

SPRINT NEXTEL CORP  
Form 10-K/A  
March 31, 2006

**UNITED STATES**

**SECURITIES AND EXCHANGE COMMISSION**

**Washington, D.C. 20549**

**FORM 10-K/A**

x **ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d)**  
**OF THE SECURITIES EXCHANGE ACT OF 1934**  
**For the fiscal year ended December 31, 2005**

**OR**

.. **TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d)**  
**OF THE SECURITIES EXCHANGE ACT OF 1934**  
**For the transition period from \_\_\_\_\_ to \_\_\_\_\_**

**Commission file number 1-04721**

**SPRINT NEXTEL CORPORATION**

(Exact name of registrant as specified in its charter)

|                                                                                               |                                                              |
|-----------------------------------------------------------------------------------------------|--------------------------------------------------------------|
| <b>KANSAS</b><br>(State or other jurisdiction of<br>incorporation or organization)            | <b>48-0457967</b><br>(I.R.S. Employer<br>Identification No.) |
| <b>2001 Edmund Halley Drive, Reston, Virginia</b><br>(Address of principal executive offices) | <b>20191</b><br>(Zip Code)                                   |
| <b>Registrant's telephone number, including area code:</b>                                    | <b>(703) 433-4000</b>                                        |
| <b>Securities registered pursuant to Section 12(b) of the Act:</b>                            |                                                              |

| <b>Title of each class</b>                                                                          | <b>Name of each exchange on which registered</b>   |
|-----------------------------------------------------------------------------------------------------|----------------------------------------------------|
| Common Stock, Series 1, \$2.00<br>par value, and Rights<br>Guarantees of Sprint Capital Corporation | New York Stock Exchange<br>New York Stock Exchange |

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6.875% Notes due 2028

**Securities registered pursuant to Section 12(g) of the Act: None**

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes  No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes  No

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

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

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer

Large accelerated filer  Accelerated Filer  Non-accelerated Filer   
Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act) Yes  No

Aggregate market value of voting and non-voting common stock equity held by non-affiliates at June 30, 2005, was \$37,255,897,903.

**COMMON SHARES OUTSTANDING AT FEBRUARY 28, 2006:**

VOTING COMMON STOCK

|          |               |
|----------|---------------|
| Series 1 | 2,849,846,056 |
| Series 2 | 79,831,333    |

|                         |            |
|-------------------------|------------|
| NON-VOTING COMMON STOCK | 37,594,109 |
|-------------------------|------------|

**Documents incorporated by reference**

Portions of the registrant's definitive proxy statement filed under Regulation 14A promulgated by the Securities and Exchange Commission under the Securities Exchange Act of 1934, which definitive proxy statement was filed on March 17, 2006, are incorporated by reference in Part III.

**EXPLANATORY NOTE**

We are filing this Form 10-K/A to amend Part II, Item 8 of our Annual Report filed on Form 10-K for the fiscal year ended December 31, 2005, which we filed with the Securities and Exchange Commission on March 7, 2006, to include a new note 26 in the Notes to the Consolidated Financial Statements appearing at the end of the annual report on Form 10-K/A. Note 26 includes certain consolidating financial information for IWO Holdings, Inc., a wholly owned subsidiary of Sprint Nextel Corporation, together with the subsidiary guarantors of IWO Holdings, Inc., as of and for the period from acquisition (October 20, 2005) to December 31, 2005, and Sprint Nextel Corporation on a stand-alone basis, Sprint Nextel's other subsidiaries on a combined basis, and Sprint Nextel and all of its subsidiaries on a consolidated basis as of and for the year ended December 31, 2005.

The information included in note 26 was not required for our annual report on Form 10-K. We, however, have elected to include this information in this Form 10-K/A based on Sprint Nextel's subsequent determination to guarantee certain indebtedness of IWO Holdings. Specifically, Sprint Nextel entered into a guarantee, dated March 22, 2006, in favor of the holders of Senior Secured Floating Rate Notes due 2012 of IWO Holdings, and a guarantee, dated March 22, 2006, in favor of the holders of 10.75% Senior Discount Notes due 2015 of IWO Holdings. Each guarantee represents the full and unconditional guarantee by Sprint Nextel of the obligations under the applicable notes, and other obligations under the respective indentures under which the notes were issued. No subsidiary of Sprint Nextel, other than the subsidiaries of IWO Holdings, Inc., guarantees these securities.

In connection with the filing of this annual report on Form 10-K/A and pursuant to Rules 12b-15, 13a-14(a) and 13a-14(b) under the Exchange Act, we are including currently dated certifications. This Form 10-K/A does not reflect events occurring after the filing of our annual report on Form 10-K on March 7, 2006 or include, or otherwise modify or update, the disclosure contained therein in any way other than as required to reflect the amendments discussed above.

**Item 8. Financial Statements and Supplementary Data**

The consolidated financial statements required by this item begin on page F-1 of this annual report on Form 10-K/A and are incorporated herein by reference. The financial statement schedule required under Regulation S-X is filed pursuant to Item 15 of this annual report on Form 10-K/A and is incorporated herein by reference.

**SIGNATURES**

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

SPRINT NEXTEL CORPORATION  
(Registrant)

By /s/ Gary D. Forsee  
Gary D. Forsee

Chief Executive Officer

Date: March 31, 2006

**SPRINT NEXTEL CORPORATION**

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| <i>Exhibits</i>                                                                                                                                                |                           |
| (23) (a) Consent of KPMG LLP, Independent Registered Public Accounting Firm                                                                                    |                           |
| (23) (b) Consent of Ernst & Young LLP, Independent Registered Public Accounting Firm                                                                           |                           |
| (31) (a) Certification of Chief Executive Officer Pursuant to Securities Exchange Act of 1934 Rule<br>13a-14(a)                                                |                           |
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| (32) (a) Certification of Chief Executive Officer Pursuant to 18 U.S.C. Section 1350, As adopted Pursuant to Section 906 of the<br>Sarbanes-Oxley Act of 2002. |                           |
| (32) (b) Certification of Chief Financial Officer Pursuant to 18 U.S.C. Section 1350, As adopted Pursuant to Section 906 of the<br>Sarbanes-Oxley Act of 2002. |                           |



**MANAGEMENT REPORT**

Our management is responsible for the integrity and objectivity of the information contained in this document. Management is responsible for the consistency of reporting this information and for ensuring that accounting principles generally accepted in the United States are used.

