

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

Form 10-K

FOR ANNUAL AND TRANSITION REPORTS

**PURSUANT TO SECTIONS 13 OR 15(d) OF THE
SECURITIES EXCHANGE ACT OF 1934**

(Mark One)

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

For the fiscal year ended December 31, 2002

or

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

For the transition period from to

Commission file number 001-15451

United Parcel Service, Inc.

(Exact Name of Registrant as Specified in Its Charter)

Delaware
*(State or Other Jurisdiction of
Incorporation or Organization)*
55 Glenlake Parkway, N.E.
Atlanta, Georgia
(Address of Principal Executive Offices)

58-2480149
*(I.R.S. Employer
Identification No.)*
30328
(Zip Code)

(404) 828-6000

(Registrant's telephone number, including area code)

Securities registered pursuant to Section 12(b) of the Act:

Title of Each Class

Name of Each Exchange on Which Registered

Class B common stock, par value \$.01 per share

New York Stock Exchange

Securities registered pursuant to Section 12(g) of the Act:

Class A common stock, par value \$.01 per share

(Title of Class)

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 No

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.

Indicate by check mark whether the registrant is an accelerated filer (as defined in Exchange Act Rule 12b-2). Yes No

The aggregate market value of the class B common stock held by non-affiliates of the registrant as of February 1, 2003 was approximately \$30,253,493,290 (based on the closing price of such stock as of the last business day of the registrant's most recently completed second fiscal quarter). As of February 1, 2003, non-affiliates held 601,948,080 shares of class A common stock and 489,935,114 shares of class B common stock. The registrant's class A common stock is not listed on a national securities exchange or traded in an organized over-the-counter market, but each share of the registrant's class A common stock is convertible into one share of the registrant's class B common stock.

As of February 1, 2003, there were 633,145,907 outstanding shares of class A common stock and 490,705,730 outstanding shares of class B common stock.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the registrant's definitive proxy statement for its annual meeting of shareowners scheduled for May 8, 2003 are incorporated by reference into Part III of this report.

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PART I

Item 1. Business

Overview

We are the world's largest package delivery company and a leading global provider of specialized transportation and logistics services. We were founded in 1907 as a private messenger and delivery service in the Seattle, Washington area. Over the past 96 years, we have expanded from a small regional parcel delivery service into a global company. We deliver packages each business day for 1.8 million shipping customers to 6 million consignees. In 2002, we delivered an average of more than 13 million pieces per day worldwide. Total revenue in 2002 was over \$31 billion. We focus on the movement of goods, information and funds, and we seek to position ourselves as the world's premier enabler of global commerce.

Our primary business is the time-definite delivery of packages and documents throughout the United States and in over 200 other countries and territories. We have established a global transportation infrastructure and developed a comprehensive portfolio of guaranteed delivery services, and we support these services with advanced technology. We provide integrated supply chain solutions for major companies worldwide. We are the industry leader in the delivery of goods purchased over the Internet.

Competitive Strengths

Our competitive strengths include:

Global Reach and Scale. We believe that our integrated global ground and air network is the most extensive in the industry. We operate a ground fleet of more than 88,000 vehicles, ranging from custom-built delivery vehicles to large tractors and trailers, and almost 600 airplanes. In the U.S., we estimate that our integrated door-to-door delivery system carries goods having a value in excess of 6% of the U.S. gross domestic product, and we reach all U.S. businesses and residential addresses. We are the ninth largest airline in North America and eleventh largest in the world. Our primary air hub is located in Louisville, Kentucky.

We established our first European operation in Germany in 1975 and expanded it as the single market created by the European Union drove the need for pan-European delivery services. We believe we have the most comprehensive integrated delivery and information services portfolio of any carrier in Europe.

Through more than two dozen alliances with Asian delivery companies that supplement company-owned operations, we currently serve more than 40 Asia Pacific countries and territories. With the fastest growing middle classes in the world, China and India represent two of our most promising opportunities.

We also are the largest air cargo carrier and a leading logistics provider in Latin America and the Caribbean. We have formed alliances with a number of service providers in countries throughout that region.

Technology Systems. We continue to be a global leader in merging technology with business processes to improve operations and provide new or enhanced services to customers worldwide. We have developed a strong global capability as a mover of electronic information. We daily transmit approximately 3 million packets of tracking data via wireless networks, and we currently collect electronic data on about 90 percent of the packages that move through our system each day — more than any of our competitors.

Technology powers virtually every service we offer and every operation we perform. Our technology initiatives continue to be driven by the needs of customers. We provide the infrastructure for an Internet presence that extends to more than 60,000 customer web sites that integrate UPS tools. We offer a variety of on-line service options that enable our customers to integrate UPS functionality into their own businesses — not only to conveniently send, manage and track their shipments, but to provide their own customers with better information services.

E-Commerce Capabilities. We are a leading participant in and facilitator of global e-commerce, which we define as the use of networked computer technology to facilitate the buying and selling of goods and services. According to Forrester Research, by 2004, business-to-business e-commerce will grow to \$6.3

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trillion, and online transactions will account for 17% of business trade volume in the U.S. and 18% of world exports. Forrester Research also has projected that online retail sales will grow to \$217.8 billion by 2007, which would comprise 8% of all retail sales. We enable our customers around the world to thrive in this environment by providing a portfolio of technology solutions that streamline their shipment processing and integrate critical transportation information into their business processes.

Broad, Flexible Range of Distribution Services. Our portfolio of services enables customers to choose the delivery option that is most appropriate for their requirements. All of our delivery service offerings are guaranteed.

Our express air services are integrated with our vast ground delivery system. This integrated air and ground network enhances efficiency, improves productivity and provides us with the flexibility to transport packages using the most reliable and cost-effective transportation mode or combination of modes. Our sophisticated engineering systems allow us to optimize our network efficiency and asset utilization on a daily basis.

Customer Relationships. We focus on building and maintaining long-term customer relationships. We deliver packages each business day for 1.8 million shipping customers to 6 million consignees. In addition, thousands of other customers access us daily through UPS On-Call PickupSM for air delivery services, about 45,000 letter drop-boxes, over 8,000 independently owned authorized shipping outlets, and through more than 4,000 independently owned and operated Mail Boxes Etc.[®] locations. In February 2003, we announced a plan to allow all Mail Boxes Etc. franchisees in the contiguous U.S. to convert their retail centers to The UPS StoreSM.

We place significant value on the quality of our customer relationships, and we conduct comprehensive research to monitor customer perceptions. Since 1993, we have conducted telephone interviews with shipping decision-makers virtually every business day to determine their satisfaction with delivery providers and perception of performance on 17 key categories of service factors. Results from this survey for the second half of 2002 were the highest we ever have achieved.

Brand Equity. We have built the leading and most trusted brand in our industry. Our reputation for quality service, reliability and product innovation is unmatched. The distinctive appearance of our vehicles and the friendliness and helpfulness of our drivers are major contributors to our brand equity.

Over the past several years, we successfully have expanded our brand to stand for much more than U.S. ground delivery. The UPS brand now is recognized in the U.S. and around the world as a global provider of time-definite services. We are taking advantage of our strong brand equity to expand our product offerings in the supply chain solutions arena in order to help our customers build their businesses and become more profitable.

Distinctive People and Culture. We believe that the dedication of our employees results in large part from our distinctive “employee-owner” concept. Our employee stock ownership tradition dates from 1927, when our founders, who believed that employee stock ownership was a vital foundation for successful business, first offered stock to employees. To facilitate employee stock ownership, we maintain several stock-based compensation programs.

Our long-standing policy of “promotion from within” complements our tradition of employee ownership, and this policy makes it generally unnecessary for us to hire managers and executive officers from outside UPS. The vast majority of our management team began their careers as full-time or part-time hourly UPS employees, and have since spent their entire careers with us. Our chief executive officer and most of our executive officers have more than 30 years of service with us and have accumulated a meaningful ownership stake in our company. Therefore, our executive officers have a strong incentive to effectively manage UPS, which benefits all of our shareowners.

Financial Strength. Our balance sheet reflects financial strength that few companies can match. As of December 31, 2002, we had a balance of cash, cash equivalents, marketable securities and short-term investments of approximately \$3 billion and shareowners’ equity of \$12.5 billion. Long-term debt was

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\$3.5 billion. Our financial strength has given us the resources to achieve global scale and to make investments in technology, transportation equipment and buildings needed to facilitate our growth.

Growth Strategy

Our growth strategy takes advantage of our competitive strengths while maintaining our focus on meeting or exceeding our customers' requirements. The principal components of our growth strategy are:

Build on Our Leadership Position in Our U.S. Business. Our U.S. package operation is the foundation of our business and the primary engine for our future growth. We believe that our tradition of reliable package delivery service, our experienced and dedicated employees and our unmatched integrated air and ground network provide us with the advantages of reputation, service quality and economies of scale that differentiate us from our competitors. Our strategy is to increase core domestic revenues through cross-selling our existing and new services to our large and diverse customer base, to limit the rate of expense growth and to employ technology-driven efficiencies to increase operating profit.

Continue International Expansion. We have built a strong international presence through significant investments over a number of years. The international package delivery market has grown, and continues to grow, at a faster rate than the U.S. market. We plan to utilize our worldwide infrastructure and broad product portfolio to continue to grow high-margin premium services and to implement cost, process and technology improvements in our international operations.

Europe is our largest market outside the United States, followed by Asia. Both of these regions offer significant opportunities for growth as the European Union expands into the Eastern Bloc countries and creates even greater economic cohesion. Growth in Asia will be driven by improving demographic and economic trends in China, South Korea and India.

Provide Comprehensive Supply Chain Solutions. Many businesses outsource the management of all or part of their supply chains to streamline and gain efficiencies, to strengthen their balance sheets and to improve service. We anticipate that there will be further demand for a global service offering that incorporates transportation, distribution and international trade services with financial and information services. We believe that we are well positioned to capitalize on this growth for the following reasons:

- We manage supply chains for major companies in 120 countries, with about 25 million square feet of distribution space and over 750 facilities worldwide.
- We focus on technology, reengineering and management-based solutions for our customers rather than solely on more traditional asset-based logistics such as warehouses and vehicle fleets.
- We provide a broad range of transportation solutions to customers worldwide, including air, ocean and ground freight, as well as customs brokerage and trade and materials management.
- We offer a portfolio of financial services that provide customers with short- and long-term financing, secured lending, working capital, government guaranteed lending, lines of credit, global trade financing, credit cards, equipment leasing and insurance.

Leverage Our Leading-Edge Technology and E-Commerce Advantage. We believe that e-commerce will drive smaller and more frequent shipments and provide a strong complement to our core delivery service offerings.

Our goals are to provide our customers with easy-to-use, flexible technology offerings that streamline their shipment processing and integrate critical transportation information into their business processes, helping them create supply chain efficiencies, improve their cash flows and serve their customers. Our leading-edge technology has enabled our e-commerce partners to integrate our shipping functionality into their e-commerce product suites. Our partners' products are being installed throughout the Internet, and we expect these integrated systems to provide us with a competitive advantage as they allow our customers to provide better decision-making information and improve customer service.

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Pursue Strategic Acquisitions and Global Alliances. Strategic acquisitions and global alliances play a significant role in spurring growth. We look for opportunities that:

- complement our core business;
- build our global brand;
- enhance our technological capabilities or service offerings;
- lower our costs; and
- expand our geographic presence and managerial expertise.

Domestic Package Products and Services

For most of our history, we have been engaged primarily in the delivery of packages traveling by ground transportation. We expanded this service gradually, and today our standard ground service is available to every address in the 48 contiguous United States. We handle packages that weigh no more than 150 pounds and are no larger than 108 inches in length and 130 inches in combined length and girth.

In addition to our standard ground delivery product, *UPS Hundredweight Service*® offers discounted rates to customers sending multiple package shipments having a combined weight of 200 pounds or more, or air shipments totaling 100 pounds or more, addressed to one recipient at one address and shipped on the same day. Customers realize significant savings on these shipments compared to less-than-truckload (or LTL) or air freight forwarder rates.

We provide domestic air delivery throughout the United States. *UPS Next Day Air*® offers guaranteed next business day delivery by 10:30 a.m. to more than 74% of the United States population and delivery by noon to areas covering an additional 15% of the population. We offer Saturday delivery for UPS Next Day Air shipments for an additional fee.

UPS domestic air products include:

UPS Next Day Air® *Early A.M.*®

UPS Next Day Air®

UPS Next Day Air Saver®

UPS 2nd Day Air A.M.®

UPS 2nd Day Air

3 Day Select®

We offer additional services, such as Consignee Billing, Delivery Confirmation and UPS ReturnsSM, to customers that require customized package distribution solutions.

International Package Products and Services

We deliver international shipments to more than 200 countries and territories worldwide, and we provide guaranteed overnight delivery to the world's major business centers. We offer a complete portfolio of import, export and domestic services. This portfolio includes guaranteed 8:00 a.m., 8:30 a.m., 10:30 a.m. and 12:00 p.m. next business day delivery to major cities around the world, as well as scheduled day-definite air and ground services. We offer complete customs clearance service for any mode of transportation, regardless of carrier.

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UPS international services include:

*UPS Worldwide Express*SM
*UPS Worldwide Express Plus*SM
*UPS Worldwide Express*SM *NAI*
UPS Express Saver

*UPS Worldwide Expedited*SM
UPS Standard

*UPS WorldEase*SM

We also have a portfolio of UPS domestic services in 20 major countries throughout the world, which provide our customers time-definite delivery options for packages moving between points in those countries.

Europe is our largest market outside the United States. We experienced double-digit export volume growth in Europe during 2002, outpacing market growth. Transborder services, or the movement of packages within Europe, are proving to be the growth engine in this region. We have announced plans to expand our major air hub in Cologne, Germany.

We continue to invest in infrastructure and technology in Asia. In April 2002, we opened a new intra-Asia hub at Clark Air Force Base in Pampanga, Philippines to enable future growth in the region. This hub allows us to compete more effectively in the Asian express market and improve our Europe/Asia service. We have acquired landing slots on the new runway at Tokyo's Narita Airport, which will enhance access and connections to the new intra-Asia hub. We recently received from the U.S. Department of Transportation an interim grant of authority to expand service to and through Hong Kong, and we also have applied for permanent authority to fly from Hong Kong to other cities, specifically to our Cologne hub in Europe. We continue our development efforts in the fast-growing China market.

We believe that there is significant untapped potential for us to expand our service offerings in Latin America. To this end, we have introduced overnight delivery between key cities in the Mercosur and other trade blocs and opened our Americas International Gateway in Miami, Florida. This new gateway complements our current operations in Florida and Latin America and represents our commitment to the Americas market.

Mexico also is important to our international activity. We created UPS Trade DirectSM Cross Border service to manage movements to the U.S. from the maquiladoras in Mexico. This service combines UPS's small package, freight and brokerage capabilities to create an integrated, streamlined and economical solution for customers with complex cross-border distribution needs. This solution also will be available for Canadian firms wishing to gain distribution efficiencies as they ship to U.S. customers.

During 2002, we also introduced UPS Trade Direct Ocean, a service that transforms ocean container movements into pre-labeled small packages or LTL shipments. When the goods arrive in the U.S., packages are deconsolidated and entered into the UPS system, eliminating the receiving, sorting and handling necessary in distribution centers. This service significantly cuts the supply chain cycle from point of origin to consignee. It provides our customers with faster time to market, reduced costs and increased visibility into, and better management of, the supply chain.

Non-Package Products and Services

Supply Chain Services

In February 2002, we began a three-phased approach to integrating our supply chain business units. First, we created UPS Supply Chain SolutionsSM, a streamlined organization that combined the sales and marketing functions of our supply chain subsidiaries. This new organization makes it easier for customers to access our expanding range of logistics, freight, financial and consulting services in order to improve the performance of their global supply chains. Then, we developed a shared services approach to finance, accounting, human resources and information technology that supports these subsidiaries. Lastly, we combined UPS Logistics Group and UPS Freight Services. Effective January 2003, these organizations began to operate on a

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geographic rather than on a service basis. The combined operations function in 120 countries. Integrating these business units offers several benefits, including better customer service, easier cross-selling, reduced costs and greater growth opportunities.

UPS Supply Chain Solutions meets customers' supply chain needs by selecting the most appropriate solution from a portfolio of over 60 services. Among these are:

- *Logistics and Distribution*: supply chain management, distribution center design, planning and management, order fulfillment, inventory management, receiving and shipping, service parts logistics, reverse logistics and cross docking.
- *International Trade Management*: freight forwarding, full-service customs brokerage and international trade consulting.
- *Transportation and Freight*: air, ocean, rail and ground freight utilizing UPS and other carriers, and multimodal transportation network management.
- *Financial*: asset-based lending, global trade finance and export-import lending.
- *Consulting*: supply chain design and re-engineering.

Electronic Services

We provide a variety of UPS on-line solutions that support automated shipping and tracking.

- *UPS OnLine®* WorldShip® helps shippers streamline their shipping activities by processing shipments, printing address labels, tracking packages and providing management reports, all from a desktop computer.
- *UPS Internet Shipping* is a quick and convenient way to ship packages using the web without installing additional software.
- *UPS OnLine Host Access* provides electronic connectivity between UPS and the shipper's host computer system, linking UPS shipping information directly to all parts of the customer's organization.
- *UPS OnLine Compatible Solutions*, provided by third-party vendors, offer similar benefits to customers who want to automate their shipping and tracking processes.

Our website strategy is to provide our customers with the convenience of all the functions that they otherwise would perform over the phone or at one of our shipping outlets. Package tracking, pick-up requests, rate quotes, account opening, wireless registration, drop-off locator, transit times and supply ordering services all are available at the customer's desktop. The site also displays full domestic and international service information.

UPS.com receives more than 86 million hits and processes over 7.9 million package tracking transactions daily. A growing number of those tracking requests now come from customers in the 35 countries that have wireless access to UPS tracking information. Businesses in 46 countries also can download UPS OnLine Tools to their own websites for direct use by their customers. This allows users to access the information they need without leaving our customers' websites.

Sales and Marketing

Our field sales organization includes about 3,600 domestic and 1,200 international account executives worldwide. Account executives are assigned to individual operating districts. For our largest multi-site customers, we have an organization of regionally based account managers who report directly to our corporate office.

We also have three supplemental sales forces. In the U.S., we have an international business sales force, which is focused on international business out of major U.S. business centers, and a UPS Hundredweight

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Service sales force, which focuses on LTL volume. Globally, we have an e-commerce sales team, which focuses on UPS technology solutions for businesses.

Our marketing organization is generally organized along similar lines. At the corporate level, the marketing group is engaged in brand management, rate-making and revenue management policy, market and customer research, product development, product management, marketing alliances and e-commerce, including the non-technical aspects of our web presence. Advertising, public relations and most formal marketing communications are centrally conceived and controlled.

Individual district and region marketing personnel are engaged in business planning, bid preparation and other revenue management activities, and in coordinating alignment with corporate marketing initiatives. Individual regions and districts may engage in local promotional and public relations activities pertinent to their locales.

Employees

During 2002, we had approximately 360,000 employees.

We have received numerous awards and wide recognition as an employer-of-choice, including the following:

- We recently were named one of *Fortune Magazine's* "Diversity Elite — 50 Best Companies for Minorities" for the fourth consecutive year.
- We were named the NAACP Corporate Citizen of the Year for 2002.
- We received the Ron Brown Award for Corporate Leadership in 2001.
- *Hispanic Magazine* recognized us as a leader in its "13th Annual Corporate 100."
- We were named to DiversityInc.com's "Diversity Top 30."

As of December 31, 2002, we had approximately 230,000 employees (64% of our total employees) employed under a national master agreement and various supplemental agreements with local unions affiliated with the International Brotherhood of Teamsters. On October 7, 2002, the Teamsters ratified a new master agreement with UPS that runs through July 31, 2008. The new agreement is retroactive to August 1, 2002. The majority of our pilots are employed under a collective bargaining agreement with the Independent Pilots Association, which becomes amendable January 1, 2004. Our airline mechanics are covered by a collective bargaining agreement with Teamsters Local 2727, which becomes amendable on November 1, 2006. In addition, the majority 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. These agreements run through July 31, 2009.

We believe that our relations with our employees are good.

Competition

We are the largest package delivery company in the world, in terms of both revenue and volume. We offer a broad array of services in the package delivery industry and, therefore, compete with many different companies and services on a local, regional, national and international basis. Our competitors include the postal services of the United States and other nations, various motor carriers, express companies, freight forwarders, air couriers and others. Our major competitors include the United States Postal Service, FedEx, Airborne Express, DHL Worldwide Express, Deutsche Post and TNT Post Group.

We believe competition increasingly is based on a carrier's ability to integrate its distribution and information systems with its customers' systems to provide unique transportation solutions at competitive prices. We rely on our vast infrastructure and service portfolio to attract and maintain customers. As we expand our supply chain and other non-package businesses, we compete with a number of participants in the supply chain, financial services and information technology industries.

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Government Regulation

Both the U.S. Department of Transportation and the Federal Aviation Administration regulate air transportation services.

The DOT's authority primarily relates to economic aspects of air transportation, such as discriminatory pricing, non-competitive practices, interlocking relations and cooperative agreements. The DOT also regulates, subject to the authority of the President of the United States, international routes, fares, rates and practices, and is authorized to investigate and take action against discriminatory treatment of U.S. air carriers abroad. We are subject to U.S. customs laws and related DOT regulations regarding the import and export of shipments to and from the U.S. In addition, our customs brokerage entities are subject to those same laws and regulations as they relate to the filing of documents on behalf of client importers and exporters.

The FAA's authority primarily relates to safety aspects of air transportation, including aircraft standards and maintenance, personnel and ground facilities. In 1988, the FAA granted us an operating certificate, which remains in effect so long as we meet the operational requirements of federal aviation regulations.

The FAA has issued rules mandating repairs on all Boeing Company and McDonnell-Douglas Corporation aircraft that have completed a specified number of flights, and also has issued rules requiring a corrosion control program for Boeing Company aircraft. Our total expenditures under these programs for 2002 were about \$17 million. The future cost of repairs pursuant to these programs may fluctuate. All mandated repairs have been completed, or are scheduled to be completed, within the timeframes specified by the FAA.

In response to the September 11, 2001 terrorist attacks, on September 22, 2001, President Bush signed into law the Air Transportation Safety and System Stabilization Act, a \$15 billion emergency economic assistance package to mitigate the dramatic financial losses experienced by the nation's air carriers. We submitted a claim for compensation to the DOT and recognized a pre-tax amount of \$74 million in 2001 related to this reimbursement as a credit to other operating expenses. We may become subject to additional regulation (by the FAA or by other federal or state agencies) as a result of increased security concerns in the aftermath of September 11.

Our ground transportation of packages in the U.S. is subject to the DOT's jurisdiction with respect to the regulation of routes and to both the DOT's and the states' jurisdiction with respect to the regulation of safety, insurance and hazardous materials.

We are subject to similar regulation in many non-U.S. jurisdictions. In addition, we are subject to non-U.S. government regulation of aviation rights to and beyond non-U.S. jurisdictions, and non-U.S. customs regulation.

The Postal Reorganization Act of 1970 created the U.S. Postal Service as an independent establishment of the executive branch of the federal government, and vested the power to recommend domestic postal rates in a regulatory body, the Postal Rate Commission. We believe that the U.S. Postal Service consistently attempts to set rates for its monopoly services, particularly First Class letter mail, above the cost of providing those services, in order to use the excess revenues to subsidize its expedited, parcel, international and other competitive services. Therefore, we participate in the proceedings before the Postal Rate Commission in an attempt to secure fair postal rates for competitive services.

We are subject to numerous other laws and regulations in connection with our non-package businesses, including customs regulations, Food and Drug Administration regulation of our transportation of pharmaceuticals and state and federal lending regulations.

Where You Can Find More Information

We make our annual reports on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, and all amendments to these reports filed pursuant to Section 13(a) or 15(d) of the Securities Exchange Act of 1934, available free of charge on our website, located at <http://www.ups.com>, as soon as reasonably practicable after they are filed with or furnished to the SEC.

See Footnote 12 to our consolidated financial statements for financial information regarding our industry segments and geographic areas in which we operate.

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Item 1A. Executive Officers of the Registrant

Name and Office	Age	Principal Occupation and Employment For the Last Five Years
David P. Abney Senior Vice President and President, UPS International	47	Senior Vice President and President, UPS International (2003 to present), UPS/Fritz Companies Integration Manager (2001-2002), UPS SonicAir Manager (1995-2000), Utah District Manager (1992- 1994).
John J. Beystehner Senior Vice President	51	Senior Vice President (1999 to present), Marketing Group Manager (2001 to present), Worldwide Sales Group Manager (1997 to present), Airline Operations Manager (1994 to 1997).
Calvin Darden Senior Vice President and Director	53	Senior Vice President and U.S. Operations Manager (1998 to present), Director (2001 to present), Corporate Quality Manager (1995 to 1998).
D. Scott Davis Senior Vice President, Chief Financial Officer and Treasurer	51	Senior Vice President, Chief Financial Officer and Treasurer (2001 to present), Vice President — Finance (2000 to 2001), Chief Executive Officer of Overseas Partners Ltd. (1998 to 2000), Accounting Manager (1996 to 1998).
Michael L. Eskew Chairman and Chief Executive Officer	53	Chairman and Chief Executive Officer (2002 to present), Vice Chairman (2000 to 2001), Executive Vice President (1999 to 2001), Director (1998 to present), Corporate Development Group Manager (1999 to 2000), Senior Vice President (1996 to 1999), Engineering Group Manager (1996 to 2000).
Kenneth W. Lacy Senior Vice President and Chief Information Officer	53	Senior Vice President and Chief Information Officer (1996 to present).
Christopher D. Mahoney Senior Vice President	55	Senior Vice President (1998 to present), Transportation Group Manager (2001 to present), Labor Relations Group Manager (2001 to present), U.S. Operations Manager (1998 to 2001), Region Manager (1990 to 1998).

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Name and Office	Age	Principal Occupation and Employment For the Last Five Years
Joseph R. Moderow Senior Vice President, Secretary and Director	54	Senior Vice President and Secretary (1986 to present), Director (1988 to present), Legal and Public Affairs Group Manager (1989 to present).
Joseph M. Pyne Senior Vice President	55	Senior Vice President (1996 to present), Supply Chain Solutions Group Manager (2002 to present), Corporate Development Group Manager (2000 to 2002), Marketing Group Manager (1996 to 2001).
Lea N. Soupata Senior Vice President and Director	52	Senior Vice President and Human Resources Group Manager (1995 to present), Director (1998 to present).
Thomas H. Weidemeyer Senior Vice President, Chief Operating Officer, President — UPS Airlines and Director	55	Chief Operating Officer (2001 to present), Director (1998 to present), Senior Vice President (1994 to present), Engineering Group Manager (2000 to present), Corporate Compliance Officer (2001 to present), Transportation Group Manager (1997 to 2001), Labor Relations Group Manager (1997 to 2001), President — UPS Airlines (1994 to present).

Item 2. Properties

Operating Facilities

We own our headquarters, which are located in Atlanta, Georgia and consist of about 735,000 square feet of office space on an office campus, and our UPS Supply Chain Solutions group's headquarters, which are located in Alpharetta, Georgia and consist of about 310,000 square feet of office space.

We also own our 27 principal U.S. package operating facilities, which have floor spaces that range from about 310,000 to 693,000 square feet. In addition, we have a 1.9 million square foot operating facility near Chicago, Illinois, which is designed to streamline shipments between East Coast and West Coast destinations, and we own or lease about 1,500 additional smaller package operating facilities in the U.S. The smaller of these facilities have vehicles and drivers stationed for the pickup of packages and facilities for the sorting, transfer and delivery of packages. The larger of these facilities also service our vehicles and equipment and employ specialized mechanical installations for the sorting and handling of packages.

We own or lease almost 600 facilities that support our international package operations and over 750 facilities that support our non-package operations. Our non-package operations maintain facilities with about 25 million square feet of floor space.

We believe that our facilities are adequate to support our current operations.

Our aircraft are operated in a hub and spokes pattern in the U.S. Our principal air hub in the U.S. is located in Louisville, Kentucky, with regional air hubs in Columbia, South Carolina; Dallas, Texas; Hartford, Connecticut; Ontario, California; Philadelphia, Pennsylvania; and Rockford, Illinois. These hubs house facilities for the sorting, transfer and delivery of packages. Our European air hub is located in Cologne, Germany, and our Asia-Pacific air hub is located in Taipei, Taiwan. Our intra-Asia air hub is located at Clark Air Force Base in Pampanga, Philippines, and our regional air hub in Canada is located in Hamilton, Ontario.

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In September 2002, we celebrated the opening of our new WorldportSM facility at the Louisville, Kentucky air hub. This \$1 billion expansion of our global all-points air facility is the centerpiece of our global distribution network. The project more than doubles the size of the sorting complex to 4 million square feet and automates the express package sorting process with advanced, customized technology. The expansion is the largest capital project in our history and increases the hub's sorting capacity to 304,000 packages per hour — or more than 84 packages every second. The expanded capacity and automated sorting translate to greater reliability and faster transit times for customers.

Our computer operations are consolidated in a 435,000 square foot owned facility, the Ramapo Ridge facility, which is located on a 39-acre site in Mahwah, New Jersey. We also own a 175,000 square foot facility located on a 25-acre site in Alpharetta, Georgia, which serves as a backup to the main computer operations facility in New Jersey. This facility provides production functions and backup capacity in the event that a power outage or other disaster incapacitates the main data center. It also helps us to meet communication needs.

Fleet

Aircraft

The following table shows information about our aircraft fleet as of December 31, 2002:

Description	Owned and Capital Leases	Short-term Leased or Chartered From Others	On Order	Under Option
McDonnell-Douglas DC-8-71	23	—	—	—
McDonnell-Douglas DC-8-73	26	—	—	—
Boeing 727-100	51	—	—	—
Boeing 727-200	5	—	—	—
Boeing 747-100	11	—	—	—
Boeing 747-200	4	4	—	—
Boeing 757-200	75	—	—	—
Boeing 767-300	32	—	—	—
Boeing MD-11	6	—	11	18
Airbus A300-600	24	—	66	42
Other	—	322	—	—
Total	257	326	77	60

We maintain an inventory of spare engines and parts for each aircraft.

All of the aircraft we own meet Stage III federal noise regulations and can operate at airports that have aircraft noise restrictions. We became the first major airline to successfully operate a 100% Stage III fleet more than three years in advance of the date required by federal regulations.

During 2002, we took delivery of six Airbus A300-600 aircraft and three Boeing MD-11 aircraft. We have firm commitments to purchase 11 Boeing MD-11 aircraft between 2003 and 2004 and 66 Airbus A300-600 aircraft between 2003 and 2009. We expect to take delivery of four Boeing MD-11 aircraft and eight Airbus A300-600 aircraft during 2003. We also have options to purchase 18 Boeing MD-11 aircraft between 2005 and 2010 and 42 Airbus A300-600 aircraft between 2004 and 2012.

Vehicles

We operate a ground fleet of more than 88,000 vehicles, ranging from custom-built delivery vehicles to large tractors and trailers.

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Our ground support fleet consists of over 25,000 pieces of equipment designed specifically to support our aircraft fleet, ranging from non-powered container dollies and racks to powered aircraft main deck loaders and cargo tractors. We also have about 31,000 containers used to transport cargo in our aircraft.

Safety

We promote safety throughout our operations.

