31 were as follows (in millions):

	2012	2011	2010
Current provision (benefit)			
Domestic:			
Federal	$ (120)	$ 79	$ 36
State and local	80	48	54
Foreign	181	198	207
	141	325	297
Deferred provision (benefit)			
Domestic:			
Federal	947	485	408
State and local	21	12	15
Foreign		(9)	(10)
	968	488	413
	$ 1,109	$ 813	$ 710

Our current federal income tax expenses in 2012, 2011 and 2010 were significantly reduced by accelerated depreciation deductions we claimed under provisions of the Tax Relief and the Small Business Jobs Acts of 2010, the American Recovery and Reinvestment Tax Act of 2009, and the Economic Stimulus Act of 2008. Those Acts, designed to stimulate new business investment in the U.S., accelerated our depreciation deductions for new qualifying investments, such as our new Boeing 777 Freighter (B777F) aircraft. These are timing benefits only, in that the depreciation would have otherwise been recognized in later years.

Pre-tax earnings of foreign operations for 2012, 2011 and 2010 were $358 million, $472 million and $555 million, respectively, which represent only a portion of total results associated with international shipments.

A reconciliation of the statutory federal income tax rate to the effective income tax rate for the years ended May 31 was as follows:

	2012	2011	2010
Statutory U.S. income tax rate	35.0%	35.0%	35.0%
Increase (decrease) resulting from:			
State and local income taxes, net of federal benefit	2.1	1.7	2.4
Other, net	(1.8)	(0.8)	0.1
Effective tax rate	35.3%	35.9%	37.5%

Our 2012 rate was lower than our 2011 rate primarily due to favorable audit developments. The 2011 rate was lower than our 2010 rate primarily due to increased permanently reinvested foreign earnings and a lower state rate driven by favorable audit and legislative developments.

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The significant components of deferred tax assets and liabilities as of May 31 were as follows (in millions):

	2012		2011	
	Deferred Tax Assets	Deferred Tax Liabilities	Deferred Tax Assets	Deferred Tax Liabilities
Property, equipment, leases and intangibles	$ 248	$ 3,436	$ 274	$ 2,675
Employee benefits	2,300	11	1,016	34
Self-insurance accruals	495		519	
Other	338	271	422	269
Net operating loss/credit carryforwards	179		172	
Valuation allowances	(145)		(151)	
	$ 3,415	$ 3,718	$ 2,252	$ 2,978

The net deferred tax liabilities as of May 31 have been classified in the balance sheets as follows (in millions):

	2012	2011
Current deferred tax asset	$ 533	$ 610
Noncurrent deferred tax liability	(836)	(1,336)
	$ (303)	$ (726)

We have $560 million of net operating loss carryovers in various foreign jurisdictions and $510 million of state operating loss carryovers. The valuation allowances primarily represent amounts reserved for operating loss and tax credit carryforwards, which expire over varying periods starting in 2013. As a result of this and other factors, we believe that a substantial portion of these deferred tax assets may not be realized.

Permanently reinvested earnings of our foreign subsidiaries amounted to $1 billion at the end of 2012 and $640 million at the end of 2011. We have not recognized deferred taxes for U.S. federal income tax purposes on those earnings. In 2012, our permanent reinvestment strategy with respect to unremitted earnings of our foreign subsidiaries provided a 1.3% benefit to our effective tax rate. Were the earnings to be distributed, in the form of dividends or otherwise, these earnings could be subject to U.S. federal income tax and non-U.S. withholding taxes. Unrecognized foreign tax credits potentially could be available to reduce a portion of any U.S. tax liability. Determination of the amount of unrecognized deferred U.S. income tax liability is not practicable due to uncertainties related to the timing and source of any potential distribution of such funds, along with other important factors such as the amount of associated foreign tax credits. Cash in offshore jurisdictions associated with our permanent reinvestment strategy totaled $410 million at the end of 2012 and $300 million at the end of 2011.

We file income tax returns in the U.S., various U.S. state and local jurisdictions, and various foreign jurisdictions. The Internal Revenue Service is currently auditing our consolidated U.S. income tax returns for the 2010 and 2011 tax years. We are no longer subject to U.S. federal income tax examination for years through 2009 except for specific and immaterial U.S. federal income tax positions that are in various stages of litigation. We anticipate resolution of part or all of this litigation could occur within 2013, but it would not have a material effect on our consolidated financial statements. We are also subject to ongoing audits in state, local and foreign tax jurisdictions throughout the world.

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A reconciliation of the beginning and ending amount of unrecognized tax benefits is as follows (in millions):

	xxxxxx 2012	xxxxxx 2011	xxxxxx 2010
Balance at beginning of year	$ 69	$ 82	$ 72
Increases for tax positions taken in the current year	2	2	3
Increases for tax positions taken in prior years	4	6	14
Decreases for tax positions taken in prior years	(35)	(10)	(4)
Settlements	(3)	(11)	(3)
Increases due to acquisitions	15		
Changes due to currency translation	(1)		
Balance at end of year	$ 51	$ 69	$ 82

Our liabilities recorded for uncertain tax positions include $47 million at May 31, 2012 and $56 million at May 31, 2011 associated with positions that if favorably resolved would provide a benefit to our effective tax rate. We classify interest related to income tax liabilities as interest expense, and if applicable, penalties are recognized as a component of income tax expense. The balance of accrued interest and penalties was $29 million on May 31, 2012 and $18 million on May 31, 2011. Total interest and penalties included in our consolidated statements of income are immaterial.

It is difficult to predict the ultimate outcome or the timing of resolution for tax positions. Changes may result from the conclusion of ongoing audits, appeals or litigation in state, local, federal and foreign tax jurisdictions, or from the resolution of various proceedings between the U.S. and foreign tax authorities. Our liability for uncertain tax positions includes no matters that are individually or collectively material to us. It is reasonably possible that the amount of the benefit with respect to certain of our unrecognized tax positions will increase or decrease within the next 12 months, but an estimate of the range of the reasonably possible changes cannot be made. However, we do not expect that the resolution of any of our uncertain tax positions will be material.

NOTE 12: RETIREMENT PLANS

We sponsor programs that provide retirement benefits to most of our employees. These programs include defined benefit pension plans, defined contribution plans and postretirement healthcare plans. The accounting for pension and postretirement healthcare plans includes numerous assumptions, such as: discount rates; expected long-term investment returns on plan assets; future salary increases; employee turnover; mortality; and retirement ages. These assumptions most significantly impact our U.S. Pension Plans.

The accounting guidance related to postretirement benefits requires recognition in the balance sheet of the funded status of defined benefit pension and other postretirement benefit plans, and the recognition in accumulated other comprehensive income (AOCI) of unrecognized gains or losses and prior service costs or credits. The funded status is measured as the difference between the fair value of the plan s assets and the projected benefit obligation (PBO) of the plan. At May 31, 2012, we recorded a decrease to equity of $2.4 billion (net of tax) attributable to our plans. At May 31, 2011, we recorded a decrease to equity of $350 million (net of tax) attributable to our plans.

A summary of our retirement plans costs over the past three years is as follows (in millions):

	xxxxxxx 2012	xxxxxxx 2011	xxxxxxx 2010
U.S. domestic and international pension plans	$ 524	$ 543	$ 308
U.S. domestic and international defined contribution plans	338	257	136
Postretirement healthcare plans	70	60	42
	$ 932	$ 860	$ 486

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PENSION PLANS. Our largest pension plan covers certain U.S. employees age 21 and over, with at least one year of service. Pension benefits for most employees are accrued under a cash balance formula we call the Portable Pension Account. Under the Portable Pension Account, the retirement benefit is expressed as a dollar amount in a notional account that grows with annual credits based on pay, age and years of credited service, and interest on the notional account balance. The Portable Pension Account benefit is payable as a lump sum or an annuity at retirement at the election of the employee. The plan interest credit rate varies from year to year based on a U.S. Treasury index and corporate bond rates. Prior to 2009, certain employees earned benefits using a traditional pension formula (based on average earnings and years of service). Benefits under this formula were capped on May 31, 2008 for most employees. We also sponsor or participate in nonqualified benefit plans covering certain of our U.S. employee groups and other pension plans covering certain of our international employees. The international defined benefit pension plans provide benefits primarily based on final earnings and years of service and are funded in compliance with local laws and practices.

POSTRETIREMENT HEALTHCARE PLANS. Certain of our subsidiaries offer medical, dental and vision coverage to eligible U.S. retirees and their eligible dependents. U.S. employees covered by the principal plan become eligible for these benefits at age 55 and older, if they have permanent, continuous service of at least 10 years after attainment of age 45 if hired prior to January 1, 1988, or at least 20 years after attainment of age 35 if hired on or after January 1, 1988. Postretirement healthcare benefits are capped at 150% of the 1993 per capita projected employer cost, which has been reached and, therefore, these benefits are not subject to additional future inflation.

PENSION PLAN ASSUMPTIONS. Our pension cost is materially affected by the discount rate used to measure pension obligations, the level of plan assets available to fund those obligations and the expected long-term rate of return on plan assets.

We use a measurement date of May 31 for our pension and postretirement healthcare plans. Management reviews the assumptions used to measure pension costs on an annual basis. Economic and market conditions at the measurement date impact these assumptions from year to year. Actuarial gains or losses are generated for changes in assumptions and to the extent that actual results differ from those assumed. These actuarial gains and losses are amortized over the remaining average service lives of our active employees if they exceed a corridor amount in the aggregate. Additional information about our pension plans can be found in the Critical Accounting Estimates section of Management s Discussion and Analysis of Results of Operations and Financial Condition (MD&A) in this Annual Report on Form 10-K (Annual Report).

Weighted-average actuarial assumptions for our primary U.S. retirement plans, which represent substantially all of our PBO and accumulated postretirement benefit obligation (APBO), are as follows:

	Pension Plans			Postretirement Healthcare Plans		
	2012	2011	2010	2012	2011	2010
Discount rate used to determine benefit obligation	4.44%	5.76%	6.37%	4.55%	5.67%	6.11%
Discount rate used to determine net periodic benefit cost	5.76	6.37	7.68	5.67	6.11	7.27
Rate of increase in future compensation levels used to determine benefit obligation	4.62	4.58	4.63			
Rate of increase in future compensation levels used to determine net periodic benefit cost	4.58	4.63	4.42			
Expected long-term rate of return on assets	8.00	8.00	8.00			

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The estimated average rate of return on plan assets is the expected future long-term rate of earnings on plan assets and is a forward-looking assumption that materially affects our pension cost. Establishing the expected future rate of investment return on our pension assets is a judgmental matter. We review the expected long-term rate of return on an annual basis and revise it as appropriate. Management considers the following factors in determining this assumption:

- the duration of our pension plan liabilities, which drives the investment strategy we can employ with our pension plan assets;
- the types of investment classes in which we invest our pension plan assets and the expected compound geometric return we can reasonably expect those investment classes to earn over time; and
- the investment returns we can reasonably expect our investment management program to achieve in excess of the returns we could expect if investments were made strictly in indexed funds.

Our estimated long-term rate of return on plan assets remains at 8% for 2013, consistent with our expected rate of return in 2012 and 2011. Our actual return in each of the past three years exceeded that amount for our principal U.S. domestic pension plan. For the 15-year period ended May 31, 2012, our actual returns were 7.4%.

Pension expense is also affected by the accounting policy used to determine the value of plan assets at the measurement date. We use a calculated-value method to determine the value of plan assets, which helps mitigate short-term volatility in market performance (both increases and decreases) by amortizing certain actuarial gains or losses over a period no longer than four years. Another method used in practice applies the market value of plan assets at the measurement date. For purposes of valuing plan assets for determining 2013 pension expense, the calculated value method resulted in the same value as the market value, as it did in 2011. For determining 2012 pension expense, we used the calculated value method which resulted in a portion of the asset gain in 2011 being deferred to future years because our actual returns on plan assets significantly exceeded our assumptions.