In discharging this responsibility, management maintains a comprehensive system of internal controls and supports an extensive program of internal audits, has made organizational arrangements providing appropriate divisions of responsibility and has established communication programs aimed at assuring that its policies, procedures and principles of business conduct are understood and practiced by its employees.

The 2005 and 2004 consolidated financial statements included in this document have been audited by KPMG LLP, independent registered public accounting firm. The 2003 consolidated financial statements included in this document have been audited by Ernst & Young LLP, independent registered public accounting firm. All audits were conducted using standards of the Public Company Accounting Oversight Board (United States) and KPMG's and Ernst & Young's reports and consents are included herein.

The Board of Directors' responsibility for these consolidated financial statements is pursued mainly through its Audit Committee. The Audit Committee, composed entirely of directors who are not officers or employees of Sprint Nextel, meets periodically with the Company's internal auditors and independent registered public accounting firm, both with and without management present, to assure that their respective responsibilities are being fulfilled. The internal auditors and independent registered public accounting firm have full access to the Audit Committee to discuss auditing and financial reporting matters.

/s/ Gary D. Forsee  
Gary D. Forsee  
President and Chief Executive Officer

/s/ Paul N. Saleh  
Paul N. Saleh  
Executive Vice President and Chief Financial Officer

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**REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM**

The Board of Directors and Shareholders

Sprint Nextel Corporation:

We have audited the accompanying consolidated balance sheets of Sprint Nextel Corporation, formerly known as Sprint Corporation, and subsidiaries as of December 31, 2005 and 2004, and the related consolidated statements of operations, comprehensive income (loss), cash flows, and shareholders' equity, for the years ended December 31, 2005 and 2004. In connection with our audits of the consolidated financial statements, we also have audited the financial statement schedule, Schedule II Consolidated Valuation and Qualifying Accounts for the years ended December 31, 2005 and 2004. These consolidated financial statements and financial statement schedule are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements and financial statement schedule based on our audits.

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

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Sprint Nextel Corporation and subsidiaries as of December 31, 2005 and 2004, and the results of their operations and their cash flows for the years ended December 31, 2005 and 2004, in conformity with U.S. generally accepted accounting principles. Also in our opinion, the related financial statement schedule for the years ended December 31, 2005 and 2004, when considered in relation to the basic consolidated financial statements taken as a whole, presents fairly, in all material respects, the information set forth therein.

As discussed in Note 1 to the consolidated financial statements, the Company adopted the provisions of FASB Interpretation No. 47, *Accounting for Conditional Asset Retirement Obligations*, in the fourth quarter of 2005.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the effectiveness of Sprint Nextel Corporation's internal control over financial reporting as of December 31, 2005, based on criteria established in *Internal Control - Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO), and our report dated March 7, 2006 expressed an unqualified opinion on management's assessment of, and the effective operation of, internal control over financial reporting.

/s/ KPMG LLP

McLean, Virginia  
March 7, 2006, except as to Note 26,  
which is as of March 30, 2006.



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**REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM**

The Board of Directors and Shareholders

Sprint Nextel Corporation:

We have audited management's assessment, included in Management's Report on Internal Control over Financial Reporting, appearing in Item 9A. Controls and Procedures, that Sprint Nextel Corporation, formerly known as Sprint Corporation, maintained effective internal control over financial reporting as of December 31, 2005, based on criteria established in *Internal Control - Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). Sprint Nextel Corporation's management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting. Our responsibility is to express an opinion on management's assessment and an opinion on the effectiveness of the Company's internal control over financial reporting based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, evaluating management's assessment, testing and evaluating the design and operating effectiveness of internal control, and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, management's assessment that Sprint Nextel Corporation maintained effective internal control over financial reporting as of December 31, 2005, is fairly stated, in all material respects, based on criteria established in *Internal Control - Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). Also, in our opinion, Sprint Nextel Corporation maintained, in all material respects, effective internal control over financial reporting as of December 31, 2005, based on criteria established in *Internal Control - Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheets of Sprint Nextel Corporation and subsidiaries as of December 31, 2005 and 2004, and the related consolidated statements of operations, comprehensive income (loss), cash flows, and shareholders' equity, for the years ended December 31, 2005 and 2004, and the related financial statement schedule for the years ended December 31, 2005 and 2004, and our report dated March 7, 2006, except as to Note 26, which is as of March 30, 2006, expressed an unqualified opinion on those consolidated financial statements and the related financial statement schedule.

/s/ KPMG LLP

McLean, Virginia  
March 7, 2006

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**REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM**

The Board of Directors and Shareholders

Sprint Nextel Corporation:

We have audited the accompanying consolidated statements of operations, comprehensive income (loss), cash flows and shareholders' equity of Sprint Nextel Corporation (formerly Sprint Corporation) for the year ended December 31, 2003. Our audit also included the financial statement schedule for the year ended December 31, 2003 listed in the Index to Financial Statements, Financial Statement Schedule and Exhibits. These financial statements and the schedule are the responsibility of the management of Sprint Nextel Corporation. Our responsibility is to express an opinion on these financial statements and the schedule based on our audit.

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

In our opinion, the financial statements referred to above present fairly, in all material respects the consolidated results of operations and cash flows of Sprint Nextel Corporation for the year ended December 31, 2003, in conformity with U.S. generally accepted accounting principles. Also, in our opinion, the related financial statement schedule for the year ended December 31, 2003, when considered in relation to the basic financial statements taken as a whole, presents fairly in all material respects the information set forth therein.

