UNITED PARCEL SERVICE INC
Form 10-Q
August 02, 2013
Table of Contents

United States
Securities and Exchange Commission
Washington, D.C. 20549

Form 10-Q
(Mark One)

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

For the quarterly period ended June 30, 2013, 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 001-15451

United Parcel Service, Inc.
(Exact name of registrant as specified in its charter)

Delaware	58-2480149
(State or Other Jurisdiction of Incorporation or Organization)	(IRS Employer Identification No.)
55 Glenlake Parkway, NE Atlanta, Georgia	30328
(Address of Principal Executive Offices)	(Zip Code)

(404) 828-6000
(Registrant's telephone number, including area code)

Former name, former address and former fiscal year, if changed since last report.

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 þ No ¨

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

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See definitions of "accelerated filer", "large accelerated filer", and "smaller reporting company" in Rule 12b-2 of the Exchange Act. Check one: Large accelerated filer þ Accelerated filer ¨ Non-accelerated filer ¨ (Do not check if a smaller reporting company) Smaller reporting company ¨

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

There were 216,729,216 Class A shares, and 721,546,655 Class B shares, with a par value of $0.01 per share, outstanding at July 23, 2013.

Table of Contents

UNITED PARCEL SERVICE, INC.
QUARTERLY REPORT ON FORM 10-Q FOR THE QUARTER ENDED JUNE 30, 2013
TABLE OF CONTENTS

Table of Contents

PART I. FINANCIAL INFORMATION

Cautionary Statement About Forward-Looking Statements

This report includes certain “forward-looking statements” within the meaning of the Private Securities Litigation Reform Act of 1995. Statements in the future tense, and all statements accompanied by terms such as “believe,” “project,” “expect,” “estimate,” “assume,” “intend,” “anticipate,” “target,” “plan,” and variations thereof and similar terms are intended to forward-looking statements. We intend that all forward-looking statements we make will be subject to safe harbor protection of the federal securities laws pursuant to Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934.

Our disclosure and analysis in this report, in our Annual Report on Form 10-K for the year ended December 31, 2012 and in our other filings with the Securities and Exchange Commission contain some forward-looking statements regarding our intent, belief and current expectations about our strategic direction, prospects and future results. From time to time, we also provide forward-looking statements in other materials we release as well as oral forward-looking statements. Such statements give our current expectations or forecasts of future events; they do not relate strictly to historical or current facts. Management believes that these forward-looking statements are reasonable as and when made. However, caution should be taken not to place undue reliance on any such forward-looking statements because such statements speak only as of the date when made.

Forward-looking statements are subject to certain risks and uncertainties that could cause actual results to differ materially from our historical experience and our present expectations or anticipated results. These risks and uncertainties include, but are not limited to: general economic conditions, both in the U.S. and internationally; significant competition on a local, regional, national, and international basis; the existing complex and stringent regulation in the U.S. and internationally, changes to which can impact our business; increased security requirements that may increase our costs of operations and reduce operating efficiencies; legal, regulatory or market responses to global climate change; negotiation and ratification of labor contracts; strikes, work stoppages and slowdowns by our employees; the effects of changing prices of energy, including gasoline, diesel and jet fuel, and interruptions in supplies of these commodities; changes in exchange rates or interest rates; our ability to maintain the image of our brand; breaches in data security; disruptions to the Internet or our technology infrastructure; our ability to accurately forecast our future capital investment needs; exposure to changing economic, political and social developments in international and emerging markets; changes in business strategy, government regulations, or economic or market conditions that may result in further substantial impairment write-downs of our assets; increases in our expenses relating to employee health and retiree health and our contributions to pension benefits; the potential for various claims and litigation related to labor and employment, personal injury, property damage, business practices, environmental liability and other matters; our ability to realize the anticipated benefits from acquisitions, joint ventures or strategic alliances; our ability to manage insurance and claims expenses; and other risks discussed in our filings with the Securities and Exchange Commission from time to time, including our Annual Report on Form 10-K for the year ended December 31, 2012, in Part II, “Item1A. Risk Factors” of this Quarterly Report on Form 10-Q for the quarterly period ended June 30, 2013, and may also be described from time to time in our future reports filed with the Securities and Exchange Commission. You should consider the limitations on, and risks associated with, forward-looking statements and not unduly rely on the accuracy of predictions contained in such forward-looking statements. We do not undertake any obligation to update forward-looking statements to reflect events, circumstances, changes in expectations, or the occurrence of unanticipated events after the date of those statements.

Table of Contents

Item 1. Financial Statements
UNITED PARCEL SERVICE, INC. AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS
June 30, 2013 (unaudited) and December 31, 2012
(In millions)

	June 30, 2013	December 31, 2012
ASSETS		
Current Assets:		
Cash and cash equivalents	$4,808	$7,327
Marketable securities	1,384	597
Accounts receivable, net	5,438	6,111
Deferred income tax assets	564	583
Other current assets	1,032	973
Total Current Assets	13,226	15,591
Property, Plant and Equipment, Net	17,880	17,894
Goodwill	2,149	2,173
Intangible Assets, Net	678	603
Non-Current Investments and Restricted Cash	406	307
Derivative Assets	331	535
Deferred Income Tax Assets	963	684
Other Non-Current Assets	1,070	1,076
Total Assets	$36,703	$38,863
LIABILITIES AND SHAREOWNERS' EQUITY		
Current Liabilities:		
Current maturities of long-term debt and commercial paper	$1,086	$1,781
Accounts payable	2,008	2,278
Accrued wages and withholdings	1,858	1,927
Self-insurance reserves	749	763
Income taxes payable	221	399
Other current liabilities	1,261	1,242
Total Current Liabilities	7,183	8,390
Long-Term Debt	10,837	11,089
Pension and Postretirement Benefit Obligations	11,426	11,068
Self-Insurance Reserves	1,998	1,980
Other Non-Current Liabilities	1,629	1,603
Shareowners' Equity:		
Class A common stock (218 and 225 shares issued in 2013 and 2012)	2	3
Class B common stock (721 and 729 shares issued in 2013 and 2012)	7	7
Additional paid-in capital	—	—
Retained earnings	7,185	7,997
Accumulated other comprehensive loss	(3,577)	(3,354)
Deferred compensation obligations	67	78
Less: Treasury stock (1 share in 2013 and 2012)	(67)	(78)
Total Equity for Controlling Interests	3,617	4,653
Total Equity for Non-Controlling Interests	13	80
Total Shareowners' Equity	3,630	4,733
Total Liabilities and Shareowners' Equity	$36,703	$38,863

See notes to unaudited consolidated financial statements.

Table of Contents

UNITED PARCEL SERVICE, INC. AND SUBSIDIARIES
STATEMENTS OF CONSOLIDATED INCOME
(In millions, except per share amounts)
(unaudited)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2013	2012	2013	2012
Revenue	$13,507	$13,349	$26,941	$26,485
Operating Expenses:				
Compensation and benefits	6,981	6,747	13,949	13,582
Repairs and maintenance	309	303	618	605
Depreciation and amortization	466	459	940	918
Purchased transportation	1,731	1,733	3,511	3,450
Fuel	992	1,014	1,998	2,039
Other occupancy	225	213	478	450
Other expenses	1,061	1,090	2,125	2,082
Total Operating Expenses	11,765	11,559	23,619	23,126
Operating Profit	1,742	1,790	3,322	3,359
Other Income and (Expense):				
Investment income	3	6	8	12
Interest expense	(98)	(92)	(194)	(186)
Total Other Income and (Expense)	(95)	(86)	(186)	(174)
Income Before Income Taxes	1,647	1,704	3,136	3,185
Income Tax Expense	576	588	1,028	1,099
Net Income	$1,071	$1,116	$2,108	$2,086
Basic Earnings Per Share	$1.14	$1.16	$2.22	$2.17
Diluted Earnings Per Share	$1.13	$1.15	$2.21	$2.15

STATEMENTS OF CONSOLIDATED COMPREHENSIVE INCOME
(In millions)
(unaudited)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2013	2012	2013	2012
Net income	$1,071	$1,116	$2,108	$2,086
Change in foreign currency translation adjustment, net of tax	(24)	(158)	(327)	(67)
Change in unrealized gain (loss) on marketable securities, net of tax	(6)	2	(8)	1
Change in unrealized gain (loss) on cash flow hedges, net of tax	20	(43)	58	(84)
Change in unrecognized pension and postretirement benefit costs, net of tax	28	27	54	61
Comprehensive income	$1,089	$944	$1,885	$1,997

See notes to unaudited consolidated financial statements.

