MISSION WEST PROPERTIES INC
Form SC 13G/A
February 04, 2009

SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

SCHEDULE 13G

Under the Securities Exchange Act of 1934

(Amendment No. 3)

Mission West Properties, Inc.
(Name of Issuer)

Common Stock, $0.001 par value
(Title of Class of Securities)

605203108
(CUSIP Number)

December 31, 2008
(Date of Event Which Requires Filing of this Statement)

Check the appropriate box to designate the rule pursuant to which this Schedule is filed:

[ ] Rule 13d-1(b)

[ ] Rule 13d-1(c)

[X] Rule 13d-1(d)

* The information required in the remainder of this cover page shall not be deemed to be "filed" for the purpose of Section 18 of the Securities Exchange Act of 1934 ("Act") or otherwise subject to the liabilities of that section of the Act, but shall be subject to all other provisions of the Act (however, see the Notes).

CUSIP No. 605203108	13G	Page 2 of 4 Pages

1)	Name of Reporting Person Thelmer Aalgaard
2)	Check the Appropriate Box if a Member of a Group (See Instructions) (a) [ ] (b) [ ]
3)	SEC Use Only

4)	Citizenship or Place of Organization USA
Number of Shares Beneficially Owned by Each Reporting Person with:	5) Sole Voting Power 1,849,505
	6) Shared Voting Power
	7) Sole Dispositive Power 1,849,505
	8) Shared Dispositive Power
9)	Aggregate Amount Beneficially Owned by Each Reporting Person 1,849,505
10)	Check if the Aggregate Amount in Row (9) Excludes Certain Shares (See Instructions)
11)	Percent of Class Represented by Amount in Row (9) 8.56 % *
12)	Type of Reporting Person (See Instructions) IN

* See Item 4, below

Item 1. (a) The name of the issuer is Mission West Properties, Inc. (the "Company").

(b) The principal executive offices of the Company are located at 10050 Bandley Drive, Cupertino, California 95014.

Item 2. The address of the principal business office of the reporting person is 10050 Bandley Drive, Cupertino, California 95014.

The title of class of securities and CUSIP number for the equity securities covered by this report and citizenship are incorporated by reference from the cover page in response to this item.

Item 3. If this statement is filed pursuant to Rule 13d-1(b), or 13d-2(b) or (c), check whether the person filing is a:

This statement is being filed pursuant to 13d-1(d).

Item 4. Ownership.

The Company had 19,748,211 shares of Common Stock outstanding as of December 31, 2008.

Regarding the beneficial ownership of each reporting person, reference is made to Item 4. of the cover page. The beneficial ownership of shares of Common Stock by the reporting person is based on such reporting person's right to exchange O.P. Units for shares of Common Stock upon certain conditions under an exchange rights agreement with the Company.

The issuer's charter and such agreements limit the number of shares that can be held at any one time by the reporting persons in the aggregate to the lesser of 9% of the outstanding Common Stock and the maximum percentage that individual shareholders can own, directly or indirectly, under applicable REIT ownership limits contained in the Internal Revenue Code. Consequently, the reporting person disclaims beneficial ownership of all shares of Common Stock in excess of the maximum number of shares that such reporting person currently has the right to acquire, taking into account these ownership restrictions.

Item 5. Ownership of Five Percent or Less of a Class.

Not applicable.

Item 6. Ownership of More than Five Percent on Behalf of Another Person.

See responses in Item 4 above.

Item 7. Identification and Classification of the Subsidiary Which Acquired the Security Being Reported on by the Parent Holding Company or Control Person.

Not applicable.

Item 8. Identification and Classification of Members of the Group.

Not applicable.

Item 9. Notice of Dissolution of Group.

Not applicable.

Item 10. Certification.

Not applicable.

SIGNATURE

After reasonable inquiry and to the best of my knowledge and belief, I certify that the information set forth in this statement is true, complete and correct.

Date: February 4, 2009

/s/ Thelmer Aalgaard

Thelmer Aalgaard

nt-family:inherit;font-size:10pt;">(0.7

)%

$
803

$
862

(6.8
)%
Adjusted Operating Profit
$
451

$
454

(0.7
)%

$
842

$
862

(2.3
)%
Operating Margin
14.7
%

15.1
%

13.3

%

14.4
%

Adjusted Operating Margin
14.7
%

15.1
%

13.9
%

14.4
%

Currency Translation Benefit / (Cost)—(in millions)*:

$

$
Revenue

$
(19
)

$
(19
)
Operating Expenses

(2
)

(5
)
Operating Profit

$
(21
)

$
(24
)

---

* Net of currency hedging; amount represents the change compared to the prior year.

35

Table of Contents
UNITED PARCEL SERVICE, INC. AND SUBSIDIARIES
MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Revenue
The change in overall revenue was impacted by the following factors for the second quarter and year-to-date periods of 2013 compared with the corresponding periods of 2012:

	Volume	Rates / Product Mix	Fuel Surcharge	Currency	Total Revenue Change
Net Revenue Change Drivers:					
Second quarter 2013 vs. 2012	5.0 %	(1.5)%	(1.3)%	(0.6)%	1.6 %
Year-to-date 2013 vs. 2012	2.6 %	(0.1)%	(1.2)%	(0.3)%	1.0 %

Volume
Our overall average daily volume increased in the second quarter and year-to-date periods of 2013 compared with the corresponding periods of 2012, largely due to growth in key markets in Asia and Europe.
Export volume increased in the second quarter and year-to-date periods of 2013. Volume continued to shift towards our less premium products, such as Transborder Standard and Worldwide Expedited, as compared with our premium express products, such as Worldwide Express. Our international customers continue to be impacted by economic pressures and changes in their supply chain networks, and the combination of these factors influence their sensitivity towards the price and speed of shipments. Export volume growth was driven by Asia (largely in the Asia-to-Europe, Asia-to-U.S. and intra-Asia trade lanes) and Europe (primarily intra-Europe). However, U.S. export volume growth continued to remain weak, and decreased slightly for the second quarter of 2013.
Domestic volume increased in the second quarter and year-to-date periods of 2013 compared to 2012. Results were driven by solid volume growth in several key markets, including Italy, Canada, the U.K. and Turkey.
Rates and Product Mix
Total average revenue per piece decreased 2.8% for the second quarter of 2013 on a currency-adjusted basis (1.6% year-to-date), and was impacted by changes in base rates, customer and product mix, and fuel surcharge rates.
On December 31, 2012, we increased the base rates 6.5% for international shipments originating in the United States (Worldwide Express, Worldwide Express Plus, UPS Worldwide Expedited and UPS International Standard service), while reducing fuel surcharge indices. Rate changes for shipments originating outside the U.S. are made throughout the year and vary by geographic market.
Currency-adjusted export revenue per piece decreased 3.4% for the second quarter (2.9% year-to-date), as the shift in product mix from our premium express products to our standard products more than offset the increase in base rates. Additionally, currency-adjusted export revenue per piece was adversely impacted by a small reduction in the average weight per piece (due to changes in customer mix towards lighter-weight shipments), as well as a small impact on pricing from overcapacity in the Asia outbound freight market.
Currency-adjusted domestic revenue per piece decreased 0.4% for the second quarter (increased 0.3% year-to-date). Domestic revenue per piece was positively impacted by base rate increases; however, these base rate increases were offset by the faster domestic volume growth in our lower-yielding standard service, as well as product and customer mix changes in several developed markets.
Fuel Surcharges
On December 31, 2012, in connection with our base rate increases, we modified the fuel surcharge on certain U.S., South and Central America, and Asia-related international air services by reducing the index used to determine the fuel surcharge by 2%. The fuel surcharges for air products originating outside the United States are indexed to the DOE's Gulf Coast spot price for a gallon of kerosene-type jet fuel, while the fuel surcharges for ground products originating outside the United States are indexed to fuel prices in the international region or country where the shipment takes place. Total international fuel surcharge revenue decreased by $38 million for the second quarter of 2013 when compared with 2012 ($69 million year-to-date), primarily due to reduced fuel surcharge rates caused by

