FEDEX CORP
Form 10-Q
September 19, 2012
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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 August 31, 2012

OR

¨ **TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**
FOR THE TRANSITION PERIOD FROM ______ TO ______

Commission File Number: 1-15829

FEDEX CORPORATION

(Exact name of registrant as specified in its charter)

Delaware	**62-1721435**
(State or other jurisdiction of incorporation or organization)	**(I.R.S. Employer Identification No.)**
942 South Shady Grove Road Memphis, Tennessee	**38120**
(Address of principal executive offices)	**(ZIP Code)**

(901) 818-7500

(Registrant s telephone number, including area code)

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 has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§ 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes x 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 the definitions of large accelerated filer, accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act.

Large accelerated filer x	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 x

Indicate the number of shares outstanding of each of the issuer s classes of common stock, as of the latest practicable date.

Common Stock	Outstanding Shares at September 17, 2012
Common Stock, par value $0.10 per share	314,090,117

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FEDEX CORPORATION

CONDENSED CONSOLIDATED BALANCE SHEETS

(IN MILLIONS)

	August 31, 2012 (Unaudited)	May 31, 2012
ASSETS		
CURRENT ASSETS		
Cash and cash equivalents	$ 2,743	$ 2,843
Receivables, less allowances of $166 and $178	4,780	4,704
Spare parts, supplies and fuel, less allowances of $187 and $184	465	440
Deferred income taxes	518	533
Prepaid expenses and other	371	536
Total current assets	8,877	9,056
PROPERTY AND EQUIPMENT, AT COST	36,962	36,164
Less accumulated depreciation and amortization	19,096	18,916
Net property and equipment	17,866	17,248
OTHER LONG-TERM ASSETS		
Goodwill	2,734	2,387
Other assets	1,214	1,212
Total other long-term assets	3,948	3,599
	$ 30,691	$ 29,903

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

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FEDEX CORPORATION

CONDENSED CONSOLIDATED BALANCE SHEETS

(IN MILLIONS, EXCEPT SHARE DATA)

	August 31, 2012 (Unaudited)	May 31, 2012
LIABILITIES AND STOCKHOLDERS INVESTMENT		
CURRENT LIABILITIES		
Current portion of long-term debt	$ 117	$ 417
Accrued salaries and employee benefits	1,157	1,635
Accounts payable	1,643	1,613
Accrued expenses	1,892	1,709
Total current liabilities	4,809	5,374
LONG-TERM DEBT, LESS CURRENT PORTION	2,242	1,250
OTHER LONG-TERM LIABILITIES		
Deferred income taxes	879	836
Pension, postretirement healthcare and other benefit obligations	5,519	5,582
Self-insurance accruals	987	963
Deferred lease obligations	839	784
Deferred gains, principally related to aircraft transactions	245	251
Other liabilities	147	136
Total other long-term liabilities	8,616	8,552
COMMITMENTS AND CONTINGENCIES		
COMMON STOCKHOLDERS INVESTMENT		
Common stock, $0.10 par value; 800 million shares authorized; 317 million shares issued as of August 31, 2012 and May 31, 2012	32	32
Additional paid-in capital	2,612	2,595
Retained earnings	17,505	17,134
Accumulated other comprehensive loss	(4,847)	(4,953)
Treasury stock, at cost	(278)	(81)
Total common stockholders investment	15,024	14,727
	$ 30,691	$ 29,903

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

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FEDEX CORPORATION

CONDENSED CONSOLIDATED STATEMENTS OF INCOME

(UNAUDITED)

(IN MILLIONS, EXCEPT PER SHARE AMOUNTS)

	Three Months Ended August 31, 2012	Three Months Ended August 31, 2011
REVENUES	$ 10,792	$ 10,521
OPERATING EXPENSES:		
Salaries and employee benefits	4,103	4,004
Purchased transportation	1,680	1,518
Rentals and landing fees	618	620
Depreciation and amortization	573	509
Fuel	1,138	1,244
Maintenance and repairs	542	551
Other	1,396	1,338
	10,050	9,784
OPERATING INCOME	742	737
OTHER INCOME (EXPENSE):		
Interest, net	(10)	(11)
Other, net	(5)	(2)
	(15)	(13)
INCOME BEFORE INCOME TAXES	727	724
PROVISION FOR INCOME TAXES	268	260
NET INCOME	$ 459	$ 464
EARNINGS PER COMMON SHARE:		
Basic	$ 1.46	$ 1.46
Diluted	$ 1.45	$ 1.46
DIVIDENDS DECLARED PER COMMON SHARE	$ 0.28	$ 0.26