The investment strategy for pension plan assets is to utilize a diversified mix of global public and private equity portfolios, together with fixed-income portfolios, to earn a long-term investment return that meets our pension plan obligations. Our pension plan assets are invested primarily in listed securities, and our pension plans hold only a minimal investment in FedEx common stock that is entirely at the discretion of third-party pension fund investment managers. Our largest holding classes are Corporate Fixed Income Securities, U.S. Large Cap Equities, which is indexed to the S&P 500 Index, and Government Fixed Income Securities. Accordingly, we do not have any significant concentrations of risk. Active management strategies are utilized within the plan in an effort to realize investment returns in excess of market indices. As part of our strategy to manage future pension costs and net funded status volatility, we have transitioned to a liability-driven investment strategy with a greater concentration of fixed-income securities to better align plan assets with liabilities. Our investment strategy also includes the limited use of derivative financial instruments on a discretionary basis to improve investment returns and manage exposure to market risk. In all cases, our investment managers are prohibited from using derivatives for speculative purposes and are not permitted to use derivatives to leverage a portfolio.

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Following is a description of the valuation methodologies used for investments measured at fair value:

Cash and cash equivalents. These Level 1 investments include cash, cash equivalents and foreign currency valued using exchange rates. The Level 2 investments include commingled funds valued using the net asset value.

Domestic and international equities. These Level 1 investments are valued at the closing price or last trade reported on the major market on which the individual securities are traded. The Level 2 investments are commingled funds valued using the net asset value.

Private equity. The valuation of these Level 3 investments requires significant judgment due to the absence of quoted market prices, the inherent lack of liquidity and the long-term nature of such assets. Investments are valued based upon recommendations of our investment managers incorporating factors such as contributions and distributions, market transactions, market comparables and performance multiples.

Fixed income. We determine the fair value of these Level 2 corporate bonds, U.S. government securities and other fixed income securities by using bid evaluation pricing models or quoted prices of securities with similar characteristics.

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The fair values of investments by level and asset category and the weighted-average asset allocations for our domestic pension plans at the measurement date are presented in the following table (in millions):

Plan Assets at Measurement Date

2012

Asset Class	Fair Value	Actual %	Target %	Quoted Prices in Active Markets Level 1	Other Observable Inputs Level 2	Unobservable Inputs Level 3
Cash and cash equivalents	$ 618	4 %	1 %	$ 8	$ 610	
Domestic equities						
U.S. large cap equity	4,248	25	24	9	4,239	
U.S. SMID cap equity	1,368	8	9	1,368		
International equities	1,657	10	12	1,395	262	
Private equities	402	2	5			$ 402
Fixed income securities			49			
Corporate	4,565	27			4,565	
Government	4,175	24			4,175	
Mortgage backed and other	59				59	
Other	(79)			(85)	6	
	$ 17,013	100 %	100 %	$ 2,695	$ 13,916	$ 402

2011

Asset Class	Fair Value	Actual %	Target %	Quoted Prices in Active Markets Level 1	Other Observable Inputs Level 2	Unobservable Inputs Level 3
Cash and cash equivalents	$ 409	3 %	1 %	$ 107	$ 302	
Domestic equities						
U.S. large cap equity	4,280	27	24	26	4,254	
U.S. SMID cap equity	1,481	10	9	1,481		
International equities	2,013	13	12	1,702	311	
Private equities	403	3	5			$ 403
Fixed income securities			49			
Corporate	3,794	24			3,794	
Government	3,135	20			3,135	
Mortgage backed and other	66				66	
Other	(63)			(59)	(4)	
	$ 15,518	100 %	100 %	$ 3,257	$ 11,858	$ 403

The change in fair value of Level 3 assets that use significant unobservable inputs is shown in the table below (in millions):

	2012	2011
Balance at beginning of year	$ 403	$ 399
Actual return on plan assets:		
Assets held during current year	3	27
Assets sold during the year	38	36
Purchases, sales and settlements	(42)	(59)

Balance at end of the year	$ 402	$ 403

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The following table provides a reconciliation of the changes in the pension and postretirement healthcare plans benefit obligations and fair value of assets over the two-year period ended May 31, 2012 and a statement of the funded status as of May 31, 2012 and 2011 (in millions):

	XXX,XXX,X	XXX,XXX,X	XXX,XXX,X	XXX,XXX,X
	Pension Plans		Postretirement Healthcare Plans	
	2012	2011	2012	2011
Accumulated Benefit Obligation (ABO)	$ 21,556	$ 16,806		
Changes in Projected Benefit Obligation (PBO) and Accumulated Postretirement Benefit Obligation (APBO)				
PBO/APBO at the beginning of year	$ 17,372	$ 14,484	$ 648	$ 565
Service cost	593	521	35	31
Interest cost	976	900	36	34
Actuarial loss	3,789	1,875	98	44
Benefits paid	(502)	(468)	(51)	(48)
Other	(41)	60	24	22
PBO/APBO at the end of year	$ 22,187	$ 17,372	$ 790	$ 648
Change in Plan Assets				
Fair value of plan assets at the beginning of year	$ 15,841	$ 13,295	$	$
Actual return on plan assets	1,235	2,425		
Company contributions	780	557	27	26
Benefits paid	(502)	(468)	(51)	(48)
Other	(20)	32	24	22
Fair value of plan assets at the end of year	$ 17,334	$ 15,841	$	$
Funded Status of the Plans	$ (4,853)	$ (1,531)	$ (790)	$ (648)
Amount Recognized in the Balance Sheet at May 31:				
Current pension, postretirement healthcare and other benefit obligations	$ (35)	$ (33)	$ (33)	$ (31)
Noncurrent pension, postretirement healthcare and other benefit obligations	(4,818)	(1,498)	(757)	(617)
Net amount recognized	$ (4,853)	$ (1,531)	$ (790)	$ (648)
Amounts Recognized in AOCI and not yet reflected in Net Periodic Benefit Cost:				
Net actuarial loss (gain)	$ 8,866	$ 5,386	$ 13	$ (85)
Prior service (credit) cost and other	(897)	(993)	2	2
Total	$ 7,969	$ 4,393	$ 15	$ (83)

Amounts Recognized in AOCI and not yet reflected in Net Periodic Benefit Cost expected to be amortized in next year s

Net Periodic Benefit Cost:				
Net actuarial loss (gain)	$ 516	$ 307	$	$ (1)
Prior service credit and other	(114)	(112)		
Total	$ 402	$ 195	$	$ (1)

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Our pension plans included the following components at May 31, 2012 and 2011 (in millions):

	ABO	PBO	Fair Value of Plan Assets	Funded Status
2012				
Qualified	$ 20,667	$ 21,192	$ 17,013	$ (4,179)
Nonqualified	352	355		(355)
International Plans	537	640	321	(319)
Total	$ 21,556	$ 22,187	$ 17,334	$ (4,853)
2011				
Qualified	$ 16,024	$ 16,445	$ 15,518	$ (927)
Nonqualified	335	339		(339)
International Plans	447	588	323	(265)
Total	$ 16,806	$ 17,372	$ 15,841	$ (1,531)

The table above provides the ABO, PBO, fair value of plan assets and funded status of our pension plans on an aggregated basis. The following table presents our plans on a disaggregated basis to show those plans (as a group) whose assets did not exceed their liabilities. These plans are comprised of our unfunded nonqualified plans, certain international plans and our U.S. Pension Plans. At May 31, 2012 and 2011, the fair value of plan assets for pension plans with a PBO or ABO in excess of plan assets were as follows (in millions):

	PBO Exceeds the Fair Value of Plan Assets	
	2012	2011
Pension Benefits		
Fair value of plan assets	$ 17,334	$ 15,815
PBO	(22,187)	(17,346)
Net funded status	$ (4,853)	$ (1,531)

	ABO Exceeds the Fair Value of Plan Assets	
	2012	2011
Pension Benefits		
ABO[(1)]	$ (21,555)	$ (16,530)
Fair value of plan assets	17,333	15,538
PBO	(22,185)	(17,014)
Net funded status	$ (4,852)	$ (1,476)

(1) ABO not used in determination of funded status.

Contributions to our U.S. Pension Plans for the years ended May 31 were as follows (in millions):

	2012	2011
Required	$ 496	$ 359
Voluntary	226	121
	$ 722	$ 480

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Net periodic benefit cost for the three years ended May 31 were as follows (in millions):

	XXXXXX	XXXXXX	XXXXXX	XXXXXX	XXXXXX	XXXXXX
		Pension Plans			Postretirement Healthcare Plans	
	2012	2011	2010	2012	2011	2010
Service cost	$ 593	$ 521	$ 417	$ 35	$ 31	$ 24
Interest cost	976	900	823	36	34	30
Expected return on plan assets	(1,240)	(1,062)	(955)			
Recognized actuarial losses (gains) and other	195	184	23	(1)	(5)	(12)
Net periodic benefit cost	$ 524	$ 543	$ 308	$ 70	$ 60	$ 42

Pension costs in 2012 were slightly lower than 2011, as the benefit of significant investment returns on our pension plan assets in 2011 offset the negative impact of a lower discount rate at our May 31, 2011 measurement date.

Amounts recognized in OCI for all plans were as follows (in millions):

	2012				2011			
	Pension Plans		Postretirement Healthcare Plans		Pension Plans		Postretirement Healthcare Plans	
	Gross Amount	Net of Tax Amount	Gross Amount	Net of Tax Amount	Gross Amount	Net of Tax Amount	Gross Amount	Net of Tax Amount
Net loss and other arising during period	$ 3,777	$ 2,371	$ 97	$ 61	$ 511	$ 321	$ 44	$ 26
Loss from settlements and curtailments					(13)	(8)		
Amortizations:								
Prior services credit	113	71			113	71		
Actuarial (losses) gains and other	(311)	(195)	1		(284)	(178)	5	3
Total recognized in OCI	$ 3,579	$ 2,247	$ 98	$ 61	$ 327	$ 206	$ 49	$ 29

Benefit payments, which reflect expected future service, are expected to be paid as follows for the years ending May 31 (millions):

	Pension Plans	Postretirement Healthcare Plans
2013	$ 640	$ 33
2014	723	34
2015	803	36
2016	861	38
2017	922	40
2018-2022	6,289	246

These estimates are based on assumptions about future events. Actual benefit payments may vary significantly from these estimates.

Future medical benefit claims costs are estimated to increase at an annual rate of 8.0% during 2013, decreasing to an annual growth rate of 4.5% in 2029 and thereafter. Future dental benefit costs are estimated to increase at an annual rate of 6.9% during 2013, decreasing to an annual growth rate of 4.5% in 2029 and thereafter. A 1% change in these annual trend rates would not have a significant impact on the APBO at May 31, 2012 or 2012 benefit expense because the level of these benefits is capped.

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NOTE 13: BUSINESS SEGMENT INFORMATION

FedEx Express, FedEx Ground and FedEx Freight represent our major service lines and, along with FedEx Services, form the core of our reportable segments. Our reportable segments include the following businesses:

FedEx Express Segment	FedEx Express (express transportation) FedEx Trade Networks (air and ocean freight forwarding and customs brokerage) FedEx SupplyChain Systems (logistics services)
FedEx Ground Segment	FedEx Ground (small-package ground delivery) FedEx SmartPost (small-parcel consolidator)
FedEx Freight Segment	FedEx Freight (LTL freight transportation) FedEx Custom Critical (time-critical transportation)
FedEx Services Segment	FedEx Services (sales, marketing, information technology, communications and back-office functions) FedEx TechConnect (customer service, technical support, billings and collections) FedEx Office (document and business services and package acceptance)

FedEx Services Segment

The FedEx Services segment operates combined sales, marketing, administrative and information technology functions in shared services operations that support our transportation businesses and allow us to obtain synergies from the combination of these functions. For the international regions of FedEx Express, some of these functions are performed on a regional basis by FedEx Express and reported in the FedEx Express segment in expense line items outside of intercompany charges. The FedEx Services segment includes: FedEx Services, which provides sales, marketing, information technology, communications and back-office support to our other companies; FedEx TechConnect, which is responsible for customer service, technical support, billings and collections for U.S. customers of our major business units; and FedEx Office, which provides an array of document and business services and retail access to our customers for our package transportation businesses.