Our Automotive Fleet Safety Program is built with the following components:

- *Selection.* Five out of every six drivers come from our part-time ranks. Therefore, many of our new drivers are familiar with our philosophies, policies, practices and training programs.
- *Training.* Training is the cornerstone of our Fleet Safety Program. Our approach starts with training the trainer. All trainers undergo a rigorous training workshop to ensure that they have the skills and motivation to effectively train novice drivers. A new driver's employment includes five hours of classroom training and 15 hours of on-road training, followed by three safety training rides integrated into his or her training cycle.
- *Responsibility.* Our operations managers are responsible for their drivers' safety records. We investigate every accident. If we determine that an accident could have been prevented, we re-train the driver.
- *Preventive Maintenance.* An integral part of our Fleet Safety Program is a comprehensive Preventive Maintenance Program. Our fleet is tracked by computer to ensure that each vehicle is serviced before a breakdown or accident is likely to occur.
- *Honor Plan.* A well-defined safe driver honor plan recognizes and rewards our drivers when they achieve success. We have over 3,000 drivers who have driven for 25 years or more without an avoidable accident.

Our workplace safety program is built upon a comprehensive health and safety process. The foundation of this process is our employee-management health and safety committees. The workplace safety process focuses on employee conditioning and safety-related habits. Our employee co-chaired health and safety committees complete comprehensive facility audits and injury analyses, and recommend facility and work process changes.

Item 3. *Legal Proceedings*

On August 9, 1999, the United States Tax Court held that we were liable for tax on income of Overseas Partners Ltd. ("OPL"), a Bermuda company that had reinsured excess value ("EV") package insurance purchased by our customers beginning in 1984, and that we were liable for additional tax for the 1983 and 1984 tax years. The Court held that for the 1984 tax year we were liable for taxes of \$31 million on income reported by OPL, penalties and penalty interest of \$93 million, and interest for a total after-tax exposure estimated at approximately \$246 million.

The IRS took similar positions to those advanced in the Tax Court decision for tax years subsequent to 1984. Based on the Tax Court decision, we estimated that our total after-tax exposure for tax years 1984 through 1999 could have been as high as \$2.353 billion.

In our second quarter 1999 financial statements, we recorded a tax assessment charge of \$1.786 billion, which included an amount for related state tax liabilities. The charge included taxes of \$915 million and interest of \$871 million. This assessment resulted in a tax benefit of \$344 million related to the interest component of the assessment. As a result, our net charge to net income for the tax assessment was \$1.442 billion, increasing our total after-tax reserve at that time with respect to these matters to \$1.672 billion. The tax benefit of deductible interest was included in income taxes in 1999; however, since none of the income on which this tax assessment was based was our income, we did not classify the tax charge as income taxes.

We determined the size of our reserve with respect to these matters in accordance with accounting principles generally accepted in the United States of America. In 1999, we estimated our most likely liability

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based on the initial Tax Court decision. In making this determination, we concluded that, based on the Tax Court decision, it was more likely that we would be required to pay taxes on income reported by OPL and interest, but that it was not probable that we would be required to pay any penalties and penalty interest. In our prior estimation, if penalties and penalty interest ultimately were determined to be payable, we would have had to record an additional charge of up to \$681 million.

Further, as a result of the unfavorable Tax Court decision, and in order to stop the potential accrual of additional interest that might ultimately have been determined to be due to the IRS, on August 31, 1999 we paid \$1.349 billion, and on August 8, 2000 we paid an additional \$91 million, to the IRS related to these matters for the 1984 through 1994 tax years. We included the profit of the EV insurance program, using the IRS's methodology for calculating these amounts, for both 1998 and 1999 in filings we made with the IRS in 1999. In February 2000, we paid \$339 million to the IRS related to these matters for the 1995 through 1997 tax years.

On June 20, 2001, the United States Court of Appeals for the Eleventh Circuit reversed the Tax Court's decision. On September 13, 2001, the Eleventh Circuit denied the IRS's petition to have the appeal reheard en banc. The IRS did not attempt to appeal the case to the U.S. Supreme Court and, consequently, the case was remanded to the Tax Court to consider alternative arguments raised by the parties.

In January 2003, we and the IRS finalized settlement of all outstanding tax issues related to EV package insurance. Under the settlement of these issues, we agreed to adjustments that will result in income tax due of approximately \$562 million, additions to tax of \$60 million and related interest. The amount due to the IRS as a result of the settlement is less than amounts we previously had accrued (as described above). As a result, we recorded income, before taxes, of \$1.023 billion (\$776 million after tax) during the fourth quarter of 2002. The refunds and credits associated with this settlement are expected to occur over the next several years.

The EV program that was the subject of the Tax Court decision has been changed since September 1999. The revised arrangement should eliminate the issues considered by the Tax Court and the Eleventh Circuit related to OPL.

The IRS has proposed adjustments, unrelated to the EV package insurance matters discussed above, regarding the allowance of deductions and certain losses, the characterization of expenses as capital rather than ordinary, the treatment of certain income, and our entitlement to the investment tax credit and the research tax credit in the 1985 through 1990 tax years. The proposed adjustments would result in \$10 million of additional income tax expense. The IRS has also issued a report taking a similar position with respect to some of these issues for each of the years from 1991 through 1994. That report proposes adjustments that would result in \$50 million in additional income tax expense. In November 2002, the IRS issued a report taking a similar position with respect to some of these issues for each of the years 1995 through 1998. That report proposes adjustments that would result in \$13 million in additional income tax expense. For the 1985 through 1998 tax years, unpaid interest on these adjustments through December 31, 2002 could aggregate up to approximately \$381 million, after the benefit of related tax deductions. We expect that we will prevail on substantially all of these issues. Specifically, we believe that our practice of expensing the items that the IRS alleges should have been capitalized is consistent with the practices of other industry participants. The IRS may take similar positions with respect to some of these issues for each of the years 1999 through 2002. The IRS's proposed adjustments include penalties and penalty interest. We believe that the possibility that such penalties and penalty interest will be sustained is remote. We believe that the eventual resolution of these issues will not have a material adverse effect on our financial condition, results of operations or liquidity.

We are named as a defendant in 23 pending lawsuits that seek to hold us liable for the collection of premiums for EV insurance in connection with package shipments since 1984. Based on state and federal tort, contract and statutory claims, these cases generally claim that we failed to remit collected EV premiums to an independent insurer; we failed to provide promised EV insurance; we acted as an insurer without complying with state insurance laws and regulations; and the price for EV insurance was excessive.

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These actions all were filed after the August 9, 1999 Tax Court decision. As discussed above, on June 20, 2001, the U.S. Court of Appeals for the Eleventh Circuit ruled in our favor and reversed the Tax Court decision.

These 23 cases have been consolidated for pre-trial purposes in a multi-district litigation proceeding (“MDL Proceeding”) in federal court in New York. The Court has ruled on motions to dismiss, granting our motions to dismiss with respect to all of the plaintiffs’ tort claims and all of their breach of contract claims prior to August 26, 1994. Claims asserted under specific federal statutes, and breach of contract claims commencing on August 26, 1994, may proceed at this time. We intend to continue to seek dismissal of these remaining claims.

The defendants in the MDL Proceeding, including UPS, have stipulated to conditional certification of a plaintiff class in most of the lawsuits challenging the EV insurance program for our shippers. Class certification is a procedural step that allows claims to be resolved at one time as to all potential claimants; it does not depend on or reflect the merits of the underlying claims. Defendants may move later to set aside or modify the class certification.

The cases subject to the class certification stipulation will proceed to a single trial before the federal court presiding over the MDL Proceeding, instead of being returned for trial to the numerous federal courts around the country from which they were transferred. In addition, plaintiffs in the five cases with pending motions to remand to state court have withdrawn these motions.

In addition to the cases in which UPS is named as a defendant, there also is an action, *Smith v. Mail Boxes Etc.*, against Mail Boxes Etc. and its franchisees relating to UPS EV insurance purchased through Mail Boxes Etc. centers. This case also has been consolidated into the MDL Proceeding. The plaintiff has moved to have the case remanded back to state court.

We believe that the allegations in these cases have no merit and intend to continue to defend them vigorously. The ultimate resolution of these cases cannot presently be determined.

In addition, we are a defendant in various other lawsuits that arose in the normal course of business. We believe that the eventual resolution of these cases will not have a material adverse effect on our financial condition, results of operations or liquidity.

Item 4. *Submission of Matters to a Vote of Security Holders*

None

PART II

Item 5. *Market for Registrant’s Common Equity and Related Stockholder Matters*

Our class A common stock is not listed on a national securities exchange or traded in an organized over-the-counter market. Our class B common stock trades on the New York Stock Exchange under the ticker symbol “UPS”.

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The following is a summary of our Class B common stock price activity and dividend information for 2002 and 2001.

	High	Low	Close	Dividends Declared
2002:				
First Quarter	\$61.24	\$54.25	\$60.80	\$ 0.19
Second Quarter	\$63.00	\$57.75	\$61.75	\$ 0.19
Third Quarter	\$67.10	\$58.80	\$62.53	\$ 0.19
Fourth Quarter	\$64.50	\$58.50	\$63.08	\$ 0.19
2001:				
First Quarter	\$62.50	\$54.57	\$56.90	\$ 0.19
Second Quarter	\$60.00	\$52.00	\$57.80	\$ 0.19
Third Quarter	\$58.75	\$46.15	\$51.98	\$ 0.19
Fourth Quarter	\$57.15	\$49.80	\$54.50	\$ 0.19

As of February 26, 2003, there were 171,649 and 13,550 record holders of Class A and Class B stock, respectively.

The policy of our board of directors is to declare dividends each year out of current earnings. The declaration of future dividends is subject to the discretion of the board of directors in light of all relevant facts, including earnings, general business conditions and working capital requirements.

On February 13, 2003, our board declared a dividend of \$0.21 per share.

Item 6. Selected Financial Data

The following table sets forth selected financial data for each of the five years in the period ended December 31, 2002 (amounts in millions, except per share amounts). This financial data should be read together with our consolidated financial statements and the related notes, Management's Discussion and Analysis of Financial Condition and Results of Operations and other financial data appearing elsewhere in this report.

Selected Income Statement Data	Years Ended December 31,				
	2002	2001	2000	1999	1998
Revenue:					
U.S. domestic package	\$23,924	\$23,997	\$24,002	\$22,313	\$20,650
International package	4,680	4,245	4,078	3,718	3,386
Non-package	2,668	2,079	1,418	841	560
Total revenue	31,272	30,321	29,498	26,872	24,596
Operating expenses:					
Compensation and benefits	17,944	17,397	16,546	15,285	14,346
Other	9,232	8,962	8,440	7,682	7,247
Total operating expenses	27,176	26,359	24,986	22,967	21,593
Operating profit					
U.S. domestic package	3,576	3,620	3,929	3,506	2,815
International package	322	125	277	230	30
Non-package	198	217	306	169	158
Total operating profit	4,096	3,962	4,512	3,905	3,003
Other income (expense):					
Investment income	63	159	527	197	126
Interest expense	(173)	(184)	(205)	(228)	(227)
Tax assessment	1,023	—	—	(1,786)	—
Total other income (expense)	913	(25)	322	(1,817)	(101)
Income before income taxes	5,009	3,937	4,834	2,088	2,902
Income taxes	(1,755)	(1,512)	(1,900)	(1,205)	(1,161)
Cumulative effect of changes in accounting principles	(72)	(26)	—	—	—
Net income	\$ 3,182	\$ 2,399	\$ 2,934	\$ 883	\$ 1,741

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Selected Income Statement Data	Years Ended December 31,				
	2002	2001	2000	1999	1998
Per share amounts:					
Basic earnings per share	\$ 2.84	\$ 2.13	\$ 2.54	\$ 0.79	\$ 1.59
Diluted earnings per share	\$ 2.81	\$ 2.10	\$ 2.50	\$ 0.77	\$ 1.57
Dividends declared per share	\$ 0.76	\$ 0.76	\$ 0.68	\$ 0.58	\$ 0.43
Weighted Average Shares Outstanding					
Basic	1,120	1,126	1,153	1,121	1,093
Diluted	1,134	1,144	1,175	1,141	1,108
As Adjusted Net Income Data:					
Net income before impact of non-recurring items	\$2,422 ⁽¹⁾	\$2,425 ⁽²⁾	\$2,795 ⁽³⁾	\$2,325 ⁽⁴⁾	\$1,741
As a percentage of revenue	7.7%	8.8%	9.5%	8.7%	7.1%
Basic earnings per share	\$ 2.16	\$ 2.15	\$ 2.42	\$ 2.07	\$ 1.59
Diluted earnings per share	\$ 2.14	\$ 2.12	\$ 2.38	\$ 2.04	\$ 1.57
	2002	2001	As of December 31, 2000	1999	1998
Selected Balance Sheet Data					
Working capital	\$ 3,183	\$ 2,811	\$ 2,623	\$ 5,994	\$ 1,355
Long-term debt	\$ 3,495	\$ 4,648	\$ 2,981	\$ 1,912	\$ 2,191
Total assets	\$26,357	\$24,636	\$21,662	\$23,028	\$17,067
Shareowners' equity	\$12,455	\$10,248	\$ 9,735	\$12,474	\$ 7,173

- (1) Excludes (on an after-tax basis) \$121 million gain related to change in vacation policy, \$65 million restructuring charge and related expenses, \$72 million charge related to the adoption of FAS 142, and \$776 million gain related to the settlement of a previously established tax assessment liability.
- (2) Excludes \$26 million after-tax charge related to the adoption of FAS 133.
- (3) Excludes (on an after-tax basis) \$145 million in investment gains, a \$29 million gain on the sale of our UPS Truck Leasing subsidiary, and a \$35 million charge related to an arbitration ruling under our 1997 contract with the Teamsters.
- (4) Excludes a \$1.442 billion tax assessment charge.

Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations

The following discussion is intended to provide our investors with an understanding of our results of operations for the most recent years and our current financial condition. This discussion should be read together with our consolidated financial statements and the related notes that appear elsewhere in this report.

Operations

The following tables set forth information showing the change in revenue, average daily package volume and average revenue per piece, both in dollars or amounts and in percentage terms:

	Year Ended December 31,		Change	
	2002	2001	\$	%
Revenue (in millions):				
U.S. domestic package:				
Next Day Air	\$ 5,349	\$ 5,433	\$ (84)	(1.5)%
Deferred	2,868	2,893	(25)	(0.9)
Ground	15,707	15,671	36	0.2
Total U.S. domestic package	23,924	23,997	(73)	(0.3)
International package:				
Domestic	943	907	36	4.0
Export	3,276	2,931	345	11.8
Cargo	461	407	54	13.3
Total International package	4,680	4,245	435	10.2
Non-package:				
UPS Logistics Group	1,024	738	286	38.8
UPS Freight Services	945	741	204	27.5
Other	699	600	99	16.5
Total Non-package	2,668	2,079	589	28.3
Consolidated	\$31,272	\$30,321	\$ 951	3.1%
Average Daily Package Volume (in thousands):				
			#	
U.S. domestic package:				
Next Day Air	1,111	1,116	(5)	(0.4)%
Deferred	895	917	(22)	(2.4)
Ground	10,112	10,317	(205)	(2.0)
Total U.S. domestic package	12,118	12,350	(232)	(1.9)
International package:				
Domestic	779	805	(26)	(3.2)
Export	443	408	35	8.6
Total International package	1,222	1,213	9	0.7
Consolidated	13,340	13,563	(223)	(1.6)%
Operating days in period	252	252		
Average Revenue Per Piece:				
U.S. domestic package:				
			\$	
Next Day Air	\$ 19.11	\$ 19.32	\$(0.21)	(1.1)%
Deferred	12.72	12.52	0.20	1.6
Ground	6.16	6.03	0.13	2.2
Total U.S. domestic package	7.83	7.71	0.12	1.6
International package:				
Domestic	4.80	4.47	0.33	7.4
Export	29.35	28.51	0.84	2.9
Total International package	13.70	12.56	1.14	9.1
Consolidated	\$ 8.37	\$ 8.14	\$ 0.23	2.8%

Operating Profit

The following tables set forth information showing the change in operating profit, both in dollars (in millions) and in percentage terms:

Operating Segment	Year Ended December 31,		Change	
	2002	2001	\$	%
U.S. domestic package	\$3,576	\$3,620	\$ (44)	(1.2)%
International package	322	125	197	157.6
Non-package	198	217	(19)	(8.8)
Consolidated Operating Profit	\$4,096	\$3,962	\$134	3.4%

Operating Segment	Year Ended December 31,		Change	
	2001	2000	\$	%
U.S. domestic package	\$3,620	\$3,929	\$(309)	(7.9)%
International package	125	277	(152)	(54.9)
Non-package	217	306	(89)	(29.1)
Consolidated Operating Profit	\$3,962	\$4,512	\$(550)	(12.2)%

U. S. Domestic Package Operations

2002 compared to 2001

U.S. domestic package revenue decreased \$73 million, or 0.3%, for the year. This decrease was driven by a 1.9% decrease in average daily package volume, and partially offset by a 1.6% increase in revenue per piece. The decline in volume was a result of the impact of volume diversion to competitors in connection with the agreement reached on a new six-year contract with the International Brotherhood of Teamsters, combined with the continued weakness in the U.S. economy. The decline in volume was most pronounced in the period surrounding the July 31, 2002 expiration date of the existing contract.

On January 7, 2002, we increased rates for standard ground shipments an average of 3.5% for commercial deliveries. The ground residential charge increased \$0.05 to \$1.10 over the commercial ground rate, and this charge also was applied to express deliveries. The additional delivery area surcharge, which is added to ground deliveries in certain less accessible areas, remained at \$1.50, and also was applied to express deliveries. Rates for UPS Hundredweight increased 5.9%.

We also increased rates for UPS Next Day Air, UPS Next Day Air Saver, UPS 2nd Day Air, and 3 Day Select an average of 4.0%. The surcharge for UPS Next Day Air Early A.M. increased from \$27.50 to \$28.50. Rates for international shipments originating in the U.S. (UPS Worldwide Express, UPS Worldwide Express Plus, UPS Worldwide Expedited and UPS Standard service) increased an average of 3.9%. Rate changes for shipments originating outside the U.S. were made throughout the year and varied by geographic market.

An index-based fuel surcharge continued during 2002. The index-based surcharge, which resets on a monthly basis, replaced a fixed fuel surcharge of 1.25%, which was originally implemented prior to 2001. The current surcharge is based on the National U.S. Average On-Highway Diesel Fuel Prices as reported by the U.S. Department of Energy. Based on published rates, the average fuel surcharge for the year ended December 31, 2002 was 0.78%. Approximately \$251 million in revenue was recorded in 2002 as a result of our fuel surcharge, a decrease of \$97 million from the prior year.

U.S. domestic package operating profit decreased \$44 million, or 1.2%, for the year ended December 31, 2002. Operating profit was affected by a non-recurring benefit to operating expense of \$175 million that occurred in 2002 related to a change in our vacation policy for non-union employees. Excluding this item, U.S. domestic package operating profit decreased \$219 million, or 6.0% for the year, due to the decrease in average daily volume discussed previously and an increase in operating expenses (discussed further below). In 2001,

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we recorded a credit to expense related to the Air Transportation Safety and System Stabilization Act, which benefited the U.S. domestic package segment by \$28 million.

2001 compared to 2000

U.S. domestic package revenue was flat in 2001 compared to 2000, primarily as a result of a 1.0% decrease in average daily package volume, offset by a 1.7% increase in average revenue per piece. The decrease in volume resulted from the declining U.S. economy during 2001. For the first quarter of 2001, average daily domestic volume was up 1.3%. However, average daily domestic volume was down 0.9% during the second quarter, down 3.4% during the third quarter, and down 0.8% during the fourth quarter. The third quarter decline was largely a result of the events of September 11. Also affecting the comparison were two extra operating days in 2000 compared to 2001.

During the first quarter of 2001, we increased rates for standard ground shipments an average of 3.1% for commercial deliveries. The ground residential charge increased \$0.05 to \$1.05 over the commercial ground rate, and we increased rates for UPS Next Day Air, UPS Next Day Air Saver, UPS 2nd Day Air, and 3 Day Select an average of 3.7%. The surcharge for UPS Next Day Air Early A.M. increased from \$25.00 to \$27.50. Rates for international shipments originating in the U.S. (UPS Worldwide Express, UPS Worldwide Express Plus, UPS Worldwide Expedited and UPS Standard service) increased by 2.9%. Rate changes for shipments originating outside the U.S. were made throughout 2001 and varied by geographic market. In addition, all package rates during 2001, until December 10th, included a 1.25% fuel surcharge. Effective December 10, 2001, we implemented an index-based surcharge, which initially reduced the surcharge rate to 0.75% and resets on a monthly basis. Approximately \$348 million in revenue was recorded in 2001 as a result of our fuel surcharge, an increase of \$218 million over the prior year.

U.S. domestic package operating profit decreased by \$309 million due primarily to the decline in volume discussed previously. This decrease was mitigated by cost control initiatives implemented during the year. These initiatives focused on many of our semi-variable costs and included curtailing non-union hiring, eliminating new consulting projects, reevaluating all capital expenditures and information technology projects in process, plus a variety of other items.

International Package Operations

2002 compared to 2001

For the year ended December 31, 2002, international package revenue improved \$435 million, or 10.2% (8.1% currency-adjusted), due primarily to volume growth for our export products and strong revenue per piece improvements. This volume growth was driven primarily by the Europe region, which had an increase in average daily export volume of 13.6%, and the Asia-Pacific region, which had an increase in average daily export volume of 17.1%. In total, international package average daily volume increased 0.7% and average revenue per piece increased 9.1% (6.8% currency-adjusted).

The improvement in operating profit for our international package operations was \$197 million for the year. In 2002, operating profit benefited from an \$11 million reduction to expense related to the change in vacation policy. Excluding the effect of this item, operating profit increased by \$186 million, or 148.8% for the year, \$22 million of which was due to currency fluctuations. The increase in operating profit was primarily due to export volume growth of 8.6% and a strong increase in revenue per piece. In addition, the shutdown of the U.S. West Coast ports during the latter part of 2002 had a beneficial impact on our international package results. In 2002, this segment benefited by \$11 million from the elimination of goodwill amortization. In 2001, operating profit benefited from a \$46 million credit to expense related to the Air Transportation Safety and System Stabilization Act.

2001 compared to 2000

The increase in international package revenue in 2001 was due primarily to an increase in cargo revenue and a 10.9% volume growth for our export products, offset by a decline in the revenue per piece for these

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products. The increase in cargo revenue resulted primarily from increased volume, which was driven by the integration of our Challenge Air operations in Latin America. Our Europe region was a significant contributor to the export volume increase. Excluding the impact of currency fluctuations, average revenue per piece increased 1.7%. Overall average daily package volume increased over 5% for international operations.

The decline in the operating profit of our international package operations during 2001 resulted primarily from increased expenses, particularly those expenses associated with aircraft used in this segment (maintenance, rental and fuel) as we continued to add airlift capabilities to further expand our international presence. We recorded \$11 million of goodwill amortization in our international package segment in both 2001 and 2000.

Non-Package Operations

2002 compared to 2001

Non-package revenue increased \$589 million, or 28.3%, during 2002. 20.4% of this revenue growth was due to acquisitions and the remaining 7.9% was organic.

UPS Logistics Group revenue was up \$286 million or 38.8% for the year, of which approximately half was due to acquisitions. UPS Freight Services revenue grew \$204 million, or 27.5%, primarily due to having a full year of revenue from Fritz Companies Inc., which we acquired in May 2001. Revenue growth at UPS Freight Services was hindered by the sale of the FedEx brokerage business in March 2002. Adjusting for the effect of this sale, Freight Services would have reported organic revenue growth of approximately 4% during 2002.

Non-package operating profit decreased by \$19 million, or 8.8%, for the year. Operating profit was affected by a restructuring charge and related expenses of \$106 million primarily related to the integration of our Freight Services and Logistics Group operations, and an \$11 million reduction to expense related to a change in our vacation policy. Excluding the impact of these items, non-package operating profit increased by \$76 million, or 35.0%. In 2002, this segment benefited from a \$61 million reduction in goodwill expense as a result of the elimination of goodwill amortization. Non-package operating profit includes \$112 million (compared to \$113 million in 2001) of intersegment profit, with a corresponding amount of operating expense, which reduces operating profit, in the U.S. domestic package segment.

2001 compared to 2000

The increase in non-package revenue in 2001 resulted primarily from the impact of acquisitions, particularly Fritz, which was included in our Freight Services unit. Non-package revenue also increased due to the continued growth of the UPS Logistics Group. The Logistics Group revenue increase was primarily due to increases in our supply chain management and service parts logistics offerings. Other non-package revenue also increased as a result of acquisitions (First International Bancorp and Mail Boxes Etc.), offset by a decrease in third-party air operations revenue due to the discontinuation of our charter passenger services.

The decrease in non-package operating profit was partially due to the \$49 million gain we recognized from the sale of our UPS Truck Leasing subsidiary in the first quarter of 2000. The remaining decrease was due to start-up, integration and operating costs for several subsidiaries that we were developing or acquired, along with goodwill amortization expense associated with acquisitions. During 2001, we recorded \$61 million of goodwill amortization in our non-package segment, which was an increase of \$33 million over 2000. Non-package operating profit included \$113 million (compared to \$101 million in 2000) of intersegment profit.

Operating Expenses and Operating Margin

2002 compared to 2001

Consolidated operating expenses increased by \$817 million, or 3.1%, for the year ended December 31, 2002. In 2002, operating expenses were affected by the \$106 million restructuring charge and related expenses in our non-package segment, and the \$197 million credit to expense related to the change in our vacation policy. Excluding the effect of these items, operating expenses increased by \$908 million, or 3.4%, for the year.

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Excluding the \$197 million credit to expense related to the change in vacation policy, compensation and benefits increased by \$744 million, or 4.3%, for the year, primarily due to increased costs associated with health and retirement benefits. Other operating expenses increased by \$164 million, or 1.8%, excluding the \$106 million restructuring charge and related expenses.

The non-package segment accounted for \$513 million of the \$908 million total increase in operating expenses. This was principally due to acquisitions that we completed during the first nine months of 2001. In 2002, operating expenses benefited from the absence of \$72 million of expense related to the elimination of goodwill amortization. In 2001, other operating expenses were reduced by \$74 million for compensation under the Air Transportation Safety and System Stabilization Act.

Adjusting for the effects of the restructuring charge and related expenses and vacation policy change, our operating margin, defined as operating profit as a percentage of revenue, decreased from 13.1% during 2001 to 12.8% during 2002. This decline is primarily due to a 90 basis point decline in the operating margin for our U.S. domestic package segment, which experienced a volume-driven decline in profit.

2001 compared to 2000

In 2001, operating expenses increased by \$1.373 billion, or 5.5%, with compensation and benefits up \$851 million and other operating expenses up \$522 million. The 5.1% increase in compensation and benefits included a \$101 million reduction in pension benefits expense. Depreciation and amortization and other occupancy expenses (primarily rent and utilities) accounted for over one-half of the 6.2% increase in other operating expenses. Much of the increase in operating expenses was related to expanding our capabilities and service offerings for our non-package segment. Excluding the non-package segment, operating expenses increased by 2.5% over 2000. Depreciation and amortization expense included \$72 million of goodwill amortization, a \$33 million increase from 2000.

Our adjusted operating margin declined from 15.3% for 2000 to 13.1% for 2001. This decline continued the trend that began in the fourth quarter of 2000 as the economy began to weaken.

Investment Income/Interest Expense

2002 compared to 2001

The decrease in investment income of \$96 million for 2002 is primarily due to a combination of lower interest rates and lower balances available for investment.

2001 compared to 2000

The decrease in investment income of \$368 million for 2001 is due to two factors relating to 2000. First, in the first quarter of 2000, we recognized a \$241 million gain on investments held by our Strategic Enterprise Fund in two companies that were acquired by other companies. In addition, we earned income on the \$5.3 billion in net IPO proceeds available for investment prior to the tender offer that occurred in early March 2000, and the \$1.2 billion in IPO proceeds that were not utilized for the tender offer.

Net Income and Earnings Per Share

2002 compared to 2001

Net income for 2002 was \$3.182 billion, an increase of \$783 million from \$2.399 billion in 2001, resulting in an increase in diluted earnings per share to \$2.81 in 2002 from \$2.10 in 2001. Adjusting for the non-recurring FAS 133 cumulative expense adjustment, net of tax, of \$26 million, our net income in 2001 would have been \$2.425 billion, or \$2.12 per diluted share. In 2002, our results were affected by the fourth quarter restructuring charge and related expenses of \$106 million, the non-recurring FAS 142 cumulative expense adjustment of \$72 million, the credit to compensation and benefits resulting from the change in our vacation policy for non-union employees of \$197 million, and the credit related to the reversal of a portion of the previously established tax assessment liability of \$1.023 billion. Excluding the impact of these non-recurring items, our 2002 net income would have been \$2.422 billion, or \$2.14 per diluted share (compared to \$2.12 in 2001).

2001 compared to 2000

Net income for 2001 amounted to \$2.399 billion, or \$2.10 per diluted share, compared to \$2.934 billion, or \$2.50 per diluted share, for 2000. Our 2000 results reflected certain non-recurring items, which include the gains on our Strategic Enterprise Fund investments and the sale of our Truck Leasing subsidiary, offset partially by a charge for retroactive costs associated with creating new full-time jobs from existing part-time Teamster jobs. Our 2001 results reflect a FAS 133 cumulative expense adjustment, net of tax, of \$26 million. Excluding these non-recurring transactions for each of these periods, adjusted net income for 2001 would have been \$2.425 billion, a decrease of \$370 million from adjusted net income of \$2.795 billion for 2000. Adjusted diluted earnings per share decreased from \$2.38 in 2000 to \$2.12 in 2001.

Liquidity and Capital Resources

Our primary source of liquidity is our cash flow from operations. We maintain significant cash, cash equivalents, marketable securities and short-term investments, amounting to \$3.014 billion at December 31, 2002.

As part of our continuing share repurchase program, \$1.0 billion was authorized for share repurchases in February 2002, of which \$705 million was still available as of December 31, 2002.

We maintain two commercial paper programs under which we are authorized to borrow up to \$7.0 billion. Approximately \$1.036 billion was outstanding under these programs as of December 31, 2002, all of which was classified as a current liability. The average interest rate on the amount outstanding at December 31, 2002 was 1.3%. In addition, we maintain an extendible commercial notes program under which we are authorized to borrow up to \$500 million. No amounts were outstanding under this program at December 31, 2002.

We maintain two credit agreements with a consortium of banks that provide revolving credit facilities of \$1.25 billion each, with one expiring on April 24, 2003 and the other expiring on April 27, 2005. Interest on any amounts we borrow under these facilities would be charged at 90-day LIBOR plus 15 basis points. There were no borrowings under either of these agreements as of December 31, 2002.

We also maintain a \$1.0 billion European medium-term note program. Under this program, we may issue notes from time to time, denominated in a variety of currencies. At December 31, 2002, \$1.0 billion was available under this program.

We have a \$2.0 billion shelf registration statement under which we may issue debt securities in the U.S. There was approximately \$1.552 billion issued under this shelf registration statement at December 31, 2002. As of December 31, 2002, \$910 million in notes have been issued under the UPS Notes program. These notes have various terms and maturities, all with fixed interest rates. The notes are callable at various stated times after issuance, and \$345 million of the notes have been called since the inception of the program. As of December 31, 2002, \$565 million in UPS Notes were outstanding.

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On August 9, 1999, the United States Tax Court held that we were liable for tax on income of Overseas Partners Ltd. (“OPL”), a Bermuda company that had reinsured excess value (“EV”) package insurance purchased by our customers beginning in 1984, and that we were liable for additional tax for the 1983 and 1984 tax years. The Court held that for the 1984 tax year we were liable for taxes of \$31 million on income reported by OPL, penalties and penalty interest of \$93 million, and interest for a total after-tax exposure estimated at approximately \$246 million.

The IRS took similar positions to those advanced in the Tax Court decision for tax years subsequent to 1984. Based on the Tax Court decision, we estimated that our total after-tax exposure for tax years 1984 through 1999 could have been as high as \$2.353 billion.