declining fuel prices and the reduction in the index; however, this was partially offset by increased international air volume.

36

Operating Expenses

Overall adjusted operating expenses for the segment increased $51 million for the second quarter of 2013 compared with the same period in 2012 ($80 million year-to-date). This increase was driven by the cost of pick-up and delivery, which increased $38 million for the second quarter ($52 million year-to-date), largely due to higher package volume. The cost of operating our international integrated air and ground network increased $11 million for the quarter ($9 million year-to-date), also largely due to higher package volume; however, network costs were mitigated by a 1.2% reduction in average daily aircraft block hours resulting from ongoing modifications to our air network. This was achieved even with a 5.0% increase in second quarter international export volume and several air product service enhancements that occurred during 2013.

The remaining increases in adjusted operating expenses for the quarter and year-to-date periods were largely due to the costs of package sorting, which was impacted by volume growth, and indirect operating costs, which were affected by increased expenses associated with aviation security.

Excluding the impact of currency exchange rate changes, the total adjusted cost per piece for the segment decreased 3.0% for the second quarter of 2013 compared with the same period of 2012 (1.1% year-to-date).

Operating Profit and Margin

Adjusted operating profit contracted by 0.7% for the second quarter of 2013 compared with 2012 (2.3% year-to-date), while the adjusted operating margin decreased 40 basis points (50 basis points year-to-date). The solid volume growth in 2013 was largely offset by reductions in revenue per piece, leading to only slight growth in revenue. The net impact of fuel (fuel surcharge revenue decreased at a faster rate than fuel expense) and currency remeasurement and translation losses resulted in an adverse impact on operating profit of approximately $55 million when comparing the second quarter of 2013 with 2012 ($85 million year-to-date). The combination of low revenue growth and the adverse impact of fuel and currency led to the reduction in operating margin.

Table of Contents
UNITED PARCEL SERVICE, INC. AND SUBSIDIARIES
MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Supply Chain & Freight Operations

	Three Months Ended June 30, 2013	Three Months Ended June 30, 2012	Change %	Six Months Ended June 30, 2013	Six Months Ended June 30, 2012	Change %
Freight LTL Statistics:						
Revenue (in millions)	$635	$597	6.4 %	$1,231	$1,155	6.6 %
Revenue Per Hundredweight	$21.61	$21.50	0.5 %	$21.73	$21.48	1.2 %
Shipments (in thousands)	2,717	2,583	5.2 %	5,235	5,051	3.6 %
Shipments Per Day (in thousands)	42.5	40.4	5.2 %	41.2	39.5	4.3 %
Gross Weight Hauled (in millions of lbs)	2,939	2,778	5.8 %	5,668	5,375	5.5 %
Weight Per Shipment (in lbs)	1,082	1,076	0.6 %	1,083	1,064	1.8 %
Operating Days in Period	64	64		127	128	
Revenue (in millions):						
Forwarding and Logistics	$1,333	$1,485	(10.2)%	$2,693	$2,909	(7.4)%
Freight	731	660	10.8 %	1,419	1,278	11.0 %
Other	140	132	6.1 %	277	256	8.2 %
Total Revenue	$2,204	$2,277	(3.2)%	$4,389	$4,443	(1.2)%
Operating Expenses (in millions):	$2,045	$2,075	(1.4)%	$4,087	$4,075	0.3 %
Operating Profit (in millions)	$159	$202	(21.3)%	$302	$368	(17.9)%
Operating Margin	7.2 %	8.9 %		6.9 %	8.3 %	
Currency Translation Benefit / (Cost) – (in millions)*:			$			$
Revenue			$(5)			$(12)
Operating Expenses			5			11
Operating Profit			$—			$(1)

* Amount represents the change compared to the prior year.

Revenue

Forwarding and logistics revenue decreased $152 million in the second quarter of 2013 compared with the corresponding period in 2012 ($216 million year-to-date). Forwarding revenue decreased in the second quarter and year-to-date periods of 2013, primarily due to lower tonnage and rates charged to our customers in our international air forwarding business. The reduction in tonnage was impacted by weak overall market demand and increased competition for air forwarding services, while the reduction in rates was largely due to industry overcapacity in key trade lanes, particularly the Asia-outbound market. Revenue for our logistics products increased in the second quarter and year-to-date periods of 2013 compared with 2012, as we experienced solid growth in our mail services and healthcare distribution solutions.

Freight revenue increased $71 million for the second quarter of 2013 ($141 million year to date), driven by an increase in LTL revenue per hundredweight, tonnage and average daily LTL shipments; however, these factors were partially offset by having one less operating day in the year-to-date period of 2013 compared with 2012. The increase in LTL revenue per hundredweight was largely due to our focus on yield management, as well as general rate increases averaging 5.9% that took effect on July 16, 2012 and on June 10, 2013, covering non-contractual shipments in the United States, Canada and Mexico. Fuel surcharge revenue increased by $5 million for the second quarter of 2013 compared with the corresponding period of the prior year ($15 million year-to-date), due to changes in diesel fuel prices and overall LTL shipment volume. In addition, our Truckload division experienced increased volume and revenue, primarily related to our dedicated and non-dedicated service offerings.

38

Table of Contents

UNITED PARCEL SERVICE, INC. AND SUBSIDIARIES
MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The other businesses within Supply Chain & Freight increased revenue by $8 million for the quarter ($21 million year-to-date), primarily due to growth at UPS Capital, The UPS Store and UPS Customer Solutions.

Operating Expenses

Forwarding and logistics operating expenses decreased $106 million for the second quarter of 2013 compared with the same period of 2012 ($115 million year-to-date), due to several factors. Purchased transportation expense declined by $63 million in the second quarter ($75 million year-to-date), primarily due to lower tonnage in our international air freight forwarding business. Compensation and benefits expense declined by $16 million in the second quarter ($23 million year-to-date), largely due to reduced payroll costs. The remaining decrease in expense was impacted by lower fuel costs, bad debt expense, and various other items.