Table of Contents

UNITED PARCEL SERVICE, INC. AND SUBSIDIARIES
STATEMENTS OF CONSOLIDATED CASH FLOWS
(In millions)
(unaudited)

	Six Months Ended June 30, 2013	2012
Cash Flows From Operating Activities:		
Net income	$2,108	$2,086
Adjustments to reconcile net income to net cash from operating activities:		
Depreciation and amortization	940	918
Pension and postretirement benefit expense	562	473
Pension and postretirement benefit contributions	(114)	(450)
Self-insurance reserves	4	70
Deferred taxes, credits and other	(328)	(148)
Stock compensation expense	288	295
Other (gains) losses	(98)	115
Changes in assets and liabilities, net of effect of acquisitions:		
Accounts receivable	542	490
Other current assets	(15)	(50)
Accounts payable	(209)	(163)
Accrued wages and withholdings	(49)	(34)
Other current liabilities	(134)	304
Other operating activities	(66)	(56)
Net cash from operating activities	3,431	3,850
Cash Flows From Investing Activities:		
Capital expenditures	(990)	(949)
Proceeds from disposals of property, plant and equipment	24	32
Purchases of marketable securities	(1,615)	(1,940)
Sales and maturities of marketable securities	717	2,604
Net decrease in finance receivables	19	42
Cash paid for business acquisitions	—	(100)
Other investing activities	(8)	4
Net cash used in investing activities	(1,853)	(307)
Cash Flows From Financing Activities:		
Net change in short-term debt	1,045	1,877
Proceeds from long-term borrowings	100	4
Repayments of long-term borrowings	(1,861)	(8)
Purchases of common stock	(1,867)	(885)
Issuances of common stock	293	194
Dividends	(1,140)	(1,068)
Other financing activities	(611)	44
Net cash provided by (used in) financing activities	(4,041)	158
Effect Of Exchange Rate Changes On Cash And Cash Equivalents	(56)	(17)
Net Increase (Decrease) In Cash And Cash Equivalents	(2,519)	3,684
Cash And Cash Equivalents:		
Beginning of period	7,327	3,034
End of period	$4,808	$6,718

See notes to unaudited consolidated financial statements.

Table of Contents

UNITED PARCEL SERVICE, INC. AND SUBSIDIARIES
NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS
NOTE 1. BASIS OF PRESENTATION
Principles of Consolidation
In our opinion, the accompanying interim, unaudited, consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States for interim financial information and with the instructions to Form 10-Q and Rule 10-01 of Regulation S-X. These consolidated financial statements contain all adjustments (consisting of normal recurring accruals) necessary to present fairly our financial position as of June 30, 2013, our results of operations for the three and six months ended June 30, 2013 and 2012, and cash flows for the six months ended June 30, 2013 and 2012. The results reported in these consolidated financial statements should not be regarded as necessarily indicative of results that may be expected for the entire year. The interim consolidated financial statements should be read in conjunction with the audited consolidated financial statements and notes thereto included in our Annual Report on Form 10-K for the year ended December 31, 2012.
For interim consolidated financial statement purposes, we provide for accruals under our various employee benefit plans and self-insurance reserves for each three month period based on one quarter of the estimated annual expense.
Certain prior year amounts have been reclassified to conform to the current year presentation. These reclassifications had no impact on our financial position or results of operations.
Fair Value of Financial Instruments
The carrying amounts of our cash and cash equivalents, accounts receivable, finance receivables and accounts payable approximate fair value as of June 30, 2013. The fair values of our investment securities are disclosed in note 4, our short and long-term debt in note 8 and our derivative instruments in note 13. We utilized Level 1 inputs in the fair value hierarchy of valuation techniques to determine the fair value of our cash and cash equivalents, and Level 2 inputs to determine the fair value of our accounts receivable, finance receivables and accounts payable.
Accounting Estimates
The preparation of the accompanying interim, unaudited, consolidated financial statements requires management to make estimates and judgments that affect the reported amounts of assets and liabilities and the disclosure of contingencies at the date of the consolidated financial statements, as well as the reported amounts of revenues and expenses during the reporting period. Estimates have been prepared on the basis of the most current and best information and actual results could differ materially from those estimates.

NOTE 2. RECENT ACCOUNTING PRONOUNCEMENTS
Adoption of New Accounting Standards
In February 2013, the FASB issued an accounting standards update that adds new disclosure requirements for items reclassified out of accumulated other comprehensive income. This update requires that companies present either in a single note or parenthetically on the face of the financial statements, the effect of significant amounts reclassified from each component of accumulated other comprehensive income based on its source (e.g., the release due to cash flow hedges from interest rate contracts) and the income statement line items affected by the reclassification (e.g., interest income or interest expense). If a component is not required to be reclassified to net income in its entirety (e.g., the net periodic pension cost), companies would instead cross reference to the related footnote for additional information (e.g., the pension footnote). This update was effective for us beginning in the first quarter of 2013, and we have included the applicable disclosures in note 10.
Other accounting pronouncements adopted during the periods covered by the consolidated financial statements had an immaterial impact on our consolidated financial position and results of operations.
Accounting Standards Issued But Not Yet Effective
Accounting pronouncements issued, but not effective until after June 30, 2013, are not expected to have a significant impact on our consolidated financial position or results of operations.

Table of Contents

UNITED PARCEL SERVICE, INC. AND SUBSIDIARIES
NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

NOTE 3. STOCK-BASED COMPENSATION

We issue employee share-based awards under the UPS Incentive Compensation Plan, which permits the grant of nonqualified and incentive stock options, stock appreciation rights, restricted stock and stock units, and restricted performance shares and performance units, to eligible employees (Restricted stock and stock units, and restricted performance shares and performance units are herein referred to as "Restricted Units"). The primary compensation programs offered under the UPS Incentive Compensation Plan include the UPS Management Incentive Award program, the UPS Long-Term Incentive Performance Award program and the UPS Stock Option program. We also maintain an employee stock purchase plan which allows eligible employees to purchase shares of UPS class A common stock at a discount. Additionally, our matching contributions to the primary employee defined contribution plan are made in shares of UPS class A common stock.

Management Incentive Award

During the first quarter of 2013, we granted Restricted Units under the Management Incentive Award program to eligible U.S.-based management employees. Restricted Units under the Management Incentive Award program will generally vest over a five-year period with approximately 20% of the award vesting on January 15th of each of the years following the grant date (except in the case of death, disability, or retirement, in which case immediate vesting occurs). The entire grant is expensed on a straight-line basis over the requisite service period. Based on the date that the eligible management population and performance targets were approved for the Management Incentive Award program, we determined the award measurement date to be February 5, 2013 (for U.S.-based employees) and April 1, 2013 (for international-based employees); therefore, the Restricted Unit grant was valued for stock compensation expense purposes using the closing New York Stock Exchange price of $80.80 and $84.47 on those dates, respectively.

Long-Term Incentive Performance Award

During the first quarter of 2013, we granted target Restricted Units under the UPS Long-Term Incentive Performance Award program to eligible management employees. Of the total 2013 target award, 90% of the target award will be divided into three substantially equal tranches, one for each calendar year in the three-year award cycle from 2013 to 2015, using performance criteria targets established each year. For 2013, those targets consist of consolidated operating return on invested capital and growth in consolidated revenue. The remaining 10% of the total 2013 target award will be based upon our achievement of adjusted earnings per share in 2015 compared to a target established at the grant date.

The number of Restricted Units earned each year will be the target number adjusted for the percentage achievement of performance criteria targets for the year. The percentage of achievement used to determine the Restricted Units earned may be a percentage less than or more than 100% of the target Restricted Units for each tranche. Based on the date that the eligible management population and performance targets were approved for the 2013 performance tranches, we determined the award measurement date to be March 1, 2013; therefore the target Restricted Units grant was valued for stock compensation expense purposes using the closing New York Stock Exchange price of $82.87 on that date.

Nonqualified Stock Options

During the first quarter of 2013, we granted nonqualified stock option awards to a limited group of eligible senior management employees under the UPS Stock Option program. Stock option awards generally vest over a five-year period with approximately 20% of the award vesting at each anniversary date of the grant (except in the case of death, disability, or retirement, in which case immediate vesting occurs). The options granted will expire ten years after the date of the grant. In the first quarter of 2013 and 2012, we granted 0.2 million stock options each year at a weighted average grant price of $82.93 and $76.94, respectively. The weighted average fair value of our employee stock options granted, as determined by the Black-Scholes valuation model, was $15.50 and $14.88 for 2013 and 2012, respectively, using the following assumptions:

	2013	2012

Expected life (in years)	7.5		7.5	
Risk-free interest rate	1.38	%	1.63	%
Expected volatility	24.85	%	25.06	%
Expected dividend yield	2.75	%	2.77	%

Compensation expense for share-based awards recognized in net income for the three months ended June 30, 2013 and 2012 was $131 and $133 million pre-tax, respectively. Compensation expense for share-based awards recognized in net income for the six months ended June 30, 2013 and 2012 was $288 and $295 million pre-tax, respectively.

Table of Contents
UNITED PARCEL SERVICE, INC. AND SUBSIDIARIES
NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

NOTE 4. INVESTMENTS AND RESTRICTED CASH

The following is a summary of marketable securities classified as available-for-sale as of June 30, 2013 and December 31, 2012 (in millions):

	Cost	Unrealized Gains	Unrealized Losses	Estimated Fair Value
June 30, 2013				
Current marketable securities:				
U.S. government and agency debt securities	$352	$1	$(2)	$351
Mortgage and asset-backed debt securities	75	—	(1)	74
Corporate debt securities	874	1	(2)	873
U.S. state and local municipal debt securities	17	—	—	17
Other debt and equity securities	69	—	—	69
Total marketable securities	$1,387	$2	$(5)	$1,384

	Cost	Unrealized Gains	Unrealized Losses	Estimated Fair Value
December 31, 2012				
Current marketable securities:				
U.S. government and agency debt securities	$236	$2	$—	$238
Mortgage and asset-backed debt securities	171	3	—	174
Corporate debt securities	158	5	—	163
U.S. state and local municipal debt securities	15	—	—	15
Other debt and equity securities	7	—	—	7
Total marketable securities	$587	$10	$—	$597

Investment Other-Than-Temporary Impairments

We have concluded that no other-than-temporary impairment losses existed as of June 30, 2013. In making this determination, we considered the financial condition and prospects of the issuers, the magnitude of the losses compared with the investments' cost, the length of time the investments have been in an unrealized loss position, the probability that we will be unable to collect all amounts due according to the contractual terms of the securities, the credit rating of the securities and our ability and intent to hold these investments until the anticipated recovery in market value occurs.