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

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FEDEX CORPORATION

CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

(UNAUDITED)

(IN MILLIONS)

	Three Months Ended August 31, 2012	Three Months Ended August 31, 2011
NET INCOME	$ 459	$ 464
OTHER COMPREHENSIVE INCOME:		
Foreign currency translation adjustments, net of tax of $4 in 2012 and 2011	43	19
Amortization of unrealized pension actuarial gains/losses and other, net of tax of $37 in 2012 and $18 in 2011	63	30
COMPREHENSIVE INCOME	$ 565	$ 513

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

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FEDEX CORPORATION

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(UNAUDITED)

(IN MILLIONS)

	Three Months Ended August 31, 2012	Three Months Ended August 31, 2011
Operating Activities:		
Net income	$ 459	$ 464
Adjustments to reconcile net income to cash provided by operating activities:		
Depreciation and amortization	573	509
Provision for uncollectible accounts	47	43
Stock-based compensation	40	37
Deferred income taxes and other noncash items	122	131
Changes in assets and liabilities:		
Receivables	3	(41)
Other assets	147	1
Accounts payable and other liabilities	(474)	(263)
Other, net	(14)	(21)
Cash provided by operating activities	903	860
Investing Activities:		
Capital expenditures	(972)	(1,110)
Business acquisitions, net of cash acquired	(483)	(111)
Proceeds from asset dispositions and other	12	5
Cash used in investing activities	(1,443)	(1,216)
Financing Activities:		
Principal payments on debt	(301)	(17)
Proceeds from debt issuance	991	
Proceeds from stock issuances	30	28
Excess tax benefit on the exercise of stock options	4	4
Dividends paid	(44)	(41)
Purchase of treasury stock	(246)	
Other, net	(9)	
Cash provided by (used in) financing activities	425	(26)
Effect of exchange rate changes on cash	15	13
Net decrease in cash and cash equivalents	(100)	(369)
Cash and cash equivalents at beginning of period	2,843	2,328

Cash and cash equivalents at end of period	$	2,743	$	1,959

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

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FEDEX CORPORATION

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(UNAUDITED)

(1) General

SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES. These interim financial statements of FedEx Corporation (FedEx) have been prepared in accordance with accounting principles generally accepted in the United States and Securities and Exchange Commission (SEC) instructions for interim financial information, and should be read in conjunction with our Annual Report on Form 10-K for the year ended May 31, 2012 (Annual Report). Accordingly, significant accounting policies and other disclosures normally provided have been omitted since such items are disclosed in our Annual Report.

In the opinion of management, the accompanying unaudited condensed consolidated financial statements reflect all adjustments (including normal recurring adjustments) necessary to present fairly our financial position as of August 31, 2012, and the results of our operations and cash flows for the three-month periods ended August 31, 2012 and 2011. Operating results for the three-month period ended August 31, 2012 are not necessarily indicative of the results that may be expected for the year ending May 31, 2013.

Except as otherwise specified, references to years indicate our fiscal year ending May 31, 2013 or ended May 31 of the year referenced and comparisons are to the corresponding period of the prior year.

BUSINESS ACQUISITIONS. In the first quarter of 2013, we have continued to expand the international service offerings of FedEx Express by completing the following business acquisitions:

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

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

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

These acquisitions give us more robust transportation networks within these countries and added capabilities in these important international markets.

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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 and therefore, pro forma financial information has not been presented. The estimated fair values of the assets and liabilities related to these acquisitions have been included in the accompanying unaudited balance sheet based on a preliminary allocation of the purchase price (summarized in the table below in millions). These allocations will be finalized as soon as the information becomes available, which shall not exceed one year from the acquisition date.

Cash and cash equivalents	$	24
Receivables		117
Other current assets		5
Property and equipment		88
Goodwill		333
Intangible assets		58
Other non-current assets		68
Current liabilities		(170)
Long-term liabilities		(16)
Total purchase price	$	507

The portion of the purchase price allocated to goodwill is not deductible for U.S. income tax purposes. The intangible assets acquired consist primarily of customer-related intangible assets, which will be amortized on an accelerated basis over their average estimated useful lives of nine years, with the majority of the amortization recognized during the first five years.

STOCK-BASED COMPENSATION. We have two types of equity-based compensation: stock options and restricted stock. The key terms of the stock option and restricted stock awards granted under our incentive stock plans and all financial disclosures about these programs are set forth in our Annual Report.