Freight operating expenses increased $73 million in the second quarter of 2013 ($122 million year-to-date), while the total cost per LTL shipment increased 2.2% (1.8% year-to-date). The largest component of this increase related to the cost of operating our linehaul network, which grew by $18 million for the second quarter ($36 million year-to-date), as a result of a 5.8% average daily tonnage increase, coupled with wage and purchased transportation increases. Our Truckload division experienced a $15 million increase in costs for the quarter ($27 million year-to-date), largely related to the expansion of our dedicated and non-dedicated services. The remaining increase in expense for the second quarter and year-to-date periods of 2013 was impacted by increases in pick-up and delivery costs, healthcare costs and pension expense.

Operating expenses for the other businesses within Supply Chain & Freight increased $3 million in the second quarter of 2013 compared with 2012 ($5 million year-to-date).

Operating Profit and Margin

Operating profit for the forwarding and logistics unit decreased by $46 million in the second quarter of 2013 compared to the same period in 2012 ($101 million year-to-date). This decrease was primarily due to reduced profitability in our international air forwarding business, which resulted from increased competition combined with weak overall air freight market demand due to continued economic weakness in Europe, slowing growth in China and a sluggish U.S. economy. Additionally, our customer concentration among the technology and military sectors negatively impacted our results, as demand in these sectors was relatively weaker than the remainder of the air freight market. This lower demand pressured the rates we charge to our customers, which more than offset the reduced rates we incur from third-party transportation carriers, and thereby led to a compression in our operating margin. Operating profit for our logistics business declined in the second quarter and year-to-date periods of 2013 compared with 2012, largely due to increased investments in facilities and information technology platforms in our healthcare logistics business, as well as the gain on the sale of a facility in 2012.

Operating profit for our freight unit was flat in the second quarter of 2013 compared to the same period in 2012, while increasing $19 million on a year-to-date basis. For the year-to-date period of 2013 compared with 2012, operating profit increased as improvements in average daily LTL volume, yields and productivity measures (including gains in pick-up and delivery stops per hour, dock bills per hour and linehaul network utilization), more than offset the impact of having one less operating day.

The combined operating profit for all of our other businesses in this segment increased $5 million during the second quarter ($16 million year-to-date), primarily due to higher operating profit at UPS Capital and The UPS Store.

Table of Contents

UNITED PARCEL SERVICE, INC. AND SUBSIDIARIES
MANAGEMENT’S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Consolidated Operating Expenses

	Three Months Ended June 30,		Change	Six Months Ended June 30,		Change
	2013	2012	%	2013	2012	%
Operating Expenses (in millions):						
Compensation and Benefits	$6,981	$6,747	3.5 %	$13,949	$13,582	2.7 %
Repairs and Maintenance	309	303	2.0 %	618	605	2.1 %
Depreciation and Amortization	466	459	1.5 %	940	918	2.4 %
Purchased Transportation	1,731	1,733	(0.1)%	3,511	3,450	1.8 %
Fuel	992	1,014	(2.2)%	1,998	2,039	(2.0)%
Other Occupancy	225	213	5.6 %	478	450	6.2 %
Other Expenses	1,061	1,090	(2.7)%	2,125	2,082	2.1 %
TNT Termination Fee and Related Expenses	—	—		(284)	—	
Gain Upon Liquidation of Foreign Subsidiary	—	—		245	—	
Adjusted Other Expenses	1,061	1,090	(2.7)%	2,086	2,082	0.2 %
Total Operating Expenses	$11,765	$11,559	1.8 %	$23,619	$23,126	2.1 %
Adjusted Total Operating Expenses	$11,765	$11,559	1.8 %	23,580	$23,126	2.0 %
			$			$
Currency Translation (Benefit) Cost			$(3)			$(6)

Compensation and Benefits

Employee payroll costs increased $123 million for the second quarter of 2013 compared with 2012 ($227 million year-to-date), largely due to contractual union wage rate increases, a 0.9% increase in average daily union labor hours, and a merit salary increase for management employees; however, this was partially offset by an overall reduction in the number of management personnel.

Benefits expense increased $111 million for the second quarter of 2013 compared with 2012 ($140 million year-to-date), primarily due to higher pension expense, increased vacation, holiday and excused absence expense, and higher health and welfare costs; however, these items were partially offset by changes in the expense associated with our self-insurance for worker’s compensation claims. These factors are discussed further as follows:

- Pension expense increased $68 million for the second quarter of 2013 compared with 2012 ($131 million year-to-date), due to higher union contribution rates for multiemployer pension plans combined with increased service and interest costs for company-sponsored plans. The increase in service and interest costs for company-sponsored plans was largely due to continued service accruals and lower discount rates.
- Vacation, holiday and excused absence expense increased $32 million for the second quarter compared with 2012 ($34 million year-to-date), due to increased vacation entitlements earned based on employees' years of service.
- Health and welfare costs increased $5 million for the second quarter of 2013 compared with 2012 ($49 million year-to-date), largely due to higher medical claims and the impact of several provisions of the Patient Protection and Affordable Care Act of 2010.

Table of Contents
UNITED PARCEL SERVICE, INC. AND SUBSIDIARIES
MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

- The expense associated with our self-insurance programs for worker's compensation claims decreased $3 million for the second quarter of 2013 compared with 2012 ($92 million year-to-date). Insurance reserves are established for estimates of the loss that we will ultimately incur on reported worker's compensation claims, as well as estimates of claims that have been incurred but not reported, and take into account a number of factors including our history of claim losses, payroll growth and the impact of safety improvement initiatives. In 2013, we experienced favorable actuarial expense adjustments as the frequency and severity of claims was less than previously projected, due to the impact of ongoing safety improvement and claim management initiatives.

Repairs and Maintenance

The increase in repairs and maintenance expense was largely due to increased automotive maintenance costs in our global package and freight operations. These increased costs were impacted by the increase in miles driven in the second quarter and year-to-date periods of 2013 compared with 2012.

Depreciation and Amortization

The increase in depreciation and amortization expense for the second quarter of 2013 was primarily due to a $13 million increase in depreciation expense on vehicles ($23 million year-to-date). This increase was driven by the replacement of older, fully-depreciated vehicles, technology upgrades on new vehicles and an overall increase in the size of our vehicle fleet in our U.S. Domestic package and UPS Freight operations.

Purchased Transportation

Purchased transportation expense charged to us by third-party air, ocean and truck carriers was approximately flat for the second quarter of 2013 compared with 2012, but increased $61 million year-to-date. The changes in expense for the second quarter and year-to-date periods were driven by several factors:

- The purchased transportation expense for our forwarding & logistics business declined $63 million for the second quarter ($75 million year-to-date), largely due to lower tonnage in our international air freight forwarding business.
- Our U.S. Domestic Package segment incurred a $13 million expense increase for the quarter ($50 million year-to-date), primarily due to higher rates passed to us from rail carriers, and higher fees paid to the U.S. Postal Service associated with the volume growth in our SurePost product.
- Our International Package segment incurred a $31 million expense increase for the quarter ($44 million year-to-date) primarily due to international volume growth.
- Our UPS Freight business incurred a $20 million increase for the quarter ($42 million year-to-date) largely due to growth in LTL volume and higher rates passed to us from rail carriers.