In our second quarter 1999 financial statements, we recorded a tax assessment charge of \$1.786 billion, which included an amount for related state tax liabilities. The charge included taxes of \$915 million and interest of \$871 million. This assessment resulted in a tax benefit of \$344 million related to the interest component of the assessment. As a result, our net charge to net income for the tax assessment was \$1.442 billion, increasing our total after-tax reserve at that time with respect to these matters to \$1.672 billion. The tax benefit of deductible interest was included in income taxes in 1999; however, since none of the income on which this tax assessment was based was our income, we did not classify the tax charge as income taxes.

We determined the size of our reserve with respect to these matters in accordance with accounting principles generally accepted in the United States of America. In 1999, we estimated our most likely liability based on the initial Tax Court decision. In making this determination, we concluded that, based on the Tax Court decision, it was more likely that we would be required to pay taxes on income reported by OPL and interest, but that it was not probable that we would be required to pay any penalties and penalty interest. In our prior estimation, if penalties and penalty interest ultimately were determined to be payable, we would have had to record an additional charge of up to \$681 million.

Further, as a result of the unfavorable Tax Court decision, and in order to stop the potential accrual of additional interest that might ultimately have been determined to be due to the IRS, on August 31, 1999 we paid \$1.349 billion, and on August 8, 2000 paid an additional \$91 million, to the IRS related to these matters for the 1984 through 1994 tax years. We included the profit of the EV insurance program, using the IRS’s methodology for calculating these amounts, for both 1998 and 1999 in filings we made with the IRS in 1999. In February 2000, we paid \$339 million to the IRS related to these matters for the 1995 through 1997 tax years.

On June 20, 2001, the United States Court of Appeals for the Eleventh Circuit reversed the Tax Court’s decision. On September 13, 2001, the Eleventh Circuit denied the IRS’s petition to have the appeal reheard en banc. The IRS did not appeal the case to the U.S. Supreme Court and, consequently, the case was remanded to the Tax Court to consider alternative arguments raised by the parties.

In January 2003, we and the IRS finalized settlement of all outstanding tax issues related to EV package insurance. Under the settlement of these issues, we agreed to adjustments that will result in income tax due of approximately \$562 million, additions to tax of \$60 million and related interest. The amount due to the IRS as a result of the settlement is less than amounts we previously had accrued (as described above). As a result of the settlement, we recorded income, before taxes, of \$1.023 billion (\$776 million after tax) during the fourth quarter of 2002. The refunds and credits associated with this settlement are expected to occur over the next several years.

The EV program that was the subject of the Tax Court decision has been changed since September 1999. The revised arrangement should eliminate the issues considered by the Tax Court and the Eleventh Circuit related to OPL.

The IRS has proposed adjustments, unrelated to the EV package insurance matters discussed above, regarding the allowance of deductions and certain losses, the characterization of expenses as capital rather than ordinary, the treatment of certain income, and our entitlement to the investment tax credit and the research tax credit in the 1985 through 1990 tax years. The proposed adjustments would result in \$10 million of additional income tax expense. The IRS has also issued a report taking a similar position with respect to

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some of these issues for each of the years from 1991 through 1994. That report proposes adjustments that would result in \$50 million in additional income tax expense. In November 2002, the IRS issued a report taking a similar position with respect to some of these issues for each of the years from 1995 through 1998. That report proposes adjustments that would result in \$13 million in additional income tax expense. For the 1985 through 1998 tax years, unpaid interest on these adjustments through December 31, 2002 could aggregate up to approximately \$381 million, after the benefit of related tax deductions. We expect that we will prevail on substantially all of these issues. Specifically, we believe that our practice of expensing the items that the IRS alleges should have been capitalized is consistent with the practices of other industry participants. The IRS may take similar positions with respect to some of these issues for each of the years 1999 through 2002. The IRS's proposed adjustments include penalties and penalty interest. We believe that the possibility that such penalties and penalty interest will be sustained is remote. We believe that the eventual resolution of these issues will not have a material adverse effect on our financial condition, results of operations or liquidity.

We are named as a defendant in 23 pending lawsuits that seek to hold us liable for the collection of premiums for EV insurance in connection with package shipments since 1984. Based on state and federal tort, contract and statutory claims, these cases generally claim that we failed to remit collected EV premiums to an independent insurer; we failed to provide promised EV insurance; we acted as an insurer without complying with state insurance laws and regulations; and the price for EV insurance was excessive.

These actions were filed after the August 9, 1999 Tax Court decision. As discussed above, on June 20, 2001, the U.S. Court of Appeals for the Eleventh Circuit ruled in our favor and reversed the Tax Court decision.

These 23 cases have been consolidated for pre-trial purposes in a multi-district litigation proceeding ("MDL Proceeding") in federal court in New York. The Court has ruled on the motions to dismiss, granting our motions with respect to all of the plaintiffs' tort claims and all of their breach of contract claims prior to August 26, 1994. Claims asserted under specific federal statutes, and breach of contract claims commencing on August 26, 1994, may proceed at this time. We intend to continue to seek dismissal of these remaining claims.

The defendants in the MDL Proceeding, including UPS, have stipulated to conditional certification of a plaintiff class in most of the lawsuits challenging the EV insurance program for our shippers. Class certification is a procedural step that allows claims to be resolved at one time as to all potential claimants; it does not depend on or reflect the merits of the underlying claims. Defendants may move later to set aside or modify the class certification.

The cases subject to the class certification stipulation will proceed to a single trial before the federal court presiding over the MDL Proceeding, instead of being returned for trial to the numerous federal courts around the country from which they were transferred. In addition, plaintiffs in the five cases with pending motions to remand to state court have withdrawn these motions.

In addition to the cases in which UPS is named as a defendant, there also is an action, *Smith v. Mail Boxes Etc.*, against Mail Boxes Etc. and its franchisees relating to UPS EV insurance purchased through Mail Boxes Etc. centers. This case also has been consolidated into the MDL Proceeding. The plaintiff has moved to have the case remanded back to state court.

We believe that the allegations in these cases have no merit and intend to continue to defend them vigorously. The ultimate resolution of these cases cannot presently be determined.

In addition, we are a defendant in various other lawsuits that arose in the normal course of business. We believe that the eventual resolution of these cases will not have a material adverse effect on our financial condition, results of operations or liquidity.

Due to the events of September 11, 2001, increased security requirements for air carriers may be forthcoming; however, we do not anticipate that such measures will have a material adverse effect on our financial condition, results of operations or liquidity. In addition, our insurance premiums have risen and we have taken several actions, including self-insuring certain risks, to mitigate the expense increase.

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As of December 31, 2002, we had approximately 230,000 employees (64% of our total employees) employed under a national master agreement and various supplemental agreements with local unions affiliated with the Teamsters. On October 7, 2002, the Teamsters ratified a new master agreement with UPS that runs through July 31, 2008. The new agreement is retroactive to August 1, 2002. The majority of our pilots are employed under a collective bargaining agreement with the Independent Pilots Association, which becomes amendable January 1, 2004. Our airline mechanics are covered by a collective bargaining agreement with Teamsters Local 2727, which becomes amendable on November 1, 2006. In addition, the majority 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. These agreements run through July 31, 2009.

In November 2002, we announced rate increases, which took effect on January 6, 2003, that are in line with previous rate increases. We increased rates for standard ground shipments an average of 3.9% for commercial deliveries. The ground residential surcharge increased \$0.05 to \$1.15 over the commercial ground rate. The additional delivery area surcharge added to residential deliveries in certain less accessible areas increased \$0.25 to \$1.75. Rates for UPS Hundredweight increased 5.9%. In addition, we increased rates for UPS Next Day Air an average of 3.4% and increased rates for deferred services by 4.5%. Rates for international shipments originating in the U.S. (UPS Worldwide Express, UPS Worldwide Express Plus, UPS Worldwide Expedited and UPS International Standard service) increased an average of 3.9%. Rate changes for shipments originating outside the U.S. generally are made throughout the year and vary by geographic market. The index-based fuel surcharge remains in effect, and currently is 1.50%.

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, through 2009.

Following is a summary of capital expenditures (in millions):

	2002	2001	2000
Buildings and facilities	\$ 528	\$ 763	\$ 947
Aircraft and parts	638	932	645
Vehicles	41	303	156
Information technology	451	374	399
	<u>\$1,658</u>	<u>\$2,372</u>	<u>\$2,147</u>

We anticipate capital expenditures of approximately \$2.0 billion in 2003. These expenditures will provide for replacement of existing capacity and anticipated future growth and include the projected cost of capitalized software.

A discussion of our anticipated future payments under operating leases, capital leases, debt obligations, and purchase commitments is provided in Note 8 to the consolidated financial statements. A discussion of our unfunded lending commitments is provided in Note 3 to the consolidated financial statements.

Market Risk

We are exposed to market risk from changes in certain commodity prices, foreign currency exchange rates, interest rates, and equity prices. All of these market risks arise 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 following analysis provides quantitative information regarding our exposure to commodity price risk, foreign currency exchange risk, interest rate risk, and equity price risk. We utilize valuation models to evaluate the sensitivity of the fair value of financial instruments with exposure to market risk that assume instantaneous, parallel shifts in exchange rates, interest rate yield curves, and commodity and equity prices. For options and instruments with non-linear returns, models appropriate to the instrument are utilized to

determine the impact of market shifts. There are certain limitations inherent in the sensitivity analyses presented, primarily due to the assumption that exchange rates change in a parallel fashion and that interest rates change instantaneously. In addition, the analyses are unable to reflect the complex market reactions that normally would arise from the market shifts modeled.

A discussion of our accounting policies for derivative instruments and further disclosures are provided in Note 16 to the consolidated financial statements.

Commodity Price Risk

We are exposed to an increase in the prices of refined fuels, principally jet-A, diesel, and unleaded gasoline, which are used in the transportation of packages. Additionally, we are exposed to an increase in the prices of other energy products, primarily natural gas and electricity, used in our operating facilities throughout the world. We use a combination of options, swaps, and futures contracts to provide some protection from rising fuel and energy prices. These derivative instruments generally cover forecasted fuel and energy consumption for periods up to one year. The net fair value of such contracts subject to price risk, excluding the underlying exposures, as of December 31, 2002 and 2001 was an asset (liability) of \$34 and \$(27) million, respectively. The potential loss in the fair value of these derivative contracts, assuming a hypothetical 10% change in the underlying commodity price, would be approximately \$38 million at December 31, 2002. This amount excludes the offsetting impact of the price risk inherent in the physical purchase of the underlying commodities.

Foreign Currency Exchange Risk

We have foreign currency risks related to our revenue, operating expenses, and financing transactions in currencies other than the local currencies in which we operate. We are exposed to currency risk from the potential changes in functional currency values of our foreign currency-denominated assets, liabilities, and cash flows. Our most significant foreign currency exposures relate to the Euro and the British Pound Sterling. We use a combination of purchased and written options and forward contracts to hedge cash flow currency exposures. As of December 31, 2002 and 2001, the net fair value of the hedging instruments described above was an asset (liability) of approximately \$(3) and \$4 million, respectively. The potential loss in fair value for such instruments from a hypothetical 10% adverse change in quoted foreign currency exchange rates would be approximately \$42 million at December 31, 2002. This sensitivity analysis assumes a parallel shift in the foreign currency exchange rates. Exchange rates rarely move in the same direction. The assumption that exchange rates change in a parallel fashion may overstate the impact of changing exchange rates on assets and liabilities denominated in a foreign currency.

Interest Rate Risk

As described in Note 8 to the consolidated financial statements, we have various debt instruments, including debt associated with capital leases, that are issued at fixed rates of interest. Such financial instruments are exposed to fluctuations in fair value resulting from changes in market interest rates. The fair value of our total long-term debt, including current maturities, at December 31, 2002 and 2001 was \$4.926 and \$5.338 billion, respectively. The potential decrease in fair value resulting from a hypothetical 100 basis point increase in interest rates would be approximately \$264 million at December 31, 2002.

We use a combination of derivative instruments, including interest rate swaps and cross-currency interest rate swaps, as part of our program to manage the fixed and floating interest rate mix of our total debt portfolio and related overall cost of borrowing. These swaps are entered into concurrently with the issuance of the debt that they are intended to modify, and the notional amount, interest payment, and maturity dates of the swaps match the terms of the associated debt. Interest rate swaps allow us to maintain a target range of floating rate debt. The net fair value of our interest rate swaps at December 31, 2002 and 2001 was an asset (liability) of \$(62) and \$(74) million, respectively. The potential decrease in fair value resulting from a hypothetical 100 basis point increase in interest rates would be approximately \$37 million at December 31, 2002.

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As described in Note 2 to the consolidated financial statements, we have certain investments in securities that are purchased at fixed rates of interest. At December 31, 2002 and 2001, the fair value of our investments in debt securities was \$481 and \$691 million, respectively. The potential decrease in fair value resulting from a hypothetical 100 basis point increase in interest rates would be approximately \$7 million at December 31, 2002.

Additionally, as described in Note 3 to the consolidated financial statements, we hold certain finance receivables, primarily commercial loans and finance leases, at fixed rates of interest. These assets are exposed to fluctuations in fair value resulting from changes in market interest rates. At December 31, 2002 and 2001, the fair value of our investments in finance receivables was \$1.492 billion and \$982 million, respectively. The potential decrease in fair value resulting from a hypothetical 100 basis point increase in interest rates would be approximately \$5 million at December 31, 2002.

Equity Price Risk

We hold investments in various equity securities that are subject to price risk, and for certain of these securities, we utilize options to hedge this price risk. At December 31, 2002 and 2001, the fair value of such investments was \$322 and \$382 million, respectively. The potential loss in the fair value of such investments, assuming a 10% decline in equity prices net of the offsetting impact of any hedges, would be approximately \$10 million.

Credit Risk

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 large banks and financial institutions that meet established credit guidelines. We do not expect to incur any losses as a result of counterparty default.

Future Accounting Changes

In June 2002, the FASB issued Statement No. 146 "Accounting for Costs Associated with Exit or Disposal Activities" ("FAS 146"). FAS 146 provides guidance on the recognition and measurement of liabilities associated with exit or disposal activities and requires that such liabilities be recognized when incurred. This statement is effective for exit or disposal activities initiated on or after January 1, 2003.

As discussed in Note 17, we implemented a restructuring program involving the integration of our Freight Services and Logistics Group operations in the fourth quarter of 2002. As this restructuring program was initiated in 2002, we accounted for this restructuring program using the existing guidance in EITF 94-3 "Liability Recognition for Certain Employee Termination Benefits and Other Costs to Exit an Activity (Including Certain Costs Incurred in a Restructuring)". Therefore, the adoption of FAS 146 on January 1, 2003 had no effect on our results of operations or financial condition. In the fourth quarter of 2002, we recorded a pre-tax restructuring charge and related expenses in the amount of \$106 million, which is classified in other operating expenses.

In 2003, we plan to adopt the fair value measurement provisions of FASB Statement No. 123, "Accounting for Stock-Based Compensation" ("FAS 123"), which is considered the preferable accounting method for stock-based employee compensation. Under FAS 148, "Accounting for Stock-Based Compensation — Transition and Disclosure", we have elected to adopt the measurement provisions of FAS 123 using the prospective method. Under this approach, all future employee stock option grants and other stock-based compensation will be expensed to compensation and benefits over the vesting period based on the fair value at the date the stock-based compensation is granted. We will continue to provide pro forma income and earnings per share information related to prior awards. The expensing of stock-based compensation is expected to reduce diluted earnings per share by approximately \$0.02 in 2003. By 2006, we expect to realize the full impact of adopting FAS 123, and estimate that diluted earnings per share will be reduced by approximately \$0.08 in that year.

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In November 2002, the FASB issued Interpretation No. 45 “Guarantor’s Accounting and Disclosure Requirements for Guarantees, Including Indirect Guarantees of Indebtedness of Others” (“FIN 45”). FIN 45 requires that a liability be recognized at fair value at the inception of certain guarantees for the obligations undertaken by the guarantor. FIN 45 also requires additional disclosures for certain guarantee contracts. The disclosure provisions of FIN 45 are effective for financial statements ending after December 15, 2002, while the recognition and initial measurement provisions are applicable on a prospective basis to guarantees issued or modified after December 31, 2002. We are currently evaluating the impact of the recognition and measurement provisions of FIN 45 on our financial statements.

In January 2003, the FASB issued Interpretation No. 46 “Consolidation of Variable Interest Entities” (“FIN 46”). FIN 46 provides guidance on the identification of variable interest entities, and the assessment of a company’s interests in a variable interest entity to determine whether consolidation is appropriate. FIN 46 requires the consolidation of a variable interest entity by the primary beneficiary if the entity does not effectively disperse risks among the parties involved. FIN 46 applies immediately to variable interest entities created after January 31, 2003, and is effective for periods beginning after June 15, 2003 for existing variable interest entities. As we have no material exposures to special purpose entities or other off-balance sheet arrangements, we anticipate that the effects of adopting FIN 46 will not be material to our results of operations or financial condition.

Critical Accounting Policies and Estimates

Our discussion and analysis of our financial condition and results of operations are based on our consolidated financial statements, which are prepared in accordance with accounting principles generally accepted in the United States of America. As indicated in Note 1 to our consolidated financial statements, the amounts of assets, liabilities, revenue and expenses reported in our financial statements are affected by estimates and judgments that are necessary to comply with generally accepted accounting principles. We base our estimates on prior experience and other assumptions that we consider reasonable to our circumstances. Actual results could differ from our estimates, which would affect the related amounts reported in our financial statements. While estimates and judgments are applied in arriving at many reported amounts, we believe that the following matters may involve a higher degree of judgment and complexity.

Contingencies

As discussed in Note 10 to our consolidated financial statements, we are involved in various legal proceedings and contingencies. We have recorded liabilities for these matters in accordance with Statement of Financial Accounting Standards No. 5, “Accounting for Contingencies” (“FAS 5”). FAS 5 requires a liability to be recorded based on our estimate of the probable cost of the resolution of a contingency. The actual resolution of these contingencies may differ from our estimates. If a contingency is settled for an amount greater than our estimate, a future charge to income would result. Likewise, if a contingency is settled for an amount that is less than our estimate, a future credit to income would result.

Goodwill Impairment

The Financial Accounting Standards Board issued Statement No. 142, “Goodwill and Other Intangible Assets,” (“FAS 142”) in June 2001. As a result of the issuance of this new standard, goodwill is no longer amortized, but is subjected to annual impairment testing. Goodwill impairment testing requires that we estimate the fair value of our goodwill and compare that estimate to the amount of goodwill recorded on our balance sheet. The estimation of fair value requires that we make judgments concerning future cash flows and appropriate discount rates. Our estimate of the fair value of goodwill could change over time based on a variety of factors, including the actual operating performance of the underlying reporting units. Upon adoption of FAS 142, we recorded a non-cash impairment charge of \$72 million (\$0.06 per diluted share), as of January 1, 2002, related to our Mail Technologies business. The primary factor resulting in the impairment charge was the lower than anticipated growth experienced in the expedited mail delivery business. As of December 31, 2002, our recorded goodwill was \$1.070 billion.

Self-Insurance Accruals

We self-insure estimated costs associated with workers' compensation claims, automotive liability, and general business liabilities, up to certain limits. Insurance reserves are established for estimates of the loss that we will ultimately incur on reported claims, as well as estimates of claims that have been incurred but not yet reported. The recorded levels of these reserves are determined by outside actuaries, who incorporate historical loss experience and judgments about the present and expected levels of cost per claim. Trends in actual experience are a significant factor in the determination of such reserves. We believe our estimated reserves for such claims are adequate, however actual experience in claim frequency and/or severity could materially differ from our estimates and affect our results of operations.

Pension and Postretirement Medical Benefits

The Company's pension and other postretirement benefit costs are calculated using various actuarial assumptions and methodologies as prescribed by Statement of Financial Accounting Standards No. 87, "Employers' Accounting for Pensions" and Statement of Financial Accounting Standards No. 106, "Employers' Accounting for Postretirement Benefits Other than Pensions." These assumptions include discount rates, health care cost trend rates, inflation, rate of compensation increases, expected return on plan assets, mortality rates, and other factors. Actual results that differ from our assumptions are accumulated and amortized over future periods and, therefore, generally affect our recognized expense and recorded obligation in such future periods. We believe that the assumptions utilized in recording the obligations under our plans are reasonable based on input from our outside actuaries and information as to historical experience and performance. Differences in actual experience or changes in assumptions may affect our pension and other postretirement obligations and future expense. The impact of decreasing the expected long-term rate of return on plan assets to 9.21% and the decrease in the discount rate to 6.75%, combined with other factors, will increase our pension plan expense by approximately \$135 million in 2003.

Financial Instruments

As discussed in Notes 2, 3, 8, and 16 to our consolidated financial statements, and in the "Market Risk" section of this report, we hold and issue financial instruments that contain elements of market risk. Certain of these financial instruments are required to be recorded at fair value. Fair values are based on listed market prices, when such prices are available. To the extent that listed market prices are not available, fair value is determined based on other relevant factors, including dealer price quotations. Certain financial instruments, including over-the-counter derivative instruments, are valued using pricing models that consider, among other factors, contractual and market prices, correlations, time value, credit spreads and yield curve volatility factors. Changes in the fixed income, equity, foreign exchange and commodity markets will impact our estimates of fair value in the future, potentially affecting our results of operations.

Forward-Looking Statements

"Management's Discussion and Analysis of Financial Condition and Results of Operations," "Liquidity and Capital Resources" and other parts of this report contain "forward-looking" statements about matters that inherently are difficult to predict. These statements include statements regarding our intent, belief and current expectations about our strategic direction, prospects and future results. We have described some of the important factors that affect these statements as we discussed each subject. Forward-looking statements involve risks and uncertainties, and certain factors may cause actual results to differ materially from those contained in the forward-looking statements.

Risk Factors

The following are some of the factors that could cause our actual results to differ materially from the expected results described in our forward-looking statements:

- The effect of general economic and other conditions in the markets in which we operate, both in the United States and internationally. Our operations in international markets also are affected by currency exchange and inflation risks.

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- Strikes, work stoppages and slowdowns by our employees. Such actions may affect our ability to meet our customers' needs, and customers may do more business with our competitors if they believe that such actions may adversely affect our ability to provide service. We may face permanent loss of customers if we are unable to provide uninterrupted service. The terms of future collective bargaining agreements also may affect our competitive position and results of operations.
- The impact of complex and stringent aviation, transportation, environmental, labor, employment and other governmental laws and regulations, and the impact of new laws and regulations that may result from increased security concerns following the events of September 11, 2001. Our failure to comply with applicable laws, ordinances or regulations could result in substantial fines or possible revocation of our authority to conduct our operations.
- The impact of 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. Our industry is undergoing rapid consolidation, and the combining entities are competing aggressively for business at low rates.
- Possible disruption of supplies, or an increase in the prices, of gasoline, diesel fuel and jet fuel for our aircraft and delivery vehicles as a result of war or other factors. We require significant quantities of gasoline and fuel and are exposed to the commodity price risk associated with variations in the market price for petroleum products.
- Cyclical and seasonal fluctuations in our operating results due to decreased demand for our services.

Item 7A. *Quantitative and Qualitative Disclosures about Market Risk*

Information about market risk can be found in Item 7 of this report under the caption "Market Risk."

Item 8. *Financial Statements and Supplementary Data*

Our financial statements are filed together with this report. See the Index to Financial Statements and Financial Statement Schedules on page F-1 for a list of the financial statements filed together with this report. Supplementary data appear in Note 19 to our financial statements.

Item 9. *Changes in and Disagreements with Accountants on Accounting and Financial Disclosure*

None.

PART III

Item 10. *Directors and Executive Officers of the Registrant*

Information about our directors is presented under the caption "Election of Directors" in our definitive Proxy Statement for the Annual Meeting of Shareowners to be held on May 8, 2003 and is incorporated herein by reference.

Information about our executive officers can be found in Part I, Item 1A, of this report under the caption "Executive Officers of the Registrant" in accordance with Instruction 3 of Item 401(b) of Regulation S-K and General Instruction G(3) of Form 10-K.

Information about our compliance with Section 16 of the Exchange Act of 1934, as amended, is presented under the caption "Section 16(a) Beneficial Ownership Reporting Compliance" in our definitive Proxy Statement for the Annual Meeting of Shareowners to be held on May 8, 2003 and is incorporated herein by reference.

Item 11. *Executive Compensation*

Information about executive compensation is presented under the caption "Compensation of Executive Officers and Directors," excluding the information under the caption "Report of the Compensation

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Committee,” in our definitive Proxy Statement for the Annual Meeting of Shareowners to be held on May 8, 2003 and is incorporated herein by reference.

Item 12. Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters

Information about security ownership is presented under the caption “Beneficial Ownership of Common Stock” in our definitive Proxy Statement for the Annual Meeting of Shareowners to be held on May 8, 2003 and is incorporated herein by reference.

Information about our equity compensation plans is presented under the caption “Equity Compensation Plans” in our definitive Proxy Statement for the Annual Meeting of Shareowners to be held on May 8, 2003 and is incorporated herein by reference.

Item 13. Certain Relationships and Related Transactions

None.

Item 14. Controls and Procedures

During the 90-day period prior to the filing date of 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. Based upon, and as of the date of, that evaluation, our Chief Executive Officer and Chief Financial Officer concluded that the disclosure controls and procedures were effective, in all material respects, to ensure that information required to be disclosed in the reports we file and submit under the Exchange Act is recorded, processed, summarized and reported as and when required.

There have been no significant changes in our internal controls or in other factors that could significantly affect internal controls subsequent to the date we carried out this evaluation. There were no significant deficiencies or material weaknesses identified in the evaluation and therefore, no corrective actions were taken.

PART IV

Item 15. Exhibits, Financial Statement Schedules, and Reports on Form 8-K

(a) 1. Financial Statements.

See the Index to Financial Statements on page F-1 for a list of the financial statements filed with this report.

2. Financial Statement Schedules.

None.

3. List of Exhibits.

See the Exhibit Index for a list of the exhibits incorporated by reference into or filed with this report.

(b) Reports on Form 8-K.

None.

(c) Exhibits required by Item 601 of Regulation S-K.

See the Exhibit Index for a list of the exhibits incorporated by reference into or filed with this report.

(d) Financial Statement Schedules.

None.

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, United Parcel Service, Inc. has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

UNITED PARCEL SERVICE, INC.
(REGISTRANT)

By: /s/ MICHAEL L. ESKEW

Michael L. Eskew
*Chairman and
Chief Executive Officer*

Date: March 6, 2003

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the Registrant and in the capacities and on the dates indicated.

<u>Signature</u>	<u>Title</u>	<u>Date</u>
<hr/> <i>/s/ WILLIAM H. BROWN, III</i> William H. Brown, III	Director	March 6, 2003
<hr/> <i>/s/ D. SCOTT DAVIS</i> D. Scott Davis	Senior Vice President, Chief Financial Officer and Treasurer (Principal Financial and Accounting Officer)	March 6, 2003
<hr/> <i>/s/ CALVIN DARDEN</i> Calvin Darden	Senior Vice President and Director	March 6, 2003
<hr/> <i>/s/ MICHAEL L. ESKEW</i> Michael L. Eskew	Chairman, Chief Executive Officer and Director (Principal Executive Officer)	March 6, 2003
<hr/> <i>/s/ JAMES P. KELLY</i> James P. Kelly	Director	March 6, 2003
<hr/> Ann M. Livermore	Director	
<hr/> Gary E. MacDougal	Director	
<hr/> <i>/s/ JOSEPH R. MODEROW</i> Joseph R. Moderow	Senior Vice President, Secretary and Director	March 6, 2003
<hr/> Victor A. Pelson	Director	

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Signature	Title	Date
/s/ LEA N. SOUPATA	Senior Vice President and Director	March 6, 2003
Lea N. Soupata	Director	
Robert M. Teeter	Director	
John W. Thompson	Director	
Carol B. Tomé		
/s/ THOMAS H. WEIDEMEYER	Senior Vice President, Chief Operating Officer and Director	March 6, 2003
Thomas H. Weidemeyer		

CERTIFICATIONS

I, Michael L. Eskew, certify that:

1. I have reviewed this annual report on Form 10-K of United Parcel Service, Inc.;
2. Based on my knowledge, this annual report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this annual report;
3. Based on my knowledge, the financial statements, and other financial information included in this annual report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this annual report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-14 and 15d-14) for the registrant and have:
 - a. designed such disclosure controls and procedures to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this annual report is being prepared;
 - b. evaluated the effectiveness of the registrant's disclosures controls and procedures as of a date within 90 days prior to the filing date of this annual report (the "Evaluation Date"); and
 - c. presented in this annual report our conclusions about the effectiveness of the disclosure controls and procedures based on our evaluation as of the Evaluation Date;
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation, to the registrant's auditors and the audit committee of the registrant's board of directors:
 - a. all significant deficiencies in the design or operation of internal controls which could adversely affect the registrant's ability to record, process, summarize and report financial data and have identified for the registrant's auditors any material weaknesses in internal controls; and
 - b. any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal controls; and
6. The registrant's other certifying officer and I have indicated in this annual report whether or not there were significant changes in internal controls or in other factors that could significantly affect internal controls subsequent to the date of our most recent evaluation, including any corrective actions with regard to significant deficiencies and material weaknesses.

Date: March 6, 2003

/s/ MICHAEL L. ESKEW

Michael L. Eskew
Chairman and Chief Executive Officer

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I, D. Scott Davis, certify that:

1. I have reviewed this annual report on Form 10-K of United Parcel Service, Inc.;
2. Based on my knowledge, this annual report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this annual report;
3. Based on my knowledge, the financial statements, and other financial information included in this annual report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this annual report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-14 and 15d-14) for the registrant and have:
 - a. designed such disclosure controls and procedures to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this annual report is being prepared;
 - b. evaluated the effectiveness of the registrant's disclosures controls and procedures as of a date within 90 days prior to the filing date of this annual report (the "Evaluation Date"); and
 - c. presented in this annual report our conclusions about the effectiveness of the disclosure controls and procedures based on our evaluation as of the Evaluation Date;
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation, to the registrant's auditors and the audit committee of the registrant's board of directors:
 - a. all significant deficiencies in the design or operation of internal controls which could adversely affect the registrant's ability to record, process, summarize and report financial data and have identified for the registrant's auditors any material weaknesses in internal controls; and
 - b. any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal controls; and
6. The registrant's other certifying officer and I have indicated in this annual report whether or not there were significant changes in internal controls or in other factors that could significantly affect internal controls subsequent to the date of our most recent evaluation, including any corrective actions with regard to significant deficiencies and material weaknesses.

Date: March 6, 2003

/s/ D. SCOTT DAVIS

D. Scott Davis
Chief Financial Officer

UNITED PARCEL SERVICE, INC.
AND SUBSIDIARIES
INDEX TO FINANCIAL STATEMENTS AND
FINANCIAL STATEMENT SCHEDULES

Item 8. *Financial Statements*

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UNITED PARCEL SERVICE, INC. AND SUBSIDIARIES

INDEPENDENT AUDITORS' REPORT

Board of Directors and Shareowners

United Parcel Service, Inc.
Atlanta, Georgia

We have audited the accompanying consolidated balance sheets of United Parcel Service, Inc. and its subsidiaries as of December 31, 2002 and 2001, and the related consolidated statements of income, shareowners' equity, and cash flows for each of the three years in the period ended December 31, 2002. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

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

In our opinion, such consolidated financial statements present fairly, in all material respects, the financial position of United Parcel Service, Inc. and its subsidiaries at December 31, 2002 and 2001, and the results of their operations and their cash flows for each of the three years in the period ended December 31, 2002 in conformity with accounting principles generally accepted in the United States of America.

As described in Note 1 to the consolidated financial statements, the Company adopted Statement of Financial Accounting Standards No. 133, "Accounting for Derivative Instruments and Hedging Activities," effective January 1, 2001, and Statement of Financial Accounting Standards No. 142, "Goodwill and Other Intangible Assets," effective January 1, 2002.