Our stock-based compensation expense was $40 million for the three-month period ended August 31, 2012 and $37 million for the three-month period ended August 31, 2011. Due to its immateriality, additional disclosures related to stock-based compensation have been excluded from this quarterly report.

NEW ACCOUNTING GUIDANCE. New accounting rules and disclosure requirements can significantly impact our reported results and the comparability of our financial statements.

On June 1, 2012, we adopted the authoritative guidance issued by the Financial Accounting Standards Board (FASB) on the presentation of comprehensive income. The new guidance requires companies to report components of comprehensive income by including comprehensive income on the face of the income statement or in a separate statement of comprehensive income. We adopted this guidance by including a separate statement of comprehensive income in the first quarter of 2013. In addition, we adopted the FASB s amendments to the fair value measurements and disclosure requirements during the first quarter of 2013, which expands existing disclosure requirements regarding the fair value of our long-term debt.

We believe that no other new accounting guidance was adopted or issued during the first three months of 2013 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.

TREASURY SHARES. During the first quarter of 2013, we repurchased 2.7 million shares of FedEx common stock at an average price of $91 per share for a total of $246 million. As of August 31, 2012, 188,000 shares remained under existing share repurchase authorizations.

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DIVIDENDS DECLARED PER COMMON SHARE. On August 17, 2012, our Board of Directors declared a dividend of $0.14 per share of common stock. The dividend will be paid on October 1, 2012 to stockholders of record as of the close of business on September 10, 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.

(2) Financing Arrangements

In September 2012, we expect to file a new shelf registration statement with the SEC that will allow us to sell, in one or more future offerings, any combination of our unsecured debt securities and common stock.

During the first quarter of 2013, we repaid our $300 million 9.65% unsecured notes that matured on June 15, 2012 using cash from operations.

In July 2012, we issued $1 billion of senior unsecured debt under a then current shelf registration statement, comprised of $500 million of 2.625% fixed-rate notes due in August 2022 and $500 million of 3.875% fixed-rate notes due in August 2042. Interest on these notes is payable semi-annually. We are utilizing the net proceeds for working capital and general corporate purposes.

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 August 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 August 31, 2012, no commercial paper was outstanding and the entire $1 billion under the revolving credit facility was available for future borrowings.

Long-term debt, exclusive of capital leases, had a carrying value of $2.2 billion compared with an estimated fair value of $2.6 billion at August 31, 2012 and $1.5 billion compared with an estimated fair value of $2.0 billion at May 31, 2012. The estimated fair values were determined based on quoted market prices and the current rates offered for debt with similar terms and maturities. The fair value of our long-term debt is classified as Level 2 within the fair value hierarchy. This classification is defined as a fair value determined using market-based inputs other than quoted prices that are observable for the liability, either directly or indirectly.

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(3) Computation of Earnings Per Share

The calculation of basic and diluted earnings per common share for the three-month periods ended August 31was as follows (in millions, except per share amounts):

	2012	2011
Basic earnings per common share:		
Net earnings allocable to common shares[1]	$ 458	$ 463
Weighted-average common shares	315	316
Basic earnings per common share	$ 1.46	$ 1.46
Diluted earnings per common share:		
Net earnings allocable to common shares[1]	$ 458	$ 463
Weighted-average common shares	315	316
Dilutive effect of share-based awards	1	2
Weighted-average diluted shares	316	318
Diluted earnings per common share	$ 1.45	$ 1.46
Anti-dilutive options excluded from diluted earnings per common share	13.9	13.2

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

(4) 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. Key terms of our retirement plans are provided in our Annual Report. Our retirement plans costs for the three-month periods ended August 31 were as follows (in millions):

	2012	2011
U.S. domestic and international pension plans	$ 169	$ 132
U.S. domestic and international defined contribution plans	88	86
Postretirement healthcare plans	19	18
	$ 276	$ 236

Net periodic benefit cost of the pension and postretirement healthcare plans for the three-month periods ended August 31 included the following components (in millions):

	Pension Plans		Postretirement Healthcare Plans	
	2012	2011	2012	2011
Service cost	$ 173	$ 148	$ 10	$ 9
Interest cost	242	244	9	9
Expected return on plan assets	(346)	(309)		
Recognized actuarial losses (gains) and other	100	49		
	$ 169	$ 132	$ 19	$ 18

Required contributions to our tax qualified U.S. domestic pension plans (U.S. Pension Plans) for the three-month periods ended August 31 were $140 million in 2012 and $99 million in 2011. In September 2012, we made an additional contribution of $140 million to our U.S. Pension Plans. Our U.S. Pension Plans have ample funds to meet expected benefit payments.