Fuel

The decrease in fuel expense for the second quarter of 2013 was primarily due to the decline in prices for jet-A fuel and diesel, which decreased expense by $27 million ($29 million year-to-date), net of hedging. This was partially offset during the second quarter by an increase in vehicle miles driven and lower fuel efficiency, which increased expense by $5 million; however, usage decreased for the year-to-date period of 2013 compared with 2012 by $12 million, primarily due to a reduction in aircraft block hours.

Other Occupancy

The increase in other occupancy expense in the second quarter and year-to-date periods of 2013 was primarily due to increases in real estate and vehicle taxes, higher snow removal costs at our operating facilities, and an increase in utilities expenses. The relatively cold winter in the United States in 2013 compared with 2012 impacted the increase in snow removal costs, while higher natural gas and electricity prices affected the increase in utilities expenses.

Other Expenses

The decrease in adjusted other expenses for the second quarter of 2013 compared with 2012 was largely due to decreases in outside professional fees and bad debt expense. Outside professional fees had increased in the second quarter of 2012 related to our proposed TNT Express N.V. acquisition.

41

Table of Contents
UNITED PARCEL SERVICE, INC. AND SUBSIDIARIES
MANAGEMENT’S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

On a year-to-date basis, adjusted other expenses increased slightly in 2013 compared with 2012. This increase was largely due to increases in auto liability insurance, foreign currency remeasurement losses and transportation equipment rentals; however, these factors were largely offset by a reduction in bad debt expense, outside professional fees and employee expense reimbursements.

Investment Income and Interest Expense

	Three Months Ended June 30,		Change	Six Months Ended June 30,		Change
	2013	2012	%	2013	2012	%
(in millions)						
Investment Income	$3	$6	(50.0)%	$8	$12	(33.3)%
Interest Expense	$(98)	$(92)	6.5%	$(194)	$(186)	4.3%

Investment Income
The decrease in investment income for the second quarter and year-to-date periods of 2013 compared with the same periods of 2012 was primarily due to lower interest rates earned on invested assets, as well as a decline in realized gains on sales of investments. These declines were partially offset by an increase in the average balance of invested assets in the second quarter and year-to-date periods of 2013 compared with 2012.
Interest Expense
Interest expense increased in the second quarter and year-to-date periods of 2013 compared to 2012, largely due to the imputation of interest expense on the multiemployer pension withdrawal liability related to the New England Pension Fund. This was partially offset by a lower effective interest rate incurred on our variable rate debt and interest rate swaps in the second quarter and year-to-date periods of 2013 compared with 2012.
Income Tax Expense

	Three Months Ended June 30,		Change	Six Months Ended June 30,		Change
	2013	2012	%	2013	2012	%
(in millions)						
Income Tax Expense	$576	$588	(2.0)%	$1,028	$1,099	(6.5)%
TNT Termination Fee and Related Expenses	—	—		107	—	
Gain Upon Liquidation of Foreign Subsidiary	—	—		(32)	—	
Adjusted Income Tax Expense	$576	$588	(2.0)%	$1,103	$1,099	0.4%
Effective Tax Rate	35.0%	34.5%		32.8%	34.5%	
Adjusted Effective Tax Rate	35.0%	34.5%		34.7%	34.5%	

Our effective tax rate increased by 50 basis points for the second quarter of 2013 compared with the same period of 2012, primarily due to a decrease in U.S. Federal and state tax credits relative to total pre-tax income, as well as unfavorable changes in the proportion of our taxable income in certain non-U.S. jurisdictions relative to total pre-tax income.
On a year-to-date basis, our effective tax rate declined to 32.8% in 2013 from 34.5% in 2012, as a portion of the gain from liquidating a foreign subsidiary was non-taxable. Our adjusted effective tax rate on a year-to-date basis increased to 34.7% in 2013 compared with 34.5% in 2012, due to the aforementioned trends with U.S. Federal and state tax credits and non-U.S. taxable income relative to total pre-tax income.

Table of Contents

UNITED PARCEL SERVICE, INC. AND SUBSIDIARIES
MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Liquidity and Capital Resources

Net Cash From Operating Activities

The following is a summary of the significant sources (uses) of cash from operating activities (amounts in millions):

	Six Months Ended June 30,	
	2013	2012
Net income	$2,108	$2,086
Non-cash operating activities (a)	1,368	1,723
Pension and postretirement plan contributions (UPS-sponsored plans)	(114)	(450)
Income tax receivables and payables	(163)	259
Changes in working capital and other noncurrent assets and liabilities	298	288
Other sources (uses) of cash from operating activities	(66)	(56)
Net cash from operating activities	$3,431	$3,850

(a) Represents depreciation and amortization, gains and losses on derivative transactions and foreign exchange, deferred income taxes, provisions for uncollectible accounts, pension and postretirement benefit expense, stock compensation expense, impairment charges and other non-cash items.

Operating cash flow was negatively impacted in 2013, compared with 2012, by certain TNT Express transaction-related charges, as well as changes in income tax receivables and payables. We paid a termination fee to TNT Express of €200 million ($268 million) under the agreement to terminate the merger protocol in the first quarter of 2013. The cash payments for income taxes increased in 2013 compared with 2012, and were impacted by the timing of current tax deductions.

The adverse impact of these items on our operating cash flow in 2013 compared with 2012 was partially offset by reduced pension and postretirement medical defined benefit plan contributions. Contributions to our company-sponsored defined benefit plans have varied based primarily on whether any minimum funding requirements are present for the individual plans. The decline in contributions to our defined benefit plans was largely related to the UPS IBT Pension Plan ($355 million in contributions in the first six months of 2012; no contributions in 2013). The remaining contributions in both years were largely related to our international pension and U.S. postretirement medical plans. As discussed in note 6 to the unaudited consolidated financial statements, we expect to contribute $98 million to our company-sponsored pension and postretirement medical benefit plans over the remainder of 2013.

As of June 30, 2013, the total of our worldwide holdings of cash and cash equivalents was $4.808 billion. Approximately 45%-55% of our cash and cash equivalents are typically held by foreign subsidiaries throughout the year. The amount of cash held by our U.S. and foreign subsidiaries fluctuates throughout the year due to a variety of factors, including the timing of cash receipts and disbursements in the normal course of business. Cash provided by operating activities in the United States continues to be our primary source of funds to finance domestic operating needs, capital expenditures, share repurchases and dividend payments to shareowners. To the extent that such amounts represent previously untaxed earnings, the cash held by foreign subsidiaries would be subject to tax if such amounts were repatriated in the form of dividends; however, not all international cash balances would have to be repatriated in the form of a dividend if returned to the U.S. When amounts earned by foreign subsidiaries are expected to be indefinitely reinvested, no accrual for taxes is provided.