/s/ Ernst & Young LLP

Kansas City, Missouri

February 3, 2004, except for

Note 3, as to which the date is April 23, 2004, and

Note 23, as to which the date is November 2, 2004

## SPRINT NEXTEL CORPORATION

## CONSOLIDATED STATEMENTS OF OPERATIONS

For the Years Ended December 31, 2005, 2004 and 2003

|                                                                           | 2005                                           | 2004       | 2003      |
|---------------------------------------------------------------------------|------------------------------------------------|------------|-----------|
|                                                                           | <i>(in millions, except per share amounts)</i> |            |           |
| <b>Net operating revenues</b>                                             | \$ 34,680                                      | \$ 27,428  | \$ 26,197 |
| <b>Operating expenses</b>                                                 |                                                |            |           |
| Costs of services and products (exclusive of depreciation included below) | 14,384                                         | 11,576     | 10,592    |
| Selling, general and administrative                                       | 10,076                                         | 7,704      | 7,674     |
| Restructuring and asset impairments                                       | 125                                            | 3,731      | 1,951     |
| Depreciation                                                              | 4,933                                          | 4,713      | 4,972     |
| Amortization                                                              | 1,336                                          | 7          | 1         |
|                                                                           | 30,854                                         | 27,731     | 25,190    |
| <b>Operating income (loss)</b>                                            | 3,826                                          | (303)      | 1,007     |
| <b>Other income (expense)</b>                                             |                                                |            |           |
| Interest expense                                                          | (1,351)                                        | (1,282)    | (1,437)   |
| Interest income                                                           | 238                                            | 61         | 51        |
| Equity in earnings (losses) of unconsolidated subsidiaries, net           | 110                                            | (39)       | (77)      |
| Loss on retirement of debt                                                |                                                | (60)       | (21)      |
| Other, net                                                                | 83                                             | 20         | (27)      |
|                                                                           | (920)                                          | (1,300)    | (1,511)   |
| <b>Income (loss) from continuing operations before income taxes</b>       | 2,906                                          | (1,603)    | (504)     |
| <b>Income tax (expense) benefit</b>                                       | (1,105)                                        | 591        | 212       |
| <b>Income (loss) from continuing operations</b>                           | 1,801                                          | (1,012)    | (292)     |
| Discontinued operations, net                                              |                                                |            | 1,324     |
| Cumulative effect of change in accounting principle, net                  | (16)                                           |            | 258       |
| <b>Net income (loss)</b>                                                  | 1,785                                          | (1,012)    | 1,290     |
| Earnings allocated to participating securities                            |                                                | (9)        |           |
| Preferred stock dividends                                                 | (7)                                            | (7)        | (7)       |
| <b>Income (loss) available to common shareholders</b>                     | \$ 1,778                                       | \$ (1,028) | \$ 1,283  |
| <b>Basic earnings (loss) per common share</b>                             |                                                |            |           |
| Continuing operations                                                     | \$ 0.88                                        | \$ (0.71)  | \$ (0.21) |
| Discontinued operations                                                   |                                                |            | 0.94      |
| Cumulative effect of change in accounting principle                       | (0.01)                                         |            | 0.18      |
| Total                                                                     | \$ 0.87                                        | \$ (0.71)  | \$ 0.91   |
| <b>Basic weighted average common shares outstanding</b>                   | 2,033                                          | 1,443      | 1,415     |
| <b>Diluted earnings (loss) per common share</b>                           |                                                |            |           |
| Continuing operations                                                     | \$ 0.87                                        | \$ (0.71)  | \$ (0.21) |
| Discontinued operations                                                   |                                                |            | 0.94      |

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|                                                           |    |       |    |        |         |
|-----------------------------------------------------------|----|-------|----|--------|---------|
| Cumulative effect of change in accounting principle       |    |       |    |        | 0.18    |
| Total                                                     | \$ | 0.87  | \$ | (0.71) | \$ 0.91 |
| <b>Diluted weighted average common shares outstanding</b> |    | 2,054 |    | 1,443  | 1,415   |

*See accompanying Notes to the Consolidated Financial Statements.*

## SPRINT NEXTEL CORPORATION

## CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS)

For the Years Ended December 31, 2005, 2004 and 2003

|                                                                                                                   | 2005     | 2004<br><i>(in millions)</i> | 2003     |
|-------------------------------------------------------------------------------------------------------------------|----------|------------------------------|----------|
| <b>Net income (loss)</b>                                                                                          | \$ 1,785 | \$ (1,012)                   | \$ 1,290 |
| <b>Other comprehensive income (loss)</b>                                                                          |          |                              |          |
| Unrealized holding gains on available-for-sale securities                                                         | 101      | 33                           | 78       |
| Income tax expense                                                                                                | (37)     | (12)                         | (30)     |
| Net unrealized holding gains on available-for-sale securities                                                     | 64       | 21                           | 48       |
| Reclassification adjustment for realized gains on available-for-sale securities included in net income (loss)     | (26)     | (28)                         | (7)      |
| Income tax benefit                                                                                                | 10       | 10                           | 3        |
| Net reclassification adjustment for realized gains on available-for-sale securities included in net income (loss) | (16)     | (18)                         | (4)      |
| Unrealized gains (losses) on qualifying cash flow hedges                                                          | 2        | (11)                         | (60)     |
| Income tax (expense) benefit                                                                                      | (2)      | 4                            | 23       |
| Net unrealized losses on qualifying cash flow hedges                                                              |          | (7)                          | (37)     |
| Reclassification adjustment for losses on cash flow hedges included in net income (loss)                          | 15       | 15                           |          |
| Income tax expense                                                                                                | (5)      | (5)                          |          |
| Net reclassification adjustment for losses on cash flow hedges included in net income (loss)                      | 10       | 10                           |          |
| Net foreign currency translation adjustment                                                                       | (9)      | 20                           | (2)      |
| Additional minimum pension obligation                                                                             | (98)     | (38)                         | (37)     |
| Income tax benefit                                                                                                | 39       | 17                           | 12       |
| Net additional minimum pension obligation                                                                         | (59)     | (21)                         | (25)     |
| Total other comprehensive (loss) income                                                                           | (10)     | 5                            | (20)     |
| <b>Comprehensive income (loss)</b>                                                                                | \$ 1,775 | \$ (1,007)                   | \$ 1,270 |

See accompanying Notes to the Consolidated Financial Statements.