The FedEx Services segment provides direct and indirect support to our transportation businesses, and we allocate all of the net operating costs of the FedEx Services segment (including the net operating results of FedEx Office) to reflect the full cost of operating our transportation businesses in the results of those segments. Within the FedEx Services segment allocation, the net operating results of FedEx Office, which are an immaterial component of our allocations, are allocated to FedEx Express and FedEx Ground. The allocations of net operating costs are based on metrics such as relative revenues or estimated services provided. We believe these allocations approximate the net cost of providing these functions. We review and evaluate the performance of our transportation segments based on operating income (inclusive of FedEx Services segment allocations). For the FedEx Services segment, performance is evaluated based on the impact of its total allocated net operating costs on our transportation segments.

The operating expenses line item Intercompany charges on the accompanying unaudited financial summaries of our transportation segments in MD&A reflects the allocations from the FedEx Services segment to the respective transportation segments. The Intercompany charges caption also includes charges and credits for administrative services provided between operating companies and certain other costs such as corporate management fees related to services received for general corporate oversight, including executive officers and certain legal and finance functions. We believe these allocations approximate the net cost of providing these functions.

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Other Intersegment Transactions

Certain FedEx operating companies provide transportation and related services for other FedEx companies outside their reportable segment. Billings for such services are based on negotiated rates, which we believe approximate fair value, and are reflected as revenues of the billing segment. These rates are adjusted from time to time based on market conditions. Such intersegment revenues and expenses are eliminated in our consolidated results and are not separately identified in the following segment information, because the amounts are not material.

The following table provides a reconciliation of reportable segment revenues, depreciation and amortization, operating income (loss) and segment assets to consolidated financial statement totals for the years ended or as of May 31 (in millions):

	XXXX.XX FedEx Express Segment[1]	XXXX.XX FedEx Ground Segment	XXXX.XX FedEx Freight Segment[2]	XXXX.XX FedEx Services Segment	XXXX.XX Other and Eliminations	XXXX.XX Consolidated Total
Revenues						
2012	$ 26,515	$ 9,573	$ 5,282	$ 1,671	$ (361)	$ 42,680
2011	24,581	8,485	4,911	1,684	(357)	39,304
2010	21,555	7,439	4,321	1,770	(351)	34,734
Depreciation and amortization						
2012	$ 1,169	$ 389	$ 185	$ 369	$ 1	$ 2,113
2011	1,059	337	205	371	1	1,973
2010	1,016	334	198	408	2	1,958
Operating income (loss)						
2012	$ 1,260	$ 1,764	$ 162	$	$	$ 3,186
2011	1,228	1,325	(175)			2,378
2010	1,127	1,024	(153)			1,998
Segment assets[3]						
2012	$ 17,981	$ 6,154	$ 2,807	$ 4,546	$ (1,585)	$ 29,903
2011	16,463	5,048	2,664	4,278	(1,068)	27,385
2010	14,819	4,118	2,786	4,079	(900)	24,902

(1) FedEx Express segment 2012 operating expenses include an impairment charge of $134 million resulting from the decision to retire 24 aircraft and related engines and a reversal of a $66 million legal reserve associated with the ATA Airlines lawsuit which was initially recorded in 2011.

(2) FedEx Freight segment 2011 operating expenses include $133 million in costs associated with the combination of our FedEx Freight and FedEx National LTL operations, effective January 30, 2011.

(3) Segment assets include intercompany receivables.

The following table provides a reconciliation of reportable segment capital expenditures to consolidated totals for the years ended May 31 (in millions):

	FedEx Express Segment	FedEx Ground Segment	FedEx Freight Segment	FedEx Services Segment	Other	Consolidated Total
2012	$ 2,689	$ 536	$ 340	$ 437	$ 5	$ 4,007
2011	2,467	426	153	387	1	3,434
2010	1,864	400	212	340		2,816

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The following table presents revenue by service type and geographic information for the years ended or as of May 31 (in millions):

REVENUE BY SERVICE TYPE

	2012	2011	2010
FedEx Express segment:			
Package:			
U.S. overnight box	$ 6,546	$ 6,128	$ 5,602
U.S. overnight envelope	1,747	1,736	1,640
U.S. deferred	3,001	2,805	2,589
Total U.S. domestic package revenue	11,294	10,669	9,831
International priority[1]	8,708	8,228	7,087
International domestic[2]	853	653	578
Total package revenue	20,855	19,550	17,496
Freight:			
U.S.	2,498	2,188	1,980
International priority [1]	1,827	1,722	1,303
International airfreight	307	283	251
Total freight revenue	4,632	4,193	3,534
Other[3]	1,028	838	525
Total FedEx Express segment	26,515	24,581	21,555
FedEx Ground segment:			
FedEx Ground	8,791	7,855	6,958
FedEx SmartPost	782	630	481
Total FedEx Ground segment	9,573	8,485	7,439
FedEx Freight segment	5,282	4,911	4,321
FedEx Services segment	1,671	1,684	1,770
Other and eliminations	(361)	(357)	(351)
	$ 42,680	$ 39,304	$ 34,734

GEOGRAPHICAL INFORMATION[4]			
Revenues:			
U.S.	$ 29,837	$ 27,461	$ 24,852
International:			
FedEx Express segment	12,370	11,437	9,547
FedEx Ground segment	216	177	140
FedEx Freight segment	101	84	60
FedEx Services segment	156	145	135

Total international revenue		12,843		11,843		9,882
	$	42,680	$	39,304	$	34,734
Noncurrent assets:						
U.S.	$	18,874	$	17,235	$	16,089
International		1,973		1,865		1,529
	$	20,847	$	19,100	$	17,618

(1) International priority includes FedEx International Priority and FedEx International Economy services.

(2) International domestic revenues include our international intra-country domestic express operations, including acquisitions in India (February 2011) and Mexico (July 2011).

(3) Other revenues include FedEx Trade Networks and, beginning in the second quarter of 2010, FedEx SupplyChain Systems.

(4) International revenue includes shipments that either originate in or are destined to locations outside the United States. Noncurrent assets include property and equipment, goodwill and other long-term assets. Our flight equipment registered in the U.S. is included as U.S. assets; however, many of our aircraft operate internationally.

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NOTE 14: SUPPLEMENTAL CASH FLOW INFORMATION

Cash paid for interest expense and income taxes for the years ended May 31 was as follows (in millions):

	2012	2011	2010
Cash payments for:			
Interest (net of capitalized interest)	$ 52	$ 93	$ 88
Income taxes	$ 403	$ 493	$ 322
Income tax refunds received	(146)	(106)	(279)
Cash tax payments, net	$ 257	$ 387	$ 43

NOTE 15: GUARANTEES AND INDEMNIFICATIONS

In conjunction with certain transactions, primarily the lease, sale or purchase of operating assets or services in the ordinary course of business, we may provide routine guarantees or indemnifications (e.g., environmental, fuel, tax and software infringement), the terms of which range in duration, and often they are not limited and have no specified maximum obligation. As a result, the overall maximum potential amount of the obligation under such guarantees and indemnifications cannot be reasonably estimated. Historically, we have not been required to make significant payments under our guarantee or indemnification obligations and no amounts have been recognized in our financial statements for the underlying fair value of these obligations.

Special facility revenue bonds have been issued by certain municipalities primarily to finance the acquisition and construction of various airport facilities and equipment. These facilities were leased to us and are accounted for as either capital leases or operating leases. FedEx Express has unconditionally guaranteed $667 million in principal of these bonds (with total future principal and interest payments of approximately $852 million as of May 31, 2012) through these leases. Of the $667 million bond principal guaranteed, $116 million was included in capital lease obligations in our balance sheet at May 31, 2012. The remaining $551 million has been accounted for as operating leases.

NOTE 16: COMMITMENTS

Annual purchase commitments under various contracts as of May 31, 2012 were as follows (in millions):

	Aircraft and Aircraft Related	Facilities and Other[1]	Total
2013	$ 965	$ 849	$ 1,814
2014	558	191	749
2015	824	139	963
2016	912	78	990
2017	1,009	52	1,061
Thereafter	5,166	134	5,300

(1) Primarily vehicles, facilities, advertising contracts and $550 million of quarterly contributions to our U.S. Pension Plans.

The amounts reflected in the table above for purchase commitments represent noncancelable agreements to purchase goods or services. As of May 31, 2012, our obligation to purchase 13 B777Fs was conditioned upon there being no event that causes FedEx Express or its employees not to be covered by the Railway Labor Act of 1926, as amended (RLA). Commitments to purchase aircraft in passenger configuration do not include the attendant costs to modify these aircraft for cargo transport unless we have entered into noncancelable commitments to modify such aircraft. Open purchase orders that are cancelable are not considered unconditional purchase obligations for financial reporting purposes and are not included in the table above.

In December 2011, FedEx Express entered into an agreement to acquire 27 new Boeing 767-300 Freighter (B767F) aircraft, with the first three arriving in 2014 followed by six per year from 2015 to 2018. In conjunction with the execution of the B767F aircraft purchase agreement, FedEx Express also delayed the delivery of nine B777F aircraft, five of which were deferred from 2014 and one per year from 2015 to 2018, to better align air network capacity to demand. FedEx Express also removed the RLA condition from two of the 15 B777F aircraft and exercised two B777F options for aircraft to be delivered at the end of the delivery schedule.

We had $661 million in deposits and progress payments as of May 31, 2012 on aircraft purchases and other planned aircraft-related transactions. These deposits are classified in the Other assets caption of our consolidated balance sheets. In addition to our commitment to purchase B777Fs and B767Fs, our aircraft purchase commitments include the Boeing 757 (B757) in passenger configuration, which will require additional costs to modify for cargo transport. Aircraft and aircraft-related contracts are subject to price escalations. The following table is a summary of the key aircraft we are committed to purchase as of May 31, 2012, with the year of expected delivery:

	B757	B767F	B777F	Total
2013	10		4	14
2014		3	2	5
2015		6	2	8
2016		6	2	8
2017		6	2	8
Thereafter		6	16	22
Total	10	27	28	65

On June 29, 2012, FedEx Express entered into a supplemental agreement to purchase nine additional B767F aircraft. Additionally, FedEx Express exercised ten B767F options available under the December 2011 agreement and purchased the right to 15 additional options. Four of these 19 additional B767F aircraft purchases are subject to the RLA condition. These 19 additional B767F aircraft are expected to be delivered from fiscal 2015 to 2019 and will replace current MD10-10 and A310-200 aircraft to continue to improve efficiency and technology of FedEx Express s aircraft fleet.

In conjunction with the additional B767F aircraft purchases, four currently contracted B777F aircraft deliveries that were subject to the RLA condition (two scheduled for delivery in fiscal 2016 and two scheduled for delivery in fiscal 2017) were converted to equivalent purchase value for B767F aircraft. With consideration of these two agreements, there are nine B777F purchase obligations subject to the RLA condition. These aircraft transactions are not included in the table above, as they occurred subsequent to May 31, 2012.

NOTE 17: CONTINGENCIES

Wage-and-Hour. We are a defendant in a number of lawsuits containing various class-action allegations of wage-and-hour violations. The plaintiffs in these lawsuits allege, among other things, that they were forced to work off the clock, were not paid overtime or were not provided work breaks or other benefits. The complaints generally seek unspecified monetary damages, injunctive relief, or both. We do not believe that a material loss is reasonably possible with respect to any of these matters.

Independent Contractor Lawsuits and State Administrative Proceedings. FedEx Ground is involved in numerous class-action lawsuits (including 30 that have been certified as class actions), individual lawsuits and state tax and other administrative proceedings that claim that the company s owner-operators should be treated as employees, rather than independent contractors.

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Most of the class-action lawsuits were consolidated for administration of the pre-trial proceedings by a single federal court, the U.S. District Court for the Northern District of Indiana. The multidistrict litigation court granted class certification in 28 cases and denied it in 14 cases. On December 13, 2010, the court entered an opinion and order addressing all outstanding motions for summary judgment on the status of the owner-operators (*i.e.,* independent contractor vs. employee). In sum, the court has now ruled on our summary judgment motions and entered judgment in favor of FedEx Ground on all claims in 20 of the 28 multidistrict litigation cases that had been certified as class actions, finding that the owner-operators in those cases were contractors as a matter of the law of the following states: Alabama, Arizona, Georgia, Indiana, Kansas (the court previously dismissed without prejudice the nationwide class claim under the Employee Retirement Income Security Act of 1974 based on the plaintiffs failure to exhaust administrative remedies), Louisiana, Maryland, Minnesota, New Jersey, New York, North Carolina, Ohio, Pennsylvania, Rhode Island, South Carolina, Tennessee, Texas, Utah, West Virginia and Wisconsin. The plaintiffs filed notices of appeal in all of these 20 cases. The Seventh Circuit heard the appeal in the Kansas case in January 2012 and, in July 2012, issued an opinion that did not make a determination with respect to the correctness of the district court s decision and, instead, certified two questions to the Kansas Supreme Court related to the classification of the plaintiffs as independent contractors under the Kansas Wage Payment Act.