Table of Contents

Net Cash Used In Investing Activities

Our primary sources (uses) of cash for investing activities were as follows (amounts in millions):

	Six Months Ended June 30,	
	2013	2012
Net cash used in investing activities	$(1,853)	$(307)
Capital Expenditures:		
Buildings and facilities	$(183)	$(217)
Aircraft and parts	(274)	(368)
Vehicles	(281)	(147)
Information technology	(252)	(217)
	$(990)	$(949)
Capital Expenditures as a % of Revenue	3.7%	3.6%
Other Investing Activities:		
Proceeds from disposals of property, plant and equipment	$24	$32
Net decrease in finance receivables	$19	$42
Net sales (purchases) of marketable securities	$(898)	$664
Cash paid for business acquisitions	$—	$(100)
Other sources (uses) of cash for investing activities	$(8)	$4

We have commitments for the purchase of aircraft, vehicles, equipment and real estate to provide for the replacement of existing capacity and anticipated future growth. We generally fund our capital expenditures with our cash from operations. Capital spending on real estate declined in 2013 compared with 2012, as the expansion of our Cologne air hub nears completion. Capital spending on aircraft is primarily related to contract deposits and final payments associated with the delivery of aircraft under our Boeing 767-300 order, which will be completed in 2013. Capital spending on vehicles increased in 2013 in our U.S. and international package businesses and our freight unit, due to vehicle replacements, technology enhancements and new vehicle orders to support volume growth. Capital spending on technology increased in 2013, largely due to new capitalized software projects.

Future capital spending for anticipated growth and replacement assets will depend on a variety of factors, including economic and industry conditions. We anticipate that our capital expenditures for 2013 will be approximately $2.4 billion, or approximately 4% of revenue.

The net decrease in finance receivables was primarily due to loan sales in our business credit and leasing portfolios. The purchases and sales of marketable securities are largely determined by liquidity needs and the periodic rebalancing of investment types, and will therefore fluctuate from period to period. The cash paid for business acquisitions in 2012 was primarily related to our acquisition of Kiala S.A. Other investing activities include the cash settlement of derivative contracts used in our currency and commodity hedging programs, as well as capital contributions into certain investment partnerships.

Table of Contents
UNITED PARCEL SERVICE, INC. AND SUBSIDIARIES
MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Net Cash Provided by Financing Activities

Our primary sources (uses) of cash for financing activities are as follows (amounts in millions, except per share data):

	Six Months Ended June 30, 2013	2012
Net cash provided by (used in) financing activities	$(4,041)	$158
Share Repurchases:		
Cash expended for shares repurchased	$(1,867)	$(885)
Number of shares repurchased	(21.8)	(11.3)
Shares outstanding at period end	938	958
Percent reduction in shares outstanding	(1.6)%	(0.5)%
Dividends:		
Dividends declared per share	$1.24	$1.14
Cash expended for dividend payments	$(1,140)	$(1,068)
Borrowings:		
Net borrowings (repayment) of debt principal	$(716)	$1,873
Other Financing Activities:		
Cash received for common stock issuances	$293	$194
Other sources (uses) of cash for financing activities	$(611)	$44
Capitalization (as of June 30 each year):		
Total debt outstanding at period end	$11,923	$13,023
Total shareowners' equity at period end	3,630	7,725
Total capitalization	$15,553	$20,748
Debt to Total Capitalization %	76.7%	62.8%

We repurchased a total of 21.8 million shares of class A and class B common stock for $1.836 billion in the first six months of 2013, and 11.3 million shares for $870 million for the first six months of 2012 ($1.867 billion and $885 million in repurchases for 2013 and 2012, respectively, are reported on the cash flow statement due to the timing of settlements). 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. As of June 30, 2013, we had $8.825 billion of this share repurchase authorization available. 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. We anticipate repurchasing approximately $4.0 billion of shares in 2013.

The declaration of dividends is subject to the discretion of the Board of Directors and will depend on various factors, including our net income, financial condition, cash requirements, future prospects and other relevant factors. We increased our quarterly cash dividend payment to $0.62 per share in 2013, compared with the previous $0.57 quarterly dividend rate in 2012. We expect to continue the practice of paying regular cash dividends.

Issuances of debt in the first six months of 2013 and 2012 consisted primarily of commercial paper. Repayments of debt in 2013 consisted primarily of the $1.75 billion 4.5% senior notes that matured in January 2013. We consider the overall fixed and floating interest rate mix of our portfolio and the related overall cost of borrowing when planning for future issuances and non-scheduled repayments of debt.

Table of Contents
UNITED PARCEL SERVICE, INC. AND SUBSIDIARIES
MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The cash outflows in other financing activities were primarily due to premiums paid and received on capped call options for the purchase of UPS class B shares, and the purchase of noncontrolling interests. During the first six months of 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 first six months of 2012, we received $206 million in premiums for options that were entered into during 2011 that expired in 2012. Additionally, we paid $70 million in 2013 to purchase the noncontrolling interest in a joint venture that operates in the Middle East, Turkey and portions of the Central Asia region. The remaining cash outflows in other financing activities for both 2013 and 2012 were related to tax withholdings on vested employee stock awards.

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.

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.

Our Moody's and Standard & Poor's short-term credit ratings are P-1 and A-1, respectively. Our Moody's and Standard & Poor's long-term credit ratings are Aa3 and A+, respectively. We currently have a negative outlook from Standard & Poor's and a stable outlook from Moody's.

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.

Except as described in this quarterly report, the nature and amounts of our payment obligations under our debt, capital and operating lease agreements, purchase commitments, and other liabilities as of June 30, 2013 have not materially changed from those described in our Annual Report on Form 10-K for the year ended December 31, 2012.

We believe that funds from operations and borrowing programs will provide adequate sources of liquidity and capital resources to meet our expected long-term needs for the operation of our business, including anticipated capital expenditures, such as commitments for aircraft purchases, for the foreseeable future.

Guarantees and Other Off-Balance Sheet Arrangements

We do not have guarantees or other off-balance sheet financing arrangements, including variable interest entities, which we believe could have a material impact on our financial condition or liquidity.

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.

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.

47

UNITED PARCEL SERVICE, INC. AND SUBSIDIARIES
MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

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.

Table of Contents

UNITED PARCEL SERVICE, INC. AND SUBSIDIARIES
MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

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.

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.

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.

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 to the consolidated financial statements. 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.

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 to the consolidated financial statements.

Table of Contents

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

Item 3. Quantitative and Qualitative Disclosures About Market Risk

We are exposed to market risk from changes in foreign currency exchange rates, interest rates, equity prices, and certain commodity prices. This market risk arises in the normal course of business, as we do not engage in speculative trading activities. In order to manage the risk arising from these exposures, we utilize a variety of foreign exchange, interest rate, equity and commodity forward contracts, options, and swaps.