**SPRINT NEXTEL CORPORATION**  
**CONSOLIDATED BALANCE SHEETS**

As of December 31, 2005 and 2004

|                                                                                                                                                      | 2005                                    | 2004          |
|------------------------------------------------------------------------------------------------------------------------------------------------------|-----------------------------------------|---------------|
|                                                                                                                                                      | <i>(in millions, except share data)</i> |               |
| <b>ASSETS</b>                                                                                                                                        |                                         |               |
| <b>Current assets</b>                                                                                                                                |                                         |               |
| Cash and cash equivalents                                                                                                                            | \$ 8,902                                | \$ 4,176      |
| Marketable securities                                                                                                                                | 1,763                                   | 445           |
| Accounts receivable, net                                                                                                                             | 4,827                                   | 3,107         |
| Inventories                                                                                                                                          | 950                                     | 651           |
| Deferred tax asset                                                                                                                                   | 1,811                                   | 1,049         |
| Prepaid expenses and other current assets                                                                                                            | 839                                     | 547           |
| <b>Total current assets</b>                                                                                                                          | <b>19,092</b>                           | <b>9,975</b>  |
| <b>Investments</b>                                                                                                                                   | <b>2,369</b>                            | <b>277</b>    |
| <b>Property, plant and equipment, net</b>                                                                                                            | <b>31,133</b>                           | <b>22,628</b> |
| <b>Intangible assets</b>                                                                                                                             |                                         |               |
| Goodwill                                                                                                                                             | 21,315                                  | 4,401         |
| FCC licenses                                                                                                                                         | 18,023                                  | 3,376         |
| Customer relationships, net                                                                                                                          | 8,651                                   | 29            |
| Other intangible assets, net                                                                                                                         | 1,345                                   | 30            |
| <b>Other assets</b>                                                                                                                                  | <b>652</b>                              | <b>605</b>    |
|                                                                                                                                                      | \$ 102,580                              | \$ 41,321     |
| <b>LIABILITIES AND SHAREHOLDERS EQUITY</b>                                                                                                           |                                         |               |
| <b>Current liabilities</b>                                                                                                                           |                                         |               |
| Accounts payable                                                                                                                                     | \$ 3,827                                | \$ 2,671      |
| Accrued expenses and other                                                                                                                           | 5,176                                   | 2,943         |
| Current portion of long-term debt and capital lease obligations                                                                                      | 5,047                                   | 1,288         |
| <b>Total current liabilities</b>                                                                                                                     | <b>14,050</b>                           | <b>6,902</b>  |
| <b>Long-term debt and capital lease obligations</b>                                                                                                  | <b>20,632</b>                           | <b>15,916</b> |
| <b>Deferred income taxes</b>                                                                                                                         | <b>11,687</b>                           | <b>2,176</b>  |
| <b>Postretirement and other benefit obligations</b>                                                                                                  | <b>1,385</b>                            | <b>1,445</b>  |
| <b>Other liabilities</b>                                                                                                                             | <b>2,642</b>                            | <b>1,114</b>  |
| <b>Total liabilities</b>                                                                                                                             | <b>50,396</b>                           | <b>27,553</b> |
| <b>Seventh series redeemable preferred stock</b>                                                                                                     | <b>247</b>                              | <b>247</b>    |
| <b>Shareholders equity</b>                                                                                                                           |                                         |               |
| Common stock                                                                                                                                         |                                         |               |
| Voting, par value \$2.00 per share, 6.500 billion and 3.000 billion shares authorized, 2.923 billion and 1.475 billion shares issued and outstanding | 5,846                                   | 2,950         |
| Non-voting, par value \$0.01 per share, 100 million and 0 shares authorized, 38 million and 0 shares issued and outstanding                          |                                         |               |
| Paid-in capital                                                                                                                                      | 46,136                                  | 11,873        |
| Retained earnings (deficit)                                                                                                                          | 681                                     | (586)         |
| Accumulated other comprehensive loss                                                                                                                 | (726)                                   | (716)         |
| <b>Total shareholders equity</b>                                                                                                                     | <b>51,937</b>                           | <b>13,521</b> |

\$ 102,580      \$ 41,321

*See accompanying Notes to the Consolidated Financial Statements.*

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## SPRINT NEXTEL CORPORATION