Maturity Information

The amortized cost and estimated fair value of marketable securities at June 30, 2013, by contractual maturity, are shown below (in millions). Actual maturities may differ from contractual maturities because the issuers of the securities may have the right to prepay obligations without prepayment penalties.

	Cost	Estimated Fair Value
Due in one year or less	$832	$833
Due after one year through three years	413	412
Due after three years through five years	23	22
Due after five years	117	115
	1,385	1,382
Equity securities	2	2
	$1,387	$1,384

Table of Contents
UNITED PARCEL SERVICE, INC. AND SUBSIDIARIES
NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

Non-Current Investments and Restricted Cash
We had $387 and $288 million of restricted cash related to our self-insurance requirements as of June 30, 2013 and December 31, 2012, respectively, which is reported in “Non-Current Investments and Restricted Cash” on the consolidated balance sheets. This restricted cash is invested in money market funds and similar cash-equivalent type assets.
At June 30, 2013 and December 31, 2012, we held a $19 million investment in a variable life insurance policy to fund benefits for the UPS Excess Coordinating Benefit Plan. This investment is classified as “Non-Current Investments and Restricted Cash” in the consolidated balance sheets with the quarterly change in investment value recognized in the statements of consolidated income.
Fair Value Measurements
Marketable securities utilizing Level 1 inputs include active exchange-traded equity securities and equity index funds, and most U.S. Government debt securities, as these securities all have quoted prices in active markets. Marketable securities utilizing Level 2 inputs include asset-backed securities, corporate bonds and municipal bonds. These securities are valued using market corroborated pricing, matrix pricing or other models that utilize observable inputs such as yield curves.
We maintain holdings in certain investment partnerships that are measured at fair value utilizing Level 3 inputs (classified as “other investments” in the tables below and as “Other Non-Current Assets” in the consolidated balance sheets). These partnership holdings do not have quoted prices, nor can they be valued using inputs based on observable market data. These investments are valued internally using a discounted cash flow model with two significant inputs: (1) the after-tax cash flow projections for each partnership, and (2) the risk-adjusted discount rate consistent with the duration of the expected cash flows for each partnership. The weighted-average discount rates used to value these investments were 8.44% and 7.75% as of June 30, 2013 and December 31, 2012, respectively. These inputs and the resulting fair values are updated on a quarterly basis.
The following table presents information about our investments measured at fair value on a recurring basis as of June 30, 2013 and December 31, 2012, and indicates the fair value hierarchy of the valuation techniques utilized to determine such fair value (in millions):

	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Balance
June 30, 2013				
Marketable Securities:				
U.S. government and agency debt securities	$350	$ 1	$—	$351
Mortgage and asset-backed debt securities	—	74	—	74
Corporate debt securities	—	873	—	873
U.S. state and local municipal debt securities	—	17	—	17
Other debt and equity securities	—	69	—	69
Total marketable securities	350	1,034	—	1,384
Other investments	19	—	136	155
Total	$369	$ 1,034	$136	$1,539

Table of Contents
UNITED PARCEL SERVICE, INC. AND SUBSIDIARIES
NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Balance
December 31, 2012				
Marketable Securities:				
U.S. government and agency debt securities	$237	$ 1	$—	$238
Mortgage and asset-backed debt securities	—	174	—	174
Corporate debt securities	—	163	—	163
U.S. state and local municipal debt securities	—	15	—	15
Other debt and equity securities	—	7	—	7
Total marketable securities	237	360	—	597
Other investments	19	—	163	182
Total	$256	$ 360	$163	$779

The following table presents the changes in the above Level 3 instruments measured on a recurring basis for the three months ended June 30, 2013 and 2012 (in millions):

	Marketable Securities	Other Investments	Total
Balance on April 1, 2013	$—	$150	$150
Transfers into (out of) Level 3	—	—	—
Net realized and unrealized gains (losses):			
Included in earnings (in investment income)	—	(14)	(14)
Included in accumulated other comprehensive income (pre-tax)	—	—	—
Purchases	—	—	—
Sales	—	—	—
Balance on June 30, 2013	$—	$136	$136

	Marketable Securities	Other Investments	Total
Balance on April 1, 2012	$—	$204	$204
Transfers into (out of) Level 3	—	—	—
Net realized and unrealized gains (losses):			
Included in earnings (in investment income)	—	(14)	(14)
Included in accumulated other comprehensive income (pre-tax)	—	—	—
Purchases	—	—	—
Sales	—	—	—
Balance on June 30, 2012	$—	$190	$190

Table of Contents
UNITED PARCEL SERVICE, INC. AND SUBSIDIARIES
NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

The following table presents the changes in the above Level 3 instruments measured on a recurring basis for the six months ended June 30, 2013 and 2012 (in millions):

	Marketable Securities	Other Investments	Total
Balance on January 1, 2013	$—	163	163
Transfers into (out of) Level 3	—	—	—
Net realized and unrealized gains (losses):		—	
Included in earnings (in investment income)	—	(27)	(27)
Included in accumulated other comprehensive income (pre-tax)	—	—	—
Purchases	—	—	—
Sales	—	—	—
Balance on June 30, 2013	$—	$136	$136

	Marketable Securities	Other Investments	Total
Balance on January 1, 2012	$—	217	217
Transfers into (out of) Level 3	—	—	—
Net realized and unrealized gains (losses):			
Included in earnings (in investment income)	—	(27)	(27)
Included in accumulated other comprehensive income (pre-tax)	—	—	—
Purchases	—	—	—
Sales	—	—	—
Balance on June 30, 2012	$—	$190	$190

There were no transfers of investments between Level 1 and Level 2 during the three and six months ended June 30, 2013 and 2012.

NOTE 5. PROPERTY, PLANT AND EQUIPMENT

Property, plant and equipment as of June 30, 2013 and December 31, 2012 consist of the following (in millions):

	2013	2012
Vehicles	$6,445	$6,344
Aircraft	15,544	15,164
Land	1,122	1,122
Buildings	3,199	3,138
Building and leasehold improvements	3,072	3,049
Plant equipment	7,101	7,010
Technology equipment	1,608	1,675
Equipment under operating leases	60	69
Construction-in-progress	348	470
	38,499	38,041
Less: Accumulated depreciation and amortization	(20,619)	(20,147)
	$17,880	$17,894

We continually monitor our aircraft fleet utilization in light of current and projected volume levels, aircraft fuel prices and other factors. Additionally, we monitor our other property, plant and equipment categories for any indicators that the carrying value of the assets exceeds the fair value. There were no indicators of impairment in our property, plant and equipment, and no impairment charges were recorded, during the three and six months ended June 30, 2013 and 2012.

Table of Contents

UNITED PARCEL SERVICE, INC. AND SUBSIDIARIES
NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

NOTE 6. EMPLOYEE BENEFIT PLANS

Company-Sponsored Benefit Plans

Information about net periodic benefit cost for our company-sponsored pension and postretirement benefit plans is as follows for the three and six months ended June 30, 2013 and 2012 (in millions):

	U.S. Pension Benefits		U.S. Postretirement Medical Benefits		International Pension Benefits	
	2013	2012	2013	2012	2013	2012
Three Months Ended June 30:						
Service cost	$337	$250	$26	$22	$11	$14
Interest cost	363	352	47	52	11	10
Expected return on assets	(537)	(493)	(9)	(5)	(14)	(12)
Amortization of:						
Transition obligation	—	—	—	—	—	—
Prior service cost	43	44	1	1	—	—
Other net (gain) loss	—	—	—	—	—	—
Actuarial (gain) loss	—	—	—	—	—	—
Net periodic benefit cost	$206	$153	$65	$70	$8	$12

	U.S. Pension Benefits		U.S. Postretirement Medical Benefits		International Pension Benefits	
	2013	2012	2013	2012	2013	2012
Six Months Ended June 30:						
Service cost	$675	$499	$52	$44	$26	$29
Interest cost	725	705	93	104	22	21
Expected return on assets	(1,074)	(985)	(17)	(9)	(28)	(24)
Amortization of:						
Transition obligation	—	—	—	—	—	—
Prior service cost	86	87	2	2	—	—
Other net (gain) loss	—	—	—	—	—	—
Actuarial (gain) loss	—	—	—	—	—	—
Net periodic benefit cost	$412	$306	$130	$141	$20	$26

During the first six months of 2013, we contributed $53 million and $61 million to our company-sponsored pension and postretirement medical benefit plans, respectively. We also expect to contribute $48 and $50 million over the remainder of the year to the pension and U.S. postretirement medical benefit plans, respectively.