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(5) Business Segment Information

We provide 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 include 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.

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.

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The operating expenses line item Intercompany charges on the accompanying unaudited financial summaries of our transportation segments in Management s Discussion and Analysis of Results of Operations and Financial Condition 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.

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 and operating income to our unaudited condensed consolidated financial statement totals for the three-month periods ended August 31 (in millions):

	2012	2011
Revenues		
FedEx Express segment	$ 6,632	$ 6,592
FedEx Ground segment	2,462	2,278
FedEx Freight segment	1,399	1,328
FedEx Services segment	389	411
Other and eliminations	(90)	(88)
	$ 10,792	$ 10,521
Operating Income		
FedEx Express segment	$ 207	$ 288
FedEx Ground segment	445	407
FedEx Freight segment	90	42
	$ 742	$ 737

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(6) Commitments

As of August 31, 2012, our purchase commitments under various contracts for the remainder of 2013 and annually thereafter were as follows (in millions):

	Aircraft and Aircraft-Related	Other[1]	Total
2013 (remainder)	$ 596	$ 640	$ 1,236
2014	577	204	781
2015	966	115	1,081
2016	978	78	1,056
2017	978	53	1,031
Thereafter	5,803	139	5,942

(1) Primarily vehicles, facilities, advertising contracts, and for the remainder of 2013, a total of $420 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. 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.

On June 29, 2012, FedEx Express entered into a supplemental agreement to purchase nine additional Boeing 767-300 Freighter (B767F) aircraft. Additionally, FedEx Express exercised ten B767F options acquired in December 2011 and purchased the right to 15 additional purchase options. Four of these 19 additional B767F aircraft purchases were 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). 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 modernize our aircraft fleet at FedEx Express.

In conjunction with the additional B767F aircraft purchases, four previously contracted Boeing 777 Freighter (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. Nine B777F purchase obligations remain subject to the RLA condition.

We had $565 million in deposits and progress payments as of August 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 August 31, 2012, with the year of expected delivery:

	B757	B767F	B777F	Total
2013 (remainder)	8		2	10
2014		3	2	5
2015		9	2	11
2016		10		10
2017		10		10
Thereafter		14	16	30
Total	8	46	22	76

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 August 31, 2012 is as follows (in millions):

		Operating Leases		
	Capital Leases	Aircraft and Related Equipment	Facilities and Other	Total Operating Leases
2013 (remainder)	$ 118	$ 431	$ 1,040	$ 1,471
2014	2	462	1,310	1,772
2015	2	448	1,178	1,626
2016	2	453	985	1,438
2017	1	391	1,085	1,476
Thereafter	11	1,150	5,007	6,157
Total	136	$ 3,335	$ 10,605	$ 13,940
Less amount representing interest	8			
Present value of net minimum lease payments	$ 128			

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.

(7) 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.

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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.

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 other 19 cases that are before the Seventh Circuit remain stayed pending a decision of the Kansas Supreme Court.

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 argument in February 2012. In July 2012, the Washington Supreme Court affirmed the Washington Court of Appeals reversal of the jury verdict and remanded the case to the trial court.

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.

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In August 2012, another one of the contractor-model lawsuits that was not part of the multidistrict litigation, *Scovil v. FedEx Ground*, was certified as a class action by the federal district court in Maine. The court certified two state law claims seeking overtime and alleged illegal deductions, and class notices will be sent out to 143 potential class members. The court also previously certified an opt-in class for the Fair Labor Standards Act claims, and 21 people opted into this class.

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 attorney general in New York filed a lawsuit against FedEx Ground challenging the validity of the contractor model.

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. In the third quarter of 2012, we 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.

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.

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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.

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.

(8) Supplemental Cash Flow Information

Cash paid for interest expense and income taxes for the three-month periods ended August 31was as follows (in millions):

	2012	2011
Cash payments for:		
Interest (net of capitalized interest)	$ 45	$ 43
Income taxes	$ 54	$ 65
Income tax refunds received	(184)	
Cash tax (refunds) payments, net	$ (130)	$ 65

(9) 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 $2.0 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.