## CONSOLIDATED STATEMENTS OF CASH FLOWS

For the Years Ended December 31, 2005, 2004 and 2003

|                                                                                          | 2005               | 2004           | 2003<br>(revised) |
|------------------------------------------------------------------------------------------|--------------------|----------------|-------------------|
|                                                                                          | <i>see note 14</i> |                |                   |
|                                                                                          | (in millions)      |                |                   |
| <b>Cash flows from operating activities</b>                                              |                    |                |                   |
| Net income (loss)                                                                        | \$ 1,785           | \$ (1,012)     | \$ 1,290          |
| Adjustments to reconcile net income (loss) to net cash provided by operating activities: |                    |                |                   |
| Discontinued operations, net                                                             |                    |                | (1,324)           |
| Cumulative effect of change in accounting principle, net                                 | 16                 |                | (258)             |
| Provision for losses on accounts receivable                                              | 441                | 386            | 422               |
| Depreciation and amortization                                                            | 6,269              | 4,720          | 4,973             |
| Equity in (earnings) losses of unconsolidated subsidiaries, net                          | (110)              | 39             | 77                |
| Deferred income taxes                                                                    | 830                | (576)          | 439               |
| Gain on sale of assets, net                                                              | (43)               | (14)           | (4)               |
| Losses on impairment of assets                                                           | 127                | 3,540          | 1,873             |
| Other, net                                                                               | 436                | 281            | 161               |
| Changes in assets and liabilities, net of effects of acquisitions:                       |                    |                |                   |
| Accounts receivable                                                                      | (442)              | (617)          | (347)             |
| Inventories and other current assets                                                     | 11                 | (22)           | 204               |
| Accounts payable and other current liabilities                                           | 299                | (117)          | (856)             |
| Proceeds from communications towers lease transaction                                    | 1,195              |                |                   |
| Noncurrent assets and liabilities, net                                                   | (136)              | 17             | (115)             |
| <b>Net cash provided by operating activities</b>                                         | <b>10,678</b>      | <b>6,625</b>   | <b>6,535</b>      |
| <b>Cash flows from investing activities</b>                                              |                    |                |                   |
| Capital expenditures                                                                     | (5,057)            | (3,980)        | (3,797)           |
| Cash acquired in Nextel merger, net of cash paid                                         | 1,183              |                |                   |
| Purchase of PCS Affiliates, net of cash acquired                                         | (1,371)            |                |                   |
| Proceeds from divestiture of directory business                                          |                    |                | 2,213             |
| Purchases of marketable securities                                                       | (821)              | (542)          | (439)             |
| Proceeds from maturities and sales of marketable securities                              | 808                | 444            |                   |
| Proceeds from sales of assets and investments                                            | 648                | 77             | 101               |
| Distributions from (investments in) unconsolidated subsidiaries, net                     | 167                | (20)           | (32)              |
| Other, net                                                                               | (281)              | (35)           |                   |
| <b>Net cash used in investing activities</b>                                             | <b>(4,724)</b>     | <b>(4,056)</b> | <b>(1,954)</b>    |
| <b>Cash flows from financing activities</b>                                              |                    |                |                   |
| Borrowings under bank credit facility                                                    | 3,200              |                | 44                |
| Repayments under bank credit facility                                                    | (3,200)            |                |                   |
| Purchase and retirements of debt securities                                              | (1,170)            | (1,884)        | (2,952)           |
| Proceeds from issuance of common stock                                                   | 432                | 1,874          | 12                |
| Dividends paid                                                                           | (525)              | (670)          | (457)             |
| Other, net                                                                               | 35                 |                | 24                |
| <b>Net cash used in financing activities</b>                                             | <b>(1,228)</b>     | <b>(680)</b>   | <b>(3,329)</b>    |
| <b>Net increase in cash and cash equivalents</b>                                         | <b>4,726</b>       | <b>1,889</b>   | <b>1,252</b>      |



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|                                                |          |          |          |
|------------------------------------------------|----------|----------|----------|
| Cash and cash equivalents, beginning of period | 4,176    | 2,287    | 1,035    |
| Cash and cash equivalents, end of period       | \$ 8,902 | \$ 4,176 | \$ 2,287 |

*See accompanying Notes to the Consolidated Financial Statements.*

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## SPRINT NEXTEL CORPORATION

## CONSOLIDATED STATEMENTS OF SHAREHOLDERS EQUITY

For the Years Ended December 31, 2005, 2004 and 2003

(in millions)

|                                                                   | Voting       |          | Non-voting   |        | Class A |        | PCS          |          | Paid-in<br>Capital | Accumulated          |                                        | Total     |
|-------------------------------------------------------------------|--------------|----------|--------------|--------|---------|--------|--------------|----------|--------------------|----------------------|----------------------------------------|-----------|
|                                                                   | Common Stock |          | Common Stock |        | FT      |        | Common Stock |          |                    | Retained             | Other                                  |           |
|                                                                   | Shares       | Amount   | Shares       | Amount | Shares  | Amount | Shares       | Amount   |                    | Earning<br>(Deficit) | Comprehensive<br>(Loss) <sup>(1)</sup> |           |
| <b>Balance, January 1, 2003</b>                                   | 895          | \$ 1,790 |              |        | 43      | \$ 22  | 1,000        | \$ 1,000 | \$ 9,931           | \$ 66                | \$ (701)                               | \$ 12,108 |
| Net income                                                        |              |          |              |        |         |        |              |          |                    | 1,290                |                                        | 1,290     |
| Common stock dividends                                            |              |          |              |        |         |        |              |          |                    | (450)                |                                        | (450)     |
| Preferred stock dividends                                         |              |          |              |        |         |        |              |          | (7)                |                      |                                        | (7)       |
| Conversion of PCS common stock<br>underlying Class A common stock |              |          |              |        |         | (22)   | 22           | 22       |                    |                      |                                        |           |
| Cancellation of Class A FT<br>common stock                        |              |          |              |        | (43)    |        |              |          |                    |                      |                                        |           |
| Common stock issued                                               | 9            | 19       |              |        |         |        | 13           | 13       | 160                |                      |                                        | 192       |
| Stock-based compensation<br>expense                               |              |          |              |        |         |        |              |          | 52                 |                      |                                        | 52        |
| Additional minimum pension<br>liability                           |              |          |              |        |         |        |              |          |                    |                      | (25)                                   | (25)      |
| Other, net                                                        |              |          |              |        |         |        |              |          | (52)               |                      | 5                                      | (47)      |
| <b>Balance, December 31, 2003</b>                                 | 904          | 1,809    |              |        |         |        | 1,035        | 1,035    | 10,084             | 906                  | (721)                                  | 13,113    |
| Net loss                                                          |              |          |              |        |         |        |              |          |                    | (1,012)              |                                        | (1,012)   |
| Common stock dividends <sup>(2)</sup>                             |              |          |              |        |         |        |              |          | (183)              | (480)                |                                        | (663)     |
| Preferred stock dividends                                         |              |          |              |        |         |        |              |          | (7)                |                      |                                        | (7)       |
| Common stock issued                                               | 52           | 104      |              |        |         |        | 2            | 2        | 1,855              |                      |                                        | 1,961     |
| Stock-based compensation<br>expense                               |              |          |              |        |         |        |              |          | 129                |                      |                                        | 129       |
| Additional minimum pension<br>liability                           |              |          |              |        |         |        |              |          |                    |                      | (21)                                   | (21)      |
| Conversion of PCS common stock<br>into FON or voting common stock | 519          | 1,037    |              |        |         |        | (1,037)      | (1,037)  |                    |                      |                                        |           |
| Other, net                                                        |              |          |              |        |         |        |              |          | (5)                |                      | 26                                     | 21        |
| <b>Balance, December 31, 2004</b>                                 | 1,475        | 2,950    |              |        |         |        |              |          | 11,873             | (586)                | (716)                                  | 13,521    |
| Net income                                                        |              |          |              |        |         |        |              |          |                    | 1,785                |                                        | 1,785     |
| Common stock dividends                                            |              |          |              |        |         |        |              |          |                    | (518)                |                                        | (518)     |
| Preferred stock dividends                                         |              |          |              |        |         |        |              |          | (7)                |                      |                                        | (7)       |
| Common stock issued to Nextel<br>shareholders                     | 1,414        | 2,829    | 38           |        |         |        |              |          | 32,816             |                      |                                        | 35,645    |
| Common stock issued                                               | 34           | 67       |              |        |         |        |              |          | 458                |                      |                                        | 525       |
| Conversion of Nextel vested<br>stock-based awards upon merger     |              |          |              |        |         |        |              |          | 639                |                      |                                        | 639       |
| Stock-based compensation<br>expense                               |              |          |              |        |         |        |              |          | 302                |                      |                                        | 302       |
| Tax benefit from stock<br>compensation                            |              |          |              |        |         |        |              |          | 38                 |                      |                                        | 38        |
| Additional minimum pension<br>liability                           |              |          |              |        |         |        |              |          |                    |                      | (59)                                   | (59)      |
| Other, net                                                        |              |          |              |        |         |        |              |          | 17                 |                      | 49                                     | 66        |
| <b>Balance, December 31, 2005</b>                                 | 2,923        | \$ 5,846 | 38           | \$     |         | \$     |              | \$       | \$ 46,136          | \$ 681               | \$ (726)                               | \$ 51,937 |