Collective Bargaining Agreements

As of December 31, 2012, we had approximately 249,000 employees employed under a national master agreement and various supplemental agreements with local unions affiliated with the International Brotherhood of Teamsters (“Teamsters”). These agreements run through July 31, 2013. On April 25, 2013, we reached a tentative agreement with the Teamsters on two new five-year contracts in the U.S. Domestic Package and UPS Freight business units. During the second quarter, UPS Teamster-represented employees in the U.S. Domestic Package business unit voted to approve the new agreement, while some local U.S. Domestic Package agreements and the agreement covering UPS Freight employees will require additional negotiation and approval before the new agreement is ratified. Before expiration, the Company and the Teamsters agreed to extensions of both existing five-year contracts and all local riders, supplements, and addenda. The extensions are open-ended and can be terminated by either party on thirty days' notice. Subject to ratification by the UPS Teamster-represented employees, the new agreements will be retroactively effective as of August 1, 2013. As of the date of this filing, there can be no assurance that our efforts will be successful or that the ultimate resolution of these matters will not adversely affect our business, financial position, results of operations or liquidity.

11

Table of Contents

UNITED PARCEL SERVICE, INC. AND SUBSIDIARIES
NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

We have approximately 2,600 pilots who are employed under a collective bargaining agreement with the Independent Pilots Association, which became amendable at the end of 2011. Our airline mechanics are covered by a collective bargaining agreement with Teamsters Local 2727, which runs through November 1, 2013. In addition, approximately 3,100 of our ground mechanics who are not employed under agreements with the Teamsters are employed under collective bargaining agreements with the International Association of Machinists and Aerospace Workers ("IAM"). Our agreement with the IAM runs through July 31, 2014.

Multiemployer Benefit Plans

We contribute to a number of multiemployer defined benefit and health and welfare plans under terms of collective bargaining agreements that cover our union represented employees. Our current collective bargaining agreements set forth the annual contribution increases allotted to the plans that we participate in, and we are in compliance with these contribution rates. These limitations will remain in effect throughout the terms of the existing collective bargaining agreements.

NOTE 7. GOODWILL AND INTANGIBLE ASSETS

The following table indicates the allocation of goodwill by reportable segment as of June 30, 2013 and December 31, 2012 (in millions):

	U.S. Domestic Package	International Package	Supply Chain & Freight	Consolidated
December 31, 2012:	$—	$430	$ 1,743	$2,173
Acquired	—	—	—	—
Currency / Other	—	(16)	(8)	(24)
June 30, 2013:	$—	$414	$ 1,735	$2,149

The change in goodwill for both the International Package and Supply Chain & Freight segments was due to the impact of changes in the value of the U.S. Dollar on the translation of non-U.S. Dollar goodwill balances.

The following is a summary of intangible assets as of June 30, 2013 and December 31, 2012 (in millions):

	Gross Carrying Amount	Accumulated Amortization	Net Carrying Value
June 30, 2013:			
Trademarks, licenses, patents, and other	$200	$(89)	$111
Customer lists	130	(84)	46
Franchise rights	117	(67)	50
Capitalized software	2,331	(1,860)	471
Total Intangible Assets, Net	$2,778	$(2,100)	$678
December 31, 2012:			
Trademarks, licenses, patents, and other	$163	$(80)	$83
Customer lists	131	(79)	52
Franchise rights	117	(64)	53
Capitalized software	2,197	(1,782)	415
Total Intangible Assets, Net	$2,608	$(2,005)	$603

Table of Contents
UNITED PARCEL SERVICE, INC. AND SUBSIDIARIES
NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

NOTE 8. DEBT AND FINANCING ARRANGEMENTS
The carrying value of our outstanding debt as of June 30, 2013 and December 31, 2012 consists of the following (in millions):

	Principal Amount	Maturity	Carrying Value 2013	Carrying Value 2012
Commercial paper	$1,045	2013	$1,045	$—
Fixed-rate senior notes:				
4.50% senior notes	—	2013	—	1,751
3.875% senior notes	1,000	2014	1,020	1,033
1.125% senior notes	375	2017	365	373
5.50% senior notes	750	2018	823	851
5.125% senior notes	1,000	2019	1,090	1,140
3.125% senior notes	1,500	2021	1,606	1,655
2.45% senior notes	1,000	2022	934	996
6.20% senior notes	1,500	2038	1,481	1,480
4.875% senior notes	500	2040	489	489
3.625% senior notes	375	2042	367	367
8.375% Debentures:				
8.375% debentures	424	2020	486	512
8.375% debentures	276	2030	283	284
Pound Sterling notes:				
5.50% notes	101	2031	97	103
5.13% notes	693	2050	660	699
Floating rate senior notes	377	2049-2053	373	374
Capital lease obligations	481	2013-3004	481	440
Facility notes and bonds	320	2015-2036	320	320
Other debt	3	2013-2022	3	3
Total Debt	$11,720		11,923	12,870
Less: Current Maturities			(1,086)	(1,781)
Long-term Debt			$10,837	$11,089

Debt Repayments
On January 15, 2013, our $1.75 billion 4.5% senior notes matured and were repaid in full.
Debt Classification
We have classified our 3.875% senior notes with a principal balance of $1.0 billion due in April 2014 as a long-term liability, based on our intent and ability to refinance the debt as of June 30, 2013.
Sources of Credit
We are authorized to borrow up to $10.0 billion under the U.S. commercial paper program we maintain. We had $1.045 billion outstanding under this program as of June 30, 2013, with an average interest rate of 0.05%. We also maintain a European commercial paper program under which we are authorized to borrow up to €5.0 billion in a variety of currencies. As of June 30, 2013, there were no amounts outstanding under this program. As of June 30, 2013, we have classified the entire commercial paper balance as a current liability in our consolidated balance sheets.

Table of Contents

UNITED PARCEL SERVICE, INC. AND SUBSIDIARIES
NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

We maintain two credit agreements with a consortium of banks. One of these agreements provides revolving credit facilities of $1.5 billion, and expires on March 28, 2014. Generally, amounts outstanding under this facility bear interest at a periodic fixed rate equal to LIBOR for the applicable interest period and currency denomination, plus an applicable margin. Alternatively, a fluctuating rate of interest equal to the highest of (1) JPMorgan Chase Bank’s publicly announced prime rate, (2) the Federal Funds effective rate plus 0.50%, and (3) LIBOR for a one month interest period plus 1.00%, plus an applicable margin, may be used at our discretion. In each case, the applicable margin for advances bearing interest based on LIBOR is a percentage determined by quotations from Markit Group Ltd. for our 1-year credit default swap spread, subject to a minimum rate of 0.10% and a maximum rate of 0.75%. The applicable margin for advances bearing interest based on the prime rate is 1.00% below the applicable margin for LIBOR advances (but not lower than 0.00%). We are also able to request advances under this facility based on competitive bids for the applicable interest rate. There were no amounts outstanding under this facility as of June 30, 2013.

The second agreement provides revolving credit facilities of $1.0 billion, and expires on March 29, 2018. Generally, amounts outstanding under this facility bear interest at a periodic fixed rate equal to LIBOR for the applicable interest period and currency denomination, plus an applicable margin. Alternatively, a fluctuating rate of interest equal to the highest of (1) JPMorgan Chase Bank’s publicly announced prime rate, (2) the Federal Funds effective rate plus 0.50%, and (3) LIBOR for a one month interest period plus 1.00%, plus an applicable margin, may be used at our discretion. In each case, the applicable margin for advances bearing interest based on LIBOR is a percentage determined by quotations from Markit Group Ltd. for our credit default swap spread, interpolated for a period from the date of determination of such credit default swap spread in connection with a new interest period until the latest maturity date of this facility then in effect (but not less than a period of one year). The applicable margin is subject to certain minimum rates and maximum rates based on our public debt ratings from Standard & Poor’s Rating Service and Moody’s Investors Service. The minimum applicable margin rates range from 0.100% to 0.375%, and the maximum applicable margin rates range from 0.750% to 1.250%, per annum. The applicable margin for advances bearing interest based on the prime rate is 1.00% below the applicable margin for LIBOR advances (but not less than 0.00%). We are also able to request advances under this facility based on competitive bids. There were no amounts outstanding under this facility as of June 30, 2013.

Debt Covenants

Our existing debt instruments and credit facilities subject us to certain financial covenants. As of June 30, 2013 and for all prior periods, we have satisfied these financial covenants. These covenants limit the amount of secured indebtedness that we may incur, and limit the amount of attributable debt in sale-leaseback transactions, to 10% of net tangible assets. As of June 30, 2013, 10% of net tangible assets was equivalent to $2.669 billion; however, we have no covered sale-leaseback transactions or secured indebtedness outstanding. We do not expect these covenants to have a material impact on our financial condition or liquidity.

Fair Value of Debt

Based on the borrowing rates currently available to the Company for long-term debt with similar terms and maturities, the fair value of long-term debt, including current maturities, was approximately $13.086 and $14.658 billion as of June 30, 2013 and December 31, 2012, respectively. We utilized Level 2 inputs in the fair value hierarchy of valuation techniques to determine the fair value of all of our debt instruments.

NOTE 9. LEGAL PROCEEDINGS AND CONTINGENCIES

We are involved in a number of judicial proceedings and other matters arising from the conduct of our business activities.

Although there can be no assurance as to the ultimate outcome, we have generally denied, or believe we have a meritorious defense and will deny, liability in all litigation pending against us, including (except as otherwise noted herein) the matters described below, and we intend to defend vigorously each case. We have accrued for legal claims when, and to the extent that, amounts associated with the claims become probable and can be reasonably estimated.

