AT&T INC.
Form 10-Q
August 07, 2015
UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

(Mark One)	QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
x	For the quarterly period ended June 30, 2015
	or
o	TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from to

Commission File Number 1-8610

AT&T INC.

Incorporated under the laws of the State of Delaware
I.R.S. Employer Identification Number 43-1301883

208 S. Akard St., Dallas, Texas 75202
Telephone Number: (210) 821-4105

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

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

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See definition of "accelerated filer," "large accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer [X]	Accelerated filer [ ]

Non-accelerated filer [ ] (Do not check if a smaller reporting company) Smaller reporting company [ ]

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

At July 31, 2015, there were 6,151 million common shares outstanding.

PART I - FINANCIAL INFORMATION

Item 1. Financial Statements

AT&T INC.

CONSOLIDATED STATEMENTS OF INCOME

Dollars in millions except per share amounts

(Unaudited)

	Three months ended June 30,		Six months ended June 30,	
	2015	2014	2015	2014
Operating Revenues				
Service	$29,541	$29,556	$58,503	$59,332
Equipment	3,474	3,019	7,088	5,719
Total operating revenues	33,015	32,575	65,591	65,051
Operating Expenses				
Cost of services and sales (exclusive of depreciation and amortization shown separately below)	15,140	14,212	29,721	27,533
Selling, general and administrative	7,467	8,197	15,428	16,457
Depreciation and amortization	4,696	4,550	9,274	9,167
Total operating expenses	27,303	26,959	54,423	53,157
Operating Income	5,712	5,616	11,168	11,894
Other Income (Expense)				
Interest expense	(932)	(881)	(1,831)	(1,741)
Equity in net income of affiliates	33	102	33	190
Other income (expense) – net	48	1,269	118	1,414
Total other income (expense)	(851)	490	(1,680)	(137)
Income Before Income Taxes	4,861	6,106	9,488	11,757
Income tax expense	1,715	2,485	3,066	4,402
Net Income	3,146	3,621	6,422	7,355
Less: Net Income Attributable to Noncontrolling Interest	(102)	(74)	(178)	(156)
Net Income Attributable to AT&T	$3,044	$3,547	$6,244	$7,199
Basic Earnings Per Share Attributable to AT&T	$0.58	$0.68	$1.20	$1.38
Diluted Earnings Per Share Attributable to AT&T	$0.58	$0.68	$1.20	$1.38
Weighted Average Number of Common Shares Outstanding – Basic (in millions)	5,204	5,204	5,204	5,213
Weighted Average Number of Common Shares Outstanding – with Dilution (in millions)	5,220	5,220	5,220	5,229
Dividends Declared Per Common Share	$0.47	$0.46	$0.94	$0.92

See Notes to Consolidated Financial Statements.

AT&T INC.
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
Dollars in millions
(Unaudited)

	Three months ended June 30,		Six months ended June 30,	
	2015	2014	2015	2014
Net income	$3,146	$3,621	$6,422	$7,355
Other comprehensive income (loss), net of tax:				
Foreign Currency:				
Translation adjustment (includes $0, $1, $0 and $1 attributable to noncontrolling interest), net of taxes of $1, $15, $(103) and $5	1	26	(185)	6
Reclassification adjustment included in net income, net of taxes of $0, $210, $0 and $224	-	391	-	416
Available-for-sale securities:				
Net unrealized gains, net of taxes of $0, $24, $19 and $34	-	43	34	59
Reclassification adjustment realized in net income, net of taxes of $(2), $(1), $(5) and $(8)	(4)	(3)	(9)	(14)
Cash flow hedges:				
Net unrealized gains (losses), net of taxes of $(52), $(56), $(242) and $(53)	(95)	(104)	(449)	(98)
Reclassification adjustment included in net income, net of taxes of $5, $7, $9 and $11	10	14	17	21
Defined benefit postretirement plans:				
Amortization of net prior service credit included in net income, net of taxes of $(131), $(142), $(262) and $(289)	(214)	(239)	(429)	(479)
Reclassification adjustment included in net income, net of taxes $0, $31, $0 and $33	-	58	-	61
Other comprehensive income (loss)	(302)	186	(1,021)	(28)
Total comprehensive income	2,844	3,807	5,401	7,327
Less: Total comprehensive income attributable to noncontrolling interest	(102)	(75)	(178)	(157)
Total Comprehensive Income Attributable to AT&T	$2,742	$3,732	$5,223	$7,170

See Notes to Consolidated Financial Statements.