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- (1) *As of December 31, 2005, accumulated other comprehensive loss consists of \$(818) additional minimum pension liability, offset by \$80 of unrealized net gains related to investments and derivatives and \$12 of foreign currency translation adjustment.*
  
- (2) *In 2004, voting common stock dividends were paid out of paid-in capital in the quarterly period in which retained earnings were in a deficit position. See accompanying Notes to the Consolidated Financial Statements.*

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**SPRINT NEXTEL CORPORATION**

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**

**Note 1. Summary of Operations and Significant Accounting Policies**

***Operations***

We are a global communications company offering a comprehensive suite of wireless and wireline communications products and services that are designed to meet the needs of our targeted customer groups: individuals and business and government customers. Although our operations are divided into three lines of business: Wireless, Long Distance and Local, we have organized our sales and distribution efforts to focus on the needs of two distinct customer types—individuals and businesses and government agencies, which enable us to create customer-focused communications solutions. We are one of the three largest wireless companies in the United States based on the number of wireless subscribers. We own extensive wireless networks and a global long distance, Tier 1 Internet backbone. Our Series 1 voting common stock trades on the New York Stock Exchange, or NYSE, under the symbol S.

We, together with third party affiliates, each referred to as a PCS Affiliate, and Nextel Partners, Inc., offer digital wireless service in all 50 states, Puerto Rico and the U.S. Virgin Islands. The PCS Affiliates, through commercial arrangements with us, provide wireless personal communication services, or PCS, under the Sprint® brand name in certain mid-sized and tertiary U.S. markets on wireless networks built and operated at their expense using spectrum licensed to and controlled by us. Nextel Partners provides digital wireless communications services under the Nextel brand name in certain mid-sized and tertiary U.S. markets on wireless networks built and operated at its expense.

We offer a wide array of wireless mobile telephone and wireless data transmission services on networks that utilize code division multiple access, or CDMA, and integrated Digital Enhanced Network, or iDEN®, technologies. We market wireless services provided on our CDMA network under the Sprint brand. We are deploying high-speed evolution data optimized, or EV-DO, technology across our CDMA network. We first introduced EV-DO commercially in the second quarter 2005, and we will continue to expand EV-DO into additional markets. We operate an all-digital long distance and Tier 1 Internet protocol, or IP, network, over which we provide a broad suite of wireline communications services targeted to domestic business and residential customers, multinational corporations and other communications companies.

We also provide regulated local exchange telephone services and long distance voice and data services, including digital subscriber line, or DSL, services, and other telecommunications-related services to customers in our local service areas. We also operate a wholesale product distribution business. This entire business is expected to be spun-off to our shareholders in the second quarter 2006 and will be known as Embarq Corporation. See note 25 for more information.

***Basis of Consolidation and Presentation***

On August 12, 2005, a subsidiary of ours merged with Nextel Communications, Inc. for aggregate consideration of \$37.8 billion. In connection with the Nextel merger, we changed our name to Sprint Nextel Corporation, or Sprint Nextel. On August 12, 2005, we acquired US Unwired Inc. for \$968 million in cash. We also acquired Gulf Coast Wireless Limited Partnership for \$211 million in cash on October 3, 2005 as well as IWO Holdings, Inc. for \$192 million in cash on October 20, 2005. Each of these companies is now a wholly owned subsidiary of Sprint Nextel. Each transaction was accounted for as a purchase. See note 2 for further discussion of these transactions.

The accompanying consolidated financial statements include our accounts, and those of our wholly owned subsidiaries, and subsidiaries we control, as well as variable interest entities where we are the primary beneficiary. All significant intercompany transactions and balances have been eliminated in consolidation. We use the equity method to account for equity investments in unconsolidated entities in which we exercise

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**SPRINT NEXTEL CORPORATION**

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

significant influence over operating and financial policies but do not control. We recognize all changes in our proportionate share of the unconsolidated subsidiaries' equity resulting from their equity transactions as adjustments to our investment and shareholders' equity balances. We use the cost method to account for equity investments in all other unconsolidated entities. See note 5 for additional information.