The total fair value asset (liability) of our derivative financial instruments is summarized in the following table (in millions):

	June 30, 2013	December 31, 2012
Currency Derivatives	$6	$(60)
Commodity Derivatives	—	—
Interest Rate Derivatives	234	467
	$240	$407

Our market risks, hedging strategies and financial instrument positions at June 30, 2013 have not materially changed from those disclosed in our Annual Report on Form 10-K for the year ended December 31, 2012. In 2013, we entered into several heating oil and diesel fuel swaps, and also entered into new currency options on the Euro, British Pound Sterling and Canadian Dollar, as well as terminated positions that expired during the first six months of 2013. The remaining fair value changes between December 31, 2012 and June 30, 2013 in the preceding table are primarily due to interest rate and foreign currency exchange rate changes between those dates.

The forward contracts, swaps, and options previously discussed 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.

We have agreements with substantially all of our active counterparties 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 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.

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

The information concerning market risk under the caption “Quantitative and Qualitative Disclosures about Market Risk” on pages 53-54 of our consolidated financial statements contained in our Annual Report on Form 10-K for the year ended December 31, 2012, is hereby incorporated by reference in this report.

Item 4. Controls and Procedures

Evaluation of Disclosure Controls and Procedures:

As of the end of the period covered by this report, management, including our chief executive officer and chief financial officer, evaluated the effectiveness of the design and operation of our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) of the Securities Exchange Act of 1934 (“Exchange Act”)). Based upon that evaluation, our chief executive officer and chief financial officer concluded that the disclosure controls and procedures were effective to ensure that information required to be disclosed in reports we file or submit under the Exchange Act is (1) recorded, processed, summarized and reported within the time periods specified in Securities and Exchange Commission rules and forms, and (2) accumulated and communicated to our management to allow their timely decisions regarding required disclosure.

Changes in Internal Control over Financial Reporting:

There were no changes in the Company’s internal controls over financial reporting during the quarter ended June 30, 2013 that have materially affected, or are reasonably likely to materially affect, the Company’s internal control over financial reporting.

Table of Contents

PART II. OTHER INFORMATION

Item 1. Legal Proceedings
For a discussion of legal proceedings affecting us and our subsidiaries, please see the information under the sub-caption “Contingencies” of the caption “Management’s Discussion and Analysis of Financial Condition and Results of Operations” included in this report.
Item 1A. Risk Factors
You should carefully consider the following factors, which could materially affect our business, financial condition or results of operations. You should read these Risk Factors in conjunction with “Management's Discussion and Analysis of Financial Condition and Results of Operations” in Item 2 and our Consolidated Financial Statements and related notes in Item 1.
General economic conditions, both in the U.S. and internationally, may adversely affect our results of operations.
We conduct operations in over 220 countries and territories. Our U.S. and international operations are subject to normal cycles affecting the economy in general, as well as the local economic environments in which we operate. The factors that create cyclical changes to the economy and to our business are beyond our control, and it may be difficult for us to adjust our business model to mitigate the impact of these factors. In particular, our business is affected by levels of industrial production, consumer spending and retail activity, and our business, financial position and results of operations could be materially affected by adverse developments in these aspects of the economy.
We face significant competition which could adversely affect our business, financial position and results of operations.
We face significant competition on a local, regional, national and international basis. Our competitors include the postal services of the U.S. and other nations, various motor carriers, express companies, freight forwarders, air couriers and others. Competition may also come from other sources in the future. Some of our competitors have cost and organizational structures that differ from ours and may offer services and pricing terms that we may not be willing or able to offer. If we are unable to timely and appropriately respond to competitive pressures, our business, financial position and results of operations could be adversely affected.
The transportation industry continues to consolidate and competition remains strong. As a result of consolidation, our competitors may increase their market share and improve their financial capacity, and may strengthen their competitive positions. Business combinations could also result in competitors providing a wider variety of services and products at competitive prices, which could adversely affect our financial performance.
Changes in our relationships with our significant customers, including the loss or reduction in business from one or more of them, could have an adverse impact on us.
Our top 20 customers account for less than 10% of our consolidated revenue. We do not believe the loss of any single customer would materially impair our overall financial condition or results of operations; however, collectively, some of these large customers might account for a relatively significant portion of the growth in revenue in a particular quarter or year. These customers can drive the growth in revenue for particular services based on factors such as: new customer product launches; the seasonality associated with the fourth quarter Holiday season; business mergers and acquisitions; and the overall fast growth of a customer's underlying business. These customers could choose to divert all or a portion of their business with us to one of our competitors, demand pricing concessions for our services, require us to provide enhanced services that increase our costs, or develop their own shipping and distribution capabilities. If these factors drove some of our large customers to cancel all or a portion of their business relationships with us, it could materially impact the growth in our business and the ability to meet our current and long-term financial forecasts.

Table of Contents

Our business is subject to complex and stringent regulation in the U.S. and internationally.
We are subject to complex and stringent aviation, transportation, environmental, security, labor, employment and other governmental laws and regulations, both in the U.S. and in the other countries in which we operate. In addition, our business is impacted by laws and regulations that affect global trade, including tariff and trade policies, export requirements, taxes and other restrictions and charges. Changes in laws, regulations and the related interpretations may alter the landscape in which we do business and may affect our costs of doing business. The impact of new laws and regulations cannot be predicted. Compliance with new laws and regulations may increase our operating costs or require significant capital expenditures. Any failure to comply with applicable laws or regulations in the U.S. or in any of the countries in which we operate could result in substantial fines or possible revocation of our authority to conduct our operations, which could adversely affect our financial performance.
Increased security requirements could impose substantial costs on us and we could be the target of an attack or have a security breach.
As a result of concerns about global terrorism and homeland security, governments around the world have adopted or may adopt stricter security requirements that will result in increased operating costs for businesses in the transportation industry. These requirements may change periodically as a result of regulatory and legislative requirements and in response to evolving threats. We cannot determine the effect that these new requirements will have on our cost structure or our operating results, and these rules or other future security requirements may increase our costs of operations and reduce operating efficiencies. Regardless of our compliance with security requirements or the steps we take to secure our facilities or fleet, we could be the target of an attack or security breaches could occur, which could adversely affect our operations or our reputation.
We may be affected by global climate change or by legal, regulatory or market responses to such potential change.
Concern over climate change, including the impact of global warming, has led to significant federal, state and international legislative and regulatory efforts to limit greenhouse gas (“GHG”) emissions. For example, in the past several years, the U.S. Congress has considered various bills that would regulate GHG emissions. While these bills have not yet received sufficient Congressional support for enactment, some form of federal climate change legislation is possible in the future. Even in the absence of such legislation, the Environmental Protection Agency, spurred by judicial interpretation of the Clean Air Act, may regulate GHG emissions, especially aircraft or diesel engine emissions, and this could impose substantial costs on us. These costs include an increase in the cost of the fuel and other energy we purchase and capital costs associated with updating or replacing our aircraft or vehicles prematurely. Until the timing, scope and extent of any future regulation becomes known, we cannot predict its effect on our cost structure or our operating results. It is reasonably possible that such legislation or regulation could impose material costs on us. Moreover, even without such legislation or regulation, increased awareness and any adverse publicity in the global marketplace about the GHGs emitted by companies in the airline and transportation industries could harm our reputation and reduce customer demand for our services, especially our air services.
Strikes, work stoppages and slowdowns by our employees could adversely affect our business, financial position and results of operations.
A significant number of our employees are employed under a national master agreement and various supplemental agreements with local unions affiliated with the Teamsters and our airline pilots, airline mechanics, ground mechanics and certain other employees are employed under other collective bargaining agreements. While UPS employees in the U.S. Domestic Package business unit voted to approve a new national master agreement during the second quarter of 2013, we are in the midst of negotiating certain local U.S. Domestic Package supplemental agreements and the agreement covering UPS Freight employees with the Teamsters. Strikes, work stoppages and slowdowns by our employees could adversely affect our ability to meet our customers' needs, and customers may do more business with competitors if they believe that such actions or threatened actions may adversely affect our ability to provide services. We may face permanent loss of customers if we are unable to provide uninterrupted service, and this could adversely affect our business, financial position and results of operations. The terms of future collective bargaining agreements also may affect our competitive position and results of operations.