AT&T INC.
CONSOLIDATED BALANCE SHEETS
Dollars in millions except per share amounts

	June 30, 2015 (Unaudited)	December 31, 2014
Assets		
Current Assets		
Cash and cash equivalents	$ 20,956	$ 8,603
Accounts receivable - net of allowances for doubtful accounts of $492 and $454	13,821	14,527
Prepaid expenses	834	831
Deferred income taxes	1,131	1,142
Other current assets	6,421	6,925
Total current assets	43,163	32,028
Property, plant and equipment	289,856	282,295
Less: accumulated depreciation and amortization	(175,508)	(169,397)
Property, Plant and Equipment – Net	114,348	112,898
Goodwill	70,920	69,692
Licenses	80,922	60,824
Other Intangible Assets – Net	6,385	6,139
Investments in Equity Affiliates	288	250
Other Assets	10,463	10,998
Total Assets	$ 326,489	$ 292,829
Liabilities and Stockholders' Equity		
Current Liabilities		
Debt maturing within one year	$ 8,603	$ 6,056
Accounts payable and accrued liabilities	21,560	23,592
Advanced billing and customer deposits	4,075	4,105
Accrued taxes	3,848	1,091
Dividends payable	2,441	2,438
Total current liabilities	40,527	37,282
Long-Term Debt	105,067	76,011
Deferred Credits and Other Noncurrent Liabilities		
Deferred income taxes	38,516	37,544
Postemployment benefit obligation	36,638	37,079
Other noncurrent liabilities	18,240	17,989
Total deferred credits and other noncurrent liabilities	93,394	92,612
Stockholders' Equity		
Common stock ($1 par value, 14,000,000,000 authorized at June 30, 2015 and December 31, 2014: issued 6,495,231,088 at June 30, 2015 and December 31, 2014)	6,495	6,495
Additional paid-in capital	91,032	91,108
Retained earnings	29,086	27,736
Treasury stock (1,301,916,280 at June 30, 2015 and 1,308,318,131 at December 31, 2014, at cost)	(46,793)	(47,029)
Accumulated other comprehensive income	7,039	8,060
Noncontrolling interest	642	554
Total stockholders' equity	87,501	86,924
Total Liabilities and Stockholders' Equity	$ 326,489	$ 292,829

See Notes to Consolidated Financial Statements.

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AT&T INC.
CONSOLIDATED STATEMENTS OF CASH FLOWS
Dollars in millions
(Unaudited)

	Six months ended June 30,	
	2015	2014
Operating Activities		
Net income	$6,422	$7,355
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	9,274	9,167
Undistributed earnings from investments in equity affiliates	(23)	(58)
Provision for uncollectible accounts	535	444
Deferred income tax expense	1,183	546
Net gain from sale of investments, net of impairments	(50)	(1,365)
Changes in operating assets and liabilities:		
Accounts receivable	434	(566)
Other current assets	743	(771)
Accounts payable and accrued liabilities	(1,125)	2,894
Retirement benefit funding	(455)	(280)
Other - net	(1,040)	(497)
Total adjustments	9,476	9,514
Net Cash Provided by Operating Activities	15,898	16,869
Investing Activities		
Construction and capital expenditures:		
Capital expenditures	(8,328)	(11,649)
Interest during construction	(339)	(118)
Acquisitions, net of cash acquired	(20,954)	(857)
Dispositions	72	4,921
Sale of securities	1,890	-
Return of advances to and investments in equity affiliates	-	2
Other	(1)	-
Net Cash Used in Investing Activities	(27,660)	(7,701)
Financing Activities		
Net change in short-term borrowings with original maturities of three months or less	-	134
Issuance of long-term debt	33,958	8,564
Repayment of long-term debt	(2,919)	(3,508)
Purchase of treasury stock	-	(1,396)
Issuance of treasury stock	20	27
Dividends paid	(4,873)	(4,784)
Other	(2,071)	(239)
Net Cash Provided by (Used in) Financing Activities	24,115	(1,202)
Net increase in cash and cash equivalents	12,353	7,966
Cash and cash equivalents beginning of year	8,603	3,339
Cash and Cash Equivalents End of Period	$20,956	$11,305
Cash paid (received) during the six months ended June 30 for:		
Interest	$2,178	$2,292
Income taxes, net of refunds	$(71)	$987

See Notes to Consolidated Financial Statements.