We prepare our consolidated financial statements in conformity with accounting principles generally accepted in the United States, which require management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Due to the inherent uncertainty involved in making those estimates, actual results could differ from those estimates.

Certain prior-period amounts have been reclassified to conform to the current period presentation. In 2005, we determined that recategorization of certain costs from costs of services and products to selling, general and administrative would be more consistent with current industry practices, and accordingly reclassified \$1.1 billion of expenses in each of the years ended December 31, 2004 and 2003. These costs primarily consist of certain customer care and information technology costs for the Wireless and Long Distance segments.

***Revenue Recognition***

Operating revenues primarily consist of wireless service revenues, revenues generated from handset and accessory sales and revenues from wholesale operators and PCS Affiliates, as well as long distance and local voice, data and internet revenues.

We recognize operating revenues as services are rendered or as products are delivered to customers in accordance with Securities and Exchange Commission, or SEC, Staff Accounting Bulletin No. 104, *Revenue Recognition*, and the Emerging Issues Task Force, or EITF, Issue No. 00-21, *Revenue Arrangements with Multiple Deliverables*. Revenues consist of fixed monthly recurring charges, variable usage charges, equipment charges and miscellaneous fees such as activation fees, directory assistance, operator-assisted calling, equipment protection, late payment charges and certain regulatory fees. We recognize revenue for access charges and other services charged at fixed amounts ratably over the service period, net of credits and adjustments for service discounts, billing disputes and fraud or unauthorized usage. We recognize excess usage and long distance revenue at contractual rates per minute as minutes are used. As a result of the cutoff times of our multiple billing cycles each month, we are required to estimate the amount of subscriber revenues earned but not billed from the end of each billing cycle to the end of each reporting period. These estimates are based primarily on rate plans in effect and our historical usage and billing.

Certain of our bundled products and services, primarily in Wireless, have been determined to be revenue arrangements with multiple deliverables. Total consideration received in these arrangements is allocated and measured using units of accounting within the arrangement based on relative fair values. We recognize revenue from handset sales when title to the handset passes to the dealer or end user customer. We classify handset sales as equipment revenue.

Wireless offerings include wireless phones and service contracts sold together in our company-operated stores. The activation fee revenue associated with these direct channel sales is recognized at the time the related wireless phone is sold and is classified as equipment sales. Wireless activation fees earned prior to the 2003 adoption of EITF Issue No. 00-21 are being deferred and amortized over the estimated average life of the end user customer.

Certain activation fees associated with unbundled sales in our Wireless segment are deferred and amortized over the estimated average life of the end user customer. Certain installation fees associated with our Local segment are deferred and amortized over the estimated average life of the customer.

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**SPRINT NEXTEL CORPORATION**

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

***Advertising Expense***

We recognize advertising expense as incurred. These expenses include production, media and other promotional and sponsorship costs. Advertising expenses totaled \$1.4 billion in 2005, \$989 million in 2004, and \$946 million in 2003.

***Research and Development***

We recognize research and development expense as incurred. Research and development expenses totaled \$47 million in 2005, \$32 million in 2004, and \$16 million in 2003.

***Income Taxes***

Deferred tax assets and liabilities are determined based on the temporary differences between the financial reporting and tax bases of assets and liabilities, applying enacted statutory tax rates in effect for the year in which the differences are expected to reverse. Future tax benefits, such as net operating loss carryforwards, are recognized to the extent that realization of these benefits is considered to be more likely than not. See note 13 for more information.

***Earnings (Loss) per Common Share***

Basic earnings (loss) per common share is calculated by dividing income (loss) available to common shareholders by the weighted average number of common shares outstanding during the period. Diluted earnings per common share adjust basic earnings per common share for the effects of potentially dilutive common shares. Potentially dilutive common shares primarily include the dilutive effects of shares issuable under our equity plans computed using the treasury stock method, and the dilutive effects of shares issuable upon the conversion of our convertible senior notes computed using the if-converted method.

Dilutive securities consisting of shares issuable under our equity plans used in calculating earnings per common share were 20.5 million shares for 2005. All 10.3 million shares issuable upon the assumed conversion of our convertible senior notes could potentially dilute earnings per common share in the future but were excluded from the calculation of diluted earnings per common share for 2005 due to their antidilutive effects. Additionally, about 65.6 million shares issuable under the equity plans that could also potentially dilute earnings per common share in the future were excluded from the calculation of diluted earnings per common share in 2005 as the exercise prices exceeded the average market price during this period.

Shares issuable under our equity plans were antidilutive in 2004 because we incurred net losses from continuing operations. Although not used in the determination of earnings per common share for 2004, our dilutive securities totaled 12.3 million shares in 2004. About 88 million shares issuable under the equity plans could potentially dilute earnings per common share in the future, but were excluded from the calculation of diluted earnings per common share in 2004 as the exercise prices exceeded the average market price during this period.

Shares issuable under our equity plans were antidilutive in 2003 because we incurred net losses from continuing operations. Although not used in the determination of earnings per common share for 2003, our dilutive securities totaled 3.0 million shares in 2003. About 103 million shares issuable under the equity plans could potentially dilute earnings per common share in the future, but were excluded from the calculation of diluted earnings per common share in 2003 as the exercise prices exceeded the average market price during this period.

***Stock-based Compensation***

Effective January 1, 2003, we adopted Statement of Financial Accounting Standards, or SFAS, No. 123, *Accounting for Stock-Based Compensation*, as amended by SFAS No. 148, *Accounting for Stock-Based*

## SPRINT NEXTEL CORPORATION

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

*Compensation Transition and Disclosure*, using the prospective method. Upon adoption we began expensing the fair value of stock-based compensation of all grants, modifications or settlements made on or after January 1, 2003 using a Black-Scholes option-pricing model. The following table illustrates the effect on net income (loss) and earnings per common share of stock-based compensation included in net income (loss) and the effect on net income (loss) and earnings (loss) per common share for grants issued on or before December 31, 2002, had we applied the fair value recognition provisions of SFAS No. 123.