Table of Contents

We are exposed to the effects of changing prices of energy, including gasoline, diesel and jet fuel, and interruptions in supplies of these commodities.

Changing fuel and energy costs may have a significant impact on our operations. We require significant quantities of fuel for our aircraft and delivery vehicles and are exposed to the risk associated with variations in the market price for petroleum products, including gasoline, diesel and jet fuel. We mitigate our exposure to changing fuel prices through our indexed fuel surcharges and we may also enter into hedging transactions from time to time. If we are unable to maintain or increase our fuel surcharges, higher fuel costs could adversely impact our operating results. Even if we are able to offset the cost of fuel with our surcharges, high fuel surcharges may result in a mix shift from our higher yielding air products to lower yielding ground products or an overall reduction in volume. If fuel prices rise sharply, even if we are successful in increasing our fuel surcharge, we could experience a lag time in implementing the surcharge, which could adversely affect our short-term operating results. There can be no assurance that our hedging transactions will be effective to protect us from changes in fuel prices. Moreover, we could experience a disruption in energy supplies, including our supply of gasoline, diesel and jet fuel, as a result of war, actions by producers, or other factors which are beyond our control, which could have an adverse effect on our business.

Changes in exchange rates or interest rates may have an adverse effect on our results.

We conduct business across the globe with a significant portion of our revenue derived from operations outside the United States. Our operations in international markets are affected by changes in the exchange rates for local currencies, and in particular the Euro, British Pound Sterling, Canadian Dollar, Chinese Renminbi and Hong Kong Dollar.

We are exposed to changes in interest rates, primarily on our short-term debt and that portion of our long-term debt that carries floating interest rates. The impact of a 100-basis-point change in interest rates affecting our debt is discussed in the “Quantitative and Qualitative Disclosures about Market Risk” section of this report.

We monitor and manage our exposures to changes in currency exchange rates and interest rates, and make limited use of derivative instruments to mitigate the impact of changes in these rates on our financial position and results of operations; however, changes in exchange rates and interest rates cannot always be predicted or hedged.

If we are unable to maintain our brand image and corporate reputation, our business may suffer.

Our success depends in part on our ability to maintain the image of the UPS brand and our reputation for providing excellent service to our customers. Service quality issues, actual or perceived, even when false or unfounded, could tarnish the image of our brand and may cause customers to use other companies. Also, adverse publicity surrounding labor relations, environmental concerns, security matters, political activities and the like, or attempts to connect our company to these sorts of issues, either in the United States or other countries in which we operate, could negatively affect our overall reputation and acceptance of our services by customers. Damage to our reputation and loss of brand equity could reduce demand for our services and thus have an adverse effect on our business, financial position and results of operations, and could require additional resources to rebuild our reputation and restore the value of our brand.

A significant privacy breach or IT system disruption could adversely affect our business and we may be required to increase our spending on data and system security.

We rely on information technology networks and systems, including the Internet, to process, transmit and store electronic information, and to manage or support a variety of business processes and activities. In addition, the provision of service to our customers and the operation of our network involve the storage and transmission of proprietary information and sensitive or confidential data, including personal information of customers, employees and others. Our information technology systems, some of which are managed by third-parties, may be susceptible to damage, disruptions or shutdowns due to failures during the process of upgrading or replacing software, databases or components thereof, power outages, hardware failures, computer viruses, attacks by computer hackers, telecommunication failures, user errors or catastrophic events. Groups of hackers may also act in a coordinated manner to launch distributed denial of service attacks or other coordinated attacks that may cause service outages or other interruptions. In addition, breaches in security could expose us, our customers or the individuals affected to a risk of loss or misuse of proprietary information and sensitive or confidential data. Any of these occurrences could result in disruptions in our operations, the loss of existing or potential customers, damage to our brand and reputation, and litigation and potential liability for the company. In addition, the cost and operational consequences of implementing further data or system protection measures could be significant.

54

Table of Contents

Severe weather or other natural or manmade disasters could adversely affect our business.
Severe weather conditions and other natural or manmade disasters, including storms, floods, fires and earthquakes, may result in decreased revenues, as our customers reduce their shipments, or increased costs to operate our business, which could have an adverse effect on our results of operations for a quarter or year. Any such event affecting one of our major facilities could result in a significant interruption in or disruption of our business.
We make significant capital investments in our business of which a significant portion is tied to projected volume levels.
We require significant capital investments in our business consisting of aircraft, vehicles, technology, facilities and sorting and other types of equipment to support both our existing business and anticipated growth. Forecasting projected volume involves many factors which are subject to uncertainty, such as general economic trends, changes in governmental regulation and competition. If we do not accurately forecast our future capital investment needs, we could have excess capacity or insufficient capacity, either of which would negatively affect our revenues and profitability. In addition to forecasting our capital investment requirements, we adjust other elements of our operations and cost structure in response to adverse economic conditions; however, these adjustments may not be sufficient to allow us to maintain our operating margins in a weak economy.
We derive a significant portion of our revenues from our international operations and are subject to the risks of doing business in emerging markets.
We have significant international operations and while the geographical diversity of our international operations helps ensure that we are not overly reliant on a single region or country, we are continually exposed to changing economic, political and social developments beyond our control. Emerging markets are typically more volatile than those in the developed world, and any broad-based downturn in these markets could reduce our revenues and adversely affect our business, financial position and results of operations.
We are subject to changes in markets and our business plans that have resulted, and may in the future result, in substantial write-downs of the carrying value of our assets, thereby reducing our net income.
Our regular review of the carrying value of our assets has resulted, from time to time, in significant impairments, and we may in the future be required to recognize additional impairment charges. Changes in business strategy, government regulations, or economic or market conditions have resulted and may result in further substantial impairments of our intangible, fixed or other assets at any time in the future. In addition, we have been and may be required in the future to recognize increased depreciation and amortization charges if we determine that the useful lives of our fixed assets are shorter than we originally estimated. Such changes could reduce our net income.
Employee health and retiree health and pension benefit costs represent a significant expense to us.
With approximately 399,000 employees, including approximately 323,000 in the U.S., our expenses relating to employee health and retiree health and pension benefits are significant. In recent years, we have experienced significant increases in certain of these costs, largely as a result of economic factors beyond our control, including, in particular, ongoing increases in health care costs well in excess of the rate of inflation and the decreasing trend of discount rates in which we use to value our pension liabilities. Continued increasing health care costs, volatility in investment returns and discount rates, as well as changes in laws, regulations and assumptions used to calculate retiree health and pension benefit expenses, may adversely affect our business, financial position, results of operations or require significant contributions to our pension plans. The new national master agreement with the Teamsters, which is subject to ratification, includes changes that are designed to mitigate certain of these health care expenses, but there can be no assurance that our efforts will be successful or that the failure or success of these efforts will not adversely affect our business, financial position, results of operations or liquidity.
We participate in a number of trustee-managed multiemployer pension and health and welfare plans for employees covered under collective bargaining agreements. Several factors could cause us to make significantly higher future contributions to these plans, including unfavorable investment performance, increases in health care costs, changes in demographics and increased benefits to participants. At this time, we are unable to determine the amount of additional future contributions, if any, or whether any material adverse effect on our financial condition, results of operations or liquidity could result from our participation in these plans.