Deloitte & Touche LLP

Atlanta, Georgia

January 27, 2003

UNITED PARCEL SERVICE, INC. AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS

	December 31,	
	2002	2001
	(In millions, except per share amounts)	
ASSETS		
Current Assets:		
Cash & cash equivalents	\$ 2,211	\$ 858
Marketable securities & short-term investments	803	758
Accounts receivable, net	3,756	4,078
Finance receivables, net	868	708
Other current assets	1,100	1,195
	<u>8,738</u>	<u>7,597</u>
Property, Plant & Equipment — at cost, net of accumulated depreciation & amortization of \$11,749 and \$10,620 in 2002 and 2001	13,612	13,438
Prepaid Pension Costs	1,932	1,845
Other Assets	2,075	1,756
	<u>\$26,357</u>	<u>\$24,636</u>
LIABILITIES AND SHAREOWNERS' EQUITY		
Current Liabilities:		
Current maturities of long-term debt and commercial paper	\$ 1,107	\$ 518
Accounts payable	1,908	1,899
Accrued wages & withholdings	1,084	1,169
Dividends payable	212	212
Other current liabilities	1,244	988
	<u>5,555</u>	<u>4,786</u>
Long-Term Debt	3,495	4,648
Accumulated Postretirement Benefit Obligation, Net	1,251	1,130
Deferred Taxes, Credits & Other Liabilities	3,601	3,824
Shareowners' Equity:		
Preferred stock, no par value, authorized 200 shares, none issued	—	—
Class A common stock, par value \$.01 per share, authorized 4,600 shares, issued 642 and 772 in 2002 and 2001	7	8
Class B common stock, par value \$.01 per share, authorized 5,600 shares, issued 482 and 349 in 2002 and 2001	4	3
Additional paid-in capital	387	414
Retained earnings	12,495	10,162
Accumulated other comprehensive loss	(438)	(339)
Deferred compensation arrangements	84	47
	<u>12,539</u>	<u>10,295</u>
Less: Treasury stock (1 shares in 2002 and 2001)	(84)	(47)
	<u>12,455</u>	<u>10,248</u>
	<u>\$26,357</u>	<u>\$24,636</u>

See notes to consolidated financial statements.

UNITED PARCEL SERVICE, INC. AND SUBSIDIARIES

STATEMENTS OF CONSOLIDATED INCOME

	Years Ended December 31,		
	2002	2001	2000
	(In millions, except per share amounts)		
Revenue	\$31,272	\$30,321	\$29,498
Operating Expenses:			
Compensation and benefits	17,944	17,397	16,546
Other	9,232	8,962	8,440
	27,176	26,359	24,986
Operating Profit	4,096	3,962	4,512
Other Income and (Expense):			
Investment income	63	159	527
Interest expense	(173)	(184)	(205)
Tax assessment reversal	1,023	—	—
	913	(25)	322
Income Before Income Taxes And Cumulative Effect of Changes In Accounting Principles	5,009	3,937	4,834
Income Taxes	1,755	1,512	1,900
Income Before Cumulative Effect of Changes In Accounting Principles	3,254	2,425	2,934
Cumulative Effect of Changes In Accounting Principles, Net of Taxes	(72)	(26)	—
Net Income	\$ 3,182	\$ 2,399	\$ 2,934
Basic Earnings Per Share Before Cumulative Effect Of Changes In Accounting Principles	\$ 2.91	\$ 2.15	\$ 2.54
Basic Earnings Per Share	\$ 2.84	\$ 2.13	\$ 2.54
Diluted Earnings Per Share Before Cumulative Effect Of Changes In Accounting Principles	\$ 2.87	\$ 2.12	\$ 2.50
Diluted Earnings Per Share	\$ 2.81	\$ 2.10	\$ 2.50

See notes to consolidated financial statements.

UNITED PARCEL SERVICE, INC. AND SUBSIDIARIES
STATEMENTS OF CONSOLIDATED SHAREOWNERS' EQUITY

	2002		2001		2000	
	Shares	Dollars	Shares	Dollars	Shares	Dollars
(In millions, except per share amounts)						
Class A Common Stock						
Balance at beginning of year	772	\$ 8	936	\$ 9	1,101	\$ 11
Common stock purchases	(10)	—	(26)	—	(84)	(1)
Stock award plans	11	—	13	—	15	—
Common stock issuances	2	—	1	—	1	—
Conversions of Class A to Class B common stock	(133)	(1)	(152)	(1)	(97)	(1)
Balance at end of year	<u>642</u>	<u>7</u>	<u>772</u>	<u>8</u>	<u>936</u>	<u>9</u>
Class B Common Stock						
Balance at beginning of year	349	3	199	2	109	1
Common stock purchases	—	—	(10)	—	(7)	—
Common stock issued for acquisitions	—	—	8	—	—	—
Conversions of Class A to Class B common stock	133	1	152	1	97	1
Balance at end of year	<u>482</u>	<u>4</u>	<u>349</u>	<u>3</u>	<u>199</u>	<u>2</u>
Additional Paid-In Capital						
Balance at beginning of year		414		267		5,096
Stock award plans		477		521		602
Common stock issued for acquisitions		—		510		—
Common stock purchases		(604)		(954)		(5,464)
Common stock issuances		100		70		33
Balance at end of year		<u>387</u>		<u>414</u>		<u>267</u>
Retained Earnings						
Balance at beginning of year		10,162		9,684		7,536
Net income		3,182		2,399		2,934
Dividends (\$0.76, \$0.76, and \$0.68 in 2002, 2001, and 2000 respectively)		(849)		(856)		(786)
Common stock purchases		—		(1,065)		—
Balance at end of year		<u>12,495</u>		<u>10,162</u>		<u>9,684</u>

	2002		2001		2000	
	Shares	Dollars	Shares	Dollars	Shares	Dollars
(In millions, except per share amounts)						
Accumulated Other Comprehensive Income						
Foreign currency translation adjustment:						
Balance at beginning of year		(269)		(223)		(167)
Aggregate adjustment for the year		(59)		(46)		(56)
Balance at end of year		(328)		(269)		(223)
Unrealized gain (loss) on marketable securities, net of tax:						
Balance at beginning of year		(21)		(4)		(3)
Current period changes in fair value (net of tax effect of \$(9), \$0 and \$0)		(16)		(1)		—
Reclassification to earnings (net of tax effect of \$1, \$(11) and \$0)		3		(16)		(1)
Balance at end of year		(34)		(21)		(4)
Unrealized gain (loss) on cash flow hedges, net of tax:						
Balance at beginning of year		(49)		—		—
FAS 133 transition adjustment		—		23		—
Current period changes in fair value (net of tax effect of \$6, \$(24), and \$0)		10		(39)		—
Reclassification to earnings (net of tax effect of \$9, \$(21), and \$0)		13		(33)		—
Balance at end of year		(26)		(49)		—
Additional minimum pension liability, net of tax:						
Balance at beginning of year		—		—		—
Minimum pension liability adjustment (net of tax effect of \$(31), \$0, and \$0)		(50)		—		—
Balance at end of year		(50)		—		—
Accumulated other comprehensive income at end of year		(438)		(339)		(227)
Deferred Compensation Obligations						
Balance at beginning of year		47		—		—
Common stock held for deferred compensation arrangements		37		47		—
Balance at end of year		84		47		—
Treasury Stock						
Balance at beginning of year	(1)	(47)	—	—	—	—
Common stock held for deferred compensation arrangements	—	(37)	(1)	(47)	—	—
Balance at end of year	(1)	(84)	(1)	(47)	—	—
Total Shareowners' Equity At End Of Year		\$12,455		\$10,248		\$9,735
Comprehensive Income		\$ 3,083		\$ 2,287		\$2,877

See notes to consolidated financial statements.

UNITED PARCEL SERVICE, INC. AND SUBSIDIARIES
STATEMENTS OF CONSOLIDATED CASH FLOWS

	Years Ended December 31,		
	2002	2001	2000
(In millions)			
Cash Flows From Operating Activities:			
Net income	\$ 3,182	\$ 2,399	\$ 2,934
Adjustments to reconcile net income to net cash from operating activities:			
Depreciation and amortization	1,464	1,396	1,173
Postretirement benefits	121	81	57
Deferred taxes, credits and other	162	481	(81)
Stock award plans	445	495	539
Restructuring charge and related expenses	85	—	—
Impairment of goodwill	74	—	—
Vacation policy change	(121)	—	—
Tax assessment reversal	(776)	—	—
Gain on investments and sale of business	—	—	(263)
Changes in assets and liabilities, net of effect of acquisitions:			
Accounts receivable, net	312	415	(851)
Prepaid health and welfare costs	446	(38)	(27)
Other current assets	(43)	(104)	(252)
Prepaid pension costs	(87)	(252)	(662)
Accounts payable	(56)	(313)	317
Accrued wages and withholdings	112	27	131
Dividends payable	—	20	(169)
Other current liabilities	307	(77)	(42)
Net cash from operating activities	5,627	4,530	2,804
Cash Flows From Investing Activities:			
Capital expenditures	(1,658)	(2,372)	(2,147)
Disposals of property, plant and equipment	108	165	251
Purchases of marketable securities and short-term investments	(2,303)	(3,361)	(8,127)
Sales and maturities of marketable securities and short-term investments	2,227	3,690	9,345
Net increase in finance receivables	(469)	(630)	(62)
Construction funds in escrow	—	21	90
Payments for acquisitions, net of cash acquired	(14)	(466)	(245)
Other asset receipts (payments)	(24)	(60)	(42)
Net cash (used in) investing activities	(2,133)	(3,013)	(937)
Cash Flows From Financing Activities:			
Proceeds from borrowings	419	2,312	2,297
Repayments of borrowings	(1,099)	(1,089)	(1,168)
Purchases of common stock via tender offer	—	—	(4,070)
Purchases of common stock	(604)	(2,019)	(1,395)
Issuances of common stock pursuant to stock awards and employee stock purchase plans	125	228	88
Dividends	(849)	(856)	(786)
Other transactions	(82)	(69)	(127)
Net cash (used in) financing activities	(2,090)	(1,493)	(5,161)
Effect Of Exchange Rate Changes On Cash	(51)	(45)	(31)
Net Increase (Decrease) In Cash And Cash Equivalents	1,353	(21)	(3,325)
Cash And Cash Equivalents:			
Beginning of period	858	879	4,204
End of period	\$ 2,211	\$ 858	\$ 879
Cash Paid During The Period For:			
Interest (net of amount capitalized)	\$ 190	\$ 164	\$ 363
Income taxes	\$ 1,416	\$ 1,042	\$ 1,567

See notes to consolidated financial statements.

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

Note 1. Summary of Accounting Policies

Basis of Financial Statements and Business Activities

The accompanying financial statements include the accounts of United Parcel Service, Inc., and all of its consolidated subsidiaries (collectively “UPS” or the “Company”). All intercompany balances and transactions have been eliminated.

UPS concentrates its operations in the field of transportation services, primarily domestic and international letter and package delivery. Through our non-package subsidiaries, we are also a global provider of specialized transportation, logistics, and financial services.

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Revenue Recognition

U.S. Domestic and International Package Operations — Revenue is recognized upon delivery of a letter or package.

UPS Logistics Group and UPS Freight Services — Revenue is recognized net of the expense related to the third party transportation of freight at the time the services are performed. Material management and distribution revenue is recognized upon performance of the service provided. Customs brokerage revenue is recognized upon completing documents necessary for customs entry purposes.

UPS Capital — Income on loans and direct finance leases is recognized on the interest method. Accrual of interest income is suspended at the earlier of the time at which collection of an account becomes doubtful or the account becomes 90 days delinquent. Income on operating leases is recognized on the straight-line method over the terms of the underlying leases.

Cash and Cash Equivalents

Cash and cash equivalents consist of highly liquid investments (including investments in debt, auction rate securities, and other money market instruments of \$1.780 billion and \$331 million at December 31, 2002 and 2001, respectively) that are readily convertible into cash. The carrying amount approximates fair value because of the short-term maturity of these instruments.

Marketable Securities and Short-Term Investments

Marketable securities are classified as available-for-sale and are carried at fair value, with related unrealized gains and losses reported, net of tax, as other comprehensive income (“OCI”), a separate component of shareowners’ equity. The amortized cost of debt securities is adjusted for amortization of premiums and accretion of discounts to maturity. Such amortization and accretion is included in investment income, along with interest and dividends. The cost of securities sold is based on the specific identification method; realized gains and losses resulting from such sales are included in investment income.

Investment securities are reviewed for impairment in accordance with FASB Statement No. 115 “Accounting for Certain Investments in Debt and Equity Securities”. Impairment of investment securities results in a charge to income when a market decline below cost is other than temporary.

UNITED PARCEL SERVICE, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

Property, Plant and Equipment

Property, plant and equipment are carried at cost. Depreciation and amortization are provided by the straight-line method over the estimated useful lives of the assets, which are as follows: Vehicles — 9 years; Aircraft — 12 to 20 years; Buildings — 20 to 40 years; Leasehold Improvements — lives of leases; Plant Equipment — 5 to 8 1/3 years; Technology Equipment (including capitalized software) — 3 to 5 years. The costs of major airframe and engine overhauls, as well as routine maintenance and repairs, are charged to expense as incurred.

Interest incurred during the construction period of certain property, plant and equipment is capitalized until the underlying assets are placed in service, at which time amortization of the capitalized interest begins, straight-line, over the estimated useful lives of the related assets. Capitalized interest was \$25, \$47, and \$26 million for 2002, 2001, and 2000, respectively.

Impairment of Long-Lived Assets

On January 1, 2002, we adopted Financial Accounting Standards Board (“FASB”) Statement No. 144, “Accounting for the Impairment or Disposal of Long-Lived Assets” (“FAS 144”). Under FAS 144, we review long-lived assets for impairment when circumstances indicate the carrying amount of an asset may not be recoverable based on the undiscounted future cash flows of the asset. If the carrying amount of the asset is determined not to be recoverable, a write-down to fair value is recorded. The effects of adopting FAS 144 were immaterial to our results of operations.

Goodwill and Intangible Assets

Costs of purchased businesses in excess of net assets acquired (goodwill), and intangible assets are accounted for under the provisions of FASB Statement No. 142 “Goodwill and Other Intangible Assets” (“FAS 142”). Upon adoption of FAS 142 on January 1, 2002, we were required to test all existing goodwill for impairment as of that date, and at least annually thereafter, unless changes in circumstances indicate an impairment may have occurred sooner. We are required to test goodwill on a “reporting unit” basis. A reporting unit is the operating segment unless, for businesses within that operating segment, discrete financial information is prepared and regularly reviewed by management, in which case such a component business is the reporting unit.

A fair value approach is used to test goodwill for impairment. An impairment charge is recognized for the amount, if any, by which the carrying amount of goodwill exceeds its fair value. Fair values are established using discounted cash flows. When available and as appropriate, comparative market multiples were used to corroborate discounted cash flow results.

We recorded a non-cash goodwill impairment charge of \$72 million (\$0.06 per diluted share), as of January 1, 2002, related to our Mail Technologies business. This charge is reported as a cumulative effect of a change in accounting principle and resulted in a restatement of our first quarter 2002 quarterly financial statements (see Note 19). The primary factor resulting in the impairment charge was the lower than anticipated growth experienced in the expedited mail delivery business. In conjunction with our annual test of goodwill, we recorded an additional impairment charge of \$2 million, resulting in total goodwill impairment of \$74 million for 2002.

Income Taxes

Income taxes are accounted for under FASB Statement No. 109, “Accounting for Income Taxes” (“FAS 109”). FAS 109 is an asset and liability approach that requires the recognition of deferred tax assets and liabilities for the expected future tax consequences of events that have been recognized in our financial statements or tax returns. In estimating future tax consequences, FAS 109 generally considers all expected

UNITED PARCEL SERVICE, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

future events other than proposed changes in the tax law or rates. Valuation allowances are provided if it is more likely than not that a deferred tax asset will not be realized.

Stock-Based Compensation

We have adopted the disclosure provisions of FASB Statement No. 123, “Accounting for Stock-Based Compensation” (“FAS 123”). Under FAS 123, companies have the option to measure compensation costs for stock options using the intrinsic value method prescribed by Accounting Principles Board Opinion No. 25, “Accounting for Stock Issued to Employees” (“APB 25”). Under APB 25, compensation expense is generally not recognized when both the exercise price is the same as the market price and the number of shares to be issued is set on the date the employee stock option is granted. Since our employee stock options are granted on this basis and we have chosen to use the intrinsic value method, we do not recognize compensation expense for stock option grants. We do, however, include in Note 11 pro forma disclosures of net income and earnings per share as if the fair value method of accounting had been applied.

In 2003, we plan to adopt the fair value measurement provisions of FAS 123, which is considered the preferable accounting method for stock-based employee compensation. Under FAS 148, “Accounting for Stock-Based Compensation — Transition and Disclosure”, we have elected to adopt the measurement provisions of FAS 123 using the prospective method. Under this approach, all future employee stock option grants and other stock-based compensation will be expensed to compensation and benefits over the vesting period based on the fair value at the date the stock-based compensation is granted. We will continue to provide pro forma net income and earnings per share information related to prior awards.

Derivative Instruments

Effective January 1, 2001, we adopted FASB Statement No. 133, “Accounting for Derivative Instruments and Hedging Activities” (“FAS 133”), as amended by Statements No. 137 and No. 138. FAS 133, as amended, requires all financial derivative instruments to be recorded on our balance sheet at fair value. Derivatives not designated as hedges must be adjusted to fair value through income. If a derivative is designated as a hedge, depending on the nature of the hedge, changes in its fair value that are considered to be effective, as defined, either offset the change in fair value of the hedged assets, liabilities, or firm commitments through income, or are recorded in OCI until the hedged item is recorded in income. Any portion of a change in a derivative’s fair value that is considered to be ineffective, or is excluded from the measurement of effectiveness, is recorded immediately in income.

At January 1, 2001, our financial statements were adjusted to record a cumulative effect of adopting FAS 133, as follows (in millions, except per share amounts):

	<u>Income</u>	<u>OCI</u>
Adjustment to fair value of derivative instruments	\$ (42)	\$ 37
Income tax effects	16	(14)
Adjustment, net of tax	<u>\$ (26)</u>	<u>\$ 23</u>
Effect on diluted earnings per share (a)	<u>\$(0.02)</u>	

(a) For income effect, amount shown is net of adjustment to hedged items.

The cumulative effect on income resulted primarily from marking to market the time value of option contracts used in commodity and foreign currency cash flow hedging. The cumulative effect on OCI resulted primarily from marking to market swap contracts used as cash flow hedges of anticipated foreign currency cash flows and anticipated purchases of energy products.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

New Accounting Pronouncements

In June 2002, the FASB issued Statement No. 146 “Accounting for Costs Associated with Exit or Disposal Activities” (“FAS 146”). FAS 146 provides guidance on the recognition and measurement of liabilities associated with exit or disposal activities and requires that such liabilities be recognized when incurred. This statement is effective for exit or disposal activities initiated on or after January 1, 2003.

As discussed in Note 17, we implemented a restructuring program involving the business unit integration of our Freight Services and Logistics Group operations in the fourth quarter of 2002. As this restructuring program was initiated in 2002, we accounted for this restructuring program using the existing guidance in EITF 94-3 “Liability Recognition for Certain Employee Termination Benefits and Other Costs to Exit an Activity (Including Certain Costs Incurred in a Restructuring)”. Therefore, the adoption of FAS 146 on January 1, 2003 had no effect on our results of operations or financial condition. In the fourth quarter of 2002, we recorded a pre-tax restructuring charge and related expenses in the amount of \$106 million, which is classified in other operating expenses.

In November 2002, the FASB issued Interpretation No. 45 “Guarantor’s Accounting and Disclosure Requirements for Guarantees, Including Indirect Guarantees of Indebtedness of Others” (“FIN 45”). FIN 45 requires that a liability be recognized at fair value at the inception of certain guarantees for the obligations undertaken by the guarantor. FIN 45 also requires additional disclosures for certain guarantee contracts. The disclosure provisions of FIN 45 are effective for financial statements ending after December 15, 2002, while the recognition and initial measurement provisions are applicable on a prospective basis to guarantees issued or modified after December 31, 2002. We are currently evaluating the impact of the recognition and measurement provisions of FIN 45 on our financial statements.

In January 2003, the FASB issued Interpretation No. 46 “Consolidation of Variable Interest Entities” (“FIN 46”). FIN 46 provides guidance on the identification of variable interest entities, and the assessment of a company’s interests in a variable interest entity to determine whether consolidation is appropriate. FIN 46 requires the consolidation of a variable interest entity by the primary beneficiary if the entity does not effectively disperse risks among the parties involved. FIN 46 applies immediately to variable interest entities created after January 31, 2003, and is effective for periods beginning after June 15, 2003 for existing variable interest entities. As we have no material exposures to special purpose entities or other off-balance sheet arrangements, we anticipate that the effects of adopting FIN 46 will not be material to our results of operations or financial condition.

UNITED PARCEL SERVICE, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

Changes in Presentation

Certain prior year amounts have been reclassified to conform to the current year presentation.

Note 2. Marketable Securities and Short-Term Investments

The following is a summary of marketable securities and short-term investments at December 31, 2002 and 2001 (in millions):

2002	Cost	Unrealized Gains	Unrealized Losses	Estimated Fair Value
U.S. government & agency securities	\$ 77	\$ 2	\$ —	\$ 79
U.S. mortgage & asset-backed securities	231	4	6	229
U.S. corporate securities	115	2	1	116
Other debt securities	57	—	—	57
Total debt securities	480	8	7	481
Equity securities	379	5	62	322
	\$859	\$ 13	\$ 69	\$ 803
2001	Cost	Unrealized Gains	Unrealized Losses	Estimated Fair Value
U.S. government & agency securities	\$ 75	\$ 1	\$ 1	\$ 75
U.S. mortgage & asset-backed securities	149	2	—	151
U.S. corporate securities	160	1	2	159
Other debt securities	32	—	—	32
Total debt securities	416	4	3	417
Equity securities	377	9	45	341
	\$793	\$ 13	\$ 48	\$ 758

The gross realized gains on sales of marketable securities totaled \$11, \$34, and \$69 million in 2002, 2001, and 2000, respectively. The gross realized losses totaled \$10, \$7, and \$35 million in 2002, 2001, and 2000, respectively. Impairment losses recognized on marketable securities and short-term investments totaled \$5, \$0, and \$33 million during 2002, 2001, and 2000 respectively.

The amortized cost and estimated fair value of marketable securities and short-term investments at December 31, 2002, by contractual maturity, are shown below (in millions). Actual maturities may differ from contractual maturities because the issuers of the securities may have the right to prepay obligations without prepayment penalties.

	Cost	Estimated Fair Value
Due in one year or less	\$ 24	\$ 25
Due after one year through three years	120	122
Due after three years through five years	15	15
Due after five years	321	319
	480	481
Equity securities	379	322
	\$859	\$ 803

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

Note 3. Finance Receivables

The following is a summary of finance receivables at December 31, 2002 and 2001 (in millions):

	2002	2001
Commercial term loans	\$ 523	\$372
Investment in finance leases	218	66
Asset-based lending	381	353
Receivable factoring	400	189
	<u> </u>	<u> </u>
Gross finance receivables	1,522	980
Less: allowance for credit losses	(38)	(30)
	<u> </u>	<u> </u>
Balance at December 31	\$1,484	\$950
	<u> </u>	<u> </u>

Outstanding receivable balances at December 31, 2002 and 2001 are net of unearned income of \$35 and \$11 million, respectively. When we “factor” (i.e. purchase) a customer invoice from a client, we record the customer receivable as an asset and also establish a liability for the funds due to the client, which is recorded in accounts payable on the consolidated balance sheet. The following is a reconciliation of receivable factoring balances at December 31, 2002 and 2001 (in millions):

	2002	2001
Customer receivable balances	\$ 400	\$ 189
Less: Amounts due to client	(176)	(111)
	<u> </u>	<u> </u>
Net funds employed	\$ 224	\$ 78
	<u> </u>	<u> </u>

Non-earning finance receivables were \$41 and \$24 million at December 31, 2002 and 2001, respectively. The following is a rollforward of the allowance for credit losses on finance receivables (in millions):

	2002	2001
Balance at January 1	\$ 30	\$ —
Provisions charged to operations	26	7
Net transfers related to acquisitions	—	27
Charge-offs, net of recoveries	(18)	(4)
	<u> </u>	<u> </u>
Balance at December 31	\$ 38	\$ 30
	<u> </u>	<u> </u>

The carrying value of finance receivables at December 31, 2002, by contractual maturity, is shown below (in millions). Actual maturities may differ from contractual maturities because some borrowers have the right to prepay these receivables without prepayment penalties.

	Carrying Value
Due in one year or less	\$ 882
Due after one year through three years	99
Due after three years through five years	203
Due after five years	338
	<u> </u>
	\$1,522
	<u> </u>

Based on interest rates for financial instruments with similar terms and maturities, the fair value of finance receivables is approximately \$1.492 billion and \$982 million as of December 31, 2002 and 2001,

UNITED PARCEL SERVICE, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

respectively. At December 31, 2002, we had unfunded loan commitments totaling \$778 million, consisting of standby letters of credit of \$48 million and other unfunded lending commitments of \$730 million.

Note 4. Property, Plant and Equipment

Property, plant and equipment as of December 31 consists of the following (in millions):

	2002	2001
Vehicles	\$ 3,467	\$ 3,485
Aircraft (including aircraft under capitalized leases)	10,151	9,699
Land	704	670
Buildings	2,049	1,772
Leasehold improvements	2,159	2,069
Plant equipment	4,248	3,818
Technology equipment (including capitalized software)	1,998	1,784
Equipment under operating lease	50	16
Construction-in-progress	535	745
	25,361	24,058
Less: Accumulated depreciation and amortization	(11,749)	(10,620)
	\$ 13,612	\$ 13,438

Note 5. Employee Benefit Plans

We maintain the following defined benefit pension plans (the "Plans"): UPS Retirement Plan, UPS Excess Coordinating Benefit Plan, and the UPS Pension Plan.

The UPS Retirement Plan is noncontributory and includes substantially all eligible employees of participating domestic subsidiaries who are not members of a collective bargaining unit. The Plan provides for retirement benefits based on average compensation levels earned by employees prior to retirement. Benefits payable under this Plan are subject to maximum compensation limits and the annual benefit limits for a tax qualified defined benefit plan as prescribed by the Internal Revenue Service.

The UPS Excess Coordinating Benefit Plan is a non-qualified plan that provides benefits to participants in the UPS Retirement Plan for amounts that exceed the benefit limits described above.

The UPS Pension Plan is noncontributory and includes certain eligible employees of participating domestic subsidiaries and members of collective bargaining units that elect to participate in the plan. The Plan provides for retirement benefits based on service credits earned by employees prior to retirement.

The UPS Retirement Plan and UPS Pension Plans' assets consist primarily of publicly traded securities and include approximately 6.1 and 24.1 million shares of UPS common stock at December 31, 2002 and 2001, respectively. Our funding policy is consistent with relevant federal tax regulations. Accordingly, our contributions are deductible for federal income tax purposes. Because the UPS Excess Coordinating Benefit Plan is non-qualified for federal income tax purposes, this plan is not funded.

We also sponsor postretirement medical plans that provide health care benefits to our retirees who meet certain eligibility requirements and who are not otherwise covered by multi-employer plans. Generally, this includes employees with at least 10 years of service who have reached age 55 and employees who are eligible for postretirement medical benefits from a Company-sponsored plan pursuant to collective bargaining agreements. We have the right to modify or terminate certain of these plans. In many cases, these benefits

UNITED PARCEL SERVICE, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

have been provided to retirees on a noncontributory basis; however, in certain cases, retirees are required to contribute toward the cost of the coverage.

The following tables provide a reconciliation of the changes in the plans' benefit obligations and fair value of assets, and a statement of funded status as of September 30, with certain amounts included in the balance sheet as of December 31 (in millions):

	Pension Benefits		Postretirement Medical Benefits	
	2002	2001	2002	2001
Change in Benefit Obligation				
Net benefit obligation at October 1, prior year	\$5,347	\$ 4,547	\$ 1,759	\$ 1,500
Service cost	217	192	63	55
Interest cost	413	363	134	118
Plan participants' contributions	—	—	3	2
Plan amendments	100	20	38	2
Actuarial (gain) loss	777	394	236	157
Gross benefits paid	(184)	(169)	(84)	(75)
Net benefit obligation at September 30	6,670	5,347	2,149	1,759
Change in Plan Assets				
Fair value of plan assets at October 1, prior year	6,496	7,661	372	466
Actual return on plan assets	77	(1,218)	3	(70)
Employer contributions	105	222	43	49
Plan participants' contributions	—	—	3	2
Gross benefits paid	(184)	(169)	(84)	(75)
Fair value of plan assets at September 30	6,494	6,496	337	372
Funded status at September 30	(176)	1,149	(1,812)	(1,387)
Unrecognized net actuarial (gain) loss	1,712	361	516	254
Unrecognized prior service cost	364	295	35	(4)
Unrecognized net transition obligation	31	39	—	—
Employer contributions	1	1	10	7
Net asset (liability) recorded at end of year	\$1,932	\$ 1,845	\$(1,251)	\$(1,130)

Because the UPS Excess Coordinating Plan is not funded, the Company has recorded an additional minimum pension liability for this plan of \$88 million at December 31, 2002. This liability is included in the other credits and non-current liabilities portion of Note 9. As an offset to this liability, the Company recorded a \$7 million intangible asset, representing the net unrecognized prior service cost for this plan at December 31, 2002, and the remaining \$50 million was recorded as a reduction of other comprehensive income in Shareowners' Equity (net of the tax effect of \$31 million). The unfunded accumulated benefit obligation of the UPS Excess Coordinating Benefit Plan was \$121 million as of December 31, 2002.

UNITED PARCEL SERVICE, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

Net periodic benefit cost (benefit) for the years ended December 31 included the following components (in millions):

	Pension Benefits			Postretirement Medical Benefits		
	2002	2001	2000	2002	2001	2000
Service cost	\$ 217	\$ 192	\$ 181	\$ 63	\$ 55	\$ 50
Interest cost	413	363	324	134	118	106
Expected return on assets	(654)	(616)	(471)	(33)	(42)	(34)
Amortization of:						
Transition obligation	8	8	8	—	—	—
Prior service cost	30	30	30	(1)	(1)	(1)
Actuarial (gain) loss	4	(7)	(1)	4	—	1
Net periodic benefit cost (benefit)	\$ 18	\$ (30)	\$ 71	\$167	\$130	\$122

The significant assumptions used in the measurement of our benefit obligations are as follows:

	2002	2001	2000
Expected long-term rate of earnings on plan assets	9.42%	9.50%	9.50%
Discount rate	6.75%	7.50%	7.75%
Rate of annual increase in future compensation levels for pension benefits	4.00%	4.00%	4.00%

For 2003, we plan to decrease the expected long-term rate of earnings on plan assets to 9.21%.

Future postretirement medical benefit costs were forecasted assuming an initial annual increase of 9.00% for pre-65 and post-65 medical costs, decreasing to 5.25% for pre-65 and post-65 by the year 2011 and with consistent annual increases at those ultimate levels thereafter.

Assumed health care cost trends have a significant effect on the amounts reported for the postretirement medical plans. A one-percent change in assumed health care cost trend rates would have the following effects (in millions):

	1% Increase	1% Decrease
Effect on total of service and interest cost components	\$ 7	\$ (8)
Effect on postretirement benefit obligation	\$ 87	\$ (93)

We also contribute to several multi-employer pension plans for which the above disclosure information is not determinable. Amounts charged to operations for pension contributions to these multi-employer plans were \$1.028 billion, \$977, and \$897 million during 2002, 2001, and 2000, respectively.