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AT&T INC.
CONSOLIDATED STATEMENT OF CHANGES IN STOCKHOLDERS' EQUITY
Dollars and shares in millions except per share amounts
(Unaudited)

	June 30, 2015	
	Shares	Amount
Common Stock		
Balance at beginning of year	6,495	$6,495
Issuance of stock	-	-
Balance at end of period	6,495	$6,495
Additional Paid-In Capital		
Balance at beginning of year		$91,108
Issuance of treasury stock		8
Share-based payments		(84)
Balance at end of period		$91,032
Retained Earnings		
Balance at beginning of year		$27,736
Net income attributable to AT&T ($1.20 per diluted share)		6,244
Dividends to stockholders ($0.94 per share)		(4,894)
Balance at end of period		$29,086
Treasury Stock		
Balance at beginning of year	(1,308)	$(47,029)
Repurchase of common stock	(1)	(10)
Issuance of treasury stock	7	246
Balance at end of period	(1,302)	$(46,793)
Accumulated Other Comprehensive Income Attributable to AT&T, net of tax		
Balance at beginning of year		$8,060
Other comprehensive loss attributable to AT&T		(1,021)
Balance at end of period		$7,039
Noncontrolling Interest		
Balance at beginning of year		$554
Net income attributable to noncontrolling interest		178
Distributions		(119)
Acquisition of noncontrolling interests		29
Balance at end of period		$642
Total Stockholders' Equity at beginning of year		$86,924
Total Stockholders' Equity at end of period		$87,501

See Notes to Consolidated Financial Statements.

AT&T INC.
JUNE 30, 2015

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)
Dollars in millions except per share amounts

NOTE 1. PREPARATION OF INTERIM FINANCIAL STATEMENTS

Basis of Presentation Throughout this document, AT&T Inc. is referred to as "AT&T," "we" or the "Company." We believe that these consolidated financial statements include all adjustments, consisting only of normal recurring accruals, that are necessary to present fairly the results for the presented interim periods. The results for the interim periods are not necessarily indicative of those for the full year. You should read this document in conjunction with the consolidated financial statements and accompanying notes included in our Annual Report on Form 10-K for the year ended December 31, 2014.

The consolidated financial statements include the accounts of the Company and our majority-owned subsidiaries and affiliates. Our subsidiaries and affiliates operate in the communications services industry both domestically and internationally, providing wireless communications services, traditional wireline voice services, data/broadband and Internet services, video services, telecommunications equipment, managed networking and wholesale services.

All significant intercompany transactions are eliminated in the consolidation process. Investments in less than majority-owned subsidiaries and partnerships where we have significant influence are accounted for under the equity method. Earnings from certain investments accounted for using the equity method are included for periods ended within up to one month of our period end. We also recorded our proportionate share of our equity method investees' other comprehensive income (OCI) items, including actuarial gains and losses on pension and other postretirement benefit obligations.

The preparation of financial statements in conformity with U.S. generally accepted accounting principles (GAAP) requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes, including estimates of probable losses and expenses. Actual results could differ from those estimates. Certain amounts have been reclassified to conform to the current period's presentation.

New Accounting Standards

Revenue Recognition In May 2014, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update No. 2014-09, "Revenue from Contracts with Customers (Topic 606)" (ASU 2014-09), which replaces existing revenue recognition rules with a comprehensive revenue measurement and recognition standard and expanded disclosure requirements. ASU 2014-09 becomes effective for annual reporting periods beginning after December 15, 2017, following the July 2015 approval of a one-year deferral of the effective date by the FASB. We continue to evaluate the impact of the new standard and available adoption methods.

Long-Term Debt and Debt Issuance Costs In April 2015, the FASB issued ASU No. 2015-03, "Interest—Imputation of Interest: Simplifying the Presentation of Debt Issuance Costs" (ASU 2015-03), which will result in the reclassification of debt issuance costs from "Other Assets" to inclusion as a reduction of our reportable "Long-Term Debt" balance on our consolidated balance sheets. ASU 2015-03 becomes effective January 1, 2016, subject to early adoption, and will require full retrospective application. We do not expect this new standard to have a material impact on our consolidated balance sheets.

