

## Notes to Consolidated Financial Statements

### Note 1.

#### Summary of Significant Accounting Policies

##### **a. Basis of Presentation**

Expeditors International of Washington, Inc. (“the Company”) is a global logistics company operating through a worldwide network of offices, international service centers and exclusive or non-exclusive agents. The Company’s customers include retailing and wholesaling, electronics, and manufacturing companies around the world. The Company grants credit upon approval to customers.

International trade is influenced by many factors, including economic and political conditions in the United States and abroad, currency exchange rates, and United States and foreign laws and policies relating to tariffs, trade restrictions, foreign investments and taxation. Periodically, governments consider a variety of changes to current tariffs and trade restrictions. The Company cannot predict which, if any, of these proposals may be adopted, nor can the Company predict the effects adoption of any such proposal will have on the Company’s business. Doing business in foreign locations also subjects the Company to a variety of risks and considerations not normally encountered by domestic enterprises. In addition to being affected by governmental policies concerning international trade, the Company’s business may also be affected by political developments and changes in government personnel or policies in the nations in which it does business.

The consolidated financial statements include the accounts of the Company and its subsidiaries stated in U.S. dollars, the Company’s reporting currency. In addition, the consolidated financial statements also include the accounts of operating entities where the Company maintains a parent-subsidiary relationship through unilateral control over assets and operations together with responsibility for payment of all liabilities, notwithstanding a lack of technical majority ownership of the subsidiary common stock.

All significant intercompany accounts and transactions have been eliminated in consolidation.

All dollar amounts in the notes are presented in thousands except for share data.

##### **b. Cash Equivalents**

All highly liquid investments with a maturity of three months or less at date of purchase are considered to be cash equivalents.

##### **c. Short-term Investments**

Short-term investments are designated as available-for-sale and cost approximates market at December 31, 2006 and 2005.

##### **d. Accounts Receivable**

The Company maintains an allowance for doubtful accounts, which is reviewed at least monthly for estimated losses resulting from the inability of its customers to make required payments for services. Additional allowances may be necessary in the future if the ability of its customers to pay deteriorates.

##### **e. Long-Lived Assets, Depreciation and Amortization**

Property and equipment are recorded at cost and are depreciated or amortized on the straight-line method over the

shorter of the assets' estimated useful lives or lease terms. Useful lives for major categories of property and equipment are as follows:

Buildings	28 to 40 years
Furniture, fixtures, equipment and purchased software	3 to 5 years
Vehicles	3 to 5 years

Expenditures for maintenance, repairs, and renewals of minor items are charged to earnings as incurred. Major renewals and improvements are capitalized. Upon disposition, the cost and related accumulated depreciation are removed from the accounts and the resulting gain or loss is included in income for the period.

Effective January 1, 2002, the Company ceased to amortize goodwill. Goodwill is recorded net of accumulated amortization of \$765 at December 31, 2006 and 2005. For the years ended December 31, 2006 and 2005, the Company performed the required annual impairment test during the fourth quarter and determined that no impairment had occurred.

Other intangibles consist principally of payments made to purchase customer lists of agents in countries where the Company established its own presence by opening offices. Other intangible assets are amortized over their estimated useful lives for periods up to 15 years and are reviewed for impairment if an event or circumstance indicates that an impairment loss may have been incurred.

Balances as of December 31 are as follows:

	2006	2005
<b>Other intangibles</b>	<b>\$ 19,689</b>	19,724
<b>Less accumulated amortization</b>	<b>(12,105)</b>	(10,727)
	<b>\$ 7,584</b>	8,997
<b>Aggregate amortization expense for the year ended December 31</b>	<b>\$ 1,369</b>	1,422

Estimated annual amortization expense will approximate \$1,300 during each of the next five years.

#### **f. Revenues and Revenue Recognition**

The Company derives its revenues from three principal sources: 1) airfreight, 2) ocean freight, and 3) customs brokerage and other services. These are the revenue categories presented in the financial statements.

As a non-asset based carrier, the Company does not own transportation assets. Rather, the Company generates the major portion of its air and ocean freight revenues by purchasing transportation services from direct (asset-based) carriers and reselling those services to its customers. The difference between the rate billed to customers (the sell rate), and the rate paid to the carrier (the buy rate) is termed "net revenue" or "yield". By consolidating shipments from multiple customers and concentrating its buying power, the Company is able to negotiate favorable buy rates from the direct carriers, while at the same time offering lower sell rates than customers would otherwise be able to negotiate themselves.

Airfreight revenues include the charges to the Company for carrying the shipments when the Company acts as a freight consolidator. Ocean freight revenues include the charges to the Company for carrying the shipments when the Company acts as a Non-Vessel Operating Common Carrier (NVOCC). In each case the Company is acting as an indirect carrier. When acting as an indirect carrier, the Company will issue a House Airway Bill (HAWB) or a House Ocean Bill of Lading (HOBL) to customers as the contract of carriage. In turn, when the freight is physically tendered to a direct carrier, the Company receives a contract of carriage known as a Master Airway Bill for airfreight shipments and a Master Ocean Bill of Lading for ocean shipments. At this point, the risk of loss passes to the carrier, however, in order to claim for any such loss, the customer is first obligated to pay the freight charges.

Based upon the terms in the contract of carriage, revenues related to shipments where the Company issues an HAWB or an HOBL are recognized at the time the freight is tendered to the direct carrier at origin. Costs related to the shipments are also recognized at this same time.

Revenues realized in other capacities, for instance, when the Company acts as an agent for the shipper, and does not issue an HAWB or an HOBL, include only the commissions and fees earned for the services performed. These revenues are recognized upon completion of the services.

Customs brokerage and other services involves providing services at destination, such as helping customers clear shipments through customs by preparing required documentation, calculating and providing for payment of duties and other taxes on behalf of the customers as well as arranging for any required inspections by governmental agencies, and arranging for delivery. This is a complicated function requiring technical knowledge of customs rules and regulations in the multitude of countries in which the Company has offices. Revenues related to customs brokerage and other services are recognized upon completion of the services.