We also contribute to several multi-employer health and welfare plans that cover both active and retired employees for which the above disclosure information is not determinable. Amounts charged to operations for contributions to multi-employer health and welfare plans were \$604, \$553, and \$501 million during 2002, 2001, and 2000, respectively.

We also sponsor a defined contribution plan for all employees not covered under collective bargaining agreements. The Company matches, in shares of UPS common stock, a portion of the participating employees' contributions. Matching contributions charged to expense were \$79, \$71, and \$61 million for 2002, 2001, and 2000, respectively.

In the fourth quarter of 2002, our vacation policy for non-union employees was amended to require that vacation pay be earned ratably throughout the year. Previously, an employee became vested in the full year of

UNITED PARCEL SERVICE, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

vacation pay at the beginning of each year. As a result of this policy change, a credit to compensation and benefits of \$197 million was taken in the fourth quarter to reduce the vacation pay liability as of December 31, 2002.

Note 6. Other Assets

Other assets as of December 31 consist of the following (in millions):

	2002	2001
Goodwill	\$1,070	\$1,116
Intangible assets, net of accumulated amortization	110	103
Non-current finance receivables, net of allowance for credit losses	616	242
Other non-current assets	279	295
	<u>\$2,075</u>	<u>\$1,756</u>

The following table indicates the allocation of goodwill by reportable segment (in millions):

	December 31, 2001	Goodwill Acquired	Goodwill Impaired	Currency/ Other	December 31, 2002
Goodwill by Segment:					
U.S. domestic package	\$ —	\$ —	\$ —	\$ —	\$ —
International package	102	—	—	—	102
Non-package	1,014	—	(74)	28	968
	<u>1,116</u>	<u>—</u>	<u>(74)</u>	<u>28</u>	<u>1,070</u>
Consolidated	<u>\$ 1,116</u>	<u>\$ —</u>	<u>\$ (74)</u>	<u>\$ 28</u>	<u>\$ 1,070</u>

Goodwill in the non-package segment declined as a result of the \$72 million impairment charge recorded upon the adoption of FAS 142 and the \$2 million charge resulting from our annual impairment testing (see Note 1), partially offset by the additions from the resolution of purchase price contingencies and other purchase price adjustments for acquisitions closed in 2001.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

The amortization of goodwill and indefinite-lived intangibles ceased upon the implementation of FAS 142 on January 1, 2002. The following table indicates the impact on net income and earnings per share if the non-amortization provisions of FAS 142 had been applied beginning January 1, 2000 (in millions, except per share amounts).

	Year Ended December 31,		
	2002	2001	2000
Reported net income	\$3,182	\$2,399	\$2,934
Adjustments:			
Goodwill amortization	—	72	38
Income taxes	—	(13)	(10)
Adjusted net income	3,182	2,458	2,962
Cumulative effect of changes in accounting principles	72	26	—
Adjusted net income before cumulative effect of changes in accounting principles	\$3,254	\$2,484	\$2,962
Basic earnings per share:			
Reported	\$ 2.84	\$ 2.13	\$ 2.54
Adjusted	\$ 2.84	\$ 2.18	\$ 2.57
Diluted earnings per share:			
Reported	\$ 2.81	\$ 2.10	\$ 2.50
Adjusted	\$ 2.81	\$ 2.15	\$ 2.52
Basic earnings per share before cumulative effect of changes in accounting principles:			
Reported	\$ 2.91	\$ 2.15	\$ 2.54
Adjusted	\$ 2.91	\$ 2.21	\$ 2.57
Diluted earnings per share before cumulative effect of changes in accounting principles:			
Reported	\$ 2.87	\$ 2.12	\$ 2.50
Adjusted	\$ 2.87	\$ 2.17	\$ 2.52

The following is a summary of intangible assets at December 31, 2002 and 2001 (in millions):

	Trademarks	Franchise Rights, Licenses, Patents, and Other	Intangible Pension Asset	Total Intangible Assets
December 31, 2002:				
Gross carrying amount	\$ 13	\$ 105	\$ 7	\$ 125
Accumulated amortization	—	(15)	—	(15)
Net carrying value	\$ 13	\$ 90	\$ 7	\$ 110
December 31, 2001:				
Gross carrying amount	\$ 13	\$ 95	\$ —	\$ 108
Accumulated amortization	—	(5)	—	(5)
Net carrying value	\$ 13	\$ 90	\$ —	\$ 103

Expected amortization of definite-lived intangibles for the next five years is as follows (in millions): 2003 — \$8, 2004 — \$8, 2005 — \$7, 2006 — \$6, 2007 — \$5. As of December 31, 2002 and 2001, trademarks were the only indefinite-lived intangible assets under the provisions of FAS 142.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

Note 7. Business Combinations

We regularly explore opportunities to make acquisitions that would enhance our core package delivery business and our various non-package businesses. Our acquisitions include both domestic and international transactions. During the three years ended December 31, 2002, we completed 22 acquisitions that were accounted for under the purchase method of accounting. In connection with the foregoing transactions, we paid cash (net of cash acquired) in the aggregate amount of \$14, \$466, and \$245 million in 2002, 2001, and 2000, respectively, and issued aggregate UPS Class B common shares of 8.4 million in 2001. Pro forma results of operations have not been presented for any of the acquisitions because the effects of these transactions were not material on either an individual or aggregate basis. The results of operations of each acquired company are included in our statements of consolidated income from the date of acquisition. The purchase price allocations of acquired companies can be modified up to one year after the date of acquisition, however we expect such adjustments to the purchase price allocations to be immaterial.

The fair value of the assets and liabilities recorded each year as a result of these transactions is as follows (in millions):

	2002	2001	2000
Cash and marketable securities	\$ —	\$ 182	\$ 3
Accounts receivable, net	—	415	60
Finance receivables (current and non-current), net	—	259	—
Other current assets	—	97	5
Property, plant and equipment	—	202	37
Goodwill and intangible assets	14	764	284
Other assets	—	224	1
Accounts payable	—	(538)	(62)
Other liabilities	—	(279)	(26)
Long-term debt	—	(347)	(54)
	—	—	—
Consideration paid	\$ 14	\$ 979	\$248
	—	—	—
Cash consideration paid	\$ 14	\$ 469	\$248
Stock consideration paid	\$ —	\$ 510	\$ —

During 2001, we completed several acquisitions that were added to the non-package segment. We acquired Mail Boxes Etc., the world's largest franchisor of independently owned and operated business, communication, and shipping centers worldwide, for cash of \$185 million. We acquired Fritz Companies, Inc., a freight forwarding, customs brokerage and logistics company, for 7.3 million Class B common shares valued at \$456 million. Additionally, we acquired First International Bancorp, Inc., a provider of structured trade finance, commercial and government-backed lending products, for 1.1 million Class B common shares valued at \$54 million.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

Note 8. Long-Term Debt and Commitments

Long-term debt, as of December 31, consists of the following (in millions):

	2002	2001
8 3/8% debentures, due April 1, 2020(i)	\$ 424	\$ 424
8 3/8% debentures, due April 1, 2030(i)	276	276
Commercial paper(ii)	1,036	1,694
Industrial development bonds, Philadelphia Airport facilities, due December 1, 2015(iii)	100	100
Special facilities revenue bonds, Louisville Airport facilities, due January 1, 2029(iv)	149	149
Floating rate senior notes(v)	341	341
1.75% Cash-settled convertible senior notes, due September 27, 2007(vi)	323	291
Capitalized lease obligations(vii)	469	521
UPS Notes(viii)	568	486
5.50% Pound Sterling notes, due February 12, 2031	801	725
4.5% Singapore Dollar notes, due November 11, 2004	58	54
Installment notes, mortgages and bonds at various rates	57	105
	<u>4,602</u>	<u>5,166</u>
Less current maturities	<u>(1,107)</u>	<u>(518)</u>
	<u>\$ 3,495</u>	<u>\$4,648</u>

- (i) On January 22, 1998, we exchanged \$276 million of an original \$700 million in debentures for new debentures of equal principal with a maturity of April 1, 2030. The new debentures have the same interest rate as the 8 3/8% debentures due 2020 until April 1, 2020, and, thereafter, the interest rate will be 7.62% for the final 10 years. The 2030 debentures are redeemable in whole or in part at our option at any time. The redemption price is equal to the greater of 100% of the principal amount and accrued interest or the sum of the present values of the remaining scheduled payouts of principal and interest thereon discounted to the date of redemption at a benchmark treasury yield plus five basis points plus accrued interest. The remaining \$424 million of 2020 debentures are not subject to redemption prior to maturity. Interest is payable semiannually on the first of April and October for both debentures and neither debenture is subject to sinking fund requirements.
- (ii) The weighted average interest rate on the commercial paper outstanding as of December 31, 2002 and 2001, was 1.3% and 1.9%, respectively. At December 31, 2002, the entire commercial paper balance has been classified as a current liability, while \$1.25 billion was classified as long-term debt at December 31, 2001. The amount of commercial paper outstanding in 2003 is expected to fluctuate. We are authorized to borrow up to \$7.0 billion under the two commercial paper programs we maintain as of December 31, 2002.
- (iii) The industrial development bonds bear interest at a daily variable rate. The average interest rates for 2002 and 2001 were 1.3% and 2.5%, respectively.
- (iv) The special facilities revenue bonds bear interest at a daily variable rate. The average interest rates for 2002 and 2001 were 1.4% and 2.6%, respectively.
- (v) The floating rate senior notes bear interest at one-month LIBOR less 45 basis points. The average interest rates for 2002 and 2001 were 1.4% and 3.3%, respectively. These notes are callable at various times after

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

30 years at a stated percentage of par value, and putable by the note holders at various times after 10 years at a stated percentage of par value.

- (vi) The cash-settled convertible senior notes have a par value of \$300 million, bear interest at a stated rate of 1.75% and are callable after three years. The notes may be exchanged for an amount of cash that is indexed to the trading price of our Class B common stock. In conjunction with the debt offering, we entered into a swap transaction in which we pay 30-day LIBOR less 38 basis points, and we receive the 1.75% cash coupon plus any equity appreciation payable in cash on the notes. The average interest rate payable on the swap for 2002 and 2001 was 1.4% and 3.8%, respectively.
- (vii) We have capitalized lease obligations for certain aircraft, which are included in Property, Plant and Equipment at December 31 as follows (in millions):

	2002	2001
Aircraft	\$1,169	\$ 933
Accumulated amortization	(149)	(109)
	<u>\$1,020</u>	<u>\$ 824</u>

- (viii) The UPS Notes program involves the periodic issuance of fixed rate notes in \$1,000 increments with various terms and maturities. At December 31, 2002, the coupon rates of the outstanding notes varied between 4.00% and 6.40%, and the interest payments are made either monthly or semiannually. The maturities of the notes range from 2005 to 2017. Substantially all of the fixed obligations associated with the notes were swapped to floating rates, based on different LIBOR indices plus or minus a spread. The average interest rate payable on the swaps for 2002 and 2001 was 1.5% and 2.8%, respectively.

Based on the borrowing rates currently available to the Company for long-term debt with similar terms and maturities, the fair value of long-term debt, including current maturities, is approximately \$4.9 and \$5.3 billion as of December 31, 2002 and 2001, respectively.

We lease certain aircraft, facilities, equipment and vehicles under operating leases, which expire at various dates through 2052. Certain of the leases contain escalation clauses and renewal or purchase options. The following table sets forth the aggregate minimum lease payments under capitalized and operating leases, the aggregate annual principal payments due under our long-term debt, and the aggregate amounts expected to be spent for purchase commitments (in millions).

Year	Capitalized Leases	Operating Leases	Debt Principal	Purchase Commitments
2003	\$ 68	\$ 318	\$1,056	\$ 1,140
2004	68	251	61	810
2005	93	184	13	817
2006	68	136	10	737
2007	113	104	310	740
After 2007	241	555	2,656	1,314
Total	<u>651</u>	<u>\$ 1,548</u>	<u>\$4,106</u>	<u>\$ 5,558</u>
Less: imputed interest	(182)			
Present value of minimum capitalized lease payments	469			
Less: current portion	(51)			
Long-term capitalized lease obligations	<u>\$ 418</u>			

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As of December 31, 2002, we had outstanding letters of credit totaling approximately \$1.5 billion issued in connection with routine business requirements.

We maintain two credit agreements with a consortium of banks that provide revolving credit facilities of \$1.25 billion each, with one expiring April 24, 2003 and the other April 27, 2005. Interest on any amounts we borrow under these facilities would be charged at 90-day LIBOR plus 15 basis points. At December 31, 2002, there were no outstanding borrowings under these facilities. In addition, we maintain an extendible commercial notes program under which we are authorized to borrow up to \$500 million. No amounts were outstanding under this program at December 31, 2002.

We have a \$2.0 billion shelf registration statement under which we may issue debt securities in the U.S. The debt may be denominated in a variety of currencies. There was approximately \$1.552 billion issued under this shelf registration statement at December 31, 2002. We also maintain a \$1.0 billion European medium-term note program. Under this program, we may issue notes from time to time, denominated in a variety of currencies. At December 31, 2002, \$1.0 billion was available under this program.

Note 9. Deferred Taxes, Credits and Other Liabilities

Deferred taxes, credits and other liabilities as of December 31 consist of the following (in millions):

	2002	2001
Deferred federal and state income taxes	\$2,307	\$2,711
Insurance reserves	779	787
Other credits and noncurrent liabilities	515	326
	<u>\$3,601</u>	<u>\$3,824</u>

Note 10. Legal Proceedings and Contingencies

On August 9, 1999, the United States Tax Court held that we were liable for tax on income of Overseas Partners Ltd. (“OPL”), a Bermuda company that had reinsured excess value (“EV”) package insurance purchased by our customers beginning in 1984, and that we were liable for additional tax for the 1983 and 1984 tax years. The Court held that for the 1984 tax year we were liable for taxes of \$31 million on income reported by OPL, penalties and penalty interest of \$93 million, and interest for a total after-tax exposure estimated at approximately \$246 million.

The IRS took similar positions to those advanced in the Tax Court decision for tax years subsequent to 1984. Based on the Tax Court decision, we estimated that our total after-tax exposure for tax years 1984 through 1999 could have been as high as \$2.353 billion.

In our second quarter 1999 financial statements, we recorded a tax assessment charge of \$1.786 billion, which included an amount for related state tax liabilities. The charge included taxes of \$915 million and interest of \$871 million. This assessment resulted in a tax benefit of \$344 million related to the interest component of the assessment. As a result, our net charge to net income for the tax assessment was \$1.442 billion, increasing our total after-tax reserve at that time with respect to these matters to \$1.672 billion. The tax benefit of deductible interest was included in income taxes in 1999; however, since none of the income on which this tax assessment was based was our income, we did not classify the tax charge as income taxes.

We determined the size of our reserve with respect to these matters in accordance with accounting principles generally accepted in the United States of America. In 1999, we estimated our most likely liability based on the initial Tax Court decision. In making this determination, we concluded that, based on the Tax Court decision, it was more likely that we would be required to pay taxes on income reported by OPL and interest, but that it was not probable that we would be required to pay any penalties and penalty interest. In

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our prior estimation, if penalties and penalty interest ultimately were determined to be payable, we would have had to record an additional charge of up to \$681 million.

Further, as a result of the unfavorable Tax Court decision, and in order to stop the potential accrual of additional interest that might ultimately have been determined to be due to the IRS, on August 31, 1999 we paid \$1.349 billion, and on August 8, 2000 we paid an additional \$91 million, to the IRS related to these matters for the 1984 through 1994 tax years. We included the profit of the EV insurance program, using the IRS's methodology for calculating these amounts, for both 1998 and 1999 in filings we made with the IRS in 1999. In February 2000, we paid \$339 million to the IRS related to these matters for the 1995 through 1997 tax years.

On June 20, 2001, the United States Court of Appeals for the Eleventh Circuit reversed the Tax Court's decision. On September 13, 2001, the Eleventh Circuit denied the IRS's petition to have the appeal reheard en banc. The IRS did not attempt to appeal the case to the U.S. Supreme Court and, consequently, the case was remanded to the Tax Court to consider alternative arguments raised by the parties.

In January 2003, we and the IRS finalized settlement of all outstanding tax issues related to EV package insurance. Under the settlement of these issues, we agreed to adjustments that will result in income tax due of approximately \$562 million, additions to tax of \$60 million and related interest. The amount due to the IRS as a result of the settlement is less than amounts we previously had accrued (as described above). As a result, we recorded income, before taxes, of \$1.023 billion (\$776 million after tax) during the fourth quarter of 2002. The refunds and credits associated with this settlement are expected to occur over the next several years.

The EV program that was the subject of the Tax Court decision has been changed since September 1999. The revised arrangement should eliminate the issues considered by the Tax Court and the Eleventh Circuit related to OPL.

The IRS has proposed adjustments, unrelated to the EV package insurance matters discussed above, regarding the allowance of deductions and certain losses, the characterization of expenses as capital rather than ordinary, the treatment of certain income, and our entitlement to the investment tax credit and the research tax credit in the 1985 through 1990 tax years. The proposed adjustments would result in \$10 million of additional income tax expense. The IRS has also issued a report taking a similar position with respect to some of these issues for each of the years from 1991 through 1994. That report proposes adjustments that would result in \$50 million in additional income tax expense. In November 2002, the IRS issued a report taking a similar position with respect to some of these issues for each of the years 1995 through 1998. That report proposes adjustments that would result in \$13 million in additional income tax expense. For the 1985 through 1998 tax years, unpaid interest on these adjustments through December 31, 2002 could aggregate up to approximately \$381 million, after the benefit of related tax deductions. We expect that we will prevail on substantially all of these issues. Specifically, we believe that our practice of expensing the items that the IRS alleges should have been capitalized is consistent with the practices of other industry participants. The IRS may take similar positions with respect to some of these issues for each of the years 1999 through 2002. The IRS's proposed adjustments include penalties and penalty interest. We believe that the possibility that such penalties and penalty interest will be sustained is remote. We believe that the eventual resolution of these issues will not have a material adverse effect on our financial condition, results of operations or liquidity.

We are named as a defendant in 23 pending lawsuits that seek to hold us liable for the collection of premiums for EV insurance in connection with package shipments since 1984. Based on state and federal tort, contract and statutory claims, these cases generally claim that we failed to remit collected EV premiums to an independent insurer; we failed to provide promised EV insurance; we acted as an insurer without complying with state insurance laws and regulations; and the price for EV insurance was excessive.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

These actions all were filed after the August 9, 1999 Tax Court decision. As discussed above, on June 20, 2001, the U.S. Court of Appeals for the Eleventh Circuit ruled in our favor and reversed the Tax Court decision.

These 23 cases have been consolidated for pre-trial purposes in a multi-district litigation proceeding (“MDL Proceeding”) in federal court in New York. The Court has ruled on motions to dismiss, granting our motions to dismiss with respect to all of the plaintiffs’ tort claims and all of their breach of contract claims prior to August 26, 1994. Claims asserted under specific federal statutes, and breach of contract claims commencing on August 26, 1994, may proceed at this time. We intend to continue to seek dismissal of these remaining claims.

The defendants in the MDL Proceeding, including UPS, have stipulated to conditional certification of a plaintiff class in most of the lawsuits challenging the EV insurance program for our shippers. Class certification is a procedural step that allows claims to be resolved at one time as to all potential claimants; it does not depend on or reflect the merits of the underlying claims. Defendants may move later to set aside or modify the class certification.

The cases subject to the class certification stipulation will proceed to a single trial before the federal court presiding over the MDL Proceeding, instead of being returned for trial to the numerous federal courts around the country from which they were transferred. In addition, plaintiffs in the five cases with pending motions to remand to state court have withdrawn these motions.

In addition to the cases in which UPS is named as a defendant, there also is an action, *Smith v. Mail Boxes Etc.*, against Mail Boxes Etc. and its franchisees relating to UPS EV insurance purchased through Mail Boxes Etc. centers. This case also has been consolidated into the MDL Proceeding. The plaintiff has moved to have the case remanded back to state court.

We believe that the allegations in these cases have no merit and intend to continue to defend them vigorously. The ultimate resolution of these cases cannot presently be determined.

In addition, we are a defendant in various other lawsuits that arose in the normal course of business. We believe that the eventual resolution of these cases will not have a material adverse effect on our financial condition, results of operations or liquidity.

Note 11. Capital Stock and Stock-Based Compensation

Capital Stock

UPS maintains two classes of common stock, which are distinguished from each other by their respective voting rights. Class A shares of UPS are entitled to ten votes per share, whereas Class B shares are entitled to one vote per share. Class A shares are primarily held by UPS employees, and these shares are fully convertible into Class B shares at any time. Class B shares are publicly-traded on the New York Stock Exchange (NYSE) under the symbol “UPS”.

Incentive Compensation Plan

The UPS Incentive Compensation Plan permits the grant of nonqualified stock options, incentive stock options, stock appreciation rights, restricted stock, performance shares, performance units, and management incentive awards to eligible employees. The number of shares reserved for issuance under the Plan is 112 million, with the number of shares reserved for issuance as restricted stock limited to 34 million. As of December 31, 2002, management incentive awards, stock options, restricted stock, and performance shares had been granted under the Incentive Compensation Plan.

UNITED PARCEL SERVICE, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

Management Incentive Awards

Persons earning the right to receive Management Incentive Awards are determined annually by the Compensation Committee of the UPS Board of Directors. This Committee, in its sole discretion, determines the total award, which consists of UPS Class A common stock, given in any year. Amounts expensed for Management Incentive Awards were \$556, \$651, and \$735 million during 2002, 2001, and 2000, respectively.

Nonqualified and Incentive Stock Options

The Company maintains fixed stock option plans under which options are granted to purchase shares of UPS Class A common stock. Prior to adoption of the Incentive Compensation Plan, these options were granted at the current price of UPS shares as determined by the UPS Board of Directors on the date of option grant. Stock options granted in connection with the Incentive Compensation Plan must have an exercise price at least equal to the NYSE closing price of UPS Class B common stock on the date the option was granted.

Persons earning the right to receive stock options are determined each year by the Compensation Committee and the UPS Board of Directors. Except in the case of death, disability or retirement, options granted prior to the adoption of our Incentive Compensation Plan are exercisable only during a limited period after the expiration of five years from the date of grant, while options granted under the Incentive Compensation Plan are generally exercisable after three years from the date of grant and before the expiration of the option ten years after the date of grant. All options granted are subject to earlier cancellation or exercise under certain conditions.

The following is an analysis of options to purchase shares of Class A common stock issued and outstanding:

	2002		2001		2000	
	Weighted Average Price	Shares (in thousands)	Weighted Average Price	Shares (in thousands)	Weighted Average Price	Shares (in thousands)
Outstanding at beginning of year	\$ 29.64	29,224	\$ 20.57	29,312	\$ 18.76	38,480
Exercised	15.91	(6,434)	13.50	(5,918)	11.88	(7,277)
Granted	60.22	5,760	56.90	5,522	59.38	194
Assumed in acquisitions	—	—	58.41	727	—	—
Canceled	46.08	(805)	19.94	(419)	18.77	(2,085)
Outstanding at end of year	\$ 38.73	27,745	\$ 29.64	29,224	\$ 20.57	29,312

Options were granted to eligible employees under the 1996 Stock Option Plan in March 1999, but options will no longer be granted under that plan. Beginning in November 1999, options were granted under the Incentive Compensation Plan, and a limited option grant to certain employees under this plan occurred in 2000. Beginning in 2001 and in future years, options to eligible employees will generally be granted annually during the first half of each year at the discretion of the Board of Directors.

During 2001, we assumed employee stock options in connection with our acquisitions of Fritz Companies, Inc. and First International Bancorp, Inc. (see Note 7), which were converted into options to purchase UPS Class A common shares. Existing stock option plans at Fritz Companies, Inc. were assumed by UPS; however, options will no longer be granted under these plans. Existing stock option plans at First International Bancorp, Inc. were terminated upon the completion of the acquisition.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

The following table summarizes information about stock options outstanding and exercisable at December 31, 2002:

Exercise Price Range	Options Outstanding			Options Exercisable	
	Shares (in thousands)	Average Life (in years)	Average Exercise Price	Shares (in thousands)	Average Exercise Price
\$13.94 — \$16.60	6,757	0.33	\$ 16.00	3	\$ 16.17
\$19.93 — \$21.50	6,454	1.33	21.50	6	19.93
\$34.38 — \$50.63	3,148	6.81	49.93	3,118	49.93
\$55.00 — \$59.45	5,465	8.21	56.97	39	57.36
\$60.19 — \$143.13	5,921	9.11	60.68	190	73.94
	27,745	4.73	\$ 38.73	3,356	\$ 51.29

Discounted Employee Stock Purchase Plan

During 2001, the Company initiated an employee stock purchase plan for all eligible employees. Under the plan, shares of the Company’s Class A common stock may be purchased at quarterly intervals at 90% of the lower of the NYSE closing price on the first or the last day of each quarterly period. During 2002 and 2001, employees purchased 1.8 and 0.4 million shares at average prices of \$50.79 and \$46.78 per share, respectively.

Other Stock-Based Compensation

In connection with retention agreements for certain personnel, restricted stock awards for approximately 24,000 Class A shares had been granted, but not vested, as of December 31, 2002. These awards vest over remaining terms of up to two years.

Deferred Compensation Arrangements

The Company maintains a deferred compensation plan whereby certain employees may elect to defer the gains on stock option exercises by deferring the shares received upon exercise into a rabbi trust. The shares held in this trust are classified as treasury stock, and the liability to participating employees is classified as “Deferred Compensation Arrangements” in the shareowners’ equity section of the balance sheet. The amount of shares needed to settle the liability for deferred compensation arrangements is included in the denominator in both the basic and diluted earnings per share calculations.

Pro Forma Net Income and EPS Information

The Company applies the measurement provisions of APB Opinion 25 and related Interpretations in accounting for the stock-based compensation plans. Accordingly, no compensation expense has been recorded for the stock option or discounted employee stock purchase plans during 2002, 2001, or 2000.

Pro forma information regarding net income and earnings per share has been determined as if the Company accounted for the employee stock option and discounted employee stock purchase plans under the fair value method of FAS 123. For purposes of pro forma disclosures, the estimated fair value of the options granted is amortized to expense over the vesting period of the options.

UNITED PARCEL SERVICE, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

The pro forma information is as follows (in millions except per share amounts):

	2002	2001	2000
Net income	\$3,182	\$2,399	\$2,934
Pro forma stock-based compensation expense, net of tax	(68)	(51)	(27)
Pro forma net income	\$3,114	\$2,348	\$2,907
Basic earnings per share			
As reported	\$ 2.84	\$ 2.13	\$ 2.54
Pro forma	\$ 2.78	\$ 2.08	\$ 2.52
Diluted earnings per share			
As reported	\$ 2.81	\$ 2.10	\$ 2.50
Pro forma	\$ 2.75	\$ 2.05	\$ 2.47

The fair value of each option grant is estimated using the Black-Scholes option pricing model. The assumptions used, by year, and the calculated weighted average fair value of options granted, are as follows:

	2002	2001	2000
Expected yield	1.10%	1.10%	1.00%
Risk-free interest rate	4.67%	4.64%	6.26%
Expected life in years	5	5	5
Expected volatility	20.24%	32.40%	40.00%
Weighted average fair value of options granted	\$21.27	\$25.49	\$32.67

Note 12. Segment and Geographic Information

We report our operations in three segments: U.S. domestic package operations, international package operations and non-package operations. Package operations represent our core business and are broken down into regional operations around the world. Regional operations managers are responsible for both domestic and export operations within their geographic area.

U.S. Domestic Package

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

International Package

International package operations include delivery to more than 200 countries and territories worldwide, including shipments wholly outside the U.S. as well as shipments with either origin or distribution outside the U.S.

Non-Package

Non-package operations include UPS Supply Chain Solutions Group, Mail Boxes, Etc., and our excess value package insurance business. UPS Supply Chain Solutions Group (which offers the combined services of UPS Logistics Group, UPS Freight Services, UPS Capital, UPS Consulting and UPS Mail Innovations) provides supply chain design and management, freight forwarding, customs brokerage, mail services, multi-modal transportation, consulting, and financial services. Mail Boxes, etc. delivers personalized business solutions through a worldwide network of independently owned and operated business, communication, and shipping centers.

UNITED PARCEL SERVICE, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

In evaluating financial performance, we focus on operating profit as a segment's measure of profit or loss. Operating profit is before investment income, interest expense, and income taxes. The accounting policies of the reportable segments are the same as those described in the summary of accounting policies (see Note 1), with certain expenses allocated between the segments using activity-based costing methods. Unallocated assets are comprised primarily of cash, marketable securities and short-term investments.

Segment information as of, and for the years ended December 31 is as follows (in millions):

	2002	2001	2000
Revenue:			
U.S. domestic package	\$23,924	\$23,997	\$24,002
International package	4,680	4,245	4,078
Non-package	2,668	2,079	1,418
Consolidated	<u>\$31,272</u>	<u>\$30,321</u>	<u>\$29,498</u>
Operating Profit:			
U.S. domestic package	\$ 3,576	\$ 3,620	\$ 3,929
International package	322	125	277
Non-package	198	217	306
Consolidated	<u>\$ 4,096</u>	<u>\$ 3,962</u>	<u>\$ 4,512</u>
Assets:			
U.S. domestic package	\$14,662	\$16,180	\$15,032
International package	3,271	2,969	2,756
Non-package	6,245	4,846	2,430
Unallocated	2,179	641	1,444
Consolidated	<u>\$26,357</u>	<u>\$24,636</u>	<u>\$21,662</u>

Two changes were made during the first quarter of 2002, which affect revenue reporting within the non-package segment. Neither of these changes have any effect on current or prior period income. First, effective January 1, 2002, the results of operations of the Transportation Unit of our Logistics Group were moved to our Freight Services Group. Amounts in prior periods have been reclassified for comparison purposes.

Second, our Logistics Group has historically reported revenue from freight under management on a gross basis, whereas our Freight Services Group, which was formed with the acquisition of Fritz Companies, Inc. in the second quarter of 2001, reports revenue net of freight under management. Beginning with the first quarter of 2002, we are now reporting revenue for both the Logistics Group and Freight Services net of freight under management. Amounts for prior periods have been modified to reflect revenue net of freight under management for comparison purposes.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

Following is a reconciliation of gross to net revenue for the non-package segment (in millions):

	2002	2001	2000
UPS Logistics Group gross revenue	\$ 1,269	\$ 969	\$ 621
Less freight under management	(245)	(231)	(170)
Net revenue	1,024	738	451
UPS Freight Services gross revenue	2,004	1,318	488
Less freight under management	(1,059)	(577)	(103)
Net revenue	945	741	385
Other	699	600	582
Non-package revenue	\$ 2,668	\$2,079	\$1,418

Non-package operating profit included \$112, \$113, and \$101 million for 2002, 2001, and 2000, respectively, of intersegment profit, with a corresponding amount of operating expense, which reduces operating profit, included in the U.S. domestic package segment.

Revenue by product type for the years ended December 31 is as follows (in millions):

	2002	2001	2000
U.S. domestic package:			
Next Day Air	\$ 5,349	\$ 5,433	\$ 5,664
Deferred	2,868	2,893	2,910
Ground	15,707	15,671	15,428
Total U.S. domestic package	23,924	23,997	24,002
International package:			
Domestic	943	907	904
Export	3,276	2,931	2,818
Cargo	461	407	356
Total International package	4,680	4,245	4,078
Non-package:			
UPS Logistics Group	1,024	738	451
UPS Freight Services	945	741	385
Other	699	600	582
Total Non-package	2,668	2,079	1,418
Consolidated	\$31,272	\$30,321	\$29,498

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

Geographic information as of, and for the years ended, December 31 is as follows (in millions):

	2002	2001	2000
U.S.:			
Revenue	\$26,284	\$26,163	\$26,217
Long-lived assets	\$14,129	\$13,717	\$12,477
International:			
Revenue	\$ 4,988	\$ 4,158	\$ 3,281
Long-lived assets	\$ 2,874	\$ 3,050	\$ 2,061
Consolidated:			
Revenue	\$31,272	\$30,321	\$29,498
Long-lived assets	\$17,003	\$16,767	\$14,538

Revenue, for geographic disclosure, is based on the location in which service originates. Long-lived assets include property, plant and equipment, prepaid pension costs, long-term investments, goodwill and intangible assets.