The actual costs of resolving legal claims may be substantially higher or lower than the amounts accrued for those claims.

For those matters as to which we are not able to estimate a possible loss or range of loss, we are not able to determine whether the loss will have a material adverse effect on our business, financial condition or results of operations or liquidity. For matters in this category, we have indicated in the descriptions that follow the reasons that we are unable to estimate the possible loss or range of loss.

UNITED PARCEL SERVICE, INC. AND SUBSIDIARIES
NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

Judicial Proceedings

We are a defendant in a number of lawsuits filed in state and federal courts containing various class action allegations under state wage-and-hour laws. At this time, we do not believe that any loss associated with these matters, would have a material adverse effect on our financial condition, results of operations or liquidity.

UPS and our subsidiary Mail Boxes Etc., Inc. are defendants in a lawsuit in California Superior Court about the rebranding of The UPS Store franchises. In the Morgate case, the plaintiffs are (1) 125 individual franchisees who did not rebrand to The UPS Store and (2) a certified class of all franchisees who did rebrand. With respect to the 125 individual franchisees described in (1) above, the trial court entered judgment against a bellwether individual plaintiff, which was affirmed in January 2012. In March 2013, we reached a settlement in principle with the remaining individual plaintiffs who did not rebrand. We believe this settlement will not have a material adverse effect on our financial condition, results of operations or liquidity. The trial court granted our motion for summary judgment against the certified class described in (2) above, which was reversed in January 2012. We have not reached a settlement with this class of franchisees, and the claims of the class remain pending.

There are multiple factors that prevent us from being able to estimate the amount of loss, if any, that may result from the remaining aspects of this case, including: (1) we are vigorously defending ourselves and believe we have a number of meritorious legal defenses; and (2) it remains uncertain what evidence of damages, if any, plaintiffs will be able to present. Accordingly, at this time, we are not able to estimate a possible loss or range of loss that may result from this matter or to determine whether such loss, if any, would have a material adverse effect on our financial condition, results of operations or liquidity.

In AFMS LLC v. UPS and FedEx Corporation, a lawsuit filed in federal court in the Central District of California in August 2010, the plaintiff asserts that UPS and FedEx violated U.S. antitrust law by conspiring to refuse to negotiate with third-party negotiators retained by shippers and by individually imposing policies that prevent shippers from using such negotiators. The case is scheduled to go to trial in February 2014. The Antitrust Division of the U.S. Department of Justice (“DOJ”) has an ongoing civil investigation of our policies and practices for dealing with third-party negotiators. We are cooperating with this investigation. We deny any liability with respect to these matters and intend to vigorously defend ourselves. There are multiple factors that prevent us from being able to estimate the amount of loss, if any, that may result from these matters including: (1) we believe that we have a number of meritorious defenses; (2) briefing of dispositive motions is ongoing; and (3) the DOJ investigation is ongoing. Accordingly, at this time, we are not able to estimate a possible loss or range of loss that may result from these matters or to determine whether such loss, if any, would have a material adverse effect on our financial condition, results of operations or liquidity.

In Canada, four purported class-action cases were filed against us in British Columbia (2006); Ontario (2007) and Québec (2006 and 2013). The cases each allege inadequate disclosure concerning the existence and cost of brokerage services provided by us under applicable provincial consumer protection legislation and infringement of interest restriction provisions under the Criminal Code of Canada. The British Columbia class action was declared inappropriate for certification and dismissed by the trial judge. That decision was upheld by the British Columbia Court of Appeal in March 2010, which ended the case in our favor. The Ontario class action was certified in September 2011. Partial summary judgment was granted to us and the plaintiffs by the Ontario motions court. The complaint under the Criminal Code was dismissed. No appeal is being taken from that decision. The allegations of inadequate disclosure were granted and we are appealing that decision. The motion to authorize the 2006 Québec litigation as a class action was dismissed by the motions judge in October 2012; there was no appeal, which ended that case in our favor. The 2013 Québec litigation also has been dismissed. We deny all liability and are vigorously defending the one outstanding case in Ontario. There are multiple factors that prevent us from being able to estimate the amount of loss, if any, that may result from this matter, including: (1) we are vigorously defending ourselves and believe that we have a number of meritorious legal defenses; and (2) there are unresolved questions of law and fact that could be important to the ultimate resolution of this matter. Accordingly, at this time, we are not able to estimate a possible loss or range of loss that may result from this matter or to determine whether such loss, if any, would have a material adverse effect on our financial condition, results of operation or liquidity.

Other Matters

On March 29, 2013, we entered into a Non-Prosecution Agreement (“NPA”) with the United States Attorney's Office in the Northern District of California in connection with an investigation by the Drug Enforcement Administration of shipments by illicit online pharmacies. Under the NPA, we forfeited $40 million to the government, admitted to a Statement of Facts describing the conduct leading to the agreement, and agreed to implement an online pharmacy compliance program. The term of the NPA is two years, although we can petition the government to shorten that term in its discretion to one year. The NPA did not have a material impact on our results of operations in 2013.

In August 2010, competition authorities in Brazil opened an administrative proceeding to investigate alleged anticompetitive behavior in the freight forwarding industry. Approximately 45 freight forwarding companies and individuals are named in the proceeding, including UPS, UPS SCS Transportes (Brasil) S.A., and a former employee in Brazil. UPS will have an opportunity to respond to these allegations. In November 2012, we also received a request for information related to similar matters from authorities in Singapore. UPS responded to that request in January 2013.

We are cooperating with each of these investigations, and intend to continue to vigorously defend ourselves. There are multiple factors that prevent us from being able to estimate the amount of loss, if any, that may result from these matters including: (1) we are vigorously defending each matter and believe that we have a number of meritorious legal defenses; (2) there are unresolved questions of law that could be of importance to the ultimate resolutions of these matters, including the calculation of any potential fine; and (3) there is uncertainty about the time period that is the subject of the investigations. Accordingly, at this time, we are not able to estimate a possible loss or range of loss that may result from these matters or to determine whether such loss, if any, would have a material adverse effect on our financial condition, results of operations or liquidity.

In January 2008, a class action complaint was filed in the United States District Court for the Eastern District of New York alleging price-fixing activities relating to the provision of freight forwarding services. UPS was not named in this case. In July 2009, the plaintiffs filed a First Amended Complaint naming numerous global freight forwarders as defendants. UPS and UPS Supply Chain Solutions are among the 60 defendants named in the amended complaint. The plaintiffs filed a Second Amended Complaint in October 2010, which we moved to dismiss. In August 2012, the Court granted our motion to dismiss all claims relevant to UPS in the Second Amended Complaint, with leave to amend. The plaintiffs filed a Third Amended Complaint in November 2012. We filed another motion to dismiss, which is currently pending before the Court, and will otherwise vigorously defend ourselves in this case. There are multiple factors that prevent us from being able to estimate the amount of loss, if any, that may result from these matters including: (1) the court has dismissed the complaint once but has not considered the adequacy of the amended complaint; (2) the scope and size of the proposed class is ill-defined; (3) there are significant legal questions about the adequacy and standing of the putative class representatives; and (4) we believe that we have a number of meritorious legal defenses. Accordingly, at this time, we are not able to estimate a possible loss or range of loss that may result from these matters or to determine whether such loss, if any, would have a material adverse effect on our financial condition, results of operations or liquidity.

We are a defendant in various other lawsuits that arose in the normal course of business. We do not believe that the eventual resolution of these other lawsuits (either individually or in the aggregate), including any reasonably possible losses in excess of current accruals, will have a material adverse effect on our financial condition, results of operations or liquidity.

Tax Matters

In June 2011, we received an IRS Revenue Agent Report ("RAR") covering excise taxes for tax years 2003 through 2007, in addition to the income tax matters described in note 14. The excise tax RAR proposed two alternate theories for asserting additional excise tax on transportation of property by air. We disagreed with these proposed excise tax theories and related adjustments. We filed protests and, in the third quarter of 2011, the IRS responded to our protests and forwarded the case to IRS Appeals.

Beginning in the third quarter of 2012 and continuing through the first quarter of 2013, we had settlement discussions with the Appeals team. In the first quarter of 2013, we reached settlement terms for a complete resolution of all excise tax matters and correlative income tax refund claims for the 2003 through 2007 tax years. The final resolution of these matters did not materially impact our financial condition, results of operations or liquidity.

Table of Contents

UNITED PARCEL SERVICE, INC. AND SUBSIDIARIES
NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

NOTE 10. SHAREOWNERS' EQUITY

Capital Stock, Additional Paid-In Capital and Retained Earnings

We maintain two classes of common stock, which are distinguished from each other primarily by their respective voting rights. Class A shares are entitled to 10 votes per share, whereas class B shares are entitled to one vote per share. Class A shares are primarily held by UPS employees and retirees, and these shares are fully convertible into class B shares at any time. Class B shares are publicly traded on the New York Stock Exchange under the symbol "UPS". Class A and B shares both have a $0.01 par value, and as of June 30, 2013, there were 4.6 billion class A shares and 5.6 billion class B shares authorized to be issued. Additionally, there are 200 million preferred shares, with a $0.01 par value, authorized to be issued; as of June 30, 2013, no preferred shares had been issued.