Arranging international shipments is a complex task. Each actual movement can require multiple services. In some instances, the Company is asked to perform only one of these services. However, in most instances, the Company may perform multiple services. These services include destination breakbulk services and value added ancillary services such as local transportation, export customs formalities, distribution services and logistics management. Each of these services has an associated fee which is recognized as revenue upon completion of the service.

Typically, the fees for each of these services are quoted as separate components, however, customers on occasion will request an all-inclusive rate for a set of services known in the industry as “door-to-door service.” This means that the customer is billed a single rate for all services from pickup at origin to delivery at destination. In these instances, the revenue for origin and destination services, as well as revenue that will be characterized as freight charges, is allocated to branches as set by preexisting Company policy perhaps supplemented by customer specific negotiations between the offices involved. Each of the Company’s branches are separate profit centers and the primary compensation for the branch management group comes in the form of incentive-based compensation calculated directly from the operating income of that branch. This compensation structure ensures that the allocation of revenue and expense among components of services, when provided under an all-inclusive rate, are done in an objective manner on a fair value basis in accordance with Emerging Issues Task Force (EITF) 00-21, “Revenue Arrangements with Multiple Deliverables.”

#### **g. Income Taxes**

Income taxes are accounted for under the asset and liability method of accounting. Under this method, deferred tax assets and liabilities are recognized for the future tax consequences attributed to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases, the tax effect of loss carryforwards and tax credit carryforwards. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date.

#### **h. Net Earnings per Common Share**

Diluted earnings per share is computed using the weighted average number of common shares and dilutive potential common shares outstanding. Dilutive potential common shares represent outstanding stock options and stock purchase rights. Basic earnings per share is calculated using the weighted average number of common shares outstanding without taking into consideration dilutive potential common shares outstanding.

#### **i. Stock Option Plans**

Prior to January 1, 2006, the Company applied APB Opinion No. 25, “Accounting for Stock Issued to Employees,” and related interpretations in accounting for its stock option and its employee stock purchase rights plans. Accordingly, no compensation cost had been recognized for its fixed stock option or employee stock purchase rights plans.

Effective January 1, 2006, the Company adopted Statement of Financial Accounting Standard (SFAS) No. 123 (Revised 2004), "Share-Based Payment" (SFAS 123R) using the modified retrospective transition method. Under the modified retrospective method, prior periods may be restated either as of the beginning of the year of adoption or for all periods presented. The Company has elected to restate all periods presented to include compensation expense for all unvested stock options and share awards. Accordingly, salaries and related costs for the years ended December 31, 2006, 2005 and 2004 have been increased to include compensation expense for the fair value of stock options and stock purchase rights on a straight line basis over the period they become vested. See Note 5D for further discussion of the impact of the adoption of SFAS 123R on the consolidated balance sheets, the consolidated results of operations, diluted earnings per share and consolidated statements of cash flows.

#### **j. Foreign Currency**

Foreign currency amounts attributable to foreign operations have been translated into U.S. dollars using year-end exchange rates for assets and liabilities, historical rates for equity, and weighted average rates for revenues and expenses. Unrealized gains or losses arising from fluctuations in the year-end exchange rates are generally recorded as components of other comprehensive income as adjustments from foreign currency translation. Currency fluctuations are a normal operating factor in the conduct of the Company's business and exchange transaction gains and losses are generally included in freight consolidation expenses.

The Company follows a policy of accelerating international currency settlements to manage its foreign exchange exposure. Accordingly, the Company enters into foreign currency hedging transactions only in limited locations where there are regulatory or commercial limitations on the Company's ability to move money freely around the world. Such hedging activity during 2006, 2005, and 2004 was insignificant. Net foreign currency losses realized in 2006 were \$321. Net foreign currency gains realized in 2005 and 2004 were \$862 and \$86, respectively. The Company had no foreign currency derivatives outstanding at December 31, 2006 and 2005.

#### **k. Comprehensive Income**

Comprehensive income consists of net earnings and other gains and losses affecting shareholders' equity that, under generally accepted accounting principles in the United States, are excluded from net earnings. For the Company, these consist of foreign currency translation gains and losses and unrealized gains and losses on securities, net of related income tax effects.

Accumulated other comprehensive income consists of the following:

Years ended December 31,	2006	2005
<hr/>		
(in thousands)		
<b>Foreign currency translation adjustments</b>	<b>\$ 13,765</b>	<b>(2,977)</b>
<b>Unrealized gain on securities</b>	<b>399</b>	<b>338</b>
	<hr/>	
	<b>\$ 14,164</b>	<b>(2,639)</b>

#### **l. Segment Reporting**

The Company is organized functionally in geographic operating segments. Accordingly, management focuses its attention on revenues, net revenues, operating income, identifiable assets, capital expenditures, depreciation and amortization and equity generated in each of these geographical areas when evaluating effectiveness of geographic management. The Company charges its subsidiaries and affiliates for services rendered in the United States on a cost recovery basis. Transactions among the Company's various offices are conducted using the same arms-length pricing methodologies the Company uses when its offices transact business with independent agents.

**m. Use of Estimates**

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of the 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 period. Actual results could differ from those estimates.

**n. Reclassifications**

Certain prior year amounts have been reclassified to conform with the 2006 presentation.

**o. Recent Accounting Pronouncements**

In June 2006, the FASB ratified the EITF Issue 06-3, "How Taxes Collected From Customers and Remitted to Governmental Authorities Should Be Presented in the Income Statement," (EITF 06-3). The scope of EITF 06-3 includes any tax assessed by a governmental authority that is both imposed on and concurrent with a specific revenue-producing transaction between a seller and a customer, including but not limited to sales and value-added taxes. In EITF 06-3 a consensus was reached that entities may adopt a policy of presenting these taxes in the income statement on either a gross or net basis. If these taxes are significant, an entity should disclose its policy of presenting taxes and the amount of taxes if reflected on a gross basis in the income statement. EITF 06-3 is effective for interim and annual reporting periods beginning after December 15, 2006. The Company is required to and plans to adopt EITF 06-3 in the first quarter of 2007. The Company presents revenues net of sales and value-added taxes in its consolidated statement of earnings and does not anticipate changing its policy as a result of the adoption of EITF 06-3.