The multidistrict litigation court remanded the other eight certified class actions back to the district courts where they were originally filed because its summary judgment ruling did not completely dispose of all of the claims in those lawsuits. Specifically, in the five cases in Arkansas, California, Florida, and Oregon (two certified cases), the court s ruling granted summary judgment in FedEx Ground s favor on all of the certified claims but did not decide the uncertified claims. In the three cases filed in Kentucky, Nevada and New Hampshire, the court ruled in favor of FedEx Ground on some of the claims and against FedEx Ground on at least one claim. In May 2012, the Oregon district court dismissed the two Oregon cases, but in June 2012, the plaintiffs in both cases filed notices of appeal with the Ninth Circuit Court of Appeals. In June 2012, the Kentucky district court ruled in favor of FedEx Ground on certain of the plaintiffs claims, thereby reducing our potential exposure in the matter.

In January 2008, one of the contractor-model lawsuits that is not part of the multidistrict litigation, *Anfinson v. FedEx Ground*, was certified as a class action by a Washington state court. The plaintiffs in *Anfinson* represent a class of single-route, pickup-and-delivery owner-operators in Washington from December 21, 2001 through December 31, 2005 and allege that the class members should be reimbursed as employees for their uniform expenses and should receive overtime pay. In March 2009, a jury trial in the *Anfinson* case was held, and the jury returned a verdict in favor of FedEx Ground, finding that all 320 class members were independent contractors, not employees. The plaintiffs appealed the verdict. In December 2010, the Washington Court of Appeals reversed and remanded for further proceedings, including a new trial. We filed a motion to reconsider, and this motion was denied. In March 2011, we filed a discretionary appeal with the Washington Supreme Court, and in August 2011, that petition was granted. The Washington Supreme Court heard oral arguments in February 2012.

In August 2010, another one of the contractor-model lawsuits that is not part of the multidistrict litigation, *Rascon v. FedEx Ground*, was certified as a class action by a Colorado state court. The plaintiff in *Rascon* represents a class of single-route, pickup-and-delivery owner-operators in Colorado who drove vehicles weighing less than 10,001 pounds at any time from August 27, 2005 through the present. The lawsuit seeks unpaid overtime compensation, and related penalties and attorneys fees and costs, under Colorado law. Our applications for appeal challenging this class certification decision have been rejected. We settled this matter for an immaterial amount, subject to court approval, in June 2012.

Other contractor-model cases that are not or are no longer part of the multidistrict litigation are in varying stages of litigation.

With respect to the state administrative proceedings relating to the classification of FedEx Ground s owner-operators as independent contractors, during the second quarter of 2011, the attorneys general in New York and Kentucky each filed lawsuits against FedEx Ground challenging the validity of the contractor model. In January 2012, FedEx Ground settled the lawsuit filed by the Kentucky Attorney General for an immaterial amount, and in April 2012, the lawsuit was dismissed.

While the granting of summary judgment in favor of FedEx Ground by the multidistrict litigation court in 20 of the 28 cases that had been certified as class actions remains subject to appeal, we believe that it significantly improves the likelihood that our independent contractor model will be upheld. Adverse determinations in matters related to FedEx Ground s independent contractors, however,

could, among other things, entitle certain of our contractors and their drivers to the reimbursement of certain expenses and to the benefit of wage-and-hour laws and result in employment and withholding tax and benefit liability for FedEx Ground, and could result in changes to the independent contractor status of FedEx Ground s owner-operators in certain jurisdictions. We believe that FedEx Ground s owner-operators are properly classified as independent contractors and that FedEx Ground is not an employer of the drivers of the company s independent contractors. While it is reasonably possible that potential loss in some of these lawsuits or such changes to the independent contractor status of FedEx Ground s owner-operators could be material, we cannot yet determine the amount or reasonable range of potential loss. A number of factors contribute to this. The number of plaintiffs in these lawsuits continues to change, with some being dismissed and others being added and, as to new plaintiffs, discovery is still ongoing. In addition, the parties have not yet conducted any discovery into damages, which could vary considerably from plaintiff to plaintiff. Further, the range of potential loss could be impacted considerably by future rulings on the merits of certain claims and FedEx Ground s various defenses, and on evidentiary issues. In any event, we do not believe that a material loss is probable in these matters.

ATA Airlines. In October 2010, a jury returned a verdict in favor of ATA Airlines in its breach of contract lawsuit against FedEx Express and awarded damages of $66 million, and in January 2011, the court awarded ATA pre-judgment interest of $5 million. In December 2011, the Seventh Circuit overturned the entire judgment entered against FedEx Express. ATA Airlines requested the Seventh Circuit to rehear oral argument on appeal, and in February 2012, the Seventh Circuit denied the request. We have reversed the $66 million accrual established in the second quarter of 2011. After the Seventh Circuit denied ATA Airlines request for the Seventh Circuit to rehear oral argument on appeal, ATA Airlines asked the U.S. Supreme Court to accept a discretionary appeal of the matter. We believe that it is unlikely that the U.S. Supreme Court will accept the discretionary appeal.

California Paystub Class Action. A federal court in California ruled in April 2011 that paystubs for certain FedEx Express employees in California did not meet that state s requirements to reflect pay period begin date, total overtime hours worked and the correct overtime wage rate. The ruling came in a class action lawsuit filed by a former courier seeking damages on behalf of herself and all other FedEx Express employees in California that allegedly received noncompliant paystubs. The court certified the class in June 2011. The court ruled that FedEx Express was liable to the State of California and was prepared to rule as to whether FedEx Express was liable to class members who could prove they were injured by the paystub deficiencies. The judge did not decide on the amount, if any, of liability to the State of California or to the class, but had wide discretion. Prior to any decision on the amount of liability, we reached an agreement to settle this matter for an immaterial amount in October 2011, subject to approval by the court. The court granted final approval of the settlement in July 2012.

Other Matters. In August 2010, a third-party consultant who works with shipping customers to negotiate lower rates filed a lawsuit in federal district court in California against FedEx and UPS alleging violations of U.S. antitrust law. This matter was dismissed in May 2011, but the court granted the plaintiff permission to file an amended complaint, which FedEx received in June 2011. In November 2011, the court granted our motion to dismiss this complaint, but again allowed the plaintiff to file an amended complaint. The plaintiff filed a new complaint in December 2011, and the matter remains pending before the court. In February 2011, shortly after the initial lawsuit was filed, we received a demand for the production of information and documents in connection with a civil investigation by the U.S. Department of Justice (DOJ) into the policies and practices of FedEx and UPS for dealing with third-party consultants who work with shipping customers to negotiate lower rates. We are cooperating with the investigation, do not believe that we have engaged in any anti-competitive activities and will vigorously defend ourselves in any action that may result from the investigation. While the litigation proceedings and the DOJ investigation are in an early stage and the amount of loss, if any, is dependent on a number of factors that are not yet fully developed or resolved, we do not believe that a material loss is reasonably possible.

We have received requests for information from the DOJ in the Northern District of California in connection with a criminal investigation relating to the transportation of packages for online pharmacies that may have shipped pharmaceuticals in violation of federal law. We responded to grand jury subpoenas issued in June 2008 and August 2009 and to additional requests for information pursuant to those subpoenas, and we continue to respond and cooperate with the investigation. We do not believe that we have engaged in any illegal activities and will vigorously defend ourselves in any action that may result from the investigation. We cannot estimate the amount or range of loss, if any, in this matter, as such analysis would depend on facts and law that are not yet fully developed or resolved.

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FedEx and its subsidiaries are subject to other legal proceedings that arise in the ordinary course of their business. In the opinion of management, the aggregate liability, if any, with respect to these other actions will not have a material adverse effect on our financial position, results of operations or cash flows.

NOTE 18: RELATED PARTY TRANSACTIONS

Our Chairman, President and Chief Executive Officer, Frederick W. Smith, currently holds an approximate 10% ownership interest in the National Football League Washington Redskins professional football team (Redskins) and is a member of its board of directors. FedEx has a multi-year naming rights agreement with the Redskins granting us certain marketing rights, including the right to name the Redskins stadium FedExField.

NOTE 19: SUMMARY OF QUARTERLY OPERATING RESULTS (UNAUDITED)

(in millions, except per share amounts)	First Quarter	Second Quarter	Third Quarter	Fourth Quarter
2012[1]				
Revenues	$ 10,521	$ 10,587	$ 10,564	$ 11,008
Operating income	737	780	813	856
Net income	464	497	521	550
Basic earnings per common share[2]	1.46	1.57	1.66	1.74
Diluted earnings per common share	1.46	1.57	1.65	1.73
2011[3]				
Revenues	$ 9,457	$ 9,632	$ 9,663	$ 10,552
Operating income	628	469	393	888
Net income	380	283	231	558
Basic earnings per common share[2]	1.21	0.90	0.73	1.76
Diluted earnings per common share	1.20	0.89	0.73	1.75

(1) The fourth quarter of 2012 includes an impairment charge of $134 million resulting from the decision to retire 24 aircraft and related engines at FedEx Express. The third quarter of 2012 includes the reversal of a $66 million legal reserve associated with the ATA Airlines lawsuit.

(2) The sum of the quarterly earnings per share may not equal annual amounts due to differences in the weighted-average number of shares outstanding during the respective period.

(3) The second quarter of 2011 includes a $66 million legal reserve associated with the ATA Airlines lawsuit. Costs related to the combination of our FedEx Freight and FedEx National LTL operations in 2011 were $86 million in the second quarter and $43 million in the third quarter.

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NOTE 20: CONDENSED CONSOLIDATING FINANCIAL STATEMENTS

We are required to present condensed consolidating financial information in order for the subsidiary guarantors (other than FedEx Express) of our public debt to continue to be exempt from reporting under the Securities Exchange Act of 1934, as amended.

The guarantor subsidiaries, which are wholly owned by FedEx, guarantee $1 billion of our debt. The guarantees are full and unconditional and joint and several. Our guarantor subsidiaries were not determined using geographic, service line or other similar criteria, and as a result, the Guarantor Subsidiaries and Non-guarantor Subsidiaries columns each include portions of our domestic and international operations. Accordingly, this basis of presentation is not intended to present our financial condition, results of operations or cash flows for any purpose other than to comply with the specific requirements for subsidiary guarantor reporting.