AT&T INC.
JUNE 30, 2015

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) - Continued
Dollars in millions except per share amounts
NOTE 2. EARNINGS PER SHARE
A reconciliation of the numerators and denominators of basic and diluted earnings per share for the three and six months ended June 30, 2015 and 2014, is shown in the table below:

	Three months ended June 30,		Six months ended June 30,	
	2015	2014	2015	2014
Numerators				
Numerator for basic earnings per share:				
Net Income	$3,146	$3,621	$6,422	$7,355
Less: Net income attributable to noncontrolling interest	(102)	(74)	(178)	(156)
Net Income attributable to AT&T	3,044	3,547	6,244	7,199
Dilutive potential common shares:				
Share-based payment	2	3	6	7
Numerator for diluted earnings per share	$3,046	$3,550	$6,250	$7,206
Denominators (000,000)				
Denominator for basic earnings per share:				
Weighted average number of common shares outstanding	5,204	5,204	5,204	5,213
Dilutive potential common shares:				
Share-based payment (in shares)	16	16	16	16
Denominator for diluted earnings per share	5,220	5,220	5,220	5,229
Basic earnings per share attributable to AT&T	$0.58	$0.68	$1.20	$1.38
Diluted earnings per share attributable to AT&T	$0.58	$0.68	$1.20	$1.38

AT&T INC.
JUNE 30, 2015

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) - Continued
Dollars in millions except per share amounts

NOTE 3. OTHER COMPREHENSIVE INCOME

Changes in the balances of each component included in accumulated other comprehensive income (accumulated OCI) are presented below. All amounts are net of tax and exclude noncontrolling interest.

At June 30, 2015 and for the period ended:	Foreign Currency Translation Adjustment	Net Unrealized Gains (Losses) on Available-for-Sale Securities	Net Unrealized Gains (Losses) on Cash Flow Hedges	Defined Benefit Postretirement Plans	Accumulated Other Comprehensive Income
Balance as of December 31, 2014	$ (26)	$ 498	$ 741	$ 6,847	$ 8,060
Other comprehensive income (loss) before reclassifications	(185)	34	(449)	-	(600)
Amounts reclassified from accumulated OCI	-	[1] (9)	[2] 17	[3] (429)	[4] (421)
Net other comprehensive income (loss)	(185)	25	(432)	(429)	(1,021)
Balance as of June 30, 2015	$ (211)	$ 523	$ 309	$ 6,418	$ 7,039

At June 30, 2014 and for the period ended:	Foreign Currency Translation Adjustment	Net Unrealized Gains (Losses) on Available-for-Sale Securities	Net Unrealized Gains (Losses) on Cash Flow Hedges	Defined Benefit Postretirement Plans	Accumulated Other Comprehensive Income
Balance as of December 31, 2013	$ (367)	$ 450	$ 445	$ 7,352	$ 7,880
Other comprehensive income (loss) before reclassifications	5	59	(98)	-	(34)
Amounts reclassified from accumulated OCI	416 [1]	(14) [2]	21 [3]	(418) [4]	5
Net other comprehensive income (loss)	421	45	(77)	(418)	(29)
Balance as of June 30, 2014	$ 54	$ 495	$ 368	$ 6,934	$ 7,851

[1] Translation (gain) loss reclassifications are included in Other income (expense) - net in the consolidated statements of income.

[2] (Gains) losses are included in Other income (expense) - net in the consolidated statements of income.

[3] (Gains) losses are included in Interest expense in the consolidated statements of income. See Note 6 for additional information.

[4] The amortization of prior service credits associated with postretirement benefits, net of amounts capitalized as part of construction labor, are included in Cost of services and sales and Selling, general and administrative in the consolidated statements of income (see Note 5). Actuarial loss

reclassifications related to our equity method investees are included in Other income (expense) - net in the consolidated statements of income.

AT&T INC.
JUNE 30, 2015

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) - Continued
Dollars in millions except per share amounts

NOTE 4. SEGMENT INFORMATION

Our segments are strategic business units that offer different products and services over various technology platforms and/or in different geographies that are managed accordingly. We analyze our operating segments based on segment income before income taxes. We make our capital allocation decisions based on our strategic direction of the business, needs of the network (wireless or wireline) providing services and to provide emerging services to our customers. Actuarial gains and losses from pension and other postretirement benefits, interest expense and other income (expense) – net, are managed only on a total company basis and are, accordingly, reflected only in consolidated results. Therefore, these items are not included in each segment's reportable results. The customers and long-lived assets of our reportable segments are predominantly in the United States. We have three reportable segments: (1) Wireless, (2) Wireline and (3) International.

The Wireless segment uses our nationwide network to provide consumer and business customers with wireless data and voice communications services.

The Wireline segment uses our regional, national and global network to provide consumer and business customers with data and voice communications services, AT&T U-verse® high speed Internet, video and VoIP services and managed networking to business customers.

The International segment uses the Iusacell, Unefon, and Nextel Mexico regional and national networks to provide consumer and business customers with wireless data and voice communication services in Mexico. Results from the equity method investment in América Móvil S.A. de C.V. (prior to the June 2014 disposal of our investment) are included in this segment.