In June 2006, the FASB issued Interpretation No. 48, "Accounting for Uncertainty in Income Taxes, an interpretation of FASB Statement No. 109", (FIN 48). FIN 48 clarifies the accounting for uncertainty in income taxes recognized in the Company's financial statements in accordance with SFAS No. 109, "Accounting for Income Taxes" (SFAS 109). The interpretation establishes guidelines for recognition, measurement, presentation and disclosure of uncertain tax positions taken or expected to be taken in income tax returns. FIN 48 is effective for fiscal years beginning after December 15, 2006. The Company is required to and plans to adopt the provisions of FIN 48 beginning in the first quarter of 2007. The Company does not expect the adoption of FIN 48 to have a material impact on the Company's consolidated financial condition or results of operations.

On September 13, 2006, the Securities and Exchange Commission (the "SEC") issued Staff Accounting Bulletin No. 108 (SAB 108), "Considering the Effects of Prior Year Misstatements when Qualifying Misstatements in Current Year Financial Statements," which provides interpretive guidance on the consideration of the effects of prior year misstatements in quantifying current year misstatements for the purpose of a materiality assessment. The Company is required to and has adopted SAB 108 for its fiscal year ending December 31, 2006. The adoption of SAB 108 had no impact on the Company's financial condition or results of operations.

In September 2006, the FASB issued SFAS No. 157, "Fair Value Measurements" (SFAS 157). SFAS 157 defines fair value, establishes a framework for measuring fair value in generally accepted accounting principles, and expands disclosures about fair value measurements. This Statement applies under other accounting pronouncements that require or permit fair value measurements, the FASB having previously concluded in those accounting pronouncements that fair value is the relevant measurement attribute. Accordingly, this Statement does not require any new fair value measurements. SFAS 157 is effective for financial statements issued for fiscal years beginning after November 15, 2007, and interim periods within those fiscal years. The Company is required to and plans to adopt the provisions of SFAS 157 beginning in the first quarter of 2008. The Company is currently assessing the impact of the adoption of SFAS 157.

In February 2007, the FASB issued SFAS No. 159, "The Fair Value Option for Financial Assets and Financial Liabilities" (SFAS 159). Under the provisions of SFAS 159, Companies may choose to account for eligible financial

instruments, warranties and insurance contracts at fair value on a contract-by-contract basis. Changes in fair value will be recognized in earnings each reporting period. SFAS 159 is effective for financial statements issued for fiscal years beginning after November 15, 2007, and interim periods within those fiscal years. The Company is required to and plans to adopt the provisions of SFAS 159 beginning in the first quarter of 2008. The Company is currently assessing the impact of the adoption of SFAS 159.

## Note 2.

### Other Assets

The Company regularly evaluates the recoverability of certain other assets. During 2004, the Company determined that an impairment had occurred and accordingly, a \$2,000 loss was recorded as an operating expense. No impairment occurred in 2006 or 2005.

## Note 3.

### Credit Arrangements

The Company has a \$50,000 United States bank line of credit extending through July 1, 2007. Borrowings under the line bear interest at LIBOR + .75% (6.07% at December 31, 2006) and are unsecured. As of December 31, 2006, the entire \$50,000 was available and the Company had no borrowings under this line.

The majority of the Company's foreign subsidiaries maintain bank lines of credit for short-term working capital purposes. These credit lines are supported by standby letters of credit issued by a United States bank, or guarantees issued by the Company to the foreign banks issuing the credit line. Lines of credit totaling \$19,516 and \$12,850 at December 31, 2006 and 2005, respectively, bear interest at rates up to 4% over the foreign banks' equivalent prime rates. At December 31, 2006, the Company had no amounts outstanding under these lines and was contingently liable for approximately \$62,608 under outstanding standby letters of credit and guarantees related to these lines of credit and other obligations.

The guarantees relate to obligations of the Company's foreign subsidiaries for credit extended in the ordinary course of business by direct carriers, primarily airlines, and for duty and tax deferrals available from governmental entities responsible for customs and value-added-tax (VAT) taxation. The total underlying amounts due and payable for transportation and governmental excises are properly recorded as obligations in the books of the respective foreign subsidiaries, and there would be no need to record additional expense in the unlikely event the parent company were to be required to perform.

At December 31, 2006, the Company was in compliance with all restrictive covenants of these credit lines and the associated credit facilities, including maintenance of certain minimum asset, working capital and equity balances and ratios.

## Note 4.

### Income Taxes

Income tax expense (benefit) for 2006, 2005, and 2004 includes the following components:

	Federal	State	Foreign	Total
<b>2006</b>				
<b>Current</b>	\$ 68,176	9,760	78,553	156,489
<b>Deferred</b>	2,096	2,076	—	4,172
	<u>\$ 70,272</u>	<u>11,836</u>	<u>78,553</u>	<u>160,661</u>
<b>2005</b>				
<b>Current</b>	\$ 25,776	6,851	60,438	93,065
<b>Deferred</b>	(2,830)	(870)	—	(3,700)
	<u>\$ 22,946</u>	<u>5,981</u>	<u>60,438</u>	<u>89,365</u>
<b>2004</b>				
<b>Current</b>	\$ 13,741	2,168	46,533	62,442
<b>Deferred</b>	21,253	1,276	—	22,529
	<u>\$ 34,994</u>	<u>3,444</u>	<u>46,533</u>	<u>84,971</u>

Income tax expense differs from amounts computed by applying the United States Federal income tax rate of 35% to earnings before income taxes and minority interest as a result of the following:

	2006	2005	2004
<b>Computed “expected” tax expense</b>	\$ 138,482	100,344	76,986
<b>Increase (reduction) in income taxes resulting from:</b>			
<b>State income taxes, net of Federal income tax benefit</b>	7,694	3,888	2,238
<b>Nondeductible stock compensation expense, net</b>	10,426	7,346	6,995
<b>IRC 965 tax benefit for repatriated foreign earnings</b>	2,328	(21,680)	—
<b>Other, net</b>	1,731	(533)	(1,248)
	<u>\$ 160,661</u>	<u>89,365</u>	<u>84,971</u>

In accordance with IRC 965, the Company recorded a one-time tax benefit of \$22 million in the fourth quarter of 2005. In order to qualify for this credit, the Company adopted a plan which required qualified capital expenditures of approximately \$105 million. The Company completed the required capital expenditures during 2006.