Note 13. Other Operating Expenses

The major components of other operating expenses for the years ended December 31 are as follows (in millions):

	2002	2001	2000
Repairs and maintenance	\$1,044	\$1,050	\$ 958
Depreciation and amortization	1,464	1,396	1,173
Purchased transportation	1,556	1,652	1,679
Fuel	952	1,000	954
Other occupancy	513	524	412
Restructuring charge and related expenses (Note 17)	106	—	—
Other expenses	3,597	3,340	3,264
	<u>\$9,232</u>	<u>\$8,962</u>	<u>\$8,440</u>

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

Note 14. Income Taxes

The income tax expense (benefit) for the years ended December 31 consists of the following (in millions):

	2002	2001	2000
Current:			
Federal	\$1,208	\$1,065	\$1,676
State	148	151	215
Foreign	62	38	33
Total Current	<u>1,418</u>	<u>1,254</u>	<u>1,924</u>
Deferred:			
Federal	323	225	(21)
State	14	33	(3)
Total Deferred	<u>337</u>	<u>258</u>	<u>(24)</u>
Total	<u>\$1,755</u>	<u>\$1,512</u>	<u>\$1,900</u>

Income before income taxes includes income of foreign subsidiaries of \$16, \$8, and \$9 million in 2002, 2001, and 2000, respectively.

A reconciliation of the statutory federal income tax rate to the effective income tax rate for the years ended December 31 consists of the following:

	2002	2001	2000
Statutory federal income tax rate	35.0%	35.0%	35.0%
State income taxes (net of federal benefit)	2.1	3.1	2.9
Tax assessment reversal (tax portion)	(2.8)	—	—
Other	0.7	0.3	1.4
Effective income tax rate	<u>35.0%</u>	<u>38.4%</u>	<u>39.3%</u>

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Deferred tax liabilities and assets are comprised of the following at December 31 (in millions):

	2002	2001
Excess of tax over book depreciation	\$2,600	\$2,345
Pension plans	835	709
Other	675	867
Gross deferred tax liabilities	4,110	3,921
Other postretirement benefits	582	507
Loss carryforwards (foreign)	92	69
Insurance reserves	348	252
Vacation pay accrual	179	236
Excess deposits and interest to be refunded	619	—
Other	345	307
Gross deferred tax assets	2,165	1,371
Deferred tax assets valuation allowance	(92)	(69)
Net deferred tax assets	2,073	1,302
Net deferred tax liability	2,037	2,619
Current deferred tax (asset) liability	(270)	(92)
Long-term portion — see Note 9	\$2,307	\$2,711

The valuation allowance increased by \$23, decreased by \$32, and increased by \$22 million during the years ended December 31, 2002, 2001 and 2000, respectively.

We have foreign loss carryforwards of approximately \$232 million as of December 31, 2002, the majority of which may be carried forward indefinitely. These foreign loss carryforwards have been fully reserved in the deferred tax assets valuation allowance due to the uncertainty resulting from a lack of previous foreign taxable income within certain foreign tax jurisdictions.

UNITED PARCEL SERVICE, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

Note 15. Earnings per Share

The following table sets forth the computation of basic and diluted earnings per share (in millions except per share amounts):

	2002	2001	2000
Numerator:			
Net income before the cumulative effect of changes in accounting principles	\$3,254	\$2,425	\$2,934
Denominator:			
Weighted-average shares	1,117	1,124	1,152
Deferred compensation arrangements	3	2	1
Denominator for basic earnings per share	1,120	1,126	1,153
Effect of dilutive securities:			
Contingent shares -			
Management incentive awards	4	5	6
Stock option plans	10	13	16
Denominator for diluted earnings per share	1,134	1,144	1,175
Basic Earnings Per Share Before Cumulative Effect of Changes in Accounting Principles	\$ 2.91	\$ 2.15	\$ 2.54
Diluted Earnings Per Share Before Cumulative Effect of Changes in Accounting Principles	\$ 2.87	\$ 2.12	\$ 2.50

Diluted earnings per share for the years ended December 31, 2002, 2001, and 2000 exclude the effect of 103,000, 6,627,000, and 134,000 shares, respectively, of common stock that may be issued upon the exercise of employee stock options because such effect would be antidilutive.

Note 16. Derivative Instruments and Risk Management

We are exposed to market risk, primarily related to commodity prices, foreign exchange, interest rates and equity prices. These exposures are actively monitored by management. To manage the volatility relating to these exposures, we enter into a variety of derivative financial instruments. Our objective is to reduce, where it is deemed appropriate to do so, fluctuations in earnings and cash flows associated with changes in commodity prices, foreign currency rates, interest rates and equity prices. It is our policy and practice to use derivative financial instruments only to the extent necessary to manage exposures. As we use price sensitive instruments to hedge a certain portion of our existing and anticipated transactions, we expect that any loss in value for those instruments generally would be offset by increases in the value of those hedged transactions.

We do not hold or issue derivative financial instruments for trading or speculative purposes.

Commodity Price Risk Management

We are exposed to an increase in the prices of refined fuels, principally jet-A, diesel, and unleaded gasoline. Additionally, we are exposed to an increase in the prices of other energy products, principally natural gas and electricity. We use a combination of options, swaps, and futures contracts to provide partial protection from rising fuel and energy prices. The net fair value of such contracts subject to price risk, excluding the underlying exposures, as of December 31, 2002 and 2001 was an asset (liability) of approximately \$34 and \$(27) million, respectively. We have designated and account for these contracts as cash flow hedges, and,

UNITED PARCEL SERVICE, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

therefore, the resulting gains and losses from these hedges are recognized as a component of fuel expense or other occupancy expense when the underlying fuel or energy product being hedged is consumed.

Foreign Currency Exchange Risk Management

We have foreign currency risks related to our revenue, operating expenses, and financing transactions in currencies other than the local currencies in which we operate. We are exposed to currency risk from the potential changes in functional currency values of our foreign currency denominated assets, liabilities, and cash flows. Our most significant foreign currency exposures relate to the Euro and the British Pound Sterling. We use a combination of purchased and written options and forward contracts to hedge currency cash flow exposures. As of December 31, 2002 and 2001, the net fair value of the hedging instruments described above was an asset (liability) of approximately \$(3) and \$4 million, respectively. We have designated and account for these contracts as cash flow hedges of anticipated foreign currency denominated revenue and, therefore, the resulting gains and losses from these hedges are recognized as a component of international revenue when the underlying sales occur.

Interest Rate Risk Management

Our indebtedness under our various financing arrangements creates interest rate risk. We use a combination of derivative instruments, including interest rate swaps and cross-currency interest rate swaps, as part of our program to manage the fixed and floating interest rate mix of our total debt portfolio and related overall cost of borrowing. These swaps are entered into concurrently with the issuance of the debt that they are intended to modify, and the notional amount, interest payment, and maturity dates of the swaps match the terms of the associated debt. Interest rate swaps allow us to maintain a target range of floating rate debt.

We have designated and account for these contracts as either hedges of the fair value of the associated debt instruments, or as hedges of the variability in expected future interest payments. Any periodic settlement payments are accrued monthly, as either a charge or credit to interest expense, and are not material to net income. The net fair value of our interest rate swaps at December 31, 2002 and 2001 was a liability of approximately \$(62) and \$(74) million, respectively.

Equity Price Risk Management

We hold investments in various available-for-sale equity securities which are subject to price risk. We use combinations of options to hedge the price risk exposure inherent in these securities. The fair value of such options contracts designated as hedges, as of December 31, 2002 and 2001, was an asset of approximately \$219 and \$214 million, respectively, which is classified in marketable securities and short-term investments.

Credit Risk

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 large banks and financial institutions that meet established credit guidelines. We do not expect to incur any losses as a result of counterparty default.

Derivatives Not Designated As Hedges

Derivatives not designated as hedges primarily consist of interest rate swaps that are used to hedge a portfolio of small debt instruments. Although these instruments are effective as hedges from an economic perspective, they do not qualify for hedge accounting under FAS 133, as amended. The impact from these interest rate swaps on our results was immaterial. Additionally, we have a small portfolio of stock warrants in

UNITED PARCEL SERVICE, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

public and private companies that are held for investment purposes. These warrants are recorded at fair value, and the impact of these warrants on our results was immaterial.

Income Effects of Derivatives

In the context of hedging relationships, “effectiveness” refers to the degree to which fair value changes in the hedging instrument offset corresponding changes in the hedged item. Certain elements of hedge positions cannot qualify for hedge accounting under FAS 133 whether effective or not, and must therefore be marked to market through income. Both the effective and ineffective portions of gains and losses on hedges are reported in the income statement category related to the hedged exposure. The following table summarizes the earnings effect of such items for the years ended December 31 (in millions):

	2002	2001
	—	—
Cash Flow Hedges:		
Ineffectiveness	\$ 1	\$(2)
Amounts excluded from the measure of effectiveness	—	5
Fair Value Hedges:		
Ineffectiveness	(1)	(2)
Amounts excluded from the measure of effectiveness	—	2

As of December 31, 2002, \$27 million in gains related to cash flow hedges that are currently deferred in OCI are expected to be reclassified to income over the 12 month period ending December 31, 2003. The actual amounts that will be reclassified to income over the next 12 months will vary from this amount as a result of changes in market conditions. No amounts were reclassified to income during 2002 in connection with forecasted transactions that were no longer considered probable of occurring.

At December 31, 2002, the maximum term of derivative instruments that hedge forecasted transactions, except those related to cross-currency interest rate swaps on existing financial instruments, was 5 years. We maintain cross-currency interest rate swaps that extend through 2009.

Fair Value of Financial Instruments

At December 31, 2002 and 2001, our financial instruments included cash and cash equivalents, marketable securities and short-term investments, accounts receivable, finance receivables, accounts payable, short-term and long-term borrowings, and commodity, interest rate, foreign currency, and equity options, forwards, and swaps. The fair values of cash and cash equivalents, accounts receivable, and accounts payable approximate carrying values because of the short-term nature of these instruments. The fair value of our marketable securities and short-term investments is disclosed in Note 2, finance receivables in Note 3, and debt instruments in Note 8.

Note 17. Restructuring Charge and Related Expenses

In the fourth quarter of 2002, the Company initiated a restructuring program to combine UPS Freight Services and the UPS Logistics Group into a single business unit (“Supply Chain Solutions”). In connection with this restructuring program, the Company also recorded certain costs related to the integration of activities between UPS Capital and First International Bank.

The total cost of the program is estimated at \$127 million, of which \$106 million was recorded in 2002. The program will be completed by the end of 2003. The program is designed to facilitate business growth, streamline management decision-making, reduce the cost structure, and provide higher levels of service to our customers.

UNITED PARCEL SERVICE, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

Costs of the program include employee severance costs, asset impairments, costs associated with the consolidation of facilities, and other costs directly related to the restructuring program. The costs incurred in connection with this program in 2002 are classified in other operating expenses in the income statement (see Note 13).

Set forth below is a summary of activity related to the restructuring program and resulting liability for the year ended December 31, 2002:

	Employee Severance	Asset Impairment	Facility Consolidation	Other	Total
Balance at January 1, 2002	\$ —	\$ —	\$ —	\$ —	\$ —
Expenses accrued	19	42	25	20	106
Cash spent	(4)	—	—	(8)	(12)
Charges against assets	—	(42)	(8)	—	(50)
Balance at December 31, 2002	\$ 15	\$ —	\$ 17	\$ 12	\$ 44

Employee Severance

Employee severance costs relate to severance packages for approximately 800 people. The packages are involuntary and are formula-driven based on salary levels and past service. The current and planned separations span the entire Supply Chain Solutions unit, including the operations, information technology, finance, accounting, and business development functions.

Asset Impairment

Asset impairment charges result from establishing new carrying values for assets that have been abandoned. Impaired assets consist primarily of capitalized software that is no longer used as a result of changes in business strategy due to the restructuring.

Facility Consolidation

Facility consolidation costs are associated with terminating operating leases on offices, warehouses, and other facilities.

Other Costs

Other costs consist primarily of employee relocations, legal costs associated with establishing the new organizational structure, costs associated with moving equipment, records, inventories between locations, and conforming accounting policies among recently acquired entities within Supply Chain Solutions.

Note 18. September 11, 2001 Events

In response to the September 11, 2001 terrorist attacks, the FAA issued a federal ground stop order prohibiting all flights to, from, and within the United States. Due to this order, all domestic UPS aircraft were grounded, and international flights into the United States were diverted, on September 11th and 12th. We were able to transport many of our express shipments through our extensive ground network until the FAA order was lifted and our air operations resumed on the evening of September 13th. Due to the economic disruption caused by these events, we sustained significant declines in our U.S. origin package volume during the weeks following the attacks.

On September 22, 2001, President Bush signed into law the Air Transportation Safety and System Stabilization Act (the "Act"), a \$15 billion emergency economic assistance package to mitigate the dramatic

UNITED PARCEL SERVICE, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

financial losses experienced by the nation's air carriers. The Act, among other things, provides for the following: (1) \$5 billion in compensation for direct losses incurred as a result of the federal ground stop order, and for incremental losses incurred through December 31 as a result of the attacks, (2) \$10 billion in federal loan guarantees and credits, (3) expanded war risk insurance coverage for air carriers, and (4) government assistance for short-term increases in insurance premiums. We submitted a claim for compensation to the Department of Transportation and recognized a pre-tax amount of \$74 million related to this reimbursement as a credit to the other expenses line item of other operating expenses (see Note 13) in 2001 under the provisions of EITF 01-10 "Accounting for the Impact of Terrorist Attacks of September 11, 2001".

Note 19. Quarterly Information (unaudited)

	First Quarter		Second Quarter		Third Quarter		Fourth Quarter	
	2002*	2001	2002	2001	2002	2001	2002	2001
Revenue:								
U.S. domestic package	\$5,903	\$5,976	\$5,908	\$5,981	\$5,889	\$5,806	\$6,224	\$6,234
International package	1,054	1,074	1,144	1,050	1,184	1,012	1,298	1,109
Non-package	622	385	630	460	681	580	735	654
Total revenue	7,579	7,435	7,682	7,491	7,754	7,398	8,257	7,997
Operating profit (loss):								
U.S. domestic package	862	845	899	966	809	895	1,006	914
International package	30	39	62	24	65	(4)	165	66
Non-package	55	60	67	51	76	52	—	54
Total operating profit	947	944	1,028	1,041	950	943	1,171	1,034
Net income	\$ 491	\$ 556	\$ 611	\$ 630	\$ 578	\$ 568	\$1,502	\$ 645
Earnings per share:								
Basic	\$ 0.44	\$ 0.49	\$ 0.55	\$ 0.56	\$ 0.52	\$ 0.50	\$ 1.34	\$ 0.57
Diluted	\$ 0.43	\$ 0.48	\$ 0.54	\$ 0.55	\$ 0.51	\$ 0.50	\$ 1.32	\$ 0.57

* First quarter 2002 results have been restated to reflect the \$72 million cumulative effect of change in accounting principle relating to the adoption of FAS 142.

EXHIBIT INDEX

Exhibit No.	Description
2.1	— Agreement and Plan of Merger, dated as of September 22, 1999, among United Parcel Service of America, Inc., United Parcel Service, Inc. and UPS Merger Subsidiary, Inc. (incorporated by reference to the registration statement on Form S-4 (No. 333-83349), filed on July 21, 1999, as amended).
2.2	— Agreement and Plan of Merger, dated as of January 10, 2001, by and among United Parcel Service, Inc., VND Merger Sub, Inc. and Fritz Companies, Inc. (incorporated by reference to Annex A to the registration statement on Form S-4 (No. 333-58268), filed on April 4, 2001, as amended).
2.3	— Agreement and Plan of Merger, dated as of January 15, 2001, by and among United Parcel Service, Inc., First International Bancorp, Inc. and Stag Merger Company, Inc. (incorporated by reference to Appendix A to the registration statement on Form S-4 (No. 333-58660), filed on April 11, 2001, as amended).
3.1	— Form of Restated Certificate of Incorporation of United Parcel Service, Inc. (incorporated by reference to Exhibit 3.2 to Form 10-Q for the Quarter Ended June 30, 2002).
3.2	— Form of Bylaws of United Parcel Service, Inc. (incorporated by reference to Exhibit 3.2 to the registration statement on Form S-4 (No. 333-83349), filed on July 21, 1999, as amended).
4.1	— Form of Class A Common Stock Certificate (incorporated by reference to Exhibit 4.1 to the registration statement on Form S-4 (No. 333-83349), filed on July 21, 1999, as amended).
4.2	— Form of Class B Common Stock Certificate (incorporated by reference to Exhibit 4.2 to the registration statement on Form S-4 (No. 333-83349), filed on July 21, 1999).
4.3	— Specimen Certificate of 8 3/8% Debentures due April 1, 2020 (incorporated by reference to Exhibit 4(c) to Registration Statement No. 33-32481, filed December 7, 1989).
4.4	— Indenture relating to 8 3/8% Debentures due April 1, 2020 (incorporated by reference to Exhibit 4(c) to Registration Statement No. 33-32481, filed December 7, 1989).
4.5	— Specimen Certificate of 8 3/8% Debentures due April 1, 2030 (incorporated by reference to Exhibit T-3C to Form T-3 filed December 18, 1997).
4.6	— Indenture relating to Exchange Offer Notes Due 2030 (incorporated by reference to Exhibit T-3C to Form T-3 filed December 18, 1997).
4.7	— Indenture relating to \$2,000,000,000 of debt securities (incorporated by reference to Exhibit 4.1 to Pre-Effective Amendment No. 1 to Registration Statement on Form S-3 (No. 333-08369), filed on January 26, 1999).
4.8	— Form of Supplemental Indenture relating to \$2,000,000,000 of debt securities (incorporated by reference to Exhibit 4.2 to Post-Effective Amendment No. 1 to Registration Statement on Form S-3 (No. 333-08369-01), filed on March 15, 2000).
4.9	— Underwriting Agreement relating to 1.75% Cash-Settled Convertible Senior Notes due September 27, 2007 (incorporated by reference to Exhibit 1 to Form 10-Q for the Quarter Ended September 30, 2000).
4.10	— Selling Agent Agreement relating to UPS Notes with maturities of 9 months or more from date of issue (incorporated by reference to Exhibit 1.1 to Form 8-K filed December 20, 2001) and Form of Note (incorporated by reference to Exhibit 4.1 to Form 8-K filed December 20, 2001).
4.11	— Form of Second Supplemental Indenture relating to \$2,000,000,000 of debt securities (incorporated by reference to Exhibit 4 to Form 10-Q for the Quarter Ended September 30, 2001).

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Exhibit No.	Description
10.1	— UPS Thrift Plan, as Amended and Restated, including Amendment Nos. 1 through 24 (incorporated by reference to Exhibit 10.1 to 2001 Annual Report on Form 10-K).
10.2	— †(1) Amendment No. 25 to the UPS Thrift Plan. UPS Retirement Plan (including Amendment Nos. 1-4) (incorporated by reference to Exhibit 9 to 1979 Annual Report on Form 10-K). (1) Amendment No. 5 to the UPS Retirement Plan (incorporated by reference to Exhibit 20(a) to 1980 Annual Report on Form 10-K). (2) Amendment No. 6 to the UPS Retirement Plan (incorporated by reference to Exhibit 19(a) to 1983 Annual Report on Form 10-K). (3) Amendment No. 7 to the UPS Retirement Plan (incorporated by reference to Exhibit 10(b)(3) to 1984 Annual Report on Form 10-K). (4) Amendment No. 8 to the UPS Retirement Plan (incorporated by reference to Exhibit 10(b)(4) to 1985 Annual Report on Form 10-K). (5) Amendment No. 9 to the UPS Retirement Plan (incorporated by reference to Exhibit 10(b)(5) to 1985 Annual Report on Form 10-K). (6) Amendment No. 10 to the UPS Retirement Plan (incorporated by reference to Exhibit 19(a) to 1988 Annual Report on Form 10-K). (7) Amendment No. 11 to the UPS Retirement Plan (incorporated by reference to Exhibit 19(b) to 1988 Annual Report on Form 10-K). (8) Amendment No. 12 to the UPS Retirement Plan (incorporated by reference to Exhibit 10(b)(8) to 1989 Annual Report on Form 10-K). (9) Amendment No. 13 to the UPS Retirement Plan (incorporated by Reference to Exhibit 10(b)(9) to 1989 Annual Report on Form 10-K). (10) Amendment No. 14 to the UPS Retirement Plan (incorporated by reference to Exhibit 10(b)(10) to 1990 Annual Report on Form 10-K). (11) Amendment No. 15 to the UPS Retirement Plan (incorporated by reference to Exhibit 10(b)(11) to 1992 Annual Report on Form 10-K). (12) Amendment No. 16 to the UPS Retirement Plan (incorporated by reference to Exhibit 10(b)(12) to 1994 Annual Report on Form 10-K). (13) Amendment No. 17 to the UPS Retirement Plan (incorporated by reference to Exhibit 10(b)(13) to 1994 Annual Report on Form 10-K). (14) Amendment No. 18 to the UPS Retirement Plan (incorporated by reference to Exhibit 10(b)(14) to 1995 Annual Report on Form 10-K). (15) Amendment No. 19 to the UPS Retirement Plan (incorporated by reference to Exhibit 10(b)(15) to 1995 Annual Report on Form 10-K). (16) Amendment No. 20 to the UPS Retirement Plan (incorporated by reference to Exhibit 10(b)(16) to 1995 Annual Report on Form 10-K). (17) Amendment No. 21 to the UPS Retirement Plan (incorporated by reference to Exhibit 10(b)(17) to 1996 Annual Report on Form 10-K). (18) Amendment No. 22 to the UPS Retirement Plan (incorporated by reference to Exhibit 10(b)(18) to 1997 Annual Report on Form 10-K). (19) Amendment No. 23 to the UPS Retirement Plan (incorporated by reference to Exhibit 10(b)(19) to 1998 Annual Report on Form 10-K). (20) Amendment No. 24 to the UPS Retirement Plan (incorporated by reference to Exhibit 10(b)(20) to 2000 Annual Report on Form 10-K).

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Exhibit No.	Description
	(21) Amendment No. 25 to the UPS Retirement Plan (incorporated by reference to Exhibit 10(b)(20) to 2000 Annual Report on Form 10-K).
	(22) Amendment No. 26 to the UPS Retirement Plan (incorporated by reference to Exhibit 10.2(22) to 2001 Annual Report on Form 10-K).
	†(23) Amendment No. 27 to the UPS Retirement Plan.
	†(24) Amendment No. 28 to the UPS Retirement Plan.
10.3	— UPS Savings Plan, as Amended and Restated, including Restatement Amendment Nos. 1 through 8 (incorporated by reference to Exhibit 10.3 to 2001 Annual Report on Form 10-K).
10.4	— Credit Agreement (364-Day Facility), as amended and restated, dated April 25, 2002 among United Parcel Service, Inc., the initial lenders named therein, Salomon Smith Barney Inc., as Arranger, and Bank of America, N.A. and Bank One, as Co-Documentation Agents, and Citibank, N.A., as Administrative and Syndication Agent (incorporated by reference to Exhibit 10(a) to Quarterly Report on Form 10-Q for the Quarter Ended March 31, 2002).
10.5	— Credit Agreement (Five-Year Facility), as amended and restated, dated April 26, 2001 among United Parcel Service, Inc., the initial lenders named therein, Salomon Smith Barney Inc., as Co-Arranger, Bank of America Securities, LLC, as Co-Arranger, Bank of America N.A., as Documentation Agent, and Citibank, N.A., as Administrative and Syndication Agent (incorporated by reference to Exhibit 10(b) to Quarterly Report on Form 10-Q for the Quarter Ended March 31, 2001).
10.6	— UPS Excess Coordinating Benefit Plan (incorporated by reference to Exhibit 10(s) to 1997 Annual Report on Form 10-K).
10.7	— UPS 1996 Stock Option Plan, as amended and restated (incorporated by reference to Exhibit 10(a) to Quarterly Report on Form 10-Q for the Quarter ended September 30, 1997).
10.8	— UPS Qualified Stock Ownership Plan and Trust Agreement (incorporated by reference to Exhibit 4.1 to Registration Statement No. 333-67479, filed November 18, 1998). (1) Amendment No. 1 to the UPS Qualified Stock Ownership Plan and Trust Agreement (incorporated by reference to Exhibit 10.19(1) to 1999 Annual Report on Form 10-K). (2) Amendment No. 2 to the UPS Qualified Stock Ownership Plan and Trust Agreement (incorporated by reference to Exhibit 10.19(2) to 1999 Annual Report on Form 10-K). (3) Amendment No. 3 to the UPS Qualified Stock Ownership Plan and Trust Agreement (incorporated by reference to Exhibit 10.19(3) to 1999 Annual Report on Form 10-K). (4) Amendment No. 4 to the UPS Qualified Stock Ownership Plan and Trust Agreement (incorporated by reference to Exhibit 10.19(4) to 2000 Annual Report on Form 10-K). (5) Amendment No. 5 to the UPS Qualified Stock Ownership Plan and Trust Agreement (incorporated by reference to Exhibit 10.8(5) to 2001 Annual Report on Form 10-K). (6) Amendment No. 6 to the UPS Qualified Stock Ownership Plan and Trust Agreement (incorporated by reference to Exhibit 10.8(6) to 2001 Annual Report on Form 10-K). †(7) Amendment No. 7 to the UPS Qualified Stock Ownership Plan and Trust Agreement.
10.9	— Form of United Parcel Service, Inc. Incentive Compensation Plan (incorporated by reference to the registration statement on Form S-4 (No. 333-83349), filed on July 21, 1999, as amended).
10.10	— UPS Deferred Compensation Plan (incorporated by reference to Exhibit 10.10 to 2000 Annual Report on Form 10-K).
10.11	— United Parcel Service, Inc. Nonqualified Employee Stock Purchase Plan (incorporated by reference to the registration statement on Form S-8 (No. 333-34054), filed on April 5, 2000).

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Exhibit No.	Description
10.12	— Form of United Parcel Service, Inc. Discounted Employee Stock Purchase Plan (incorporated by reference to Appendix B to Definitive Proxy Statement for 2001 Annual Meeting of Shareowners).
†21	— Subsidiaries of the Registrant.
†23	— Consent of Deloitte & Touche LLP.
†99.1	— Certificate of Chief Executive Officer Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
†99.2	— Certificate of Chief Financial Officer Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

† Filed herewith.

AMENDMENT NO. 25

TO

THE UPS THRIFT PLAN

WHEREAS, United Parcel Service of America, Inc. ("UPS"), terminated the UPS Thrift Plan (the "Plan") effective July 25, 2001 and filed a form 5310, Application for Determination for Terminating Plan with the Internal Revenue Service;

WHEREAS, the Application for Determination requires that the Plan be amended for the Uruguay Round Agreements Act of 1993 ("GATT"), the Uniformed Services Employment and Reemployment Rights Act of 1994 ("USERRA"), the Small Business Job Protection Act of 1996 ("SBJPA"), and the Taxpayer Relief Act of 1997 ("TRA-97"), law changes; and the Community Renewal Act of 2000 ("CRA-00") amendments.

WHEREAS, the Internal Revenue Service has responded to the Application for Determination and proposed certain Plan amendments that, if adopted, will bring the Plan into compliance with these required legislative changes;

NOW, THEREFORE, effective as of July 25, 2001 unless otherwise specified in the amendments that follow, the Plan is hereby amended as follows:

1. Section 1.1 (i) is amended in its entirety to read as follows:

"Employee" means a person who is in the Regular Employment of an Employer. For purposes of this Plan, a citizen of the United States who is transferred from Regular Employment with a domestic Employer to employment with a foreign corporation at least 90% of whose voting stock is owned by, or for the benefit of the stockholders of United Parcel Service of America, Inc., and as to which foreign corporation a domestic Employer Corporation has entered into an agreement pursuant to Section 3121(1) of the Internal Revenue Code of 1986 ("Code"), as amended, shall be deemed an employee of United Parcel Service of America, Inc., during such time as he remains in the Regular Employment of the foreign corporation and the foreign corporation remains covered under such agreement.

The term "Employee" shall not include an individual employed as a leased employee as that term is defined in Code Section 414(n)(2). Leased employee is defined as any person (other than an employee of the recipient) who pursuant to an agreement between the recipient and any other person ("leasing organization") has performed services for the recipient (or for the recipient and related persons) on a substantially full-time basis for a period of at least 1 year, and such services are performed under the primary direction or control of the recipient.

2. Section 10.5 (a) is amended in its entirety to read as follows:

(a) With respect to any distribution described in this Plan which constitutes an eligible rollover distribution within the meaning of Code Section 401(a)(31), the distributee thereof shall, in accordance with procedures established by the Committee, be afforded the opportunity to direct that such distribution be transferred directly to the trustee of an eligible retirement plan (a "direct rollover"). For purposes of the foregoing sentence, an "eligible retirement plan" is (1) a qualified trust within the meaning of Code Section 402 which is a defined contribution plan the terms of which permit the acceptance of rollover distributions, (2) an individual retirement account or annuity within the meaning of Code Section 408 (other than an endowment contract), or (3) an annuity plan within the meaning of Code Section 403(a), which is specified by the distributee in such form and at such time as the Committee may prescribe. Effective for plan years beginning after December 31, 1999, an "eligible rollover distribution" means any distribution to an employee of all or any portion of the balance to the credit of the employee in a qualified trust; except that such term shall not include: 1) any distribution which is one of a series of substantially equal periodic payments (not less frequently than annually) made for the life (or life expectancy) of the employee or the joint lives (or joint life expectancies) of the employee and the employee's designated beneficiary, or for a specified period of 10 years or more; 2) any distribution to the extent that such distribution is required under Code Section 401(a)(9); and 3) any hardship distribution described in Code Section 401(k)(2)(B)(i)(IV), which is attributable to an employee's elective contributions under Treasury Regulation Section 1.401(k)-1(d)(2)(ii).

3. Section 19.7 is amended by adding the following:

(c) This Section 19.7 shall apply to plan years beginning before January 1, 2000.

4. Sections 6.1, 6.2 and 19.2(i) are amended by the following model language. This model language shall be adopted in its proposed format and shall be incorporated by reference with respect to the Plan's existing language. It is intended that the model language will override the existing Plan language where

deemed appropriate and shall be come and integral part of the Plan document as of the effective dates set forth herein.

MODEL LANGUAGE

A. Model language for Code Section 415(c)(3) compensation definition.

For limitation years beginning on and after January 1, 2001, for purposes of applying the limitations described in Sections 6.1 and 6.1 of the Plan, compensation paid or made available during such limitation years shall include elective amounts that are not includable in the gross income of the employee by reason of Code Section 132(f)(4).

This amendment shall also apply to the definition of compensation for purposes of Section 19.2(i) of the Plan for plan years beginning on and after January 1, 2001.

B. Model language for Code Section 414(s) compensation definition that excludes amounts of compensation reduction elected for qualified transportation fringes.

For plan years beginning on and after January 1, 2001, compensation shall not include elective amounts that are not includable in the gross income of the employee under Code Sections 125, 132(f)(4), 402(e)(3), 402(h), or 403(b). This amendment shall apply for purposes of Section 6.2 of the Plan.

IN WITNESS WHEREOF, the undersigned certify that United Parcel Service of America, Inc., based upon action by its Board of Directors on May 3, 2002 has caused this Amendment No. 25 to the Plan to be adopted.