The following is a rollforward of our common stock, additional paid-in capital and retained earnings accounts for the six months ended June 30, 2013 and 2012 (in millions, except per share amounts):

	2013 Shares	2013 Dollars	2012 Shares	2012 Dollars
Class A Common Stock				
Balance at beginning of period	225	$3	240	$3
Common stock purchases	(4)	(1)	(3)	—
Stock award plans	5	—	4	—
Common stock issuances	2	—	2	—
Conversions of class A to class B common stock	(10)	—	(8)	—
Class A shares issued at end of period	218	$2	235	$3
Class B Common Stock				
Balance at beginning of period	729	$7	725	$7
Common stock purchases	(18)	—	(8)	—
Conversions of class A to class B common stock	10	—	8	—
Class B shares issued at end of period	721	$7	725	$7
Additional Paid-In Capital				
Balance at beginning of period		$—		$—
Stock award plans		364		291
Common stock purchases		(114)		(606)
Common stock issuances		149		144
Option premiums received (paid)		(399)		206
Unsettled portion of accelerated stock repurchase program		—		(35)
Balance at end of period		$—		$—
Retained Earnings				
Balance at beginning of period		$7,997		$10,128
Net income attributable to common shareowners		2,108		2,086
Dividends ($1.24 and $1.14 per share)		(1,199)		(1,123)
Common stock purchases		(1,721)		(264)
Balance at end of period		$7,185		$10,827

In total, we repurchased 21.8 million shares of class A and class B common stock for $1.836 billion during the six months ended June 30, 2013, and 11.3 million shares for $870 million during the six months ended June 30, 2012. On February 14, 2013, the Board of Directors approved a new share repurchase authorization of $10.0 billion, which replaced an authorization previously announced in 2012. The new share repurchase authorization has no expiration date. Share repurchases may take the form of accelerated share repurchases, open market purchases, or other such methods as we deem appropriate. The timing of our share repurchases will depend upon market conditions. Unless terminated earlier by the resolution of our Board, the program will expire when we have purchased all shares authorized for repurchase under the program.

From time to time, we enter into share repurchase programs with large financial institutions to assist in our buyback of company stock. These programs allow us to repurchase our shares at a price below the weighted average UPS share price for a given period. During the second quarter of 2013, we entered into an accelerated share repurchase program, which allowed us to repurchase $500 million of shares (5.8 million shares). The program was completed in June 2013. In order to lower the average cost of acquiring shares in our ongoing share repurchase program, we periodically enter into structured repurchase agreements involving the use of capped call options for the purchase of UPS class B shares. We pay a fixed sum of cash upon execution of each agreement in exchange for the right to receive either a pre-determined amount of cash or stock. Upon expiration of each agreement, if the closing market price of our common stock is above the pre-determined price, we will have our initial investment returned with a premium in either cash or shares (at our election). If the closing market price of our common stock is at or below the pre-determined price, we will receive the number of shares specified in the agreement. As of June 30, 2013, we paid premiums of $400 million on options for the purchase of 5.3 million shares that will settle in the second half of 2013. During the six months ended June 30, 2013, we settled options that resulted in the receipt of $1 million in premiums (in excess of our initial investment). During the six months ended June 30, 2012, we received $206 million in premiums for options that were entered into during 2011 that expired in 2012, including $6 million in premiums in excess of our initial investment.

Accumulated Other Comprehensive Income (Loss)

We experience activity in AOCI for unrealized holding gains and losses on available-for-sale securities, foreign currency translation adjustments, unrealized gains and losses from derivatives that qualify as hedges of cash flows and unrecognized pension and postretirement benefit costs. The activity in AOCI for the six months ended June 30, 2013 and 2012 is as follows (in millions):

	2013	2012
Foreign currency translation gain (loss):		
Balance at beginning of period	$134	$(160)
Reclassification to earnings (no tax impact in either period)	(161)	—
Translation adjustment (net of tax effect of $3 and $(3))	(166)	(67)
Balance at end of period	(193)	(227)
Unrealized gain (loss) on marketable securities, net of tax:		
Balance at beginning of period	6	6
Current period changes in fair value (net of tax effect of $(5) and $2)	(8)	4
Reclassification to earnings (net of tax effect of $0 and $(1))	—	(3)
Balance at end of period	(2)	7
Unrealized gain (loss) on cash flow hedges, net of tax:		
Balance at beginning of period	(286)	(204)
Current period changes in fair value (net of tax effect of $(14) and $(57))	(22)	(94)
Reclassification to earnings (net of tax effect of $48 and $6)	80	10
Balance at end of period	(228)	(288)
Unrecognized pension and postretirement benefit costs, net of tax:		
Balance at beginning of period	(3,208)	(2,745)
Reclassification to earnings (net of tax effect of $34 and $34)	54	55
Adjustment for Early Retirement Reinsurance Program (net of tax effect of $0 and $4)	—	6
Balance at end of period	(3,154)	(2,684)
Accumulated other comprehensive income (loss) at end of period	$(3,577)	$(3,192)

18

Table of Contents

UNITED PARCEL SERVICE, INC. AND SUBSIDIARIES
NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

Detail of the gains (losses) reclassified from AOCI to the statements of consolidated income for the three and six months ended June 30, 2013 and 2012 is as follows (in millions):

Three Months Ended June 30:

	2013 Amount Reclassified from AOCI	2012 Amount Reclassified from AOCI	Affected Line Item in the Income Statement
Foreign currency translation gain (loss):			
Liquidation of foreign subsidiary	$—	$—	Other expenses
Income tax (expense) benefit	—	—	Income tax expense
Impact on net income	—	—	Net income
Unrealized gain (loss) on marketable securities:			
Realized gain (loss) on sale of securities	—	1	Investment income
Income tax (expense) benefit	—	—	Income tax expense
Impact on net income	—	1	Net income
Unrealized gain (loss) on cash flow hedges:			
Interest rate contracts	(5)	(5)	Interest expense
Foreign exchange contracts	6	(19)	Interest expense
Foreign exchange contracts	(12)	9	Revenue
Commodity contracts	(38)	—	Fuel expense
Income tax (expense) benefit	18	6	Income tax expense
Impact on net income	(31)	(9)	Net income
Unrecognized pension and postretirement benefit costs:			
Prior service costs	(44)	(45)	Compensation and benefits
Income tax (expense) benefit	16	18	Income tax expense
Impact on net income	(28)	(27)	Net income
Total amount reclassified for the period	$(59)	$(35)	Net income

Table of Contents
UNITED PARCEL SERVICE, INC. AND SUBSIDIARIES
NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

Six Months Ended June 30:

	2013 Amount Reclassified from AOCI	2012 Amount Reclassified from AOCI	Affected Line Item in the Income Statement
Foreign currency translation gain (loss):			
Liquidation of foreign subsidiary	$161	$—	Other expenses
Income tax (expense) benefit	—	—	Income tax expense
Impact on net income	161	—	Net income
Unrealized gain (loss) on marketable securities:			
Realized gain (loss) on sale of securities	—	4	Investment income
Income tax (expense) benefit	—	(1)	Income tax expense
Impact on net income	—	3	Net income
Unrealized gain (loss) on cash flow hedges:			
Interest rate contracts	(10)	(10)	Interest expense
Foreign exchange contracts	(44)	(3)	Interest expense
Foreign exchange contracts	(26)	(3)	Revenue
Commodity contracts	(48)	—	Fuel expense
Income tax (expense) benefit	48	6	Income tax expense
Impact on net income	(80)	(10)	Net income
Unrecognized pension and postretirement benefit costs:			
Prior service costs	(88)	(89)	Compensation and benefits
Income tax (expense) benefit	34	34	Income tax expense
Impact on net income	(54)	(55)	Net income
Total amount reclassified for the period	$27	$(62)	Net income

Deferred Compensation Obligations and Treasury Stock
Activity in the deferred compensation program for the six months ended June 30, 2013 and 2012 is as follows (in millions):

	2013 Shares	2013 Dollars	2012 Shares	2012 Dollars
Deferred Compensation Obligations:				
Balance at beginning of period		$78		$88
Reinvested dividends		2		2
Benefit payments		(13)		(14)
Balance at end of period		$67		$76
Treasury Stock:				
Balance at beginning of period	(1)	$(78)	(2)	$(88)
Reinvested dividends	—	(2)	—	(2)
Benefit payments	—	13	—	14
Balance at end of period	(1)	$(67)	(2)	$(76)

Table of Contents

UNITED PARCEL SERVICE, INC. AND SUBSIDIARIES
NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

Noncontrolling Interests:

We have noncontrolling interests in certain consolidated subsidiaries in our International Package and Supply Chain & Freight segments. The activity related to our noncontrolling interests is presented below for the six months ended June 30, 2013 and 2012 (in millions):

	2013	2012
Noncontrolling Interests:		
Balance at beginning of period	$80	$73
Acquired noncontrolling interests	(67)	7
Dividends attributable to noncontrolling interests	—	—
Net income attributable to noncontrolling interests	—	—
Balance at end of period	$13	$80

The reduction in our noncontrolling interests in 2013 primarily relates to our purchase of the remaining noncontrolling interest in a joint venture that operates in the Middle East, Turkey and portions of the Central Asia region for $70 million. After this transaction, we own 100% of this entity.

NOTE 11. SEGMENT INFORMATION

We report our operations in three segments: U.S. Domestic Package operations, International Package operations and Supply Chain & Freight operations. Package operations represent our most significant business and are broken down into regional operations around the world. Regional operations managers are responsible for both domestic and export operations within their geographic area.