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

CONDENSED CONSOLIDATING BALANCE SHEETS

(UNAUDITED)

August 31, 2012

	Parent	Guarantor Subsidiaries	Non-guarantor Subsidiaries	Eliminations	Consolidated
ASSETS					
CURRENT ASSETS					
Cash and cash equivalents	$ 1,767	$ 442	$ 671	$ (137)	$ 2,743
Receivables, less allowances		3,793	1,021	(34)	4,780
Spare parts, supplies, fuel, prepaid expenses and other, less allowances	45	742	49		836
Deferred income taxes		499	19		518
Total current assets	1,812	5,476	1,760	(171)	8,877
PROPERTY AND EQUIPMENT, AT COST	27	34,912	2,023		36,962
Less accumulated depreciation and amortization	20	17,995	1,081		19,096
Net property and equipment	7	16,917	942		17,866
INTERCOMPANY RECEIVABLE			1,061	(1,061)	
GOODWILL		1,554	1,180		2,734
INVESTMENT IN SUBSIDIARIES	17,612	3,138		(20,750)	
OTHER ASSETS	2,818	966	216	(2,786)	1,214
	$ 22,249	$ 28,051	$ 5,159	$ (24,768)	$ 30,691
LIABILITIES AND STOCKHOLDERS INVESTMENT					
CURRENT LIABILITIES					
Current portion of long-term debt	$	$ 117	$	$	$ 117
Accrued salaries and employee benefits	55	932	170		1,157
Accounts payable	44	1,230	540	(171)	1,643
Accrued expenses	313	1,390	189		1,892
Total current liabilities	412	3,669	899	(171)	4,809
LONG-TERM DEBT, LESS CURRENT PORTION	1,992	250			2,242
INTERCOMPANY PAYABLE	566	495		(1,061)	
OTHER LONG-TERM LIABILITIES					
Deferred income taxes		3,665		(2,786)	879
Other liabilities	4,255	3,273	209		7,737
Total other long-term liabilities	4,255	6,938	209	(2,786)	8,616

STOCKHOLDERS INVESTMENT		15,024		16,699		4,051		(20,750)		15,024
	$	22,249	$	28,051	$	5,159	$	(24,768)	$	30,691

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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	4,340	3,193	183		7,716
Total other long-term liabilities	4,340	6,842	188	(2,818)	8,552
STOCKHOLDERS INVESTMENT	14,727	16,271	3,870	(20,141)	14,727

$	22,187	$	27,827	$	4,846	$	(24,957)	$	29,903

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CONDENSED CONSOLIDATING STATEMENTS OF COMPREHENSIVE INCOME

(UNAUDITED)

Three Months Ended August 31, 2012

	Parent	Guarantor Subsidiaries	Non-guarantor Subsidiaries	Eliminations	Consolidated
REVENUES	$	$ 9,094	$ 1,778	$ (80)	$ 10,792
OPERATING EXPENSES:					
Salaries and employee benefits	30	3,589	484		4,103
Purchased transportation		1,130	583	(33)	1,680
Rentals and landing fees	1	544	75	(2)	618
Depreciation and amortization		530	43		573
Fuel		1,116	22		1,138
Maintenance and repairs		515	27		542
Intercompany charges, net	(60)	(112)	172		
Other	29	1,133	279	(45)	1,396
		8,445	1,685	(80)	10,050
OPERATING INCOME		649	93		742
OTHER INCOME (EXPENSE):					
Equity in earnings of subsidiaries	459	29		(488)	
Interest, net	(23)	11	2		(10)
Intercompany charges, net	24	(29)	5		
Other, net	(1)	(2)	(2)		(5)
INCOME BEFORE INCOME TAXES	459	658	98	(488)	727
Provision for income taxes		236	32		268
NET INCOME	$ 459	$ 422	$ 66	$ (488)	$ 459
COMPREHENSIVE INCOME	$ 518	$ 428	$ 107	$ (488)	$ 565

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CONDENSED CONSOLIDATING STATEMENTS OF COMPREHENSIVE INCOME

(UNAUDITED)

Three Months Ended August 31, 2011

	Parent	Guarantor Subsidiaries	Non-guarantor Subsidiaries	Eliminations	Consolidated
REVENUES	$	$ 9,007	$ 1,584	$ (70)	$ 10,521
OPERATING EXPENSES:					
Salaries and employee benefits	33	3,531	440		4,004
Purchased transportation		1,080	464	(26)	1,518
Rentals and landing fees	1	555	65	(1)	620
Depreciation and amortization		471	38		509
Fuel		1,224	20		1,244
Maintenance and repairs		528	23		551
Intercompany charges, net	(58)	(90)	148		
Other	24	1,125	232	(43)	1,338
		8,424	1,430	(70)	9,784
OPERATING INCOME		583	154		737
OTHER INCOME (EXPENSE):					
Equity in earnings of subsidiaries	464	71		(535)	
Interest, net	(20)	8	1		(11)
Intercompany charges, net	21				