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Condensed consolidating financial statements for our guarantor subsidiaries and non-guarantor subsidiaries are presented in the following tables (in millions):

CONDENSED CONSOLIDATING BALANCE SHEETS

May 31, 2012

	Parent	Guarantor Subsidiaries	Non-guarantor Subsidiaries	Eliminations	Consolidated
ASSETS					
CURRENT ASSETS					
Cash and cash equivalents	$ 1,906	$ 417	$ 636	$ (116)	$ 2,843
Receivables, less allowances	3	3,793	943	(35)	4,704
Spare parts, supplies, fuel, prepaid expenses and other, less allowances	261	671	44		976
Deferred income taxes		514	19		533
Total current assets	2,170	5,395	1,642	(151)	9,056
PROPERTY AND EQUIPMENT, AT COST	29	34,301	1,834		36,164
Less accumulated depreciation and amortization	20	17,822	1,074		18,916
Net property and equipment	9	16,479	760		17,248
INTERCOMPANY RECEIVABLE		323	1,524	(1,847)	
GOODWILL		1,553	834		2,387
INVESTMENT IN SUBSIDIARIES	17,163	2,978		(20,141)	
OTHER ASSETS	2,845	1,099	86	(2,818)	1,212
	$ 22,187	$ 27,827	$ 4,846	$ (24,957)	$ 29,903
LIABILITIES AND STOCKHOLDERS INVESTMENT					
CURRENT LIABILITIES					
Current portion of long-term debt	$	$ 417	$	$	$ 417
Accrued salaries and employee benefits	83	1,365	187		1,635
Accounts payable	6	1,276	482	(151)	1,613
Accrued expenses	184	1,406	119		1,709
Total current liabilities	273	4,464	788	(151)	5,374
LONG-TERM DEBT, LESS CURRENT PORTION	1,000	250			1,250
INTERCOMPANY PAYABLE	1,847			(1,847)	
OTHER LONG-TERM LIABILITIES					
Deferred income taxes		3,649	5	(2,818)	836
Other liabilities	4,341	3,193	182		7,716
Total other long-term liabilities	4,341	6,842	187	(2,818)	8,552
STOCKHOLDERS INVESTMENT	14,726	16,271	3,871	(20,141)	14,727
	$ 22,187	$ 27,827	$ 4,846	$ (24,957)	$ 29,903

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CONDENSED CONSOLIDATING BALANCE SHEETS

May 31, 2011

	Parent	Guarantor Subsidiaries	Non-guarantor Subsidiaries	Eliminations	Consolidated
ASSETS					
CURRENT ASSETS					
Cash and cash equivalents	$ 1,589	$ 279	$ 546	$ (86)	$ 2,328
Receivables, less allowances		3,696	912	(27)	4,581
Spare parts, supplies, fuel, prepaid expenses and other, less allowances	77	645	44		766
Deferred income taxes		598	12		610
Total current assets	1,666	5,218	1,514	(113)	8,285
PROPERTY AND EQUIPMENT, AT COST	24	31,916	1,746		33,686
Less accumulated depreciation and amortization	18	17,071	1,054		18,143
Net property and equipment	6	14,845	692		15,543
INTERCOMPANY RECEIVABLE			1,317	(1,317)	
GOODWILL		1,564	762		2,326
INVESTMENT IN SUBSIDIARIES	15,404	2,705		(18,109)	
OTHER ASSETS	1,652	1,039	63	(1,523)	1,231
	$ 18,728	$ 25,371	$ 4,348	$ (21,062)	$ 27,385
LIABILITIES AND STOCKHOLDERS INVESTMENT					
CURRENT LIABILITIES					
Current portion of long-term debt	$	$ 18	$	$	$ 18
Accrued salaries and employee benefits	50	1,071	147		1,268
Accounts payable		1,385	430	(113)	1,702
Accrued expenses	198	1,563	133		1,894
Total current liabilities	248	4,037	710	(113)	4,882
LONG-TERM DEBT, LESS CURRENT PORTION	1,000	667			1,667
INTERCOMPANY PAYABLE	1,095	222		(1,317)	
OTHER LONG-TERM LIABILITIES					
Deferred income taxes		2,842	17	(1,523)	1,336
Other liabilities	1,165	3,001	114		4,280
Total other long-term liabilities	1,165	5,843	131	(1,523)	5,616
STOCKHOLDERS INVESTMENT	15,220	14,602	3,507	(18,109)	15,220
	$ 18,728	$ 25,371	$ 4,348	$ (21,062)	$ 27,385

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CONDENSED CONSOLIDATING STATEMENTS OF INCOME

Year Ended May 31, 2012

	Parent	Guarantor Subsidiaries	Non-guarantor Subsidiaries	Eliminations	Consolidated
REVENUES	$	$ 36,412	$ 6,569	$ (301)	$ 42,680
OPERATING EXPENSES:					
Salaries and employee benefits	114	14,153	1,832		16,099
Purchased transportation		4,509	1,944	(118)	6,335
Rentals and landing fees	5	2,221	267	(6)	2,487
Depreciation and amortization	1	1,962	150		2,113
Fuel		4,877	79		4,956
Maintenance and repairs	1	1,882	97		1,980
Impairment and other charges		134			134
Intercompany charges, net	(218)	(323)	541		
Other	97	4,482	988	(177)	5,390
		33,897	5,898	(301)	39,494
OPERATING INCOME		2,515	671		3,186
OTHER INCOME (EXPENSE):					
Equity in earnings of subsidiaries	2,032	395		(2,427)	
Interest, net	(75)	31	5		(39)
Intercompany charges, net	80	(102)	22		
Other, net	(5)	(10)	9		(6)
INCOME BEFORE INCOME TAXES	2,032	2,829	707	(2,427)	3,141
Provision for income taxes		875	234		1,109
NET INCOME	$ 2,032	$ 1,954	$ 473	$ (2,427)	$ 2,032

CONDENSED CONSOLIDATING STATEMENTS OF INCOME

Year Ended May 31, 2011

	Parent	Guarantor Subsidiaries	Non-guarantor Subsidiaries	Eliminations	Consolidated
REVENUES	$	$ 33,124	$ 6,498	$ (318)	$ 39,304
OPERATING EXPENSES:					
Salaries and employee benefits	109	13,206	1,961		15,276
Purchased transportation		4,034	1,745	(105)	5,674
Rentals and landing fees	4	2,209	253	(4)	2,462
Depreciation and amortization	1	1,784	188		1,973
Fuel		4,003	148		4,151
Maintenance and repairs	1	1,862	116		1,979
Impairment and other charges		28	61		89
Intercompany charges, net	(222)	(317)	539		
Other	107	4,392	1,032	(209)	5,322

		31,201	6,043	(318)	36,926
OPERATING INCOME		1,923	455		2,378
OTHER INCOME (EXPENSE):					
Equity in earnings of subsidiaries	1,452	200		(1,652)	
Interest, net	(88)	13	(2)		(77)
Intercompany charges, net	104	(135)	31		
Other, net	(16)	(14)	(6)		(36)
INCOME BEFORE INCOME TAXES	1,452	1,987	478	(1,652)	2,265
Provision for income taxes		677	136		813
NET INCOME	$ 1,452	$ 1,310	$ 342	$ (1,652)	$ 1,452

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CONDENSED CONSOLIDATING STATEMENTS OF INCOME

Year Ended May 31, 2010

	Parent	Guarantor Subsidiaries	Non-guarantor Subsidiaries	Eliminations	Consolidated
REVENUES	$	$ 29,360	$ 5,700	$ (326)	$ 34,734
OPERATING EXPENSES:					
Salaries and employee benefits	91	12,026	1,910		14,027
Purchased transportation		3,424	1,392	(88)	4,728
Rentals and landing fees	4	2,118	240	(3)	2,359
Depreciation and amortization	1	1,751	206		1,958
Fuel		2,946	160		3,106
Maintenance and repairs	1	1,589	125		1,715
Impairment and other charges			18		18
Intercompany charges, net	(202)	(109)	311		
Other	105	3,950	1,005	(235)	4,825
		27,695	5,367	(326)	32,736
OPERATING INCOME		1,665	333		1,998
OTHER INCOME (EXPENSE):					
Equity in earnings of subsidiaries	1,184	161		(1,345)	
Interest, net	(100)	41	(12)		(71)
Intercompany charges, net	114	(147)	33		
Other, net	(14)	(18)	(1)		(33)
INCOME BEFORE INCOME TAXES	1,184	1,702	353	(1,345)	1,894
Provision for income taxes		625	85		710
NET INCOME	$ 1,184	$ 1,077	$ 268	$ (1,345)	$ 1,184

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CONDENSED CONSOLIDATING STATEMENTS OF CASH FLOWS

Year Ended May 31, 2012

	Parent	Guarantor Subsidiaries	Non-guarantor Subsidiaries	Eliminations	Consolidated
CASH PROVIDED BY (USED IN) OPERATING ACTIVITIES	$ (88)	$ 4,383	$ 570	$ (30)	$ 4,835
INVESTING ACTIVITIES					
Capital expenditures	(5)	(3,792)	(210)		(4,007)
Business acquisition, net of cash acquired			(116)		(116)
Proceeds from asset dispositions and other		74			74
CASH USED IN INVESTING ACTIVITIES	(5)	(3,718)	(326)		(4,049)
FINANCING ACTIVITIES					
Net transfers from (to) Parent	625	(550)	(75)		
Intercompany dividends		76	(76)		
Principal payments on debt		(29)			(29)
Proceeds from stock issuances	128				128
Excess tax benefit on the exercise of stock options	18				18
Dividends paid	(164)				(164)
Purchase of treasury stock	(197)				(197)
Other, net		(19)	19		
CASH (USED IN) PROVIDED BY FINANCING ACTIVITIES	410	(522)	(132)		(244)
Effect of exchange rate changes on cash		(5)	(22)		(27)
Net increase (decrease) in cash and cash equivalents	317	138	90	(30)	515
Cash and cash equivalents at beginning of period	1,589	279	546	(86)	2,328
Cash and cash equivalents at end of period	$ 1,906	$ 417	$ 636	$ (116)	$ 2,843

CONDENSED CONSOLIDATING STATEMENTS OF CASH FLOWS

Year Ended May 31, 2011

	Parent	Guarantor Subsidiaries	Non-guarantor Subsidiaries	Eliminations	Consolidated
CASH PROVIDED BY (USED IN) OPERATING ACTIVITIES	$ 25	$ 3,978	$ 65	$ (27)	$ 4,041
INVESTING ACTIVITIES					
Capital expenditures	(1)	(3,263)	(170)		(3,434)
Business acquisition, net of cash acquired		(96)			(96)
Proceeds from asset dispositions and other		110	1		111
CASH USED IN INVESTING ACTIVITIES	(1)	(3,249)	(169)		(3,419)
FINANCING ACTIVITIES					
Net transfers from (to) Parent	530	(994)	464		
Payment on loan between subsidiaries		235	(235)		
Intercompany dividends		61	(61)		
Principal payments on debt	(250)	(12)			(262)

Proceeds from stock issuances		108							108
Excess tax benefit on the exercise of stock options		23							23
Dividends paid		(151)							(151)
Other, net		(5)		(9)		9				(5)
CASH (USED IN) PROVIDED BY FINANCING ACTIVITIES		255		(719)		177				(287)
Effect of exchange rate changes on cash				11		30				41
Net increase (decrease) in cash and cash equivalents		279		21		103		(27)		376
Cash and cash equivalents at beginning of period		1,310		258		443		(59)		1,952
Cash and cash equivalents at end of period	$	1,589	$	279	$	546	$	(86)	$	2,328

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CONDENSED CONSOLIDATING STATEMENTS OF CASH FLOWS

Year Ended May 31, 2010

	Parent	Guarantor Subsidiaries	Non-guarantor Subsidiaries	Eliminations	Consolidated
CASH PROVIDED BY (USED IN) OPERATING ACTIVITIES	$ (450)	$ 2,942	$ 653	$ (7)	$ 3,138
INVESTING ACTIVITIES					
Capital expenditures		(2,661)	(155)		(2,816)
Proceeds from asset dispositions and other		38	(3)		35
CASH USED IN INVESTING ACTIVITIES		(2,623)	(158)		(2,781)
FINANCING ACTIVITIES					
Net transfers from (to) Parent	531	(397)	(134)		
Payment on loan between subsidiaries		72	(72)		
Intercompany dividends		158	(158)		
Principal payments on debt	(500)	(153)			(653)
Proceeds from stock issuances	94				94
Excess tax benefit on the exercise of stock options	25				25
Dividends paid	(138)				(138)
Other, net	(20)	(5)	5		(20)
CASH USED IN FINANCING ACTIVITIES	(8)	(325)	(359)		(692)
Effect of exchange rate changes on cash		(8)	3		(5)
Net (decrease) increase in cash and cash equivalents	(458)	(14)	139	(7)	(340)
Cash and cash equivalents at beginning of period	1,768	272	304	(52)	2,292
Cash and cash equivalents at end of period	$ 1,310	$ 258	$ 443	$ (59)	$ 1,952

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QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

INTEREST RATES. While we currently have market risk sensitive instruments related to interest rates, we have no significant exposure to changing interest rates on our long-term debt because the interest rates are fixed on all of our long-term debt. As disclosed in Note 6 to the accompanying consolidated financial statements, we had outstanding fixed-rate, long-term debt (exclusive of capital leases) with estimated fair values of $2.0 billion at May 31, 2012 and $1.9 billion at May 31, 2011. Market risk for fixed-rate, long-term debt is estimated as the potential decrease in fair value resulting from a hypothetical 10% increase in interest rates and amounts to $30 million as of May 31, 2012 and $36 million as of May 31, 2011. The underlying fair values of our long-term debt were estimated based on quoted market prices or on the current rates offered for debt with similar terms and maturities.