The components of earnings before income taxes and minority interest are as follows:

	2006	2005	2004
<b>United States</b>	<b>\$ 117,725</b>	72,339	37,527
<b>Foreign</b>	<b>277,939</b>	214,358	182,432
	<b><u>\$ 395,664</u></b>	286,697	219,959

The tax effects of temporary differences, tax credits and operating loss carryforwards that give rise to significant portions of deferred tax assets and deferred tax liabilities at December 31, 2006 and 2005 are as follows:

Years ended December 31,	2006	2005
<i>Deferred Tax Assets:</i>		
<b>Accrued third party charges, deductible for taxes upon economic performance (i.e. actual payment)</b>	<b>\$ 3,661</b>	2,714
<b>Provision for doubtful accounts receivable</b>	<b>2,348</b>	2,724
<b>Excess of financial statement over tax depreciation</b>	<b>4,474</b>	4,828
<b>Foreign currency translation adjustment</b>	<b>—</b>	1,603
<b>Retained liability for cargo claims</b>	<b>806</b>	1,472
<b>Capital loss</b>	<b>1,140</b>	1,257
<b>Deductible stock compensation expense, net</b>	<b>12,720</b>	12,661
<b>Total gross deferred tax assets</b>	<b>25,149</b>	27,259
<i>Deferred Tax Liabilities:</i>		
<b>Unremitted foreign earnings, net of related foreign tax credits</b>	<b>(36,322)</b>	(32,174)
<b>Foreign currency translation adjustment</b>	<b>(7,413)</b>	—
<b>Other</b>	<b>(667)</b>	(1,155)
<b>Total gross deferred tax liabilities</b>	<b>\$ (44,402)</b>	(33,329)
<b>Net deferred tax liabilities</b>	<b>\$ (19,253)</b>	(6,070)
<b>Current deferred tax assets</b>	<b>\$ (7,490)</b>	(7,208)
<b>Noncurrent deferred tax liabilities</b>	<b>\$ (26,743)</b>	(13,278)

## Note 5.

### Shareholders' Equity

#### **a. Stock Repurchase Plans**

The Company has a Non-Discretionary Stock Repurchase Plan under which management is authorized to repurchase up to 20,000,000 shares of the Company's common stock in the open market with the proceeds received from the exercise of Employee and Director Stock Options. As of December 31, 2006, the Company had repurchased and retired 15,407,473 shares of common stock at an average price of \$13.24 per share over the period from 1994 through 2006.

In November 2001, the Board of Directors expanded the Company's Discretionary Stock Repurchase Plan to allow for the repurchase of such shares as may be necessary to reduce the issued and outstanding stock to 200,000,000 shares of common stock. As of December 31, 2006, the Company had repurchased and retired 9,752,196 shares of common stock at an average price of \$26.43 per share over the period from 2001 through 2006.

#### **b. Stock Option Plans**

At December 31, 2006, the Company has two stock option plans (the "1985 Plan" and the "2006 Plan") for employees under which the Board of Directors may grant officers and key employees options to purchase common stock at prices equal to or greater than market value on the date of grant. On May 3, 2006, the shareholders approved the Company's 2006 Plan, which made available a total of 3,000,000 shares of the Company's common stock for purchase upon exercise of options granted under the 2006 Plan. The 1997 Option Plan was cancelled upon the approval of the 2005 Plan. The 1985 Plan provides for non-qualified grants. The 2006 Plan provides for qualified and non-qualified grants. Under the 1985, 2005 and 2006 Plans, outstanding options generally vest and become exercisable over periods up to five years from the date of grant and expire no more than 10 years from the date of grant. Grants under the 2006 Plan are limited to not more than 100,000 shares per person. No additional shares can be granted under the 2006 Plan after April 30, 2007.

The Company also has a stock option plan ("Directors' Plan") under which non-employee directors elected at each annual meeting are granted non-qualified options to purchase 32,000 shares of common stock at prices equal to the market value on the date of grant on the first business day of the month following the meeting. On May 3, 2006, the Directors' Plan was amended by shareholder vote to require a one year vesting period. Previously, options granted under the Directors' Plan vested immediately.

Upon the exercise of non-qualified stock options and disqualifying dispositions of incentive stock options, the Company derives a tax deduction measured by the excess of the market value over the option price at the date of disqualifying disposition. The portion of the benefit from the deduction which equals the estimated fair value of the options (previously recognized as compensation expense) is recorded as a credit to the deferred tax asset for non-qualified stock options and is recorded as a credit to current tax expense for any disqualified dispositions of incentive stock options. All of the tax benefit received upon option exercise for the tax deduction in excess of the estimated fair value of the options is credited to additional paid-in capital.