The Corporate and Other column includes unallocated corporate expenses, which includes costs to support corporate-driven activities and operations, and impacts of corporate-wide decisions for which the individual operating segments are not being evaluated, including interest costs and expected return on plan assets for our pension and postretirement benefit plans as well as our actuarial gains and losses on our pension and postretirement plan valuations. Results from equity method investments in YP Holdings LLC and Otter Media (our joint venture with The Chernin Group), are also excluded from our segment results as those results are not considered in our assessment of segment performance. We have revised our prior-period presentation to conform to our current reporting.

AT&T INC.
JUNE 30, 2015

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) - Continued
Dollars in millions except per share amounts

For the three months ended June 30, 2015

	Wireless	Wireline	International	Corporate and Other	Consolidated Results
Service	$ 15,115	$ 13,981	$ 445	$ -	$ 29,541
Equipment	3,189	233	46	6	3,474
Total segment operating revenues	18,304	14,214	491	6	33,015
Operations and support expenses	11,551	10,362	529	165	22,607
Depreciation and amortization expenses	2,073	2,488	125	10	4,696
Total segment operating expenses	13,624	12,850	654	175	27,303
Segment operating income (loss)	4,680	1,364	(163)	(169)	5,712
Interest expense	-	-	-	932	932
Equity in net income of affiliates	-	1	-	32	33
Other income (expense) – net	-	-	-	48	48
Segment income (loss) before income taxes	$ 4,680	$ 1,365	$ (163)	$ (1,021)	$ 4,861

For the six months ended June 30, 2015

	Wireless	Wireline	International	Corporate and Other	Consolidated Results
Service	$ 29,927	$ 27,916	$ 660	$ -	$ 58,503
Equipment	6,563	446	67	12	7,088
Total segment operating revenues	36,490	28,362	727	12	65,591
Operations and support expenses	23,232	20,625	748	544	45,149
Depreciation and amortization expenses	4,131	4,964	169	10	9,274
Total segment operating expenses	27,363	25,589	917	554	54,423
Segment operating income (loss)	9,127	2,773	(190)	(542)	11,168
Interest expense	-	-	-	1,831	1,831
Equity in net income (loss) of affiliates	(4)	(6)	-	43	33
Other income (expense) – net	-	-	-	118	118
Segment income (loss) before income taxes	$ 9,123	$ 2,767	$ (190)	$ (2,212)	$ 9,488

AT&T INC.
JUNE 30, 2015

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) - Continued
Dollars in millions except per share amounts

For the three months ended June 30, 2014

	Wireless	Wireline	International	Corporate and Other	Consolidated Results
Service	$ 15,148	$ 14,408	$ -	$ -	$ 29,556
Equipment	2,782	229	-	8	3,019
Total segment operating revenues	17,930	14,637	-	8	32,575
Operations and support expenses	11,568	10,700	-	141	22,409
Depreciation and amortization expenses	2,035	2,514	-	1	4,550
Total segment operating expenses	13,603	13,214	-	142	26,959
Segment operating income (loss)	4,327	1,423	-	(134)	5,616
Interest expense	-	-	-	881	881
Equity in net income (loss) of affiliates	(29)	-	99	32	102
Other income (expense) – net	-	-	-	1,269	1,269
Segment income before income taxes	$ 4,298	$ 1,423	$ 99	$ 286	$ 6,106

For the six months ended June 30, 2014

	Wireless	Wireline	International	Corporate and Other	Consolidated Results
Service	$ 30,535	$ 28,797	$ -	$ -	$ 59,332
Equipment	5,261	441	-	17	5,719
Total segment operating revenues	35,796	29,238	-	17	65,051
Operations and support expenses	22,450	21,157	-	383	43,990
Depreciation and amortization expenses	3,966	5,198	-	3	9,167
Total segment operating expenses	26,416	26,355	-	386	53,157
Segment operating income (loss)	9,380	2,883	-	(369)	11,894
Interest expense	-	-	-	1,741	1,741
Equity in net income (loss) of affiliates	(49)	1	153	85	190
Other income (expense) – net	-	-	-	1,414	1,414
Segment income (loss) before income taxes	$ 9,331	$ 2,884	$ 153	$ (611)	$ 11,757

NOTE 5. PENSION AND POSTRETIREMENT BENEFITS

Substantially all of our employees are covered by one of our noncontributory pension plans. We also provide certain medical, dental, life insurance, and death benefits to certain retired employees under various plans and accrue actuarially determined postretirement benefit costs. Our objective in funding these plans, in combination with the standards of the Employee Retirement Income Security Act of 1974, as amended (ERISA), is to accumulate assets sufficient to provide benefits described in the plans to employees upon their retirement.