55

Table of Contents

We may be subject to various claims and lawsuits that could result in significant expenditures.
The nature of our business exposes us to the potential for various claims and litigation related to labor and employment, personal injury, property damage, business practices, environmental liability and other matters. Any material litigation or a catastrophic accident or series of accidents could have a material adverse effect on our business, financial position and results of operations.
We may not realize the anticipated benefits of acquisitions, joint ventures or strategic alliances.
As part of our business strategy, we may acquire businesses and form joint ventures or strategic alliances. Whether we realize the anticipated benefits from these transactions depends, in part, upon the successful integration between the businesses involved, the performance of the underlying operation, capabilities or technologies and the management of the transacted operations. Accordingly, our financial results could be adversely affected by our failure to effectively integrate the acquired operations, unanticipated performance issues, transaction-related charges or charges for impairment of long-term assets that we acquire.
Insurance and claims expenses could have a material adverse effect on our business, financial condition and results of operations.
We have a combination of both self-insurance and high-deductible insurance programs for the risks arising out of the services we provide and the nature of our global operations, including claims exposure resulting from cargo loss, personal injury, property damage, aircraft and related liabilities, business interruption and workers' compensation. Workers' compensation, automobile and general liabilities are determined using actuarial estimates of the aggregate liability for claims incurred and an estimate of incurred but not reported claims, on an undiscounted basis. Our accruals for insurance reserves reflect certain actuarial assumptions and management judgments, which are subject to a high degree of variability. If the number or severity of claims for which we are retaining risk increases, our financial condition and results of operations could be adversely affected. If we lose our ability to self-insure these risks, our insurance costs could materially increase and we may find it difficult to obtain adequate levels of insurance coverage.

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds
(c) A summary of our repurchases of our class A and class B common stock during the second quarter of 2013 is as follows (in millions, except per share amounts):

	Total Number of Shares Purchased(1)	Average Price Paid Per Share	Total Number of Shares Purchased as Part of Publicly Announced Program	Approximate Dollar Value of Shares that May Yet be Purchased Under the Program
April 1 – April 30, 2013	7.3	$85.35	6.8	$ 9,066
May 1 – May 31, 2013	1.7	87.08	1.1	8,972
June 1 – June 30, 2013	1.7	88.92	1.7	8,825
Total April 1 – June 30, 2013	10.7	$86.17	9.6	

(1) Includes shares repurchased through our publicly announced share repurchase program and shares tendered to pay the exercise price and tax withholding on employee stock options.

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. We anticipate repurchasing approximately $4.0 billion of shares in 2013.

Table of Contents

Item 3. Defaults Upon Senior Securities

None.

Item 5. Other Information

None.

Item 6. Exhibits

These exhibits are either incorporated by reference into this report or filed with this report as indicated below.

Index to Exhibits:

2.1	—	Termination Agreement, dated as of January 22, 2013, between United Parcel Service, Inc. and TNT Express N.V. (incorporated by reference to Exhibit 2.3 to the 2012 Annual Report on Form 10-K).
3.1	—	Form of Restated Certificate of Incorporation of United Parcel Service, Inc. (incorporated by reference to Exhibit 3.2 to Form 8-K filed on May 12, 2010).
3.2	—	Amended and Restated Bylaws of United Parcel Service, Inc. as of February 14, 2013 (incorporated by reference to Exhibit 3.1 to Form 8-K, filed on February 19, 2013).
10.1	—	Credit Agreement (364-Day Facility) dated March 29, 2013 among United Parcel Service, Inc., the initial lenders named therein, J.P. Morgan Securities LLC and Citigroup Global Markets, Inc. as joint lead arrangers and joint bookrunners, Barclays Bank PLC and BNP Paribas Securities Corp. as co-lead arrangers, Barclays Bank PLC and BNP Paribas as co-documentation agents, Citibank, N.A. as syndication agent, and JPMorgan Chase Bank, N.A. as administrative agent (incorporated by reference to Exhibit 10.1 to Form 10-Q for the Quarter Ending March 31, 2013).
10.2	—	Credit Agreement (5 Year Facility) dated March 29, 2013 among United Parcel Service, Inc., the initial lenders named therein, J.P. Morgan Securities LLC and Citigroup Global Markets, Inc. as joint lead arrangers and joint bookrunners, Barclays Bank PLC and BNP Paribas Securities Corp. as co-lead arrangers, Barclays Bank PLC and BNP Paribas as co-documentation agents, Citibank, N.A. as syndication agent, and JPMorgan Chase Bank, N.A. as administrative agent (incorporated by reference to Exhibit 10.2 to Form 10-Q for the Quarter Ending March 31, 2013).
11	—	Statement regarding Computation of per Share Earnings (incorporated by reference to Note 12 to “Item 1. Financial Statements” of this quarterly report on Form 10-Q).
†12	—	Computation of Ratio of Earnings to Fixed Charges.
†31.1	—	Certification of the Chief Executive Officer Pursuant to Rule 13a-14(a), as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
†31.2	—	Certification of the Chief Financial Officer Pursuant to Rule 13a-14(a), as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
†32.1	—	Certification of the Chief Executive Officer Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
†32.2	—	Certification of the Chief Financial Officer Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

††101	—	The following financial information from the Quarterly Report on Form 10-Q for the quarter ended June 30, 2013, formatted in XBRL (Extensible Business Reporting Language): (i) the Consolidated Balance Sheets, (ii) the Consolidated Statements of Income, (iii) the Consolidated Statements of Comprehensive Income, (iv) the Consolidated Statements of Cash Flows, and (v) the Notes to the Consolidated Financial Statements.

† Filed herewith.
†† Furnished electronically herewith

57

Table of Contents

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

	UNITED PARCEL SERVICE, INC. (Registrant)
Date: August 2, 2013	By: /S/ KURT P. KUEHN Kurt P. Kuehn Senior Vice President and Chief Financial Officer (Duly Authorized Officer and Principal Accounting Officer)

58