Details regarding the plans are as follows:

	Unoptioned shares					Outstanding shares	
	1985 Plan	1997 Plan	2005 Plan	2006 Plan	Directors' Plan	Number of shares	Weighted average price per share
<b>Balance at</b>							
<b>December 31, 2003</b>	6,912	2,603,900	—	—	512,000	25,190,960	\$ 10.53
<b>Options granted</b>	—	(2,140,950)	—	—	(128,000)	2,268,950	\$ 21.02
<b>Options exercised</b>	—	—	—	—	—	(3,573,772)	\$ 4.80
<b>Options forfeited</b>	—	489,350	—	—	—	(489,350)	\$ 15.32
<b>Balance at</b>							
<b>December 31, 2004</b>	6,912	952,300	—	—	384,000	23,396,788	\$ 12.32
<b>Options authorized</b>	—	—	1,809,100	—	—	—	\$ —
<b>Options transferred</b>	—	(1,190,900)	1,190,900	—	—	—	\$ —
<b>Options granted</b>	—	—	(2,903,250)	—	(128,000)	3,031,250	\$ 24.51
<b>Options exercised</b>	—	—	—	—	—	(3,612,592)	\$ 7.52
<b>Options forfeited</b>	—	234,800	53,500	—	—	(545,000)	\$ 17.26
<b>Options cancelled</b>	—	3,800	—	—	—	(3,800)	\$ 12.78
<b>Balance at</b>							
<b>December 31, 2005</b>	6,912	—	150,250	—	256,000	22,266,646	\$ 14.64
<b>Options authorized</b>	—	—	—	3,000,000	—	—	—
<b>Options granted</b>	—	—	—	(2,984,610)	(128,000)	3,112,610	\$ 44.21
<b>Options exercised</b>	—	—	—	—	—	(3,053,425)	\$ 10.60
<b>Options forfeited</b>	—	—	—	64,300	—	(415,300)	\$ 23.55
<b>Options cancelled</b>	—	—	—	—	—	(18,350)	\$ 12.15
<b>Options not granted</b>	—	—	(150,250)	—	—	—	\$ —
<b>Balance at</b>							
<b>December 31, 2006</b>	<b>6,912</b>	—	—	<b>79,690</b>	<b>128,000</b>	<b>21,892,181</b>	<b>\$ 19.23</b>

### c. Stock Purchase Plan

In May 2002, the shareholders approved the Company's 2002 Employee Stock Purchase Plan ("2002 Plan"), which became effective August 1, 2002 upon the expiration of the 1988 Employee Stock Purchase Plan ("1988 Plan") on July 31, 2002. The Company's 2002 Plan provides for 4,305,452 shares of the Company's common stock, including 305,452 remaining shares transferred from the 1988 Plan, to be reserved for issuance upon exercise of purchase rights granted to employees who elect to participate through regular payroll deductions beginning August 1 of each year. The purchase rights are exercisable on July 31 of the following year at a price equal to the lesser of (1) 85% of the fair market value of the Company's stock on July 31 or (2) 85% of the fair market value of the Company's stock on the preceding August 1. At December 31, 2006, an aggregate of 3,127,578 shares had been issued under the 2002 Plan and \$11,399 had been withheld in connection with the plan year ending July 31, 2007.

#### d. Adoption of SFAS 123R

As described in Note 1, effective January 1, 2006, the Company adopted SFAS 123R, requiring the recording of compensation expense based on an estimate of the fair value of options awarded under its fixed stock option or employee stock purchase rights plans. The Company elected to utilize the modified retrospective method of transitioning to SFAS 123R and has restated all prior periods to recognize the required stock compensation expense.

In applying the modified retrospective method, the Company has recorded compensation expense as previously stated in the Company's pro forma SFAS 123 disclosures in the footnotes to its prior period financial statements. The fair value of options used to determine this compensation expense was originally determined using the Black-Scholes model and no changes have been made to the compensation expense as originally stated in the pro forma disclosures. The original measurements and assumptions previously disclosed in the footnotes to the Company's financial statement included in its annual Form 10-K filings and, in more recent years, in its Form 10-Q filings, also have not been changed. In the process of recording the associated deferred tax assets related to this compensation expense, as required by SFAS 123R, the Company made its computations on a "grant by grant" basis. As a result of this exercise, the Company determined that recording deferred tax assets based on the disclosed pro forma amounts would have been incorrect under the provisions of SFAS No. 109, "Accounting for Income Taxes". Accordingly, in restating the results of prior years, management has elected to record adjustments to income tax expense and to properly record deferred tax assets.

Prior to the adoption of SFAS 123R, in the statement of cash flows, the tax benefits received by the Company from the exercise of certain employee stock options were added back to net earnings in determining net cash provided by operating activities. SFAS 123R requires a different presentation for that portion of the tax benefit received upon option exercise which exceeds the tax benefit that would have been recorded based on the estimated fair value of the options previously recognized as compensation expense. Accordingly, the Company has reclassified this excess tax benefit from cash provided by operating activities to cash provided by financing activities in the statement of cash flows.

The following tables summarize the adjustments to certain line items in the Company's consolidated financial statements as a result of adopting SFAS 123R for all periods presented. Certain prior year amounts have been reclassified to conform to the 2006 presentation. Third party outsourced labor costs were reclassified in the consolidated statement of earnings as a result of the growth in the Company's distribution services business. Net distributions to minority interests of immaterial amounts were reclassified to net cash used in financing activities.

Restated line items in the consolidated balance sheet:

	December 31, 2005			
	As previously reported	SFAS No. 123R Adjustments	Reclassifications	As restated
<b>Deferred Federal and state income taxes</b>	\$ 25,939	\$ (12,661)	—	\$ 13,278
<i>Shareholders' equity:</i>				
<b>Additional paid-in capital</b>	18,663	162,242	—	180,905
<b>Retained earnings</b>	895,565	(149,581)	—	745,984

Restated line items in the consolidated statement of earnings:

	Year ended December 31, 2005			
	As previously reported	SFAS No. 123R Adjustments	Reclassifications	As restated
<b>Salaries and related costs</b>	\$ 557,730	\$ 33,457	\$ 5,617	\$ 596,804
<b>Other operating expenses</b>	197,369	—	(5,617)	191,752
<b>Total operating expenses</b>	3,597,271	33,457	—	3,630,728
<b>Operating income</b>	304,510	(33,457)	—	271,053
<b>Earnings before income taxes and minority interest</b>	320,154	(33,457)	—	286,697
<b>Income tax expense</b>	94,624	(5,259)	—	89,365
<b>Net earnings before minority interest</b>	225,530	(28,198)	—	197,332
<b>Net earnings</b>	218,634	(28,198)	—	190,436
<b>Diluted earnings per share</b>	\$ .98	\$ (.12)	—	\$ .86
<b>Basic earnings per share</b>	\$ 1.03	\$ (.14)	—	\$ .89

	Year ended December 31, 2004			
	As previously reported	SFAS No. 123R Adjustments	Reclassifications	As restated
<b>Salaries and related costs</b>	\$ 479,364	\$ 29,621	\$ 4,829	\$ 513,814
<b>Other operating expenses</b>	185,828	—	(4,829)	180,999
<b>Total operating expenses</b>	3,076,454	29,621	—	3,106,075
<b>Operating income</b>	241,045	(29,621)	—	211,424
<b>Earnings before income taxes and minority interest</b>	249,580	(29,621)	—	219,959
<b>Income tax expense</b>	88,415	(3,444)	—	84,971
<b>Net earnings before minority interest</b>	161,165	(26,177)	—	134,988
<b>Net earnings</b>	156,126	(26,177)	—	129,949
<b>Diluted earnings per share</b>	\$ .71	\$ (.12)	—	\$ .59
<b>Basic earnings per share</b>	\$ .74	\$ (.13)	—	\$ .61

Restated line items in the consolidated statement of cash flows:

	Year ended December 31, 2005			
	As previously reported	SFAS No. 123R Adjustments	Reclassifications	As restated
<b>Net earnings</b>	\$ 218,634	\$ (28,198)	\$ —	\$ 190,436
<b>Deferred income tax (benefit) expense</b>	(4,779)	1,079	—	(3,700)
<b>Excess tax benefits from employee stock plans</b>	—	(13,367)	—	(13,367)
<b>Tax benefits from employee stock plans</b>	19,705	(19,705)	—	—
<b>Stock compensation expense</b>	—	33,457	—	33,457
<b>Minority interest in earnings of consolidated entities</b>	6,001	—	895	6,896
<b>Increase in accounts payable and accrued expenses</b>	103,639	—	(8,813)	94,826
<b>Increase in taxes payable, net</b>	—	13,367	7,213	20,580
<b>Other</b>	(1,363)	—	1,600	237
<b>Net cash provided by operating activities</b>	279,548	(13,367)	895	267,076
<b>Excess tax benefits from employee stock plans</b>	—	13,367	—	13,367
<b>Net distributions to minority interests</b>	—	—	(436)	(436)
<b>Net cash used in financing activities</b>	(119,754)	13,367	(436)	(106,823)
<b>Effect of exchange rate changes on cash</b>	\$ (14,116)	\$ —	\$ (459)	\$ (14,575)

	Year ended December 31, 2004			
	As previously reported	SFAS No. 123R Adjustments	Reclassifications	As restated
<b>Net earnings</b>	\$ 156,126	\$ (26,177)	\$ —	\$ 129,949
<b>Deferred income tax expense</b>	19,511	3,018	—	22,529
<b>Excess tax benefits from employee stock plans</b>	—	(12,997)	—	(12,997)
<b>Tax benefits from employee stock plans</b>	19,459	(19,459)	—	—
<b>Stock compensation expense</b>	—	29,621	—	29,621
<b>Minority interest in earnings of consolidated entities</b>	4,103	—	936	5,039
<b>Increase in accounts payable and accrued expenses</b>	113,904	—	(9,882)	104,022
<b>Increase in taxes payable, net</b>	—	12,997	6,885	19,882
<b>Other</b>	(2,545)	—	2,997	452
<b>Net cash provided by operating activities</b>	192,659	(12,997)	936	180,598
<b>Excess tax benefits from employee stock plans</b>	—	12,997	—	12,997
<b>Net distributions to minority interests</b>	—	—	(284)	(284)
<b>Net cash used in financing activities</b>	(21,762)	12,997	(284)	(9,049)
<b>Effect of exchange rate changes on cash</b>	\$ 7,234	\$ —	\$ (652)	\$ 6,582

The following tables summarize information about fixed-price stock options for the year ended December 31, 2006:

	Number of shares	Weighted average exercise price per share	Weighted average remaining contractual life	Aggregate intrinsic value (in thousands)
<b>Outstanding at December 31, 2005</b>	22,266,646	\$ 14.64		
<b>Options granted</b>	3,112,610	44.21		
<b>Options exercised</b>	(3,053,425)	10.60		
<b>Options forfeited</b>	(415,300)	23.55		
<b>Options cancelled</b>	(18,350)	12.15		
<b>Outstanding at December 31, 2006</b>	<b>21,892,181</b>	<b>\$ 19.23</b>	<b>5.81 years</b>	<b>\$ 476,987</b>
<b>Exercisable at December 31, 2006</b>	<b>11,518,446</b>	<b>\$ 11.71</b>	<b>3.99 years</b>	<b>\$ 331,821</b>

	Unvested Options	
	Number of shares	Weighted average fair value per share
<b>Balance at December 31, 2005</b>	11,368,450	\$ 9.57
<b>Options granted</b>	3,112,610	22.69
<b>Options vested</b>	(3,692,025)	7.75
<b>Options forfeited</b>	(415,300)	11.91
<b>Balance at December 31, 2006</b>	<b>10,373,735</b>	<b>\$ 14.06</b>

The fair value of each option grant is estimated on the date of grant using the Black-Scholes option pricing model with the following assumptions used for grants issued during the years ended December 31, 2006, 2005 and 2004:

For the years ended December 31,	2006	2005	2004
<b>Dividend yield</b>	.51%	.56%	.54%
<b>Volatility</b>	44 – 43%	44 – 49%	46%
<b>Risk-free interest rates</b>	4.69 – 5.11%	3.64 – 4.14%	2.1 – 4.7%
<b>Expected life (years) – stock option plans</b>	7.14 – 8.89	6.67 – 9.36	6.6 – 9.2
<b>Expected life (years) – stock purchase rights plans</b>	1	1	1
<b>Weighted average fair value of stock options granted during the period</b>	\$ 22.69	\$ 12.69	\$ 10.65
<b>Weighted average fair value of stock purchase rights granted during the period</b>	\$ 13.27	\$ 7.17	\$ 6.17

The Company's expected volatility assumptions are based on the historical volatility of the Company's stock. The expected life assumption is primarily based on historical employee exercise patterns and employee post-vesting termination behavior. The risk-free interest rate for the expected term of the option is based on the corresponding yield curve in effect at the time of grant for U.S. Treasury bonds having the same term as the expected life of the option, i.e. a ten year bond rate is used for valuing an option with a ten year expected life. The expected dividend yield is based on the Company's historical experience. The forfeiture rate used to calculate compensation expense is primarily based on historical pre-vesting employee forfeiture patterns.

The total intrinsic value of options exercised during the years ended December 31, 2006, 2005 and 2004 was approximately \$111 million, \$76 million and \$65 million, respectively. The estimated fair value of shares vested during the years ended December 31, 2006, 2005 and 2004 was approximately \$29 million, \$28 million and \$23 million, respectively.

As of December 31, 2006, the total unrecognized compensation cost related to unvested stock options is \$103 million and the weighted average period over which that cost is expected to be recognized is 1.91 years.

Total stock compensation expense and the total related tax benefit recognized for the years ended December 31, 2006, 2005 and 2004 are as follows:

For the years ended December 31,	2006	2005	2004
Stock compensation expense	<b>\$ 41,739</b>	\$ 33,457	\$ 29,621
Recognized tax benefit, net	<b>\$ 2,725</b>	\$ 5,259	\$ 3,444

Shares issued as a result of stock option exercises and employee stock plan purchases are issued as new shares outstanding by the Company's transfer agent.

#### **e. Basic and Diluted Earnings Per Share**

The following table reconciles the numerator and the denominator of the basic and diluted per share computations for earnings per share in 2006, 2005 and 2004.

	Net earnings	Weighted average shares	Earnings per share
<b>2006</b>			
<b>Basic earnings per share</b>	<b>\$ 235,094</b>	<b>213,454,579</b>	<b>\$ 1.10</b>
<b>Effect of dilutive potential common shares</b>	<b>—</b>	<b>8,768,733</b>	<b>—</b>
<b>Diluted earnings per share</b>	<b>\$ 235,094</b>	<b>222,223,312</b>	<b>\$ 1.06</b>
<b>2005</b>			
<b>Basic earnings per share</b>	\$ 190,436	213,555,102	\$ .89
<b>Effect of dilutive potential common shares</b>	—	6,675,074	—
<b>Diluted earnings per share</b>	\$ 190,436	220,230,176	\$ .86
<b>2004</b>			
<b>Basic earnings per share</b>	\$ 129,949	212,768,302	\$ .61
<b>Effect of dilutive potential common shares</b>	—	7,348,382	—
<b>Diluted earnings per share</b>	\$ 129,949	220,116,684	\$ .59

The following shares have been excluded from the computation of diluted earnings per share because the effect would have been antidilutive:

Years ended December 31,	2006	2005	2004
<b>Shares</b>	<b>132,510</b>	500	128,000

## Note 6.

### Fair Value of Financial Instruments

The Company's financial instruments, other than cash, consist primarily of cash equivalents, short-term investments, accounts receivable, short-term debt, accounts payable and accrued expenses. The fair values of these financial instruments approximate their carrying amounts based upon market interest rates or their short-term nature.

## Note 7.

### Commitments

#### a. Leases

The Company occupies office and warehouse facilities under terms of operating leases expiring up to 2015. Total rent expense for 2006, 2005 and 2004 was \$28,324, \$34,488 and \$33,197, respectively. At December 31, 2006, future minimum annual lease payments under all leases are as follows:

<b>2007</b>	\$ 37,133
<b>2008</b>	26,550
<b>2009</b>	12,035
<b>2010</b>	5,517
<b>2011</b>	2,422
Thereafter	2,418
	<u>\$ 86,075</u>

**b. Unconditional Purchase Obligations**

The Company enters into short-term agreements with asset-based providers reserving space on a guaranteed basis. The pricing of these obligations varies to some degree with market conditions. The Company only enters into agreements that management believes the Company can fulfill with relative ease. Historically, the Company has not paid for guaranteed space that it has not used. Management believes, in line with historical experience, committed purchase obligations outstanding as of December 31, 2006 of \$293,019, will be fulfilled during 2007 in the Company's ordinary course of business.

**c. Employee Benefits**

The Company has employee savings plans under which the Company provides a discretionary matching contribution. In 2006, 2005, and 2004, the Company's contributions under the plans were \$5,814, \$5,183, and \$4,383, respectively.

## Note 8.

### Contingencies

The Company is ordinarily involved in claims and lawsuits which arise in the normal course of business, none of which currently, in management's opinion, will have a significant effect on the Company's operations or financial position.