We have interest rate risk with respect to our pension and postretirement benefit obligations. Changes in interest rates impact our liabilities associated with these benefit plans as well as the amount of pension and postretirement benefit expense recognized. Declines in the value of plan assets could diminish the funded status of our pension plans and potentially increase our requirement to make contributions to the plans. Substantial investment losses on plan assets will also increase pension and postretirement benefit expense in the years following the losses.

FOREIGN CURRENCY. While we are a global provider of transportation, e-commerce and business services, the substantial majority of our transactions are denominated in U.S. dollars. The principal foreign currency exchange rate risks to which we are exposed are in the British pound, Canadian dollar, Chinese yuan, euro, Hong Kong dollar and Japanese yen. Historically, our exposure to foreign currency fluctuations is more significant with respect to our revenues than our expenses, as a significant portion of our expenses are denominated in U.S. dollars, such as aircraft and fuel expenses. During 2012 and 2011, foreign currency fluctuations positively impacted operating income. However, favorable foreign currency fluctuations also may have had an offsetting impact on the price we obtained or the demand for our services, which is not quantifiable. At May 31, 2012, the result of a uniform 10% strengthening in the value of the dollar relative to the currencies in which our transactions are denominated would result in a decrease in operating income of $75 million for 2013. This theoretical calculation assumes that each exchange rate would change in the same direction relative to the U.S. dollar. This calculation is not indicative of our actual experience in foreign currency transactions. In addition to the direct effects of changes in exchange rates, fluctuations in exchange rates also affect the volume of sales or the foreign currency sales price as competitors services become more or less attractive. The sensitivity analysis of the effects of changes in foreign currency exchange rates does not factor in a potential change in sales levels or local currency prices.

COMMODITY. While we have market risk for changes in the price of jet and vehicle fuel, this risk is largely mitigated by our fuel surcharges because our fuel surcharges are closely linked to market prices for fuel. Therefore, a hypothetical 10% change in the price of fuel would not be expected to materially affect our earnings.

However, our fuel surcharges have a timing lag (approximately six to eight weeks for FedEx Express and FedEx Ground) before they are adjusted for changes in fuel prices. Our fuel surcharge index also allows fuel prices to fluctuate approximately 2% for FedEx Express and approximately 4% for FedEx Ground before an adjustment to the fuel surcharge occurs. Accordingly, our operating income in a specific period may be significantly affected should the spot price of fuel suddenly change by a substantial amount or change by amounts that do not result in an adjustment in our fuel surcharges.

OTHER. We do not purchase or hold any derivative financial instruments for trading purposes.

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SELECTED FINANCIAL DATA

The following table sets forth (in millions, except per share amounts and other operating data) certain selected consolidated financial and operating data for FedEx as of and for the five years ended May 31, 2012. This information should be read in conjunction with the Consolidated Financial Statements, MD&A and other financial data appearing elsewhere in this Annual Report.

	2012[1]	2011[2]	2010	2009[3]	2008[4]
Operating Results					
Revenues	$ 42,680	$ 39,304	$ 34,734	$ 35,497	$ 37,953
Operating income	3,186	2,378	1,998	747	2,075
Income before income taxes	3,141	2,265	1,894	677	2,016
Net income	2,032	1,452	1,184	98	1,125
Per Share Data					
Earnings per share:					
Basic	$ 6.44	$ 4.61	$ 3.78	$ 0.31	$ 3.64
Diluted	$ 6.41	$ 4.57	$ 3.76	$ 0.31	$ 3.60
Average shares of common stock outstanding	315	315	312	311	309
Average common and common equivalent shares outstanding	317	317	314	312	312
Cash dividends declared	$ 0.52	$ 0.48	$ 0.44	$ 0.44	$ 0.30
Financial Position					
Property and equipment, net	$ 17,248	$ 15,543	$ 14,385	$ 13,417	$ 13,478
Total assets	29,903	27,385	24,902	24,244	25,633
Long-term debt, less current portion	1,250	1,667	1,668	1,930	1,506
Common stockholders investment	14,727	15,220	13,811	13,626	14,526
Other Operating Data					
FedEx Express aircraft fleet	660	688	667	654	677

(1) Results for 2012 include a $134 million ($84 million, net of tax or $0.26 per share) impairment charge resulting from the decision to retire 24 aircraft and related engines at FedEx Express and the reversal of a $66 million legal reserve associated with the ATA Airlines lawsuit which was initially recorded in the second quarter of 2011. See Notes 1 and 17 to the accompanying consolidated financial statements.

(2) Results for 2011 include charges of approximately $199 million ($104 million, net of tax and applicable variable incentive compensation impacts, or $0.33 per diluted share) for the combination of our FedEx Freight and FedEx National LTL operations and a reserve associated with a legal matter at FedEx Express. See Notes 1 and 17 to the accompanying consolidated financial statements.

(3) Results for 2009 include a charge of $1.2 billion ($1.1 billion, net of tax, or $3.45 per diluted share) primarily for impairment charges associated with goodwill and aircraft. Additionally, common stockholders investment includes an other comprehensive income charge of $1.2 billion, net of tax, for the funded status of our retirement plans at May 31, 2009.

(4) Results for 2008 include a charge of $891 million ($696 million, net of tax, or $2.23 per diluted share) recorded during the fourth quarter, predominantly for impairment charges associated with intangible assets from the FedEx Office acquisition. Additionally, results for 2008 include several 2007 acquisitions.

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REPORT OF INDEPENDENT REGISTERED

PUBLIC ACCOUNTING FIRM

The Board of Directors and Stockholders

FedEx Corporation

We have audited the consolidated financial statements of FedEx Corporation as of May 31, 2012 and 2011, and for each of the three years in the period ended May 31, 2012, and have issued our report thereon dated July 16, 2012 (included elsewhere in this Annual Report on Form 10-K). Our audits also included the financial statement schedule listed in Item 15(a) in this Annual Report on Form 10-K. This schedule is the responsibility of the Company s management. Our responsibility is to express an opinion based on our audits.

In our opinion, the financial statement schedule referred to above, when considered in relation to the basic financial statements taken as a whole, presents fairly in all material respects the information set forth therein.

/s/ Ernst & Young LLP

Memphis, Tennessee

July 16, 2012

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SCHEDULE II

FEDEX CORPORATION

VALUATION AND QUALIFYING ACCOUNTS

FOR THE YEARS ENDED MAY 31, 2012, 2011, AND 2010

(IN MILLIONS)

DESCRIPTION	BALANCE AT BEGINNING OF YEAR	ADDITIONS CHARGED TO EXPENSES	ADDITIONS CHARGED TO OTHER ACCOUNTS	DEDUCTIONS	BALANCE AT END OF YEAR
Accounts Receivable Reserves:					
Allowance for Doubtful Accounts					
2012	$ 97	$ 160	$	$ 163(a)	$ 94
2011	93	152		148(a)	97
2010	114	124		145(a)	93
Allowance for Revenue Adjustments					
2012	$ 85	$	$ 570(b)	$ 571(c)	$ 84
2011	73		532(b)	520(c)	85
2010	82		430(b)	439(c)	73
Inventory Valuation Allowance:					
2012	$ 169	$ 15	$	$	$ 184
2011	170	13		14	169
2010	175	12		17	170

(a) Uncollectible accounts written off, net of recoveries.

(b) Principally charged against revenue.

(c) Service failures, rebills and other.

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FEDEX CORPORATION

COMPUTATION OF RATIO OF EARNINGS TO FIXED CHARGES

(UNAUDITED)

(IN MILLIONS, EXCEPT RATIOS)

	Year Ended May 31,				
	2012	2011	2010	2009	2008
Earnings:					
Income before income taxes	$ 3,141	$ 2,265	$ 1,894	$ 677	$ 2,016
Add back:					
Interest expense, net of capitalized interest	52	86	79	85	98
Amortization of debt issuance costs	5	16	14	5	5
Portion of rent expense representative of interest factor	797	852	806	795	784
Earnings as adjusted	$ 3,995	$ 3,219	$ 2,793	$ 1,562	$ 2,903
Fixed Charges:					
Interest expense, net of capitalized interest	$ 52	$ 86	$ 79	$ 85	$ 98
Capitalized interest	85	71	80	71	50
Amortization of debt issuance costs	5	16	14	5	5
Portion of rent expense representative of interest factor	797	852	806	795	784
	$ 939	$ 1,025	$ 979	$ 956	$ 937
Ratio of Earnings to Fixed Charges	4.3	3.1	2.9	1.6	3.1

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EXHIBIT INDEX

Exhibit Number	Description of Exhibit
	Certificate of Incorporation and Bylaws
3.1	Third Amended and Restated Certificate of Incorporation of FedEx. (Filed as Exhibit 3.1 to FedEx s Current Report on Form 8-K dated September 26, 2011 and filed September 28, 2011, and incorporated herein by reference.)
3.2	Amended and Restated Bylaws of FedEx. (Filed as Exhibit 3.3 to FedEx s Current Report on Form 8-K dated September 26, 2011 and filed September 28, 2011, and incorporated herein by reference.)
	Facility Lease Agreements
10.1	Composite Lease Agreement dated May 21, 2007 (but effective as of January 1, 2007) between the Memphis-Shelby County Airport Authority (the Authority) and FedEx Express. (Filed as Exhibit 10.1 to FedEx s FY07 Annual Report on Form 10-K, and incorporated herein by reference.)
10.2	First Amendment dated December 29, 2009 (but effective as of September 1, 2008) to the Composite Lease Agreement dated May 21, 2007 (but effective as of January 1, 2007) between the Authority and FedEx Express. (Filed as Exhibit 10.1 to FedEx s FY10 Third Quarter Report on Form 10-Q, and incorporated herein by reference.)
10.3	Second Amendment dated March 30, 2010 (but effective as of June 1, 2009) and Third Amendment dated April 27, 2010 (but effective as of July 1, 2009), each amending the Composite Lease Agreement dated May 21, 2007 (but effective as of January 1, 2007) between the Authority and FedEx Express. (Filed as Exhibit 10.3 to FedEx s FY10 Annual Report on Form 10-K, and incorporated herein by reference.)
10.4	Fourth Amendment dated December 22, 2011 (but effective as of December 15, 2011) to the Composite Lease Agreement dated May 21, 2007 (but effective as of January 1, 2007) between the Authority and FedEx Express. (Filed as Exhibit 10.4 to FedEx s FY12 Third Quarter Report on Form 10-Q, and incorporated herein by reference.)
10.5	Special Facility Lease Agreement dated as of August 1, 1979 between the Authority and FedEx Express. (Filed as Exhibit 10.15 to FedEx Express s FY90 Annual Report on Form 10-K, and incorporated herein by reference.)
10.6	First Special Facility Supplemental Lease Agreement dated as of May 1, 1982 between the Authority and FedEx Express. (Filed as Exhibit 10.25 to FedEx Express s FY93 Annual Report on Form 10-K, and incorporated herein by reference.)
10.7	Second Special Facility Supplemental Lease Agreement dated as of November 1, 1982 between the Authority and FedEx Express. (Filed as Exhibit 10.26 to FedEx Express s FY93 Annual Report on Form 10-K, and incorporated herein by reference.)
10.8	Third Special Facility Supplemental Lease Agreement dated as of December 1, 1984 between the Authority and FedEx Express. (Filed as Exhibit 10.25 to FedEx Express s FY95 Annual Report on Form 10-K, and incorporated herein by reference.)

