FLIGHT ADVISORY
FAB
BOARD

December 3, 1988

Fred Smith
Chief Executive Officer
Federal Express Corporation
2005 Corporate Avenue
Memphis, Tennessee

Dear Fred:

In response to your letter to me dated November 30, 1988, I wish to comment on some of the statements made in that correspondence. First let me apologize for the misunderstanding about the date for the Board of Directors meeting we discussed at our luncheon meeting. I understand now that the meeting at which you plan to discuss changes to the Company pension plan is January 23, 1989.

The statement made in your letter, "...based on my experience and study, only a mix of programs can adequately cover all of the contingencies the future may hold", is one in which I concur. During our luncheon meeting we discussed this in light of the fact that the original concept for our pension plan provided this mix in a defined benefit plan of 40% of final average earnings with 25 years of service with COLA provisions and a variable contribution plan of 4-5% of annual compensation in an cash allocation that would be compounded over that 25 years of service. If you will recall, my only real concern with your original plan was the commitment of the Company to fund the programs. As stated in "Your Employee Benefits" book, contributions to the Deferred Profit Sharing Plan (DPSP) or the variable contribution part of our pension plan are "contingent upon Federal Express's level of profitability." A defined contribution plan provides for cash allocations and is treated in the same manner in which salaries are a considered, an expense item in the Company's budget. This fact is vividly exemplified by the fact that those pilots who have participated in the DPSP since its inception have lost, due to the lack of cash funding of the DPSP, approximately $180,000 in compounded dollars after 25 years of service assuming a 7% annual growth rate (refer to page 13 of the Airline Pension Survey we provided). This fact is the primary reason why I was so adamant about refunding the DPSP before any other changes are made to the retirement program.

Another point raised in your recent letter to me and I quote, "... in periods of severe disintermediation (e.g. high inflation, negative real interest rates) such as we had in the late 1970's, defined contribution programs are severely disadvantaged", is one in which I do not fully concur. I can agree that those individuals tied to a "safe harbor" investment portfolio would be disadvantaged as they would not have the option of moving all or part of their funds to other more lucrative investments, such as money market accounts or other securities market investments. This is one of the reasons the FAB has been opposed to limiting the investment options available for the pilots and have requested that more options be afforded us such as those provided for pilots at United Airlines. Another aspect of this question, is that the likelihood of having a period of disintermediation or a period of deflation for any prolonged portion of a pilot's 25 to 30 year career is not very great, thereby providing even those who select a safe harbor option a limited risk to be severely disadvantaged. In fact those individuals who, through prudent money management, invest wisely during periods of moderate financial conditions (most likely to be experienced during the majority of their 25 to 30 year career) will prosper considerably and be in a position to more than offset the effects of inflation.

As I stated to you during our recent meeting, I believe the COLA has real and substantial value as a part of our pension plan. My point is that the COLA offered by our Company is not the COLA commonly thought of by the average employee. The COLA offered to government employees is an example of one such plan that sets the standard for most peoples concept of COLA. I think it is important to recognize the difference. The most significant difference is the fact that the COLA offered by Federal Express is not computed on the current years retirement income which would include previous years COLA adjustments, but is an amount based on the initial retirement income calculated after joint and survivor benefits and social security offset have been considered. In other words, the government plan compounds COLA and the Federal Express plan does not. It is also important to note that there is a cap of 5% on the Company COLA. While I have my opinion as to value of COLA, I do not know what your opinion is concerning the real value of COLA. I request that you advise me as to what numerical percentage you have concluded is the value of COLA in our pension plan.

In your letter you also make reference to the problem of employees not earning retirement credits past age 60. Within the airline industry, companies that have defined benefit plans as their primary retirement vehicle allow for earning additional retirement credits beyond 25 years of service at a reduced amount, the most common amount being 1% per year for 5 additional years. Those airlines which have combination programs for retirement (e.g. a defined benefit plan and a defined contribution plan) offer incentives for earning additional credit in their defined benefit plan by not capping years of service. There is also incentive for an employee to continue working past age 60 to accrue funds in his/her defined contribution plan through contributions from the company and from the tremendous effect of compounding. I certainly support the concept of encouraging, through incentives, an employee to work past 25 years of service and/or age 60.

Any opinion I would have concerning whether or not the FAA will alter its rule concerning allowing pilots to continue to fly past age 60 would be subjective. If the FAA does change the rule, I suggest we meet to discuss the implication of such action.

Another issue which was not referenced in your letter, but which is of significant concern to us is early retirement. As I mentioned to you, other airlines that we surveyed compute early retirement income by applying an annual percentage rate reduction of approximately 3% to an pilot's normal retirement income. One aspect of the logic for subsidizing early retirement was to solve the problem of integrating their disability plans and their retirement plans. In other words, the advantage is to shift a pilot from an unfunded or marginally funded disability program to an already funded retirement program. Additionally, NASA studies as well as other recent technical studies indicate severe circuital rhythm problems with workers operating in combination daytime/nighttime work and sleep cycles. This gives rise for one to believe that reasons other than medical problems such as heart disease, etc. may be important considerations in providing a more reasonable early retirement option. Please advise me as to your views on how best to solve the early retirement issue.

Thank you in advance for your consideration of my opinions. I await your response.

Regards,

John W. Poag
Chairman, Flight Advisory Board

cc. Jim Barksdale
Jim Perkins
Jim Riedmeyer
Byron Hogue
Steve Priddy
All Crewmembers