In December 2014, we offered an opportunity for certain management employees who were retirement eligible as of March 31, 2015 to elect an enhanced, full lump sum payment option of their accrued pension if they retired on or before March 31, 2015. The lump sum value totaled approximately $1,200 which will be distributed in 2015. We recorded special termination benefits of approximately $150 as a result of this offer.

In 2013, we made a voluntary contribution of a preferred equity interest in AT&T Mobility II LLC, the primary holding company for our domestic wireless business, to the trust used to pay pension benefits under our qualified pension plans. The preferred equity interest had a value of $8,896 at June 30, 2015. The trust is entitled to receive cumulative cash distributions of $560 per annum, which are distributed quarterly in equal amounts and accounted for as contributions. We distributed $280 to the trust during the six months ended June 30, 2015. So long as we make the distributions, we will have no limitations on our ability to declare a dividend or repurchase shares. This preferred equity interest is a plan asset under ERISA and is recognized as such in the plan's separate financial statements. However, because the preferred equity interest is not unconditionally transferable to an unrelated party, it is not reflected in plan assets in our consolidated financial statements and instead has been eliminated in consolidation. We also agreed to make a cash contribution to the trust of $175 no later than the due date of our federal income tax return for 2014. This contribution was made in June 2015.

AT&T INC.
JUNE 30, 2015

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) - Continued
Dollars in millions except per share amounts

We recognize actuarial gains and losses on pension and postretirement plan assets in our operating results at our annual measurement date of December 31, unless earlier remeasurements are required. The following table details pension and postretirement benefit costs included in operating expenses in the accompanying consolidated statements of income, expense credits are denoted with parentheses. A portion of these expenses is capitalized as part of internal construction projects, providing a small reduction in the net expense recorded.

	Three months ended June 30,		Six months ended June 30,	
	2015	2014	2015	2014
Pension cost:				
Service cost – benefits earned during the period	$300	$282	$599	$564
Interest cost on projected benefit obligation	473	662	947	1,323
Expected return on assets	(826)	(851)	(1,652)	(1,700)
Amortization of prior service credit	(26)	(23)	(52)	(47)
Net pension (credit) cost	$(79)	$70	$(158)	$140
Postretirement cost:				
Service cost – benefits earned during the period	$56	$58	$111	$116
Interest cost on accumulated postretirement benefit obligation	241	364	483	729
Expected return on assets	(105)	(162)	(210)	(326)
Amortization of prior service credit	(319)	(362)	(639)	(724)
Net postretirement (credit) cost	$(127)	$(102)	$(255)	$(205)
Combined net pension and postretirement (credit) cost	$(206)	$(32)	$(413)	$(65)

Our combined net pension and postretirement cost decreased $174 in the second quarter and $348 for the first six months of 2015. The decrease is primarily due to the change in the method used to estimate the service and interest components of net periodic benefit cost for pension and other postretirement benefits. While this change in estimate, which was made in the fourth quarter of 2014, provides a more precise measurement of interim service and interest costs, it will not affect the measurement of our total benefit obligations as of December 31 or our annual net periodic benefit cost as the change in the service and interest costs is completely offset in the actuarial gain or loss reported. The decrease from this change was partially offset by lower amortization of prior service credits as previous postretirement plan changes have become fully amortized, our lower expected long-term rate of return on our postretirement plan assets and updated assumed mortality rates.

We also provide senior- and middle-management employees with nonqualified, unfunded supplemental retirement and savings plans. Net supplemental retirement pension benefits cost, which is not included in the table above, was $21 in the second quarter of 2015, of which $18 was interest cost, and $41 for the first six months, of which $37 was interest cost. In 2014, net supplemental retirement pension benefits cost was $29 in the second quarter, of which $28 was interest cost, and $58 for the first six months, of which $55 was interest cost.

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NOTE 6. FAIR VALUE MEASUREMENTS AND DISCLOSURE

The Fair Value Measurement and Disclosure framework provides a three-tiered fair value hierarchy that gives highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (Level 1 measurements) and the lowest priority to unobservable inputs (Level 3 measurements). The three levels of the fair value hierarchy are described below:

Level 1 Inputs to the valuation methodology are unadjusted quoted prices for identical assets or liabilities in active markets that we have the ability to access.

Level 2 Inputs to the valuation methodology include:
- Quoted prices for similar assets and liabilities in active markets.
- Quoted prices for identical or similar assets or liabilities in inactive markets.
- Inputs other than quoted market prices that are observable for the asset or liability.
- Inputs that are derived principally from or corroborated by observable market data by correlation or other means.