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Exhibit Number	Description of Exhibit
10.9	Fourth Special Facility Supplemental Lease Agreement dated as of July 1, 1992 between the Authority and FedEx Express. (Filed as Exhibit 10.20 to FedEx Express s FY92 Annual Report on Form 10-K, and incorporated herein by reference.)
10.10	Fifth Special Facility Supplemental Lease Agreement dated as of July 1, 1997 between the Authority and FedEx Express. (Filed as Exhibit 10.35 to FedEx Express s FY97 Annual Report on Form 10-K, and incorporated herein by reference.)
10.11	Sixth Special Facility Supplemental Lease Agreement dated as of December 1, 2001 between the Authority and FedEx Express. (Filed as Exhibit 10.28 to FedEx s FY02 Annual Report on Form 10-K, and incorporated herein by reference.)
10.12	Seventh Special Facility Supplemental Lease Agreement dated as of June 1, 2002 between the Authority and FedEx Express. (Filed as Exhibit 10.3 to FedEx s FY03 First Quarter Report on Form 10-Q, and incorporated herein by reference.)
10.13	Special Facility Lease Agreement dated as of July 1, 1993 between the Authority and FedEx Express. (Filed as Exhibit 10.29 to FedEx Express s FY93 Annual Report on Form 10-K, and incorporated herein by reference.)
10.14	Special Facility Ground Lease Agreement dated as of July 1, 1993 between the Authority and FedEx Express. (Filed as Exhibit 10.30 to FedEx Express s FY93 Annual Report on Form 10-K, and incorporated herein by reference.)
10.15	First Amendment dated December 29, 2009 (but effective as of September 1, 2008) to the Special Facility Ground Lease Agreement dated as of July 1, 1993 between the Authority and FedEx Express. (Filed as Exhibit 10.2 to FedEx s FY10 Third Quarter Report on Form 10-Q, and incorporated herein by reference.)
	Aircraft-Related Agreements
10.16	Boeing 777 Freighter Purchase Agreement dated as of November 7, 2006 between The Boeing Company and FedEx Express. Confidential treatment has been granted for confidential commercial and financial information, pursuant to Rule 24b-2 under the Securities Exchange Act of 1934, as amended. (Filed as Exhibit 10.1 to FedEx s FY07 Second Quarter Report on Form 10-Q, and incorporated herein by reference.)
10.17	Supplemental Agreement No. 1 dated as of June 16, 2008 to the Boeing 777 Freighter Purchase Agreement dated as of November 7, 2006 between The Boeing Company and FedEx Express. (Filed as Exhibit 10.13 to FedEx s FY08 Annual Report on Form 10-K, and incorporated herein by reference.)
10.18	Supplemental Agreement No. 2 dated as of July 14, 2008 to the Boeing 777 Freighter Purchase Agreement dated as of November 7, 2006 between The Boeing Company and FedEx Express. (Filed as Exhibit 10.3 to FedEx s FY09 Second Quarter Report on Form 10-Q, and incorporated herein by reference.)
10.19	Supplemental Agreement No. 3 dated as of December 15, 2008 (and related side letters) to the Boeing 777 Freighter Purchase Agreement dated as of November 7, 2006 between The Boeing Company and FedEx Express. Confidential treatment has been granted for confidential commercial and financial information, pursuant to Rule 24b-2 under the Securities Exchange Act of 1934, as amended. (Filed as Exhibit 10.4 to FedEx s FY09 Second Quarter Report on Form 10-Q, and incorporated herein by reference.)

Exhibit Number	Description of Exhibit
10.20	Supplemental Agreement No. 4 dated as of January 9, 2009 (and related side letters) to the Boeing 777 Freighter Purchase Agreement dated as of November 7, 2006 between The Boeing Company and FedEx Express. Confidential treatment has been granted for confidential commercial and financial information, pursuant to Rule 24b-2 under the Securities Exchange Act of 1934, as amended. (Filed as Exhibit 10.1 to FedEx s FY09 Third Quarter Report on Form 10-Q, and incorporated herein by reference.)
10.21	Side letters dated May 29, 2009 and May 19, 2009, amending the Boeing 777 Freighter Purchase Agreement dated as of November 7, 2006 between The Boeing Company and FedEx Express. Confidential treatment has been granted for confidential commercial and financial information, pursuant to Rule 24b-2 under the Securities Exchange Act of 1934, as amended. (Filed as Exhibit 10.17 to FedEx s FY09 Annual Report on Form 10-K, and incorporated herein by reference.)
10.22	Supplemental Agreement No. 5 dated as of January 11, 2010 to the Boeing 777 Freighter Purchase Agreement dated as of November 7, 2006 between The Boeing Company and FedEx Express. Confidential treatment has been granted for confidential commercial and financial information, pursuant to Rule 24b-2 under the Securities Exchange Act of 1934, as amended. (Filed as Exhibit 10.3 to FedEx s FY10 Third Quarter Report on Form 10-Q, and incorporated herein by reference.)
10.23	Supplemental Agreement No. 6 dated as of March 17, 2010, Supplemental Agreement No. 7 dated as of March 17, 2010, and Supplemental Agreement No. 8 (and related side letters) dated as of April 30, 2010, each amending the Boeing 777 Freighter Purchase Agreement dated as of November 7, 2006 between The Boeing Company and FedEx Express. Confidential treatment has been granted for confidential commercial and financial information, pursuant to Rule 24b-2 under the Securities Exchange Act of 1934, as amended. (Filed as Exhibit 10.22 to FedEx s FY10 Annual Report on Form 10-K, and incorporated herein by reference).
10.24	Supplemental Agreement No. 9 dated as of June 18, 2010, Supplemental Agreement No. 10 dated as of June 18, 2010, Supplemental Agreement No. 11 (and related side letter) dated as of August 19, 2010, and Supplemental Agreement No. 13 (and related side letter) dated as of August 27, 2010, each amending the Boeing 777 Freighter Purchase Agreement dated as of November 7, 2006 between The Boeing Company and FedEx Express. Confidential treatment has been granted for confidential commercial and financial information, pursuant to Rule 24b-2 under the Securities Exchange Act of 1934, as amended. (Filed as Exhibit 10.1 to FedEx s FY11 First Quarter Report on Form 10-Q, and incorporated herein by reference.)
10.25	Supplemental Agreement No. 12 (and related side letter) dated as of September 3, 2010, Supplemental Agreement No. 14 (and related side letter) dated as of October 25, 2010, and Supplemental Agreement No. 15 (and related side letter) dated as of October 29, 2010, each amending the Boeing 777 Freighter Purchase Agreement dated as of November 7, 2006 between The Boeing Company and FedEx Express. Confidential treatment has been granted for confidential commercial and financial information, pursuant to Rule 24b-2 under the Securities Exchange Act of 1934, as amended. (Filed as Exhibit 10.2 to FedEx s FY11 Second Quarter Report on Form 10-Q, and incorporated herein by reference.)

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Exhibit Number	Description of Exhibit
10.26	Supplemental Agreement No. 16 (and related side letters) dated as of January 31, 2011, and Supplemental Agreement No. 17 dated as of February 14, 2011, each amending the Boeing 777 Freighter Purchase Agreement dated as of November 7, 2006 between The Boeing Company and FedEx Express. Confidential treatment has been granted for confidential commercial and financial information, pursuant to Rule 24b-2 under the Securities Exchange Act of 1934, as amended. (Filed as Exhibit 10.1 to FedEx s FY11 Third Quarter Report on Form 10-Q, and incorporated herein by reference.)
10.27	Supplemental Agreement No. 18 (and related side letter) dated as of March 30, 2011 to the Boeing 777 Freighter Purchase Agreement dated as of November 7, 2006 between The Boeing Company and FedEx Express. Confidential treatment has been granted for confidential commercial and financial information, pursuant to Rule 24b-2 under the Securities Exchange Act of 1934, as amended. (Filed as Exhibit 10.26 to FedEx s FY11 Annual Report on Form 10-K, and incorporated herein by reference.)
10.28	Supplemental Agreement No. 19 (and related side letter) dated as of October 27, 2011, amending the Boeing 777 Freighter Purchase Agreement dated as of November 7, 2006 between The Boeing Company and FedEx Express. Confidential treatment has been granted for confidential commercial and financial information, pursuant to Rule 24b-2 under the Securities Exchange Act of 1934, as amended. (Filed as Exhibit 10.2 to FedEx s FY12 Second Quarter Report on Form 10-Q, and incorporated herein by reference.)
10.29	Supplemental Agreement No. 20 (and related side letters) dated as of December 14, 2011, amending the Boeing 777 Freighter Purchase Agreement dated as of November 7, 2006 between The Boeing Company and FedEx Express. Confidential treatment has been granted for confidential commercial and financial information, pursuant to Rule 24b-2 under the Securities Exchange Act of 1934, as amended. (Filed as Exhibit 10.2 to FedEx s FY12 Third Quarter Report on Form 10-Q, and incorporated herein by reference.)
10.30	Boeing 767-3S2 Freighter Purchase Agreement dated as of December 14, 2011 between The Boeing Company and FedEx Express. Confidential treatment has been granted for confidential commercial and financial information, pursuant to Rule 24b-2 under the Securities Exchange Act of 1934, as amended. (Filed as Exhibit 10.1 to FedEx s FY12 Third Quarter Report on Form 10-Q, and incorporated herein by reference.)
	U.S. Postal Service Agreement
10.31	Transportation Agreement dated July 31, 2006 between the United States Postal Service and FedEx Express. Confidential treatment has been granted for confidential commercial and financial information, pursuant to Rule 24b-2 under the Securities Exchange Act of 1934, as amended. (Filed as Exhibit 10.2 to FedEx s FY07 First Quarter Report on Form 10-Q, and incorporated herein by reference.)
10.32	Amendment dated November 30, 2006 to the Transportation Agreement dated July 31, 2006 between the United States Postal Service and FedEx Express. Confidential treatment has been granted for confidential commercial and financial information, pursuant to Rule 24b-2 under the Securities Exchange Act of 1934, as amended. (Filed as Exhibit 10.2 to FedEx s FY07 Second Quarter Report on Form 10-Q, and incorporated herein by reference.)

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Exhibit Number	Description of Exhibit
10.33	Letter Agreement dated March 8, 2007 and Letter Agreement dated May 14, 2007, each amending the Transportation Agreement dated July 31, 2006 between the United States Postal Service and FedEx Express. Confidential treatment has been granted for confidential commercial and financial information, pursuant to Rule 24b-2 under the Securities Exchange Act of 1934, as amended. (Filed as Exhibit 10.15 to FedEx s FY07 Annual Report on Form 10-K, and incorporated herein by reference.)
10.34	Amendment dated June 20, 2007 and Amendment dated July 31, 2007, each amending the Transportation Agreement dated July 31, 2006 between the United States Postal Service and FedEx Express. Confidential treatment has been granted for confidential commercial and financial information, pursuant to Rule 24b-2 under the Securities Exchange Act of 1934, as amended. (Filed as Exhibit 10.1 to FedEx s FY08 First Quarter Report on Form 10-Q, and incorporated herein by reference.)
10.35	Amendment dated December 4, 2007 to the Transportation Agreement dated July 31, 2006 between the United States Postal Service and FedEx Express. Confidential treatment has been granted for confidential commercial and financial information, pursuant to Rule 24b-2 under the Securities Exchange Act of 1934, as amended. (Filed as Exhibit 10.1 to FedEx s FY08 Third Quarter Report on Form 10-Q, and incorporated herein by reference.)
10.36	Letter Agreement dated October 23, 2008 and Amendment dated October 23, 2008, each amending the Transportation Agreement dated July 31, 2006 between the United States Postal Service and FedEx Express. Confidential treatment has been granted for confidential commercial and financial information, pursuant to Rule 24b-2 under the Securities Exchange Act of 1934, as amended. (Filed as Exhibit 10.1 to FedEx s FY09 Second Quarter Report on Form 10-Q, and incorporated herein by reference.)
10.37	Letter Agreement dated March 4, 2009, amending the Transportation Agreement dated July 31, 2006 between the United States Postal Service and FedEx Express. (Filed as Exhibit 10.24 to FedEx s FY09 Annual Report on Form 10-K, and incorporated herein by reference.)
10.38	Letter Agreement dated September 29, 2009, amending the Transportation Agreement dated July 31, 2006 between the United States Postal Service and FedEx Express. Confidential treatment has been granted for confidential commercial and financial information, pursuant to Rule 24b-2 under the Securities Exchange Act of 1934, as amended. (Filed as Exhibit 10.1 to FedEx s FY10 Second Quarter Report on Form 10-Q, and incorporated herein by reference.)
10.39	Amendment dated December 8, 2009 to the Transportation Agreement dated July 31, 2006 between the United States Postal Service and FedEx Express. Confidential treatment has been granted for confidential commercial and financial information, pursuant to Rule 24b-2 under the Securities Exchange Act of 1934, as amended. (Filed as Exhibit 10.4 to FedEx s FY10 Third Quarter Report on Form 10-Q, and incorporated herein by reference.)
10.40	Letter Agreement dated August 30, 2010, amending the Transportation Agreement dated July 31, 2006 between the United States Postal Service and FedEx Express. Confidential treatment has been granted for confidential commercial and financial information, pursuant to Rule 24b-2 under the Securities Exchange Act of 1934, as amended. (Filed as Exhibit 10.2 to FedEx s FY11 First Quarter Report on Form 10-Q, and incorporated herein by reference.)