U.S. Domestic Package

Domestic Package operations include the time-definite delivery of letters, documents and packages throughout the United States.

International Package

International Package operations include delivery to more than 220 countries and territories worldwide, including shipments wholly outside the United States, as well as U.S. export and U.S. import shipments. Our International Package reporting segment includes the operations of our Europe, Asia and Americas operating segments.

Supply Chain & Freight

Supply Chain & Freight includes the operations of our forwarding, logistics and freight units, as well as other aggregated businesses. Our forwarding and logistics business provides services in more than 195 countries and territories worldwide, and includes supply chain design and management, freight distribution, customs brokerage, mail and consulting services. UPS Freight offers a variety of less-than-truckload (“LTL”) and truckload (“TL”) services to customers in North America. Other aggregated business units within this segment include The UPS Store and UPS Capital.

In evaluating financial performance, we focus on operating profit as a segment’s measure of profit or loss. Operating profit is before investment income, interest expense and income taxes. The accounting policies of the reportable segments are the same as those described in the summary of accounting policies included in the consolidated financial statements in our Annual Report on Form 10-K for the year ended December 31, 2012, with certain expenses allocated between the segments using activity-based costing methods. Unallocated assets are comprised primarily of cash, marketable securities and investments in limited partnerships.

Table of Contents
UNITED PARCEL SERVICE, INC. AND SUBSIDIARIES
NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

Segment information for the three and six months ended June 30, 2013 and 2012 is as follows (in millions):

	Three Months Ended June 30,		Six Months Ended June 30,	
	2013	2012	2013	2012
Revenue:				
U.S. Domestic Package	$8,241	$8,058	$16,512	$16,062
International Package	3,062	3,014	6,040	5,980
Supply Chain & Freight	2,204	2,277	4,389	4,443
Consolidated	$13,507	$13,349	$26,941	$26,485
Operating Profit:				
U.S. Domestic Package	$1,132	$1,134	$2,217	$2,129
International Package	451	454	803	862
Supply Chain & Freight	159	202	302	368
Consolidated	$1,742	$1,790	$3,322	$3,359

NOTE 12. EARNINGS PER SHARE

The following table sets forth the computation of basic and diluted earnings per share for the three and six months ended June 30, 2013 and 2012 (in millions, except per share amounts):

	Three Months Ended June 30,		Six Months Ended June 30,	
	2013	2012	2013	2012
Numerator:				
Net income attributable to common shareowners	$1,071	$1,116	$2,108	$2,086
Denominator:				
Weighted average shares	941	959	945	959
Deferred compensation obligations	1	2	1	2
Vested portion of restricted shares	1	1	2	1
Denominator for basic earnings per share	943	962	948	962
Effect of dilutive securities:				
Restricted shares	8	8	7	9
Stock options	1	1	1	1
Denominator for diluted earnings per share	952	971	956	972
Basic earnings per share	$1.14	$1.16	$2.22	$2.17
Diluted earnings per share	$1.13	$1.15	$2.21	$2.15

Diluted earnings per share for the three months ended June 30, 2013 and 2012 exclude the effect of 0.0 and 2.6 million shares of common stock (0.1 and 2.6 million for the six months ended June 30, 2013 and 2012), respectively, that may be issued upon the exercise of employee stock options because such effect would be antidilutive.

NOTE 13. DERIVATIVE INSTRUMENTS AND RISK MANAGEMENT

Risk Management Policies

We are exposed to market risk, primarily related to foreign exchange rates, commodity prices and interest rates. These exposures are actively monitored by management. To manage the volatility relating to certain of these exposures, we enter into a variety of derivative financial instruments. Our objective is to reduce, where it is deemed appropriate to do so, fluctuations in earnings and cash flows associated with changes in foreign currency rates, commodity prices and interest rates. It is our policy and practice to use derivative financial instruments only to the extent necessary to manage exposures. As we use price sensitive instruments to hedge a certain portion of our existing and anticipated transactions, we expect that any loss in value for those instruments generally would be offset by increases in the value of those hedged transactions. We do not hold or issue derivative financial instruments for trading or speculative purposes.

Credit Risk Management

The forward contracts, swaps and options discussed below contain an element of risk that the counterparties may be unable to meet the terms of the agreements; however, we minimize such risk exposures for these instruments by limiting the counterparties to banks and financial institutions that meet established credit guidelines, and monitoring counterparty credit risk to prevent concentrations of credit risk with any single counterparty.

We have agreements with all of our active counterparties (covering the majority of our derivative positions) containing early termination rights and/or zero threshold bilateral collateral provisions whereby cash is required based on the net fair value of derivatives associated with those counterparties. Events such as a counterparty credit rating downgrade (depending on the ultimate rating level) could also allow us to take additional protective measures such as the early termination of trades. At June 30, 2013, we held cash collateral of $164 million under these agreements.

In connection with the agreements described above, we could also be required to provide collateral or terminate transactions with certain counterparties in the event of a downgrade of our credit rating. The amount of collateral required would be determined by the net fair value of the associated derivatives with each counterparty. At June 30, 2013, the aggregate fair value of the instruments covered by these contractual features that were in a net liability position was $198 million; and we were required to post $10 million in collateral with our counterparties as of that date.

We have not historically incurred, and do not expect to incur in the future, any losses as a result of counterparty default.

Accounting Policy for Derivative Instruments

We recognize all derivative instruments as assets or liabilities in the consolidated balance sheets at fair value. The accounting for changes in the fair value of a derivative instrument depends on whether it has been designated and qualifies as part of a hedging relationship and, further, on the type of hedging relationship. For those derivative instruments that are designated and qualify as hedging instruments, a company must designate the derivative, based upon the exposure being hedged, as a cash flow hedge, a fair value hedge or a hedge of a net investment in a foreign operation.

A cash flow hedge refers to hedging the exposure to variability in expected future cash flows that is attributable to a particular risk. For derivative instruments that are designated and qualify as a cash flow hedge, the effective portion of the gain or loss on the derivative instrument is reported as a component of AOCI, and reclassified into earnings in the same period during which the hedged transaction affects earnings. The remaining gain or loss on the derivative instrument in excess of the cumulative change in the present value of future cash flows of the hedged item, or hedge components excluded from the assessment of effectiveness, are recognized in the statements of consolidated income during the current period.

A fair value hedge refers to hedging the exposure to changes in the fair value of an existing asset or liability on the consolidated balance sheets that is attributable to a particular risk. For derivative instruments that are designated and qualify as a fair value hedge, the gain or loss on the derivative instrument is recognized in the statements of

consolidated income during the current period, as well as the offsetting gain or loss on the hedged item.
A net investment hedge refers to the use of cross currency swaps, forward contracts or foreign currency denominated debt to hedge portions of our net investments in foreign operations. For hedges that meet the effectiveness requirements, the net gains or losses attributable to changes in spot exchange rates are recorded in the cumulative translation adjustment within other AOCI. The remainder of the change in value of such instruments is recorded in earnings.

Types of Hedges

Commodity Risk Management

Currently, the fuel surcharges that we apply to our domestic and international package and LTL services are the primary means of reducing the risk of adverse fuel price changes on our business. We periodically enter into option contracts on energy commodity products to manage the price risk associated with forecasted transactions involving refined fuels, principally jet-A, diesel and unleaded gasoline. The objective of the hedges is to reduce the variability of cash flows, due to changing fuel prices, associated with the forecasted transactions involving those products. We have designated and account for these contracts as cash flow hedges of the underlying forecasted transactions involving these fuel products and, therefore, the resulting gains and losses from these hedges are recognized as a component of fuel expense or revenue when the underlying transactions occur.

Foreign Currency Risk Management

To protect against the reduction in value of forecasted foreign currency cash flows from our international package business, we maintain a foreign currency cash flow hedging program. Our most significant foreign currency exposures relate to the Euro, British Pound Sterling, Canadian Dollar, Chinese Renminbi and Hong Kong Dollar. We hedge portions of our forecasted revenue denominated in foreign currencies with option contracts. We have designated and account for these contracts as cash flow hedges of anticipated foreign currency denominated revenue and, therefore, the resulting gains and losses from these hedges are recognized as a component of international package revenue when the underlying sales transactions occur.

We also hedge portions of our anticipated cash settlements of intercompany transactions subject to foreign currency remeasurement using foreign currency forward contracts. We have designated and account for these contracts as cash flow hedges of forecasted foreign currency denominated transactions; therefore, the resulting gains and losses from these hedges are recognized as a component of other operating expense when the underlying transactions are subject to currency remeasurement.

We have foreign currency denominated debt obligations and capital lease obligations associated with our aircraft. For some of these debt obligations and leases, we hedge the foreign currency denominated contractual payments using cross-currency interest rate swaps, which effectively convert the foreign currency denominated contractual payments into U.S. Dollar denominated payments. We have designated and account for these swaps as cash flow hedges of the forecasted contractual payments; therefore, the resulting gains and losses from these hedges are recognized in the statements of consolidated income when the currency remeasurement gains and losses on the underlying debt obligations and leases are incurred.