<TABLE>
<CAPTION>

ATTEST:

UNITED PARCEL SERVICE OF
AMERICA, INC.

<S>

<C>

/s/ JOSEPH R. MODEROW

/s/ MICHAEL L. ESKEW

Joseph R. Moderow
Secretary

Michael L. Eskew
Chairman

</TABLE>

AMENDMENT NO. 27

TO THE

UPS RETIREMENT PLAN

WHEREAS, United Parcel Service of America, Inc. ("UPS") and its affiliated corporations established the UPS Retirement Plan ("Plan") for the benefit of their eligible employees, in order to provide benefits to those employees upon their retirement, disability, or death, effective as of September 1, 1961;

WHEREAS, the Plan, as adopted and amended from time to time, was amended and restated in its entirety, effective as of January 1, 1976, to comply with the Employee Retirement Income Security Act of 1974;

WHEREAS, the Plan has been amended on a number of occasions since January 1, 1976, the most recent being Amendment No. 26; and

WHEREAS, it is desired to amend the Plan to reflect the merger of certain assets and liabilities of the Overseas Partners Ltd. And Subsidiaries Retirement Plan and related trust into the Plan effective as of March 1, 2002.

NOW THEREFORE, pursuant to the authority vested in the Board of Directors by Section 7.1 of the Plan, the UPS Retirement Plan is hereby amended as follows:

1. The Plan is hereby amended effective as of March 1, 2002 to add a new Article XIV which reads as follows:

ARTICLE XIV - SPECIAL OPL RETIREMENT BENEFIT

Section 14.1 Special OPL Retirement Benefit. Notwithstanding any other provision in this Plan, the provisions in this Article XIV shall apply to the terms of the participation of any Grandfathered OPL Participant to the extent that such provisions are different from or supplement the provisions otherwise set forth in this Plan.

Section 14.2 Definitions.

- (a) "Compensation" generally has the same meaning set forth in Section 1.1(y); however, for a Grandfathered OPL Participant who completes an Hour of Service as an Employee on or after March 1, 2002 determined without regard to this Section 14.2, Compensation shall also include remuneration actually paid by OPL to such Grandfathered OPL Participant for the applicable year to the extent such remuneration was included as "compensation" under the OPL Plan.
- (b) "Employer Company" generally has the same meaning set forth in Section 1.1(b); however, solely with respect to a Grandfathered OPL Participant, OPL also shall be considered an Employer Company.
- (c) "Grandfathered OPL Participant" means a former participant in the OPL Plan who is listed on Appendix H.
- (d) "Hour of Service" generally has the same meaning set forth in Section 1.1(n); however, for a Grandfathered OPL Participant who completes an Hour of Service as an Employee on or after March 1, 2002 determined without regard to this Section 14.2, an Hour of Service shall also include an hour of service with OPL and any employer that would be considered a single employer with OPL under Section 414(b), (c), (m) and (o) of the Code to the extent such hour of service was included as an "hour of service" under the OPL Plan.

Solely for purposes of entitlement to retiree medical benefits under Article XII, including the determination of whether such Grandfathered OPL Participant is a Grandfathered Retired Participant, each Grandfathered OPL Participant shall be deemed to have an Hour of Service for each "hour of service" he or she was credited with under the OPL Plan.

- (e) "OPL" means the Overseas Partners Ltd, Overseas Partners Capital Corporation and any other employer that participated in the OPL Plan on March 1, 2002.
- (f) "OPL Minimum Benefit" means the protected minimum benefit described in Section 14.4(b).
- (g) "OPL Plan" means the Overseas Partners Ltd. and Subsidiaries Retirement Plan, as amended and restated effective as of

January 1, 2000, and as further amended through April 15, 2001.

Section 14.3 OPL RPA Point Service Assumption. A Grandfathered OPL Participant who completes an Hour of Service as an Employee on or after March 1, 2002 determined without regard to Section 14.2 shall be subject to Appendix F-1 with respect to his or her RPA Point accrual until the later of January 1, 2001 or his or her actual reemployment commencement date with an Employer Company without regard to Section 14.2(b). Beginning on the later of January 1, 2001 or his or her actual reemployment commencement date without regard to Section 14.2(b), a Grandfathered OPL Participant will accrue RPA Points under the applicable Appendix covering the Employer Company with which he or she is employed.

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Section 14.4 Grandfathered OPL Benefit.

- (a) OPL Benefits in Pay Status on March 1, 2002. With respect to any Grandfathered OPL Participant whose retirement benefit under the OPL Plan was in pay status on March 1, 2002, payment of such benefit shall continue under this Article XIV for payments due on or after April 1, 2002 in the same amount and benefit form as set forth in Appendix I, which is the benefit being paid from the OPL Plan on February 28, 2002.
- (b) OPL Minimum Benefit. The accrued benefit of a Grandfathered OPL Participant shall never be less than the Grandfathered OPL Participant's OPL Minimum Benefit, which is the OPL Minimum Accrued Benefit in Section 14.4(b)(1) adjusted by the applicable Grandfathered Actuarial Factors in Section 14.4(b)(2) and, if applicable, the applicable early retirement reduction factors set forth in Section 5.2(c)(2)(iii)(D) or the early commencement reduction factor set forth in Section 5.2(d)(2)(iii)(II), each determined without regard to whether such Grandfathered OPL Participant has an Hour of Service as an Employee on or after January 1, 1992 and based upon such Grandfathered OPL Participant's years of "benefit service" under the OPL Plan on February 28, 2002.
 - (1) OPL Minimum Accrued Benefit. The OPL Minimum Accrued Benefit of a Grandfathered OPL Participant is set forth in Appendix I, which is the Grandfathered OPL Participant's monthly benefit under the OPL Plan payable at Normal Retirement Age in the Normal Form determined as if such Grandfathered OPL Participant had terminated employment with UPS and OPL on the earlier of February 28, 2002 or the date he or she last actually terminated employment with UPS and OPL.

Termination of employment with UPS and OPL for the purpose of Sections 14.4(b) and 14.4(c) means the termination of employment with all Employer Companies and Related Employers as well as OPL and all employers that would be considered a single employer with OPL under Section 414(b), (c), (m) and (o) of the Code.

- (2) Grandfathered Actuarial Factors.
 - (A) Actuarial Equivalent. For purposes of determining a Grandfathered OPL Participant's OPL Minimum Benefit, the Actuarial Equivalent factors are as follows:

- (i) For the annuity benefit set forth in Section 14.4(c)(1),

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an interest rate of 7.5 percent and the 1983 GAM mortality table (blended 50 percent male, blended 50 percent female).

- (ii) For the annuity benefit set forth in Section 14.4(b)(1),
 - (I) with respect to the Qualified Joint and Survivor (Husband and Wife) Benefit, 90 percent of the Participant's monthly benefit payable in the Normal Form determined under Section 5.2(b), Section 5.2(c) or Section 5.2(d) increased (or decreased) by 0.5 percent for each year the spouse's or beneficiary's age is greater (or less) than

the Participant's age, with no minimum but to a maximum of 99 percent.

- (II) with respect to the Single Life with 120 Month Guarantee, 95 percent of the Participant's monthly benefit payable in the Normal Form.

(c) Special Optional Forms of Benefit Limited to OPL Minimum Benefit.

- (1) UPS Retirement Plan Termination. Subject to the rules set forth in Section 5.3, a Grandfathered OPL Participant, upon the termination of the UPS Retirement Plan, shall have the option to receive the Present Value of the Grandfathered OPL Participant's accrued benefit in the OPL Plan defined in Section 14.4(b)(1) determined as if such Grandfathered OPL Participant had terminated employment with UPS and OPL on the earlier of February 28, 2002 or the date he or she last actually terminated employment with UPS and OPL in a single cash lump sum payment or an immediate annuity which shall be the Actuarial Equivalent value of the benefit defined in Section 14.4(b)(1) determined as described above.
- (2) Present Value. For purposes of this Section 14.4(c), Present Value means the value of the Normal Form of benefit payment based the mortality table the Secretary of the Treasury prescribes, based on the prevailing commissioners' standard table (described in Section 807(d)(5)(A) of the Code) used to determine reserves for group annuity contracts issued on the date as of which present value is being determined (without regard to any other subparagraph of Section 807(d)(5) of the Code) and, for benefits paid on or before

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March 31, 2003, the annual rate of interest on 30 year Treasury securities for the month before the date of distribution or the Applicable Interest Rate, whichever rate produces the greater amount, and, for benefits paid on and after April 1, 2003, the Applicable Interest Rate.

- 2. The Plan is amended effective as of March 1, 2002 to add Appendices H and I as attached.

IN WITNESS WHEREOF, the undersigned certify that United Parcel Service of America, Inc., based upon action by its Board of Directors on May 3, 2002, has caused this Amendment No. 27 to be adopted.

<TABLE>
<CAPTION>

ATTEST:

<S>

UNITED PARCEL SERVICE
OF AMERICA, INC.

<C>

/s/ JOSEPH R. MODEROW

Joseph R. Moderow
Secretary

/s/ MICHAEL L. ESKEW

Michael L. Eskew
Chairman

</TABLE>

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AMENDMENT NO. 28

TO THE

UPS RETIREMENT PLAN

WHEREAS, United Parcel Service of America, Inc. ("UPS") and its affiliated corporations established the UPS Retirement Plan ("Plan") for the benefit of their eligible employees, in order to provide benefits to those employees upon their retirement, disability, or death, effective as of September 1, 1961; and

WHEREAS, the Plan, as adopted and amended from time to time, was amended and restated in its entirety, effective as of January 1, 1976, to comply with the Employee Retirement Income Security Act of 1974; and

WHEREAS, the Plan has been amended on a number of occasions since January 1, 1976, the most recent being Amendment No. 27; and

WHEREAS, this amendment of the Plan is adopted to reflect certain provisions of the Economic Growth and Tax Relief Reconciliation Act of 2001 ("EGTRRA"), to increase the number of consecutive Breaks in Service that will result in a loss of prior credit from 5 to 6, to cap service for the Disability Retirement benefit at 35 years, to provide a methodology for crediting Hours of Service to non-management employees who are paid on a basis other than hourly (e.g. sleeper teams), to clarify that the definition of Compensation excludes retention bonuses, referral bonuses and certain settlements to provide for benefit accruals for eligible employees of UPS Aviation Technologies, Inc. under the Plan formula or the UPS Pension Plan formula, whichever produces the greatest benefit, to conform the Plan to the Department of Labor claims regulations, to reflect past service credit for certain former employees of Rollins Logistics, Inc., Rollins Dedicated Carriage Services, Inc. and Rollins Transportation Systems, Inc., to clarify the list of Employer Companies in Appendix G;

NOW THEREFORE, pursuant to the authority vested in the Board of Directors by Section 7.1 of the Plan, the UPS Retirement Plan is hereby amended as follows:

1. SECTION 1.1(L) (2) AND (4), BENEFIT SERVICE, SECTION 2.1, ELIGIBILITY REQUIREMENTS, SECTION 6.2(B), BREAK IN SERVICE FOR VESTING PURPOSES, HEREBY ARE AMENDED EFFECTIVE AS OF JANUARY 1, 2001 TO CHANGE "FIVE" TO "SIX" SO THAT SERVICE IS DISREGARDED FOLLOWING SIX CONSECUTIVE BREAKS IN SERVICE INSTEAD OF FIVE CONSECUTIVE BREAKS IN SERVICE.
2. SECTION 1.1(L) (4), DEFINITION OF BENEFIT SERVICE, IS HEREBY AMENDED EFFECTIVE AS OF JANUARY 1, 2001 TO READ AS FOLLOWS:

(4) Benefit Service with respect to a Disabled Participant whose retirement benefits commence after December 31, 2000 shall be calculated in accordance with the applicable table in subparagraph (1) above, but there shall be included as Benefit Service all years and months while the Participant is a Disabled Participant and while the Participant continues to be "totally disabled" for purposes of the UPS Income Protection Plan (or a successor long term disability plan), as amended from time to time, determined as if such Disabled Participant had worked at least 1500 Hours of Service in each calendar year and at least 216 Hours of Service in each month in excess of a calendar year; provided, however, the total Benefit Service created under this Section 1.1(l)(4) to a Disabled Participant when aggregated with his actual Benefit Service under Section 1.1(l)(1)-(3) shall not exceed thirty-five (35) years. For the purpose of this paragraph (4), a "Disabled Participant" means a Participant who, as of the time of his or her termination of employment with all Employer Companies, has (A) five Years of Service, (B) is a full-time Employee and (C) is and continues to be "totally disabled" for purposes of the UPS Income Protection Plan (or a successor long term disability plan), as amended from time to time.

3. SECTION 1.1(N), DEFINITION OF HOUR OF SERVICE, IS HEREBY AMENDED EFFECTIVE FOR EMPLOYEES WHO COMPLETE AT LEAST ONE HOUR OF SERVICE ON OR AFTER JANUARY 1, 2003 TO READ AS FOLLOWS:

(n) "Hour of Service" means each hour for which an employee is paid or entitled to be paid for the performance of duties for an Employer Company or a Related Employer; each hour for which an employee is paid or entitled to be paid by an Employer Company or a Related Employer for periods during which no duties are performed due to vacation, holiday, illness, short-term disability or incapacity pursuant to which payments are received in the form of salary continuation or from a short-term disability plan or worker's compensation plan sponsored by the Employer Company or a Related Employer or to which the Employer Company or a Related Employer contributes, layoff, jury duty, military duty which gives rise to reemployment rights under Federal law, or paid leave of absence (including a period where an employee remains on salary continuation during a period of illness or incapacity); each hour for which back pay is awarded or agreed to by an Employer Company or a Related Employer if not already

credited under this sentence; and each hour for periods during which an employee is on an unpaid leave of absence.

Notwithstanding any of the foregoing, no more than 1040 Hours of Service will be credited to a Participant for any single continuous period during which the employee performs no duties; and no credit shall be given for a payment which is made or due under a plan maintained solely for the purpose of complying with unemployment compensation or disability insurance laws or which solely reimburses an employee for medical or medically related expenses incurred by the employee; provided, however, Hours of Service shall be credited as required under the Uniformed Services Employment and Reemployment Rights Act of 1994 effective December 12, 1994.

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A payment shall be deemed to be made by or due from the Employer Company whether made by or due from the Employer Company directly or indirectly through a trust fund, insurer or other entity to which the Employer Company contributes or pays premiums, regardless of whether such contributions are for the benefit of particular employees or are on behalf of a group of employees in the aggregate. Stated generally, Hours of Service credited to a Participant during a period of absence as described above shall be credited at the same rate at which the Participant would have normally been credited with Hours of Service but for the absence; provided however, that the crediting of Hours of Service shall in all events be consistent with the terms of Department of Labor Regulations, Section 2530.200b-2 and 3.

Notwithstanding the foregoing provisions of this Section 1.1(n) and, except as provided below, only for the purpose of determining whether a Break in Service has occurred under Section 2.1 or Section 6.2 of the Plan, there shall be treated as Hours of Service, with respect to a Participant who is an Employee on or after January 1, 1985, and who is absent from work (i) by reason of the pregnancy of the Participant, (ii) by reason of the birth of a child of the Participant, (iii) by reason of the placement of a child with the Participant in connection with the adoption of a child by the Participant, or (iv) for purposes of caring for a child of the Participant immediately following its birth or placement, either:

- (1) the Hours of Service which otherwise, normally would have been credited to such Participant but for the absence, or
- (2) if the Plan is unable to determine the number of Hours of Service described in (1), eight hours per day of absence.

No credit will be given with respect to any pregnancy or placement of a child unless the Participant complies with any reasonable request which the Committee may make for information needed to establish (i) the reason for the Participant's absence or (ii) the number of days of absence attributable to a reason for which Hours of Service will be credited under this paragraph. No more than 501 Hours of Service shall be credited to a Participant by reason of any one pregnancy or placement and no Hours of Service shall be credited under this paragraph if such Hours of Service also are credited under the first paragraph of this Section 1.1(n).

In determining the Hours of Service for an Employee classified on the payroll as a part-time employee for which specific records of hours are not kept, an Employee shall be credited with 190 Hours of Service for each regularly-scheduled calendar work month on or after January 1, 2000 in which such Participant would, under the rules described above, have earned at least one Hour of Service. Prior to January 1, 2000, such Participant shall be credited with 108 Hours of Service for each such month.

In determining the Hours of Service for an Employee classified on the payroll as (i) a full-time employee for which specific records of hours are not kept, or (ii) as non-management employees who are paid on a basis other than hourly (e.g. sleeper teams), an Employee shall be

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credited with 216 Hours of Service, for each regularly-scheduled calendar month in which such Employee would, under the rules described above, have earned at least one Hour of Service.

An individual who is treated as an employee of an Employer Company or a Related Employer solely as a result of the operation of the rules under Code Section 414(n) shall be credited with Hours of Service with an Employer Company or a Related Company as required under Code Section 414(n).

4. SECTION 5.7(B), MAXIMUM BENEFITS IS HEREBY AMENDED EFFECTIVE FOR LIMITATION YEARS ENDING AFTER DECEMBER 31, 2001 TO READ AS FOLLOWS:

- (b) Maximum Benefits.

(1) General Limitation. For limitation years ending after December 31, 2002, the maximum annual benefit payable under this Plan shall not exceed the lesser of: (i) \$160,000 as adjusted, effective January 1 of each year, under Section 415(d) of the Code in such manner as the Secretary shall prescribe (the "dollar limitation") or (ii) 100% of the Participant's average compensation (as defined in Treasury Regulation Section 1.415-2(d)) and reduced, if necessary, to reflect the applicable annual compensation limitation set forth in Section 1.1(y) of this Plan paid for the three consecutive calendar years during which he was an active Participant in the Plan, and in which he received the greatest aggregate compensation (as defined above) from the Employer Company, subject to the following:

(A) If the benefit is payable in any form other than a straight life annuity, a Qualified Joint and Survivor (Husband and Wife) Benefit, or a joint and survivor annuity with the spouse as the beneficiary, then the limitations of this subsection (1) shall be applied to the straight life annuity which is the actuarial equivalent of such benefit. The actuarially equivalent straight life annuity is equal to the greater of the annuity benefit computed using the interest rate and mortality table (or other tabular factor) specified in the Plan for adjusting benefits in the same form, and the annuity benefit computed using a 5 percent interest rate assumption and the Applicable Mortality Table. In determining the actuarially equivalent straight life annuity for a lump sum benefit, the Applicable Interest Rate will be substituted for 5 percent. No actuarial adjustment is required for the value of a qualified joint and survivor annuity, benefits that are not directly related to retirement benefits and the value of post-retirement cost-of-living increases made in accordance with Section 415(d) of the Code and the regulations thereunder.

(B) (i) If the retirement benefit of the Participant commences before the age 62, such dollar limitation shall be adjusted as described below so that it is the actuarial equivalent of an annual benefit of the dollar limitation beginning at age 62, reduced for each month by which benefits commence before the month in which the Participant attains age 62. The retirement benefit beginning prior to age 62 shall be determined as the lesser of the actuarial equivalent retirement

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benefit computed using the interest rate and mortality table (or other tabular factor) equivalence for early retirement benefits specified in the Plan, and the equivalent retirement benefit computed using a 5 percent interest rate and the Applicable Mortality Table. Any decrease in the adjusted defined benefit dollar limitation determined in accordance with this provision (B)(i) shall not reflect any mortality decrement to the extent that benefits will not be forfeited upon the death of the Participant. If any benefits are forfeited upon death, the full mortality decrement is taken into account.

(ii) If the retirement benefit of a Participant commences after age 65, the defined benefit dollar limitation shall be adjusted so that it is the actuarial equivalent of a retirement benefit of such dollar limitation beginning at age 65. The actuarial equivalent retirement benefit beginning after age 65 shall be determined as the lesser of the actuarial equivalent retirement benefit computed using the interest rate and mortality table (or other tabular factor) specified in the Plan for purposes of determining actuarial equivalence for delayed retirement benefits, and the equivalent retirement benefit computed using a 5 percent interest rate assumption and the Applicable Mortality Table.

(C) Subject to limitations imposed elsewhere in this Plan, an annual benefit of \$10,000 or less may be paid regardless of the limitations set forth in this subsection (b)(1) if the benefit paid the Participant from all defined benefit plans of the Employer Company does not exceed \$10,000 for the Plan Year or any prior Plan Year, and the Employer Company has not at any time maintained a defined contribution plan in which the Participant participated.

(D) If a Participant has less than 10 Years of service with the Employer Company at the time the Participant begins to receive retirement benefits under the Plan, the average compensation limitation, as well as the \$10,000 benefit exception described in subparagraph (b)(1)(C) above, shall be reduced by multiplying such limitation by a fraction, the numerator of which is the number of Years of Service with the Employer Company as of and including the current limitation year, and the denominator of which is 10. In the case of the dollar limitation where the Participant has less than 10 years of participation in the Plan, such limitation shall be reduced by a fraction, the numerator of which is the number of years of participation in the Plan as of and including the current limitation year, and the denominator of which is 10.

(2) Limitation Adjustment. The rate of a Participant's benefit accrual will be automatically frozen or reduced to a level necessary to prevent the limitations of this subsection (b) from being exceeded; provided, that if the limitations of this subsection (b) will be exceeded only as a result of considering another defined benefit plan sponsored by the Employer Company and this Plan as one plan, the Participant's benefit accrual under this plan will not be frozen or reduced to a level necessary to prevent the limitations of this subsection (b) from being exceeded in the event that such other defined benefit plan provides for the freezing or reduction of benefit accruals.

(3) Single Plan Rule. For purposes of this subsection (b), all defined benefit plans of the Employer Company (whether or not terminated) shall be considered as one defined benefit plan.

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(4) Automatic Adjustment. The limitations imposed by this subsection (b) shall be adjusted automatically when permitted or required by law. With respect to increases in these limitations which are permitted by law to reflect the impact of inflation, in the event that a Participant's Normal or Early Retirement Benefit, as determined in accordance with Section 5.2 as of his or her Annuity Starting Date, must be reduced by reason of the foregoing limitations in effect at such time, the following rules shall apply:

(A) A Participant's Normal or Early Retirement Benefit determined at his or her Annuity Starting Date in accordance with subsections 5.2(a) or (b), as the case may be, taking into account the Compensation limitation under Code Section 401(a)(17) and described at Section 1.1(y) which is applicable at such time (the "Compensation limitation"), and applying the applicable limitation or limitations at subsection 5.7(b)(1) or subparagraph 5.7(b)(1)(B)(i) (as applicable, the "415 limitations") shall, following the Annuity Starting Date, be adjusted upward as the result of any subsequent increase in the 415 limitations, provided however, that in no event shall such benefit exceed the Participant's Normal or Early Retirement Benefit determined as of the Participant's Annuity Starting Date in accordance with subsections 5.2(a) or (b), as the case may be, including the Compensation limitation.

(B) Notwithstanding the foregoing, in no event shall a Participant's Normal or Early Retirement Benefit, for any particular year, exceed the 415 limitation for such year (based on the Participant's age on his or her Annuity Starting Date), and no increase as described in subparagraph (A) above shall be retroactive for any preceding year.

(C) A Participant's Normal or Early Retirement benefit shall not be adjusted upward as the result of any change to the Compensation limitation following the Annuity Starting Date.

(5) Limitation Year. For purposes of this subsection (b), the limitation year is the calendar year.

(6) Employer Company. Solely for purposes of this Section 5.7(b), "Employer Company" means the Employer Company and each entity who would be determined to be a member of the Employer Company's controlled group under Section 414(b) or (c) of the Code if the standard of "more than fifty percent" was substituted for the standard of "at least eighty percent."

(7) Transitional Rules.

(A) The limitation under Section 5.7(b)(1) for an Employee who was a Participant in this Plan prior to January 1, 1983, shall be the greater of (i) the limitation contained in such Section or (ii) the Participant's accrued benefit, expressed as an annual benefit, as of December 31, 1982. For purposes of this paragraph (A), neither changes in the terms and

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conditions of this Plan nor cost of living adjustments occurring after July 1, 1982, shall be taken into account.

(B) The numerator of the defined contribution fraction shall, if necessary, be adjusted as permitted by Treasury Regulations so that the sum of the defined benefit fraction and the defined contribution fraction does not exceed 1.0 for the last limitation year beginning before January 1, 1983.

5. SECTION 5.13, DIRECT ROLLOVER, IS HEREBY AMENDED EFFECTIVE FOR DISTRIBUTIONS MADE AFTER DECEMBER 31, 2001 AS FOLLOWS:

Section 5.13 Direct Rollover.

(a) With respect to any distribution described in this Article V which constitutes an eligible rollover distribution within the meaning of Code Section 401(a)(31)(C), the distributee thereof shall, in accordance with procedures established by the Committee, be afforded the opportunity to direct that such distribution be transferred directly to the trustee of an eligible retirement plan (a "direct rollover"). For purposes of the foregoing sentence, an "eligible retirement plan" is (1) a qualified trust within the meaning of Code Section 402 which is a defined contribution plan the terms of which permit the acceptance of rollover distributions, (2) an individual retirement account or annuity within the meaning of Code Section 408 (other than an endowment contract), (3) an annuity plan within the meaning of Code Section 403(a), which is specified by the distributee in such form and at such time as the Committee may prescribe, and effective for distributions made after December 31, 2001, (4) an annuity contract described in Code Section 403(b) and (5) an eligible plan under Code Section 457(b) which is maintained by a state, political subdivision of a state, or any agency instrumentality of a state or political subdivision of a state and which agrees to separately account for amounts transferred into such plan from

this Plan. For distributions made after December 31, 2001, the definition of "eligible retirement plan" shall also apply in the case of a distribution to a surviving spouse, or to a spouse or former spouse who is the alternate payee under a qualified domestic relation order, as defined in Code Section 414(p).

(b) Notwithstanding the foregoing, if the distributee elects to have his or her eligible rollover distribution paid in part to him or her, and paid in part as a direct rollover:

(1) The direct rollover must be in an amount of \$500 or more.

(2) A direct rollover to two or more eligible retirement plans shall not be permitted.

(c) The Committee shall, within a reasonable period of time prior to making an eligible rollover distribution from this Plan, provide a written explanation to the distributee of the direct rollover option described above, as well as the provisions under which such distribution will not

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be subject to tax if transferred to an eligible retirement plan within 60 days after the date on which the distributee received the distribution.

6. ARTICLE V, AMOUNT AND PAYMENT OF BENEFITS, IS HEREBY AMENDED EFFECTIVE AS OF DECEMBER 31, 2000 TO ADD A NEW SECTION 5.14, UPS AVIATION TECHNOLOGIES, INC. EMPLOYEES, TO READ AS FOLLOWS:

Section 5.14 UPS Aviation Technologies, Inc. Employees. Notwithstanding any contrary Plan provision, a Participant who is employed by UPS Aviation Technologies, Inc. on December 31, 2000 and who was a participant in the UPS Pension Plan on that date shall receive a benefit from this Plan for his years of Benefit Service with UPS Aviation Technologies equal to the greater of the benefit described in Section 5.2 or the benefit such Participant would have earned under the UPS Pension Plan based upon the formula in effect under the Pension Plan immediately before such Participant became covered under this Plan.

7. SECTION 9.4, CLAIMS PROCEDURE, IS HEREBY AMENDED FOR NEW CLAIMS FILED ON OR AFTER JANUARY 1, 2002 AS FOLLOWS:

Section 9.4 Claims Procedure.

(a) All claims for benefits hereunder shall be directed to the Committee or to a member of the Committee designated for that purpose. Within ninety (90) days following receipt of a claim for benefits, the UPS Corporate Benefits Department manager responsible for the day-to-day operation of the Plan (the "Initial Reviewer") shall determine whether the claimant is entitled to benefits under the Plan, unless additional time is required for processing the claim. In this event, the Initial Reviewer shall, within the initial ninety day period, notify the claimant that additional time is needed, explain the reason for the extension, and indicate when a decision on the claim will be made, which must be within 180 days of the date the claim is filed.

(b) A denial by the Initial Reviewer of a claim for benefits shall be stated in writing and delivered or mailed to the claimant. Such notice shall set forth the specific reasons for the denial, written in a manner calculated to be understood by the claimant without benefit of legal or actuarial counsel. The notice shall include specific reference to the Plan provisions on which the denial is based and a description of any additional material or information necessary to perfect the claim, an explanation of why this material or information is necessary, the steps to be taken if the claimant wishes to submit his claim for review, and effective January 1, 2002, a description of the Plan's review procedures, and the time limits applicable to such procedures, and a statement of the claimant's right to bring a civil action under ERISA Section 502(a).

(c) The Committee shall afford a reasonable opportunity to any claimant whose request for benefits has been denied for a review of the decision denying the claim. The review must be requested by written application to the Committee within sixty (60) days following receipt by the claimant of written notification of denial of his claim. Pursuant to this review, the claimant

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or his duly authorized representative may review any documents, records and other information which are pertinent to the denied claim and submit issues and comments in writing. Effective January 1, 2002, a claimant may also submit documents, records, and other information relating to his claim, without regard to whether such information was submitted in connection with his claim.

(d) A decision on the claimant's appeal of the denial of benefits shall ordinarily be made by the Committee within sixty (60) days of the receipt of the request for review, unless additional time is required for a decision on review, in which event the decision shall be reviewed no later than 120 days after receipt of the request for ruling. Notice in writing of the extended time required shall be given to the claimant within sixty (60) days of his request for review.

The decision on review shall be in writing and shall include specific reasons for the decision, written in a manner calculated to be understood by the claimant, and specific reference to the Plan provisions on which the decision is based, and effective January 1, 2002, a statement that the claimant or his authorized personal representative may review any documents and records relevant to the claim determination, a statement describing any further voluntary appeals procedure, if any, and a statement of the claimant's right to bring a civil action under ERISA Section 502(a).

8. BY AMENDING ARTICLE X, GENERAL PROVISIONS, EFFECTIVE AS OF JANUARY 1, 2000 TO ADD A NEW SECTION 10.12, TO READ AS FOLLOWS:

Section 10.12 Former Rollins Employees. Notwithstanding any contrary provision of this Plan, any Employee who was employed by Rollins Logistics, Inc. Rollins Dedicated Carriage Services, Inc. or Rollins Transportation Systems, Inc. (each, "Rollins") and is identified on Appendix E as a "transfer employee" pursuant to Section 5.7 of that certain Asset Purchase Agreement dated November 12, 1999 by and among Worldwide Dedicated Services, Inc., Rollins Truck Leasing Corp., Rollins Logistics, Inc. Rollins Dedicated Carriage Services, Inc. and Rollins Transportation Systems, Inc. shall receive credit for all service completed with Rollins or any person that directly or indirectly through one or more intermediaries, controls or is controlled by, or is under common control with Rollins (a "Rollins Affiliate") or any predecessor to Rollins for purposes of the following:

(a) eligibility requirements described in Section 2.1;

(b) eligibility for a Deferred Vested Benefit as described in Section 4.4, Article V and Article VI;

(c) eligibility for an Early Retirement Benefit as described in Article V; and

(d) eligibility for retiree medical benefits described in Article XII.

Under no circumstances will service with Rollins, a Rollins Affiliate or a predecessor of Rollins be counted as Benefit Service or for purposes of determining the amount of the Participant Contribution for or the amount of retiree medical benefits under Article XII.