Level 3 Inputs to the valuation methodology are unobservable and significant to the fair value measurement.
- Fair value is often based on developed models in which there are few, if any, external observations.

The fair value measurements level of an asset or liability within the fair value hierarchy is based on the lowest level of any input that is significant to the fair value measurement. Valuation techniques used should maximize the use of observable inputs and minimize the use of unobservable inputs.

The valuation methodologies described above may produce a fair value calculation that may not be indicative of future net realizable value or reflective of future fair values. We believe our valuation methods are appropriate and consistent with other market participants. The use of different methodologies or assumptions to determine the fair value of certain financial instruments could result in a different fair value measurement at the reporting date. There have been no changes in the methodologies used since December 31, 2014.

Long-Term Debt and Other Financial Instruments
The carrying amounts and estimated fair values of our long-term debt, including current maturities and other financial instruments, are summarized as follows:

	June 30, 2015		December 31, 2014	
	Carrying Amount	Fair Value	Carrying Amount	Fair Value
Notes and debentures	$113,167	$116,669	$81,632	$90,367
Bank borrowings	5	5	5	5
Investment securities	2,758	2,758	2,735	2,735

The carrying value of debt with an original maturity of less than one year approximates market value. The fair value measurements used for notes and debentures are considered Level 2 and are determined using various methods, including quoted prices for identical or similar securities in both active and inactive markets.

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Following is the fair value leveling for available-for-sale securities and derivatives as of June 30, 2015 and December 31, 2014:

	June 30, 2015			
	Level 1	Level 2	Level 3	Total
Available-for-Sale Securities				
Domestic equities	$1,165	$-	$ -	$1,165
International equities	614	-	-	614
Fixed income bonds	-	778	-	778
Asset Derivatives[1]				
Interest rate swaps	-	170	-	170
Cross-currency swaps	-	1,280	-	1,280
Liability Derivatives[1]				
Cross-currency swaps	-	(2,568)	-	(2,568)

	December 31, 2014			
	Level 1	Level 2	Level 3	Total
Available-for-Sale Securities				
Domestic equities	$1,160	$-	$ -	$1,160
International equities	553	-	-	553
Fixed income bonds	-	836	-	836
Asset Derivatives[1]				
Interest rate swaps	-	157	-	157
Cross-currency swaps	-	1,243	-	1,243
Interest rate locks	-	5	-	5
Liability Derivatives[1]				
Cross-currency swaps	-	(1,506)	-	(1,506)
Interest rate locks	-	(133)	-	(133)

[1] Derivatives designated as hedging instruments are reflected as "Other assets," "Other noncurrent liabilities" and, for a portion of interest rate swaps, "Other current assets" in our consolidated balance sheets.

Investment Securities
Our investment securities include equities, fixed income bonds and other securities. A substantial portion of the fair values of our available-for-sale securities was estimated based on quoted market prices. Investments in securities not traded on a national securities exchange are valued using pricing models, quoted prices of securities with similar characteristics or discounted cash flows. Realized gains and losses on securities are included in "Other income (expense) – net" in the consolidated statements of income using the specific identification method. Unrealized gains and losses, net of tax, on available-for-sale securities are recorded in accumulated OCI. Unrealized losses that are considered other than temporary are recorded in "Other income (expense) – net" with the corresponding reduction to the carrying basis of the investment. Fixed income investments of $93 have maturities of less than one year, $392 within one to three years, $63 within three to five years, and $230 for five or more years.

Our cash equivalents (money market securities), short-term investments (certificate and time deposits) and customer deposits are recorded at amortized cost, and the respective carrying amounts approximate fair values. Short-term investments are recorded in "Other current assets" and our investment securities are recorded in "Other assets" on the consolidated balance sheets.

Derivative Financial Instruments

We employ derivatives to manage certain market risks, primarily interest rate risk and foreign currency exchange risk. This includes the use of interest rate swaps, interest rate locks, foreign exchange forward contracts and combined interest rate foreign exchange contracts (cross-currency swaps). We do not use derivatives for trading or speculative purposes. We record derivatives on our consolidated balance sheets at fair value that is derived from observable market data, including yield curves and foreign exchange rates (all of our derivatives are Level 2). Cash flows associated with derivative instruments are presented in the same category on the consolidated statements of cash flows as the item being hedged.

The majority of our derivatives are designated either as a hedge of the fair value of a recognized asset or liability or of an unrecognized firm commitment (fair value hedge), or as a hedge of a forecasted transaction or of the variability of cash flows to be received or paid related to a recognized asset or liability (cash flow hedge).