Interest Rate Risk Management

Our indebtedness under our various financing arrangements creates interest rate risk. We use a combination of derivative instruments, including interest rate swaps and cross-currency interest rate swaps, as part of our program to manage the fixed and floating interest rate mix of our total debt portfolio and related overall cost of borrowing. The notional amount, interest payment date and maturity date of the swaps match the terms of the associated debt being hedged. Interest rate swaps allow us to maintain a target range of floating rate debt within our capital structure.

We have designated and account for the majority of our interest rate swaps that convert fixed rate interest payments into floating rate interest payments as hedges of the fair value of the associated debt instruments. Therefore, the gains and losses resulting from fair value adjustments to the interest rate swaps and fair value adjustments to the associated debt instruments are recorded to interest expense in the period in which the gains and losses occur. We have designated and account for interest rate swaps that convert floating rate interest payments into fixed rate interest payments as cash flow hedges of the forecasted payment obligations. The gains and losses resulting from fair value adjustments to the interest rate swaps are recorded to AOCI.

We periodically hedge the forecasted fixed-coupon interest payments associated with anticipated debt offerings, using forward starting interest rate swaps, interest rate locks or similar derivatives. These agreements effectively lock a portion of our interest rate exposure between the time the agreement is entered into and the date when the debt offering is completed, thereby mitigating the impact of interest rate changes on future interest expense. These derivatives are settled commensurate with the issuance of the debt, and any gain or loss upon settlement is amortized as an adjustment to the effective interest yield on the debt.

Table of Contents
UNITED PARCEL SERVICE, INC. AND SUBSIDIARIES
NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

Outstanding Positions
As of June 30, 2013 and December 31, 2012, the notional amounts of our outstanding derivative positions were as follows (in millions):

	June 30, 2013		December 31, 2012	
Currency hedges:				
British Pound Sterling	GBP	915	GBP	797
Canadian Dollar	CAD	296	CAD	341
Euro	EUR	2,061	EUR	1,783
Indian Rupee	INR	985	INR	—
Malaysian Ringgit	MYR	700	MYR	500
Mexican Peso	MXN	3,340	MXN	—
United Arab Emirates Dirham	AED	—	AED	551
Interest rate hedges:				
Fixed to Floating Interest Rate Swaps	$	6,049	$	7,274
Floating to Fixed Interest Rate Swaps	$	781	$	781
Interest Rate Basis Swaps	$	2,500	$	2,500

Balance Sheet Recognition and Fair Value Measurements
The following table indicates the location on the consolidated balance sheets in which our derivative assets and liabilities have been recognized, the fair value hierarchy level applicable to each derivative type and the related fair values of those derivatives (in millions). The table is segregated between those derivative instruments that qualify and are designated as hedging instruments and those that are not, as well as by type of contract and whether the derivative is in an asset or liability position.
We have master netting arrangements with substantially all of our counterparties giving us the right of offset for our derivative positions. However, we have not elected to offset the fair value positions of our derivative contracts recorded on our consolidated balance sheets. The columns labeled "Net Amounts if Right of Offset had been Applied" indicate the potential net fair value positions by type of contract and location on the consolidated balance sheets had we elected to apply the right of offset.

Asset Derivatives	Balance Sheet Location	Fair Value Hierarchy Level	Gross Amounts Presented in Consolidated Balance Sheets June 30, 2013	Gross Amounts Presented in Consolidated Balance Sheets December 31, 2012	Net Amounts if Right of Offset had been Applied June 30, 2013	Net Amounts if Right of Offset had been Applied December 31, 2012
Derivatives designated as hedges:						
Foreign exchange contracts	Other current assets	Level 2	$64	$27	$64	$27
Interest rate contracts	Other current assets	Level 2	21	1	21	1
Foreign exchange contracts	Other non-current assets	Level 2	34	14	34	12
Interest rate contracts	Other non-current assets	Level 2	236	420	162	406
Derivatives not designated as hedges:						
Foreign exchange contracts	Other current assets	Level 2	22	3	21	3
Interest rate contracts	Other non-current assets	Level 2	61	101	58	91
Total Asset Derivatives			$438	$566	$360	$540

25

Table of Contents
UNITED PARCEL SERVICE, INC. AND SUBSIDIARIES
NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

Liability Derivatives	Balance Sheet Location	Fair Value Hierarchy Level	Gross Amounts Presented in Consolidated Balance Sheets June 30, 2013	Gross Amounts Presented in Consolidated Balance Sheets December 31, 2012	Net Amounts if Right of Offset had been Applied June 30, 2013	Net Amounts if Right of Offset had been Applied December 31, 2012
Derivatives designated as hedges:						
Foreign exchange contracts	Other non-current liabilities	Level 2	$113	$103	$113	$101
Interest rate contracts	Other non-current liabilities	Level 2	79	14	5	—
Derivatives not designated as hedges:						
Foreign exchange contracts	Other current liabilities	Level 2	1	1	—	1
Interest rate contracts	Other current liabilities	Level 2	1	—	1	—
Interest rate contracts	Other non-current liabilities	Level 2	4	41	1	31
Total Liability Derivatives			$198	$159	$120	$133

Our foreign currency, interest rate and energy derivatives are largely comprised of over-the-counter derivatives, which are primarily valued using pricing models that rely on market observable inputs such as yield curves, currency exchange rates and commodity forward prices; therefore, these derivatives are classified as Level 2.

Income Statement and Other Comprehensive Income Recognition

The following table indicates the amount of gains and losses that have been recognized in other comprehensive income for the three and six months ended June 30, 2013 and 2012 for those derivatives designated as cash flow hedges (in millions):

Three Months Ended June 30:

Derivative Instruments in Cash Flow Hedging Relationships	2013 Amount of Gain (Loss) Recognized in OCI on Derivative (Effective Portion)	2012 Amount of Gain (Loss) Recognized in OCI on Derivative (Effective Portion)
Interest rate contracts	$2	$(53)
Foreign exchange contracts	10	(31)
Commodity contracts	(30)	—
Total	$(18)	$(84)

Six Months Ended June 30:

Derivative Instruments in Cash Flow Hedging Relationships	2013 Amount of Gain (Loss) Recognized in OCI on Derivative (Effective Portion)	2012 Amount of Gain (Loss) Recognized in OCI on Derivative (Effective Portion)
Interest rate contracts	$3	$(61)
Foreign exchange contracts	9	(90)
Commodity contracts	(48)	—
Total	$(36)	$(151)

As of June 30, 2013, $21 million of pre-tax losses related to cash flow hedges that are currently deferred in AOCI are expected to be reclassified to income over the 12 month period ended June 30, 2014. The actual amounts that will be reclassified to income over the next 12 months will vary from this amount as a result of changes in market conditions. The maximum term over which we are hedging exposures to the variability of cash flow is 37 years.

The amount of ineffectiveness recognized in income on derivative instruments designated in cash flow hedging relationships was immaterial for the three and six months ended June 30, 2013 and 2012.

The following table indicates the amount and location in the statements of consolidated income in which derivative gains and losses, as well as the associated gains and losses on the underlying exposure, have been recognized for those derivatives designated as fair value hedges for the three and six months ended June 30, 2013 and 2012 (in millions):

Derivative Instruments in Fair Value Hedging Relationships	Location of Gain (Loss) Recognized in Income	2013 Amount of Gain (Loss) Recognized in Income	2012 Amount of Gain (Loss) Recognized in Income	Hedged Items in Fair Value Hedging Relationships	Location of Gain (Loss) Recognized In Income	2013 Amount of Gain (Loss) Recognized in Income	2012 Amount of Gain (Loss) Recognized in Income
Three Months Ended June 30:							
Interest rate contracts	Interest Expense	$(187)	$72	Fixed-Rate Debt and Capital Leases	Interest Expense	$187	$(72)
Six Months Ended June 30:							
Interest rate contracts	Interest Expense	$(233)	$36	Fixed-Rate Debt and Capital Leases	Interest Expense	$233	$(36)

Additionally, we maintain some interest rate swap and foreign exchange forward contracts that are not designated as hedges. These interest rate swap contracts are intended to provide an economic hedge of a portfolio of interest bearing receivables. These foreign exchange forward contracts are intended to provide an economic offset to foreign currency remeasurement risks for certain assets and liabilities in our consolidated balance sheets.

We also periodically terminate interest rate swaps and foreign currency options by entering into offsetting swap and foreign currency positions with different counterparties. As part of this process, we de-designate our original swap and foreign currency contracts. These transactions provide an economic offset that effectively eliminates the effects of changes in market valuation.

We have entered into several interest rate basis swaps, which effectively convert cash flows based on variable LIBOR-based interest rates to cash flows based on the prevailing federal funds interest rate. These swaps are not designated as hedges, and all amounts related to fair value changes and settlements are recorded to interest expense in the statements of consolidated income.

The following is a summary of the amounts recorded in the statements of consolidated income related to fair value changes and settlements of these interest rate swaps and foreign currency forward contracts not designated as hedges (in millions):

Derivative Instruments not Designated in Hedging Relationships	Location of Gain (Loss) Recognized in Income	2013 Amount of Gain (Loss) Recognized in Income	2012 Amount of Gain (Loss) Recognized in Income
Three Months Ended June 30:			
Interest rate contracts	Interest Expense	$(4)	$(2)
Foreign exchange contracts	Other Operating Expenses	(3)	42
Foreign exchange contracts	Investment Income	20	—
		$13	$40
Six Months Ended June 30:			
Interest rate contracts	Interest Expense	$(4)	