Exhibit Number	Description of Exhibit
10.41	Amendment dated November 22, 2010 to the Transportation Agreement dated July 31, 2006 between the United States Postal Service and FedEx Express. Confidential treatment has been granted for confidential commercial and financial information, pursuant to Rule 24b-2 under the Securities Exchange Act of 1934, as amended. (Filed as Exhibit 10.3 to FedEx s FY11 Second Quarter Report on Form 10-Q, and incorporated herein by reference.)
10.42	Letter Agreement dated September 9, 2011, amending the Transportation Agreement dated July 31, 2006 between the United States Postal Service and FedEx Express. Confidential treatment has been granted for confidential commercial and financial information, pursuant to Rule 24b-2 under the Securities Exchange Act of 1934, as amended. (Filed as Exhibit 10.3 to FedEx s FY12 Second Quarter Report on Form 10-Q, and incorporated herein by reference.)
10.43	Amendment dated December 5, 2011 to the Transportation Agreement dated July 31, 2006 between the United States Postal Service and FedEx Express. Confidential treatment has been granted for confidential commercial and financial information, pursuant to Rule 24b-2 under the Securities Exchange Act of 1934, as amended. (Filed as Exhibit 10.3 to FedEx s FY12 Third Quarter Report on Form 10-Q, and incorporated herein by reference.)
	Financing Agreement
10.44	Five-Year Credit Agreement dated as of April 26, 2011, among FedEx, JPMorgan Chase Bank, N.A., individually and as administrative agent, and certain lenders. (Filed as Exhibit 99.1 to FedEx s Current Report on Form 8-K dated April 26, 2011 and filed April 29, 2011, and incorporated herein by reference.)
	FedEx is not filing any other instruments evidencing any indebtedness because the total amount of securities authorized under any single such instrument does not exceed 10% of the total assets of FedEx and its subsidiaries on a consolidated basis. Copies of such instruments will be furnished to the Securities and Exchange Commission upon request.
	Management Contracts/Compensatory Plans or Arrangements
10.45	1993 Stock Incentive Plan and Form of Stock Option Agreement pursuant to 1993 Stock Incentive Plan, as amended. (The 1993 Stock Incentive Plan was filed as Exhibit A to FedEx Express s FY93 Definitive Proxy Statement, Commission File No. 1-7806, and is incorporated herein by reference, and the form of stock option agreement was filed as Exhibit 10.61 to FedEx Express s FY94 Annual Report on Form 10-K, and is incorporated herein by reference.)
10.46	Amendment to 1993 Stock Incentive Plan. (Filed as Exhibit 10.63 to FedEx Express s FY94 Annual Report on Form 10-K, and incorporated herein by reference.)
10.47	1995 Stock Incentive Plan and Form of Stock Option Agreement pursuant to 1995 Stock Incentive Plan. (The 1995 Stock Incentive Plan was filed as Exhibit A to FedEx Express s FY95 Definitive Proxy Statement, and is incorporated herein by reference, and the form of stock option agreement was filed as Exhibit 99.2 to FedEx Express s Registration Statement No. 333-03443 on Form S-8, and is incorporated herein by reference.)
10.48	Amendment to 1993 and 1995 Stock Incentive Plans. (Filed as Exhibit 10.79 to FedEx Express s FY97 Annual Report on Form 10-K, and incorporated herein by reference.)

Exhibit Number	Description of Exhibit
10.49	1997 Stock Incentive Plan, as amended, and Form of Stock Option Agreement pursuant to 1997 Stock Incentive Plan. (The 1997 Stock Incentive Plan was filed as Exhibit 4.3 to FedEx s Registration Statement on Form S-8, Registration No. 333-71065, and is incorporated herein by reference, and the form of stock option agreement was filed as Exhibit 4.4 to FedEx s Registration Statement No. 333-71065 on Form S-8, and is incorporated herein by reference.)
10.50	Amendment to 1997 Stock Incentive Plan. (Filed as Exhibit A to FedEx s FY98 Definitive Proxy Statement, and incorporated herein by reference.)
10.51	1999 Stock Incentive Plan and Form of Stock Option Agreement pursuant to 1999 Stock Incentive Plan. (The 1999 Stock Incentive Plan was filed as Exhibit 4.3 to FedEx s Registration Statement No. 333-34934 on Form S-8, and is incorporated herein by reference, and the form of stock option agreement was filed as Exhibit 4.4 to FedEx s Registration Statement No. 333-34934 on Form S-8, and is incorporated herein by reference.)
10.52	2002 Stock Incentive Plan and Form of Stock Option Agreement pursuant to 2002 Stock Incentive Plan. (The 2002 Stock Incentive Plan was filed as Exhibit 4.3 to FedEx s Registration Statement No. 333-100572 on Form S-8, and is incorporated herein by reference, and the form of stock option agreement was filed as Exhibit 4.4 to FedEx s Registration Statement No. 333-100572 on Form S-8, and is incorporated herein by reference.)
10.53	2001 Restricted Stock Plan and Form of Restricted Stock Agreement pursuant to 2001 Restricted Stock Plan. (Filed as Exhibit 10.60 to FedEx s FY01 Annual Report on Form 10-K, and incorporated herein by reference.)
10.54	Amendment to 2001 Restricted Stock Plan. (Filed as Exhibit 10.67 to FedEx s FY02 Annual Report on Form 10-K, and incorporated herein by reference.)
10.55	Amendment to 1995, 1997, 1999 and 2002 Stock Incentive Plans and 2001 Restricted Stock Plan. (Filed as Exhibit 10.3 to FedEx s FY04 Second Quarter Report on Form 10-Q, and incorporated herein by reference.)
10.56	FedEx Corporation Incentive Stock Plan, as amended; Amendment to FedEx Corporation Incentive Stock Plan, as amended, and 1997, 1999 and 2002 Stock Incentive Plans; Form of Terms and Conditions of stock option grant pursuant to FedEx Corporation Incentive Stock Plan, as amended; and Form of Restricted Stock Agreement pursuant to FedEx Corporation Incentive Stock Plan, as amended. (The FedEx Corporation Incentive Stock Plan, as amended, was filed as Exhibit 4.1 to FedEx s Registration Statement No. 333-156333 on Form S-8, and is incorporated herein by reference; the Amendment to FedEx Corporation Incentive Stock Plan, as amended, and 1997, 1999 and 2002 Stock Incentive Plans was filed as Exhibit 4.2 to FedEx s Registration Statement No. 333-156333 on Form S-8, and is incorporated herein by reference; the Form of Terms and Conditions of stock option grant pursuant to FedEx Corporation Incentive Stock Plan, as amended, was filed as Exhibit 4.3 to FedEx s Registration Statement No. 333-156333 on Form S-8, and is incorporated herein by reference; and the Form of Restricted Stock Agreement pursuant to FedEx Corporation Incentive Stock Plan, as amended, was filed as Exhibit 4.4 to FedEx s Registration Statement No. 333-156333 on Form S-8, and is incorporated herein by reference.)

Exhibit Number	Description of Exhibit
10.57	FedEx Corporation Incentive Stock Plan 2005 Inland Revenue Approved Sub-Plan for the United Kingdom and Form of Share Option Agreement pursuant to the FedEx Corporation Incentive Stock Plan 2005 Inland Revenue Approved Sub-Plan for the United Kingdom. (The United Kingdom Sub-Plan was filed as Exhibit 4.2 to FedEx s Registration Statement No. 333-130619 on Form S-8, and is incorporated herein by reference, and the form of share option agreement pursuant to the UK Sub-Plan was filed as Exhibit 4.3 to FedEx s Registration Statement No. 333-130619 on Form S-8, and is incorporated herein by reference.)
10.58	Amendments to 1993, 1995, 1997, 1999 and 2002 Stock Incentive Plans, as amended, 2001 Restricted Stock Plan, as amended, and FedEx Corporation Incentive Stock Plan, as amended. (Filed as Exhibit 10.48 to FedEx s FY10 Annual Report on Form 10-K, and incorporated herein by reference.)
10.59	Amendments to 1993, 1995, 1997, 1999 and 2002 Stock Incentive Plans, 2001 Restricted Stock Plan and FedEx Corporation Incentive Stock Plan. (Filed as Exhibit 10.2 to FedEx s FY11 Third Quarter Report on Form 10-Q, and incorporated herein by reference.)
10.60	FedEx Corporation 2010 Omnibus Stock Incentive Plan; Form of Terms and Conditions of stock option grant pursuant to FedEx Corporation 2010 Omnibus Stock Incentive Plan; and Form of Terms and Conditions of restricted stock grant pursuant to FedEx Corporation 2010 Omnibus Stock Incentive Plan. (The FedEx Corporation 2010 Omnibus Stock Incentive Plan was filed as Exhibit 4.3 to FedEx s Registration Statement No. 333-171232 on Form S-8, and is incorporated herein by reference; the Form of Terms and Conditions of stock option grant pursuant to FedEx Corporation 2010 Omnibus Stock Incentive Plan was filed as Exhibit 4.4 to FedEx s Registration Statement No. 333-171232 on Form S-8, and is incorporated herein by reference; and the Form of Terms and Conditions of restricted stock grant pursuant to FedEx Corporation 2010 Omnibus Stock Incentive Plan was filed as Exhibit 4.5 to FedEx s Registration Statement No. 333-171232 on Form S-8, and is incorporated herein by reference.)
10.61	Amended and Restated FedEx Corporation Retirement Parity Pension Plan. (Filed as Exhibit 10.35 to FedEx s FY08 Annual Report on Form 10-K, and incorporated herein by reference.)
10.62	FedEx Express Supplemental Long Term Disability Plan and Amendment to the Plan. (Filed as Exhibit 10.56 to FedEx s FY11 Annual Report on Form 10-K, and incorporated herein by reference.)
*10.63	Compensation Arrangements with Named Executive Officers.
10.64	Compensation Arrangements with Outside Directors. (Filed as Exhibit 10.1 to FedEx s FY12 Second Quarter Report on Form 10-Q, and incorporated herein by reference.)
10.65	FedEx s Amended and Restated Retirement Plan for Outside Directors. (Filed as Exhibit 10.2 to FedEx s FY09 Second Quarter Report on Form 10-Q, and incorporated herein by reference.)
10.66	Form of revised Management Retention Agreement, dated March 18, 2010, entered into between FedEx and each of Frederick W. Smith, David J. Bronczek, Robert B. Carter, T. Michael Glenn, Alan B. Graf, Jr., William J. Logue, David F. Rebholz and Christine P. Richards. (Filed as Exhibit 10.5 to FedEx s FY10 Third Quarter Report on Form 10-Q, and incorporated herein by reference.)

Exhibit Number	Description of Exhibit
	Other Exhibits
*12	Statement re Computation of Ratio of Earnings to Fixed Charges (presented on page 127 of this Annual Report on Form 10-K).
*21	Subsidiaries of Registrant.
*23	Consent of Ernst & Young LLP, Independent Registered Public Accounting Firm.
*24	Powers of Attorney.
*31.1	Certification of Principal Executive Officer Pursuant to Rules 13a-14(a) and 15d-14(a) under the Securities Exchange Act of 1934, as Adopted Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
*31.2	Certification of Principal Financial Officer Pursuant to Rules 13a-14(a) and 15d-14(a) under the Securities Exchange Act of 1934, as Adopted Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
*32.1	Certification of Principal Executive Officer Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
*32.2	Certification of Principal Financial Officer Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
*101.1	Interactive Data Files.

* Filed herewith.