Fair Value Hedging We designate our fixed-to-floating interest rate swaps as fair value hedges. The purpose of these swaps is to manage interest rate risk by managing our mix of fixed-rate and floating-rate debt. These swaps involve the receipt of fixed-rate amounts for floating interest rate payments over the life of the swaps without exchange of the underlying principal amount. Accrued and realized gains or losses from interest rate swaps impact interest expense in the consolidated statements of income. Unrealized gains on interest rate swaps are recorded at fair market value as assets, and unrealized losses on interest rate swaps are recorded at fair market value as liabilities. Changes in the fair values of the interest rate swaps are exactly offset by changes in the fair value of the underlying debt. Gains or losses realized upon early termination of our fair value hedges are recognized in interest expense. In the six months ended June 30, 2015 and June 30, 2014, no ineffectiveness was measured on interest rate swaps designated as fair value hedges.

Cash Flow Hedging We designate our cross-currency swaps as cash flow hedges. We have entered into multiple cross-currency swaps to hedge our exposure to variability in expected future cash flows that are attributable to foreign currency risk generated from the issuance of our Euro, British pound sterling, Canadian dollar and Swiss Franc denominated debt. These agreements include initial and final exchanges of principal from fixed foreign denominations to fixed U.S. denominated amounts, to be exchanged at a specified rate, which was determined by the market spot rate upon issuance. They also include an interest rate swap of a fixed or floating foreign-denominated rate to a fixed U.S. denominated interest rate.

Unrealized gains on derivatives designated as cash flow hedges are recorded at fair value as assets, and unrealized losses on derivatives designated as cash flow hedges are recorded at fair value as liabilities, both for the period they are outstanding. For derivative instruments designated as cash flow hedges, the effective portion is reported as a component of accumulated OCI until reclassified into interest expense in the same period the hedged transaction affects earnings. The gain or loss on the ineffective portion is recognized as "Other income (expense) – net" in the consolidated statements of income in each period. We evaluate the effectiveness of our cross-currency swaps each quarter. In the six months ended June 30, 2015 and June 30, 2014, no ineffectiveness was measured on cross-currency swaps designated as cash flow hedges.

Periodically, we enter into and designate interest rate locks to partially hedge the risk of changes in interest payments attributable to increases in the benchmark interest rate during the period leading up to the probable issuance of fixed-rate debt. We designate our interest rate locks as cash flow hedges. Gains and losses when we settle our interest rate locks are amortized into income over the life of the related debt, except where a material amount is deemed to be ineffective, which would be immediately reclassified to "Other income (expense) – net" in the consolidated statements of income. Over the next 12 months, we expect to reclassify $61 from accumulated OCI to interest expense due to the amortization of net losses on historical interest rate locks.

We hedge a portion of the exchange risk involved in anticipation of highly probable foreign currency-denominated transactions. In anticipation of these transactions, we often enter into foreign exchange contracts to provide currency at a fixed rate. Some of these instruments are designated as cash flow hedges while others remain nondesignated. Gains and losses at the time we settle or take delivery on our designated foreign exchange contracts are amortized into income in the same period the hedged transaction affects earnings, except where an amount is deemed to be ineffective, which would be immediately reclassified to "Other income (expense) – net" in the consolidated statements of income. In the six months ended June 30, 2015 and June 30, 2014, no ineffectiveness was measured on foreign exchange contracts designated as cash flow hedges.

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Collateral and Credit-Risk Contingency We have entered into agreements with our derivative counterparties establishing collateral thresholds based on respective credit ratings and netting agreements. At June 30, 2015, we had posted collateral of $1,544 (a deposit asset) and held collateral of $396 (a receipt liability). Under the agreements, if our credit rating had been downgraded one rating level by Fitch Ratings, before the final collateral exchange in June, we would have been required to post additional collateral of $69. At December 31, 2014, we had posted collateral of $530 (a deposit asset) and held collateral of $599 (a receipt liability). We do not offset the fair value of collateral, whether the right to reclaim cash collateral (a receivable) or the obligation to return cash collateral (a payable), against the fair value of the derivative instruments.

Following is the notional amount of our outstanding derivative positions:

	June 30, 2015	December 31, 2014
Interest rate swaps	$ 8,050	$ 6,550
Cross-currency swaps	27,375	26,505
Interest rate locks	-	6,750
Total	$ 35,425	$ 39,805

Following are the related hedged items affecting our financial position and performance:

Effect of Derivatives on the Consolidated Statements of Income