## Note 9.

### Business Segment Information

Financial information regarding the Company's 2006, 2005, and 2004 operations by geographic area are as follows:

	United States	Other North America	Asia	Europe	Australasia	Latin America	Middle East	Eliminations	Consolidated
<b>2006</b>									
Revenues from unaffiliated customers	\$ 932,165	120,381	2,616,098	618,999	54,948	67,463	215,912	—	4,625,966
Transfers between geographic areas	\$ 109,552	7,956	16,228	32,595	6,383	8,368	11,293	(192,375)	—
<b>Total revenues</b>	<b>\$ 1,041,717</b>	<b>128,337</b>	<b>2,632,326</b>	<b>651,594</b>	<b>61,331</b>	<b>75,831</b>	<b>227,205</b>	<b>(192,375)</b>	<b>4,625,966</b>
Net revenues	\$ 525,039	61,531	359,613	216,110	32,894	32,931	54,821	—	1,282,939
Operating income	\$ 102,041	15,433	178,265	48,366	8,887	7,519	14,605	—	375,116
Identifiable assets at year end	\$ 906,256	62,584	360,904	363,332	26,055	33,273	67,794	2,140	1,822,338
Capital expenditures	\$ 121,005	820	10,030	6,086	446	1,205	1,633	—	141,225
Depreciation and amortization	\$ 18,533	1,339	5,108	6,739	785	1,548	1,396	—	35,448
Equity	\$ 1,215,298	26,160	249,017	117,738	14,844	16,133	31,570	(600,825)	1,069,935
<b>2005</b>									
Revenues from unaffiliated customers	\$ 762,835	98,369	2,224,313	534,897	48,234	58,976	174,157	—	3,901,781
Transfers between geographic areas	\$ 87,778	5,588	13,280	24,923	5,920	7,416	8,406	(153,311)	—
<b>Total revenues</b>	<b>\$ 850,613</b>	<b>103,957</b>	<b>2,237,593</b>	<b>559,820</b>	<b>54,154</b>	<b>66,392</b>	<b>182,563</b>	<b>(153,311)</b>	<b>3,901,781</b>
Net revenues	\$ 432,530	50,823	296,925	179,238	30,135	26,772	43,186	—	1,059,609
Operating income	\$ 61,245	11,273	147,130	30,179	7,956	5,698	7,572	—	271,053
Identifiable assets at year end	\$ 805,273	51,312	322,391	294,555	21,681	26,639	47,009	(2,816)	1,566,044
Capital expenditures	\$ 78,668	882	3,374	4,534	1,084	1,290	949	—	90,781
Depreciation and amortization	\$ 15,077	1,484	4,759	6,107	830	1,198	1,433	—	30,888
Equity	\$ 1,021,761	17,329	205,027	75,146	11,108	10,679	22,030	(436,698)	926,382
<b>2004</b>									
Revenues from unaffiliated customers	\$ 628,093	77,696	1,880,135	492,651	44,042	52,347	142,535	—	3,317,499
Transfers between geographic areas	\$ 69,695	4,288	11,096	18,921	5,262	6,188	6,373	(121,823)	—
<b>Total revenues</b>	<b>\$ 697,788</b>	<b>81,984</b>	<b>1,891,231</b>	<b>511,572</b>	<b>49,304</b>	<b>58,535</b>	<b>148,908</b>	<b>(121,823)</b>	<b>3,317,499</b>
Net revenues	\$ 362,961	42,954	252,189	164,132	25,583	21,274	37,144	—	906,237
Operating income	\$ 43,093	9,872	115,716	26,330	5,742	3,742	6,929	—	211,424
Identifiable assets at year end	\$ 642,930	47,594	279,840	304,701	22,361	21,711	40,667	4,249	1,364,053
Capital expenditures	\$ 34,856	2,150	11,153	13,445	845	1,744	2,051	—	66,244
Depreciation and amortization	\$ 13,539	1,211	4,044	5,099	665	770	1,375	—	26,703
Equity	\$ 893,108	19,448	203,743	88,398	12,824	6,306	17,982	(420,665)	821,144

The Company charges its subsidiaries and affiliates for services rendered in the United States on a cost recovery basis.

No single country outside the United States represented more than 10% of the Company's total revenue, net revenue or total identifiable assets in any period presented except as noted in the table below.

	2006	2005	2004
<i>Total revenues:</i>			
<b>Hong Kong</b>	<b>15%</b>	15%	16%
<b>People's Republic of China</b>	<b>21%</b>	21%	18%
<i>Net revenues:</i>			
<b>Hong Kong</b>	— *	— *	10%
<b>People's Republic of China</b>	— *	12%	10%

\* Represents less than 10% in the period presented.

## Note 10.

### Quarterly Results (Unaudited)

	1ST	2ND	3RD	4TH
<b>2006</b>				
<b>Revenues</b>	<b>\$ 1,024,592</b>	<b>1,129,324</b>	<b>1,229,723</b>	<b>1,242,327</b>
<b>Net revenues</b>	<b>296,197</b>	<b>313,570</b>	<b>339,338</b>	<b>333,834</b>
<b>Net earnings</b>	<b>52,352</b>	<b>56,329</b>	<b>63,803</b>	<b>62,610</b>
<b>Diluted earnings per share</b>	<b>.24</b>	<b>.25</b>	<b>.29</b>	<b>.28</b>
<b>Basic earnings per share</b>	<b>.25</b>	<b>.26</b>	<b>.30</b>	<b>.29</b>
<b>2005</b>				
Revenues	\$ 825,164	927,999	1,046,442	1,102,176
Net revenues	230,683	250,660	281,925	296,341
Net earnings	31,047	36,698	48,404	74,287
Diluted earnings per share	.14	.17	.22	.34
Basic earnings per share	.15	.17	.23	.35

Net revenues are determined by deducting freight consolidation costs from total revenues. The sum of quarterly per share data may not equal the per share total reported for the year.

All share and per share information have been adjusted to reflect a 2-for-1 stock split effected in June 2006.

Certain amounts for 2005 have been restated as required by the modified retrospective method in connection with the implementation of SFAS 123R. In preparing the second quarter 2005 SFAS 123R restatements during the second quarter of 2006, an insignificant difference of \$177 was noted which should have been included for the first quarter of 2005. The insignificant amount was included in the year-to-date 2005 restated amounts reported in the second quarter of 2006. The first quarter 2005 results presented in the above schedule are the corrected restated amounts and are not the amounts originally reported in the Form 10-Q filed for the first quarter 2006.

The fourth quarter 2005 results include a \$21,680 tax benefit (\$.10 per share increase in net earnings) as a result of a one time election under IRC 965.