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9. SECTION 11.2(B), KEY EMPLOYEE, IS HEREBY AMENDED EFFECTIVE FOR PLAN YEARS BEGINNING AFTER DECEMBER 31, 2001 AS FOLLOWS:

(b) "Key Employee" means an Employee or former Employee who at any time during the Plan Year or any of the four preceding Plan Years is:

(1) For Plan Years before January 1, 2002

(A) an officer of the Employer Company having an annual compensation from the Employer Company of more than \$45,000 (provided, however, that no more than the lesser of (A) 50 Employees or (B) the greater of three Employees or 10% of the Employees shall be treated as officers under this paragraph),

(B) one of the 10 Employees having an annual compensation from the Employer Company of more than \$30,000 and owning the largest interests in the Employer Company,

(C) an owner of five percent of the outstanding stock of the Employer Company or stock possessing more than five percent of the total combined voting power of all stock of the Employer Company, or

(D) an owner of one percent of the outstanding stock of the Employer Company or stock possessing more than one percent of the total combined voting power of all stock of the Employer Company, who has an annual compensation from the Employer Company of more than \$150,000.

(2) For Plan Years beginning after December 31, 2001,

(A) an officer of the Employer Company having an annual compensation from the Employer Company of more than \$130,000, as adjusted under Section 416(i)(1) of the Code (provided, however, that no more than the lesser of (A) 50 Employees or (B) the greater of three Employees or 10% of the Employees shall be treated as officers under this paragraph),

(B) an owner of five percent of the outstanding stock of the Employer Company or stock possessing more than five percent of the total combined voting power of all stock of the Employer Company, or

(C) an owner of one percent of the outstanding stock of the Employer Company or stock possessing more than one percent of the total

combined voting power of all stock of the Employer Company, who has an annual compensation from the Employer Company of more than \$150,000.

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If two Employees have the same interest in the Employer Company, the Employee with the greater annual compensation shall be treated as having a larger interest. For purposes of determining ownership in the Employer Company (i) the constructive ownership rules of Section 318 of the Code, as modified by substituting "5 percent" for "50 percent" in subsection (a)(2)(C) thereof, shall apply, but (ii) the rules of subsections (b), (c), and (m) of Section 414 of the Code shall not apply. Each beneficiary of a Key Employee designated under this Plan is a Key Employee.

10. SECTION 11.2(F) ACCOUNT AGGREGATE, IS HEREBY AMENDED FOR PLAN YEARS BEGINNING AFTER DECEMBER 31, 2001 AS FOLLOWS:

(f) "Account Aggregate" is, with respect to a defined contribution plan,

(1) For Plan Years beginning after December 31, 2001, the sum of employee accounts plus the sum of all distributions made from such accounts during the one-year period ending on the Determination Date, provided that (1) rollover contributions and similar transfers initiated by an Employee and made after 1983, (2) the account of any Employee who was a Key Employee in a prior Plan Year but is no longer a Key Employee, and (3) any accrued benefits attributable to deductible employee contributions, and (4) the account of any individual who has not received any compensation from the Employer Company (other than benefits under any Plan maintained by the Employer Company) during the one-year period ending on the Determination Date, shall not be taken into account. In the case of a distribution made for a reason other than a separation from service, death or disability, this subsection shall be applied by substituting "five-year period" for "one-year period."

(2) For Plan Years beginning before December 31, 2001, the sum of employee accounts plus the sum of all distributions made from such accounts during the five-year period ending on the Determination Date, provided that (1) rollover contributions and similar transfers initiated by an Employee and made after 1983, (2) the account of any Employee who was a Key Employee in a prior Plan Year but is no longer a Key Employee, and (3) any accrued benefits attributable to deductible employee contributions, and (4) the account of any individual who has not received any compensation from the Employer Company (other than benefits under any Plan maintained by the Employer Company) during the five-year period ending on the Determination Date, shall not be taken into account.

A transfer from one plan of the Employer Company to any other such plan shall be considered neither a "distribution" nor a "rollover contribution" for purposes of this subsection, but a distribution from a terminated plan shall be considered a "distribution" for purposes of this subsection if such terminated plan, had it not been terminated, would have been described in Section 11.2(c)(1) or (2).

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11. SECTION 11.2(G) CUMULATIVE ACCRUED BENEFIT, IS HEREBY AMENDED FOR PLAN YEARS BEGINNING AFTER DECEMBER 31, 2001 AS FOLLOWS:

(g) "Cumulative Accrued Benefit" is, with respect to a defined benefit plan

(1) For Plan Years beginning after December 31, 2001, the sum of the present values of all accrued benefits plus the sum of distributions made with respect to such benefits during the one-year period ending on the Determination Date, provided that (1) rollover contributions and similar transfers initiated by an Employee and made after 1983, (2) the accrued benefit of any Employee who was a Key Employee in a prior Plan Year but is no longer a Key Employee, and (3) any accrued benefits attributable to deductible employee contributions, and (4) the accrued benefit of any individual who has not received any compensation from the Employer Company (other than benefits under any plan maintained by the Employer Company) during the five year period ending on the Determination Date, shall not be taken into account. In the case of a distribution made for a reason other than a separation from service, death or disability, this subsection shall be applied by substituting "five-year period" for "one-year period".

(2) For Plan Years beginning on or before December 31, 2001, the sum of the present values of all accrued benefits plus the sum of distributions made with respect to such benefits during the five-year period ending on the Determination Date, provided that (1) rollover contributions and similar transfers initiated by an Employee and made after 1983, (2) the accrued benefit of any Employee who was a Key Employee in a prior Plan Year but is no longer a Key Employee, and (3) any accrued benefits attributable to deductible employee contributions, and (4) the accrued benefit of any individual who has not received any compensation from the Employer Company (other than benefits under any plan maintained by the Employer Company) during the five year period ending on the Determination Date, shall not be taken into account.

A transfer from one plan of the Employer Company to any other such plan shall be considered neither a "distribution" nor a "rollover contribution" for purposes of this subsection, but a distribution from a terminated plan shall be considered a "distribution for purposes of this subsection if such terminated plan, had it not been terminated, would have been described in Section 11.2(c)(1) or (2).

12. SECTION 11.4 TOP HEAVY MINIMUM BENEFIT, IS HEREBY AMENDED FOR PLAN YEARS BEGINNING AFTER DECEMBER 31, 2001 AS FOLLOWS:

11.4 Top-Heavy Minimum Benefit. For each Plan Year for which the Plan is a Top-Heavy Plan, the accrued benefit derived from Employer Company contributions for each Participant who is not a Key Employee, when expressed as a single life annuity (with no ancillary benefits) beginning at his normal retirement age under the Plan, shall not be less than the product of (a) the Participant's average compensation during the Testing Period and (b) the lesser of (1) 2% multiplied by the number of the Participant's Years of Service with the Employer Company or (2) 20%. For purposes of this Section 11.4, a "Year of Service" shall not be taken into account if: (i) the Plan was not a Top-Heavy Plan for any Plan Year ending during such Year of Service, (ii)

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such Year of Service was completed in a Plan Year beginning before January 1, 1984, or (3) such Year of Service occurs during a Plan Year when the Plan benefits (within the meaning of Section 410(b) of the Code) no Key Employee or former Key Employee.

13. The Plan shall be amended to delete the current Appendix G and substitute the attached Appendix G, therefore.

14. This amendment is intended as good faith compliance with the requirements of EGTRRA and is to be construed in accordance with EGTRRA and guidance issued thereunder.

15. Except as otherwise provided, this amendment shall be effective as of the first day of the first plan year beginning after December 31, 2001.

16. Except as amended herein, the Plan as in effect before this Amendment Number 28 shall remain in full force and effect.

IN WITNESS WHEREOF, the undersigned certify that United Parcel Service of America, Inc., based upon action by its Board of Directors on this 20th day of December, 2002, has caused this Amendment No. 28 to be adopted.

<TABLE>
<CAPTION>

ATTEST:

UNITED PARCEL SERVICE
OF AMERICA, INC.

<S>

<C>

/s/ JOSEPH R. MODEROW

/s/ MICHAEL L. ESKEW

Joseph R. Moderow
Secretary

Michael L. Eskew
Chairman

</TABLE>

AMENDMENT NUMBER SEVEN
TO THE
UPS QUALIFIED STOCK OWNERSHIP PLAN AND TRUST AGREEMENT
EFFECTIVE AS OF JANUARY 1, 1998

WHEREAS, The United Parcel Service (the "Company") maintains the UPS Qualified Stock Ownership Plan and Trust Agreement (the "Plan") effective January 1, 1998; and

WHEREAS, the Plan has been amended on a number of occasions since January 1, 1998, the most recent being Amendment No. 6; and

WHEREAS, the Board reserved the right in Section 12.1 of the Plan to amend, modify or change the Plan from time to time; and

WHEREAS, it is desired to further amend the Plan to reflect certain provisions of the Economic Growth and Tax Relief Reconciliation Act of 2001 ("EGTRRA"); and

WHEREAS, this amendment is intended as a good faith compliance with the requirements of EGTRRA and is to be construed in accordance with EGTRRA and guidance issued thereunder; and

WHEREAS, except as otherwise provided, this amendment shall be effective as of the first day of the first Plan Year beginning after December 31, 2001; and

NOW, THEREFORE, the Plan is hereby amended as follows:

1. Article I is amended effective as of August 1, 2002 to renumber Sections 1.11 to 1.65 as Sections 1.12 to 1.66, respectively, (and any internal Plan cross-references are amended accordingly) and to add a new Section 1.10 which reads as follows:

Section 1.10 Catch-Up Contributions - means the sum of (1) contributions defined as "catch-up contributions" made under the Savings Plan, (2) with respect to an individual who becomes eligible to make elective deferrals under the Savings Plan during any Plan Year as a result of losing coverage under a collective bargaining agreement, his or her contributions defined as "catch-up contributions" made under a Collectively Bargained Plan prior to the latest date in such Plan Year on which he or she became eligible to make elective deferrals under the Savings Plan, and (3) with respect to an individual who was a participant in a Merged Plan who becomes eligible to make elective deferrals under the Savings Plan as a result of a merger of that plan into the Savings Plan, his or her defined as "catch-up contributions" made under such Merged Plan in the Plan Year in which he or she first became eligible to make elective deferrals under the Savings Plan.

2. The last paragraph of Section 1.15 (formerly Section 1.14) is amended to read as follows:

The annual Compensation of each Participant taken into account under the Plan shall not exceed \$200,000 for Plan Years beginning on or after January 1, 2002, as adjusted for cost-of-living increases in accordance with Code Section 401(a)(17)(B). For Plan Years beginning before January 1, 2002, the annual Compensation of each Participant taken into account under the Plan shall not exceed \$150,000 for Plan Years, as adjusted for cost-of-living increases in accordance with Code Section 401(a)(17). The cost-of-living adjustment in effect for a calendar year applies to any Plan Year beginning in such calendar year. If a Plan Year consists of fewer than 12 months, the annual compensation limit will be multiplied by a fraction, the numerator of which is the number of months in the short Plan Year, and the denominator of which is 12. The annual compensation limit does not apply for purposes of Section 5.1.

3. Article I is amended to renumber Sections 1.15 to 1.64 as Sections 1.16 to 1.65, respectively, (and any internal Plan cross-references are amended accordingly) and to add a new Section 1.15 which reads as follows:

Section 1.15 Disability - means a medically determinable physical or mental impairment as a result of which the Participant is disabled and qualified for disability benefits under (a) the United States Social Security Act, (b) a long term disability plan to which the Employer contributes for the Participant or (c) workers compensation laws.

4. The last paragraph of Section 1.20 (formerly Section 1.19) is amended to read as follows:

The annual Eligible Compensation of each Participant taken into account under the Plan shall not exceed \$200,000 for Plan Years beginning on or after January 1, 2002, as adjusted for cost-of-living increases in accordance with Code Section 401(a)(17)(B) (the "annual compensation limit"). For Plan Years

beginning before January 1, 2002, the annual Eligible Compensation of each Participant taken into account under the Plan shall not exceed \$150,000 for Plan Years, as adjusted for cost-of-living increases in accordance with Code Section 401(a)(17). The cost-of-living adjustment in effect for a calendar year applies to any Plan Year beginning in such calendar year. If a Plan Year consists of fewer than 12 months, the annual compensation limit will be multiplied by a fraction, the numerator of which is the number of months in the short Plan Year, and the denominator of which is 12. The annual compensation limit does not apply for purposes of Section 5.1.

5. Section 1.57(a) (formerly Section 1.56(a)) is amended to read as follows:

(a)

(1) Effective as of January 1, 2002, the date on which an individual terminates employment with all Affiliates by reason of a voluntarily quit, retirement, death, period of Disability of more than 52 weeks, discharge, failure to return from layoff or authorized leave of absence, or for any other reason (unless a grievance is pending), provided for periods before January 1, 2002, such separation constitutes a "separation from service" within the meaning of Code Section 401(k) and, for periods on or after January 1, 2002, such separation constitutes a "severance from employment" under the Savings Plan. A discharge will not be treated as a Separation from Service while a grievance is pending but, if the discharge is upheld, will be treated as a Separation from Service as of the date of the discharge.

(2) Effective before January 1, 2002 but on or after May 1, 2000, the date on which an individual terminates employment with all Affiliates by reason of a voluntarily quit, retirement, death, the end of a period of disability of more than 52 weeks at which time a physician certifies that the individual is currently disabled and unable to return to work for an Affiliate, discharge, failure to return from layoff or authorized leave of absence, or for any other reason (unless a grievance is pending), provided for periods before January 1, 2002, such separation constitutes a "separation from service" within the meaning of Code Section 401(k) and, for periods on or after January 1, 2002, such separation constitutes a "severance from employment" under the Savings Plan. A discharge will not be treated as a Separation from Service while a grievance is pending but, if the discharge is upheld, will be treated as a Separation from Service as of the date of the discharge.

(3) Effective before May 1, 2000, the earlier of the date under Section 1.57(a)(2) or the date on which a 12-consecutive month period ends during which the individual did not perform an Hour of Service.

6. Section 4.1(a) is amended effective as of August 1, 2002 to read as follows:

(a) On and After July 1, 2001. Subject to the rules and limitations set forth in this ARTICLE IV and in ARTICLE V, including the specific limitations set forth as matching formulas in this Section 4.1, an Employer Company shall make the following SavingsPLUS Contribution, if any, for each Accounting Period on behalf of each Participant who was employed as an Eligible Employee by such Employer Company on the last day of the Accounting Period and each Participant whose last employment as an Eligible Employee was with such Employer Company during the Accounting Period.

The SavingsPLUS Contribution made on behalf of each Participant described in this Section 4.1(a) shall be equal to

A minus B where:

(1) A equals

(i) For each Employer Company listed in Appendix 4.1(a)(1)(A), zero.;

(ii) For each Employer Company listed in Appendix 4.1(a)(1)(B), 50% of his or her Pre-Tax Contributions that do not exceed 6% of his or her Eligible Compensation for such Plan Year;

(iii) For each Employer Company listed in Appendix 4.1(a)(1)(C), 100% of his or her Pre-Tax Contributions that do not exceed 3% of his or her Eligible Compensation for such Plan Year; or

(iv) For each Employer Company listed in Appendix 4.1(a)(1)(D), the sum of 100% of his or her Pre-Tax Contributions that do not exceed 3% of his or her Eligible Compensation for such Plan Year and 50% of his or her Pre-Tax

Contributions in excess of 3% but not in excess of 6% of his or her Eligible Compensation for such Plan Year.

(2) B equals the SavingsPLUS Contribution and the matching contribution (within the meaning of Code Section 401(m)) under a Merged Plan previously made by any Employer Company with respect to him or her during such Plan Year.

Effective August 1, 2002, no SavingsPLUS Contributions will be made with respect to any Catch-Up Contributions (unless such contributions are reclassified as Pre-Tax Contributions).

7. Section 4.1 is amended effective as of July 1, 2001 to correct a scrivener's error and reinstate Sections 4.1(c), (d) and (e) which read as follows:

(c) Application of Suspense Account and Forfeitures. Excess amounts that are transferred to a Code Section 415 suspense account for a Plan Year pursuant to Section 5.1, if any, and any amounts treated as forfeitures under the Plan will be applied to reduce the SavingsPLUS Contributions for the next Plan Year (and succeeding Plan Years, if necessary).

(d) No SavingsPLUS Contributions on Refunds. No SavingsPLUS Contributions will be made with respect to any Pre-Tax Contributions that are refunded by the Savings Plan or a Collectively Bargained Plan to satisfy Code Section 401(k), Section 402(g) or Section 415. If it is determined that any portion of the SavingsPLUS Contributions credited to a Participant's SavingsPLUS Account is attributable to refunded Pre-Tax Contributions, the number of whole shares of UPS Stock attributable to the match on refunded Pre-Tax Contributions automatically will be deducted from the Participant's SavingsPLUS Account (or if the Participant has diversified his or her SavingsPLUS Account pursuant to Section 8.10, an amount equal to the value of those shares automatically will be deducted from the Participant's account under the Savings Plan) and will be transferred to a Code Section 415 suspense account (if the refund of Pre-Tax Contributions was for purposes of Code Section 415) or treated as a forfeiture

(e) Allocation. The SavingsPLUS Contribution, if any, made on behalf of each Participant will be credited to his or her SavingsPLUS Account as of the last day of each Accounting Period.

8. Section 5.1(a) is amended effective for limitation years beginning after December 31, 2001 to read as follows:

(a) General Rule. The term "limitation year" as defined in Code Section 415 and the corresponding regulations means the calendar year. Except to the extent permitted with respect to Catch-Up Contributions, the total annual additions (as described in Section 5.1(b)) allocated to a Participant's Account for any limitation year when added to the contributions that are treated as made on behalf of such Participant for such limitation year under the coordination rules in Section 5.1(c) will not exceed the lesser of

(1) 100% (25% for limitation years before January 1, 2002) of the Participant's Compensation for the limitation year;

(2) \$40,000 (\$30,000 for limitation years beginning before January 1, 2002) (as adjusted under Code Section 415(d)), or

(3) such lesser amount as the Committee deems necessary or appropriate to satisfy the requirements of Code Section 415 in light of Section 5.1(d) and the benefits, if any, accrued and the contributions, if any, made for such Participant under any other defined contribution plan maintained by an Affiliate.

If a short limitation year (less than 12 months) is created because of an amendment, the limitation described in (2) above will be prorated.

9. Section 5.2(c) is amended to read as follows:

(c) Multiple Use Limitation.

(1) For Plan Years beginning after January 1, 2002, the multiple use test described in Treas. Reg. 1.401(m)-2 and Section 5.5(c)(2) below shall not apply.

(2) For Plan Years beginning before January 1, 2002, the ACPs of all Highly Compensated Employees will be reduced (beginning with the highest of such percentages) to the extent required under Code Section 401(m) and the regulations issued under that section to prevent multiple use of the alternative test described in Code Section 401(k)(3)(A)(ii)(II) and in Code Section 401(m)(2)(A)(ii) in the same Plan Year. The reduction will be treated as an Excess Aggregate Contribution. If the ESOP feature is activated, the multiple use limitation will not apply unless this Plan (or another ESOP maintained by an Affiliate also permits elective deferrals.

10. Section 8.1 is amended to read as follows:

Section 8.1 General. A Participant may request distribution of his or her Account when he or she has a Separation from Service. In addition, a Participant may request a withdrawal from his or her Savings Plan Account before a Separation from Service to the extent provided in Section 8.7 or his or her Account before a Separation from Service to the extent provided in Section 8.7A.

11. Article VIII is amended to add a new Section 8.7A which follows Section 8.7 and precedes Section 8.8 and which reads as follows:

Section 8.7A Disability. A Participant who has been absent for more than 52 weeks on account of Disability (but who has not experienced a Separation from Service) and whose Disability continues through the date of withdrawal under this Section 8.7A may withdraw all or any portion of his or her Account at any time by submitting a request for withdrawal in accordance with the procedures adopted by the Committee for this purpose. Such withdrawal shall be subject to any additional restrictions, uniformly applied with respect to Participants similarly situated, as are prescribed by the Committee regarding the frequency and minimum amount of such withdrawal.

12. Section 8.13 is amended effective for distributions made after December 31, 2001 to read as follows:

Section 8.13 Eligible Rollover Distribution.

(a) General. Notwithstanding any provision of this Plan to the contrary that would otherwise limit a Distributee's election under this Section 8.13, a Distributee may elect, at the time and in the manner prescribed by the Committee, to have any portion of an Eligible Rollover Distribution of two hundred dollars (\$200) or more transferred to an Eligible Retirement Plan specified by the Distributee in a Direct Rollover.

(b) Definitions.

(1) Eligible Rollover Distribution. An Eligible Rollover Distribution is any distribution of all or any portion of the balance to the credit of the Distributee, except that an Eligible Rollover Distribution does not include:

(i) any distribution that is one of a series of substantially equal periodic payments (not less frequently than annually) made for the life (or life expectancy) of the Distributee or the joint lives (or joint life expectancies) of the Distributee and the Distributee's designated beneficiary, or for a specified period of ten (10) years or more;

(ii) any distribution to the extent that distribution is required under Code Section 401(a)(9);

(iii) any distribution of Pre-Tax Contributions or pre-tax contributions under a Merged Plan on account of hardship on or after January 1, 1999; and

(iv) effective for distributions made before January 1, 2002, the portion of any distribution that is not includible in gross income.

Effective for distributions made after December 31, 2001, a portion of a distribution shall not fail to be an Eligible Rollover Distribution merely because the portion consists of after-tax employee contributions which are not includible in gross income. However, such portion which consists of after-tax contributions may be paid only to an individual retirement annuity described in Code Section 408(a) or Code Section 408(b), or to a qualified defined contribution plan described in Code Section 401(a) or Code Section 403(a) that agrees to account separately for amounts so transferred, including separately accounting for the portion of such distribution which is includible in gross income and the portion of such portion which is not so includible.

(2) Eligible Retirement Plan. An Eligible Retirement Plan is an individual retirement account described in Code Section 408(a), an individual retirement annuity described in Code Section 408(b), an annuity plan described in Code Section 403(a), a qualified trust described in Code Section 401(a) and, effective for distributions made after December 31, 2001, an annuity contract described in Code Section 403(b) or an eligible plan under Code Section 457(b) which is maintained by a state, political subdivision of a state, or any agency or instrumentality of a state or political subdivision of a state and which agrees to separately account for amounts transferred into such Plan from this Plan in order to be an Eligible Retirement Plan. The definition of Eligible Retirement Plan shall also apply in the case of a distribution to a surviving spouse, or to a spouse or former spouse who is the alternate payee under a

qualified domestic relations order, as defined in Code Section 414(p).

(3) Distributee. A Distributee includes an employee or former employee. In addition, the employee's or former employee's surviving spouse and the employee's or former employee's spouse or former spouse who is the alternate payee under a qualified domestic relations order, as defined in Code Section 414(p), are Distributees with regard to the interest of the spouse or former spouse.

(4) Direct Rollover. A Direct Rollover is a payment by this Plan to the Eligible Retirement Plan specified by the Distributee.

(5) Additional Limitations. Notwithstanding the foregoing,

(i) if the Distributee elects to have his or her Eligible Rollover Distribution paid in part to him or her and paid in part as a Direct Rollover, the Direct Rollover must be in an amount of two hundred dollars (\$200) or more;

(ii) a Direct Rollover to more than one Eligible Retirement Plan will not be permitted. and

(iii) a Direct Rollover of UPS Stock may not be transferred to an Eligible Retirement Plan other than an individual retirement account as described in Code Section 408(a) and with respect to which prior to November 15, 1999, the custodian or trustee of which agrees to be bound by the terms of the UPS Stock Trust.

13. Section 13.9 is amended to read as follows:

Section 13.9 Top Heavy Plan.

(a) Determination. The Committee as of the last day of each Plan Year (the "determination date") will determine the sum of the present value of the accrued benefits of "key employees" (as defined in Code Section 416(i)(1)) and the sum of the present value of the accrued benefits of all other Employees in accordance with the rules set forth in Code Section 416(g), or will take such other action as the Committee deems appropriate to conclude that no such determination is necessary under the circumstances. If the sum of the present value of the accrued benefits of such key employees exceeds 60% of the sum of the present value of the accrued benefits of all employees as of the determination date, this Plan will be "top-heavy" for the immediately following Plan Year. For purposes of this Section, the present value of the accrued benefit of each employee will be equal to the sum of

(1) the balance of the employee's Account under this Plan (determined for this purpose as of the last day of each Plan Year, which is the "valuation date" for this Plan);

(2) the present value of the employee's accrued benefit, if any, (determined as of the most recent valuation date occurring within a 12-month period ending on the determination date) under

(i) each qualified plan (as described in Code Section 401(a)) maintained by an Affiliate (a) in which a key employee is a participant or (b) that enables any plan described in subclause (i) to meet the requirements of Code Section 401(a)(4) or Section 410 (the "required aggregation group"), and

(ii) each other qualified plan maintained by an Affiliate (other than a plan described in clause (a) that may be aggregated with this Plan and the plans described in clause (a), provided such aggregation group (including a plan described in this clause (b) continues to meet the requirements of Code Section 401(a)(4) and Section 410 (the "permissive aggregation group"); and
(3)

(i) for Plan Years beginning on or after January 1, 2002, the value of any withdrawals and distributions made from this Plan and the plans described in (2) above during the 1- year period ending on such determination date and the value of any contributions due under this Plan and the defined contribution plans described in (2) above but as yet unpaid as of such determination date. The preceding sentence shall also apply to distributions under a terminated plan which, had it not been terminated, would have been required to be aggregated with the Plan under Code Section 416(g)(2)(A)(i). In the case of a distribution made for a reason other than

separation from service, death or disability, this provision shall be applied by substituting "5-year period" for "1-year period."

(ii) for Plan Years beginning before January 1, 2002, the value of any withdrawals and distributions made from this Plan and the plans described in (2) above during the 5 year period ending on such determination date and the value of any contributions due under this Plan and the defined contribution plans described in (2) above but as yet unpaid as of such determination date;

provided, however, effective for Plan Year beginning on or after January 1, 2002, the accrued benefit of any employee will be disregarded if such employee has not performed any services for any Affiliate at any time during the one (1) year period ending on the date as of which such determination is made and, effective for Plan Years beginning before January 1, 2002, the accrued benefit of any employee will be disregarded if such employee has not performed any services for any Affiliate at any time during the five (5) year period ending on the date as of which such determination is made.

(b) Special Top-Heavy Contribution. If the Committee determines that this Plan is "top-heavy" for any Plan Year, the following special rules will apply notwithstanding any other rules to the contrary set forth elsewhere in this Plan.

(1) A contribution will be made for each Participant who is an Eligible Employee on the last day of such Plan Year that, when added to the employer contribution and forfeitures otherwise allocated on behalf of such individual for such Plan Year under this Plan and any other defined contribution plan maintained by an Affiliate, is equal to:

(i) for each such Eligible Employee who is not a participant in a top-heavy defined benefit plan maintained by the Employer or an Affiliate, the lesser of (a) 3% of such Eligible Employee's Compensation for such year or (b) the percentage at which contributions are made (or are required to be made) for such year to the key employee for whom such percentage is the highest; or

(ii) for each such Eligible Employee who also participates in a top-heavy defined benefit plan maintained by the Employer or an Affiliate, 5% of such Eligible Employee's Compensation for such year;

provided, however, that no such contribution will be made under this Section for any Eligible Employee to the extent such Eligible Employee receives the top-heavy minimum contributions (as described in Code Section 416(c)) under another defined contribution plan maintained by the Employer or an Affiliate for such Plan Year.

(2) Effective for Plan Years beginning after January 1, 2002, SavingsPLUS Contributions shall be taken into account for purposes of satisfying the minimum contribution requirements of Code Section 416(c)(2) and the Plan. The preceding sentence shall apply with respect to SavingsPLUS Contributions made under the Plan or, if the minimum contribution requirement is met in another defined contribution plan, such other plan. SavingsPLUS Contributions that are used to satisfy the minimum contribution requirements shall be treated as employer matching contributions for purposes of the actual contribution percentage test and the other requirements of Code Section 401(m)

(3) For Plan Years beginning before January 1, 2000, if the sum of the present value of the accrued benefits of key employees (computed as described in Section 13.9(a)) exceeds 90% of the sum of the present value of the accrued benefits of all employees (computed as described in Section 13.9(a)) as of the determination date this Plan will be "super top-heavy" for the immediately following Plan Year.

14. This amendment is intended as good faith compliance with the requirements of EGTRRA and is to be construed in accordance with EGTRRA and guidance issued thereunder. This amendment shall supersede the provisions of the Plan to the extent those provisions are inconsistent with the provisions of this amendment.

IN WITNESS WHEREOF, the undersigned certify that United Parcel Service of America, Inc., based upon action by its Board of Directors on December 20, 2002, has caused this Amendment Number Seven to be adopted.

<TABLE>
<CAPTION>

ATTEST:

UNITED PARCEL SERVICE
OF AMERICA, INC.

<S>

/s/ Joseph R. Moderow

Joseph R. Moderow
Secretary

<C>

/s/ Michael L. Eskew

Michael L. Eskew
Chairman

</TABLE>

SUBSIDIARIES OF UNITED PARCEL SERVICE, INC.
AS OF MARCH 5, 2003

NAME OF SUBSIDIARY -----	JURISDICTION OF ORGANIZATION -----
United Parcel Service of America, Inc.	Delaware
United Parcel Service General Services Co.	Delaware
United Parcel Service Co.	Delaware
UPS Worldwide Forwarding, Inc.	Delaware
United Parcel Service, Inc.	Ohio
United Parcel Service, Inc.	New York
UPICO Corporation	Delaware
UPS Capital Corporation	Delaware
UPS Supply Chain Solutions, Inc.	Delaware
UPS Re Ltd.	Bermuda
UPS International, Inc.	Delaware
United Parcel Service Deutschland Inc.	Delaware
C.C. & E. I, L.L.C.	Delaware

The names of particular subsidiaries are omitted pursuant to Item 601(b)(21)(ii) of Regulation S-K.

INDEPENDENT AUDITORS' CONSENT

We consent to the incorporation by reference in Registration Statements No. 333-86468 and 333-08369-01 on Form S-3 and in Registration Statements No. 333-90792, 333-93213, 333-34054, 333-61112, 333-65096, 333-65606, and 333-70708 on Form S-8 of United Parcel Service, Inc. and in Registration Statements No. 333-72127, 333-24805, 333-23969, and 333-23971 on Form S-8 of United Parcel Service of America, Inc. of our report dated January 27, 2003 (which report expresses an unqualified opinion and includes an explanatory paragraph relating to the Company's change in its method of accounting for derivative instruments and hedging activities to conform with Statement of Financial Accounting Standards No. 133, as amended and to the Company's change in its method of accounting for goodwill and other intangible assets to conform with Statement of Financial Accounting Standards No. 142), appearing in this Annual Report on Form 10-K of United Parcel Service, Inc. for the year ended December 31, 2002.

DELOITTE & TOUCHE LLP

Atlanta, Georgia
March 3, 2003

CERTIFICATION PURSUANT TO 18 U.S.C. SECTION 1350,
AS ADOPTED PURSUANT TO SECTION 906 OF THE
SARBANES-OXLEY ACT OF 2002

Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 and in connection with the Annual Report on Form 10-K of United Parcel Service, Inc. (the "Corporation") for the year ended December 31, 2002, as filed with the Securities and Exchange Commission on the date hereof (the "Report"), the undersigned, the Chairman and Chief Executive Officer of the Corporation, certifies that:

- (1) The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
- (2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Corporation.

/s/ MICHAEL L. ESKEW

Michael L. Eskew
Chairman and Chief Executive Officer
March 6, 2003

CERTIFICATION PURSUANT TO 18 U.S.C. SECTION 1350,
AS ADOPTED PURSUANT TO SECTION 906 OF THE
SARBANES-OXLEY ACT OF 2002

Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 and in connection with the Annual Report on Form 10-K of United Parcel Service, Inc. (the "Corporation") for the year ended December 31, 2002, as filed with the Securities and Exchange Commission on the date hereof (the "Report"), the undersigned, the Chief Financial Officer of the Corporation, certifies that:

- (1) The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
- (2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Corporation.

/s/ D. SCOTT DAVIS

D. Scott Davis
Chief Financial Officer
March 6, 2003