Compensation costs are expensed over the vesting period of the award using the straight-line method. The amount of compensation cost recognized at any date is at least equal to the vested portion of the award.

|                                                                                                                                                   | Year Ended December 31,                     |            |          |
|---------------------------------------------------------------------------------------------------------------------------------------------------|---------------------------------------------|------------|----------|
|                                                                                                                                                   | 2005                                        | 2004       | 2003     |
|                                                                                                                                                   | <i>(in millions, except per share data)</i> |            |          |
| Net income (loss), as reported                                                                                                                    | \$ 1,785                                    | \$ (1,012) | \$ 1,290 |
| Add: stock-based compensation expense included in reported net income (loss), net of income tax of \$111, \$47 and \$19                           | 192                                         | 82         | 33       |
| Deduct: total stock-based compensation expense determined under fair value based method for all awards, net of income tax of \$117, \$64 and \$61 | (204)                                       | (111)      | (106)    |
| Pro forma net income (loss)                                                                                                                       | \$ 1,773                                    | \$ (1,041) | \$ 1,217 |
| Earnings (loss) per common share:                                                                                                                 |                                             |            |          |
| Basic as reported                                                                                                                                 | \$ 0.87                                     | \$ (0.71)  | \$ 0.91  |
| Basic pro forma                                                                                                                                   | \$ 0.87                                     | \$ (0.73)  | \$ 0.85  |
| Diluted as reported                                                                                                                               | \$ 0.87                                     | \$ (0.71)  | \$ 0.91  |
| Diluted pro forma                                                                                                                                 | \$ 0.86                                     | \$ (0.73)  | \$ 0.85  |

We recognized pre-tax charges of \$234 million, \$81 million, and \$37 million in 2005, 2004 and 2003 related to stock-based grants issued after December 31, 2002.

In 2005, we recognized pre-tax charges of \$32 million of non-cash compensation expense in connection with Sprint employee separations as a result of the Nextel merger. The charges were associated with accounting for modifications, which accelerated vesting and extended exercise periods of stock options granted in prior periods, as required by SFAS No. 123.

Prior to April 23, 2004, we had two tracking stocks. The FON tracking stock represented all of the operations and assets of our Long Distance and Local operations. The PCS tracking stock represented the operations and assets of our Wireless operations. On April 23, 2004, we recombined these two tracking stocks. As a result, in 2004, we recognized pre-tax charges of \$48 million of non-cash compensation expense related to the recombination of FON common stock and PCS common stock. As required by SFAS No. 123, we accounted for the conversion of PCS stock options to FON stock options as a modification and accordingly applied stock option expensing to FON stock options resulting from the conversion of PCS stock options granted before January 1, 2003. In connection with this, we recognized pre-tax charges of \$37 million in 2005.

In 2003, we recognized pre-tax charges of \$15 million for non-cash expense in connection with separation agreements between us and former executives. The charges were associated with accounting for modifications, which accelerated vesting and extended vesting and exercise periods of stock options granted in prior periods, as required by SFAS No. 123.





## SPRINT NEXTEL CORPORATION

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

*Cash and Cash Equivalents*

Cash equivalents generally include highly liquid investments with original maturities of three months or less. These investments include money market funds, U.S. government and government-sponsored debt securities, corporate debt securities, municipal securities, repurchase agreements, and bank-related securities. All securities meet our investment policy guidelines and are stated at cost, which approximates market value. As of December 31, 2005, we have \$93 million of restricted cash, which is included in prepaid expenses and other current assets on the consolidated balance sheets. See note 9 for more information.

Our prior year amounts for auction rate securities have been reclassified from cash and cash equivalents to marketable securities.

*Supplemental Cash Flow Information*

|                                            | Year Ended December 31, |          |          |
|--------------------------------------------|-------------------------|----------|----------|
|                                            | 2005                    | 2004     | 2003     |
|                                            | <i>(in millions)</i>    |          |          |
| Interest paid, net of capitalized interest | \$ 1,291                | \$ 1,279 | \$ 1,424 |
| Interest received                          | 231                     | 61       | 51       |
| Income taxes paid                          | 138                     | (39)     | 83       |

Our non-cash activities included the following:

|                                                               | Year Ended December 31, |      |      |
|---------------------------------------------------------------|-------------------------|------|------|
|                                                               | 2005                    | 2004 | 2003 |
|                                                               | <i>(in millions)</i>    |      |      |
| Common stock issued:                                          |                         |      |      |
| Acquisition of Nextel                                         | \$ 35,645               | \$   | \$   |
| Vested stock option awards exchanged in acquisition of Nextel | 639                     |      |      |
| Employee benefit stock plans                                  | 90                      | 53   | 51   |
| Settlement of shareholder suit                                |                         | 5    |      |
| Earthlink common stock used to extinguish debt                | 90                      | 48   |      |

*Investments in Debt Securities*

We classify our investments in marketable debt securities as available-for-sale and, therefore, report them at fair value, based on quoted market prices. Interest on investments in debt securities is reinvested and recorded in interest income in the accompanying consolidated statements of operations. We record unrealized holding gains and losses as other comprehensive income (loss), net of related income taxes.

*Investments in Equity Securities*

We classify our investments in marketable equity securities as available-for-sale and, therefore, report them at fair value, based on available market information. We record unrealized holding gains and losses as other comprehensive income (loss), net of related income taxes. Realized gains or losses are recorded in earnings and calculated using average cost. We assess declines in the value of individual investments to determine whether the decline is other-than-temporary and thus the investment is impaired. We make this assessment by considering available evidence, including changes in general market conditions, specific industry and individual company data, the length of time and the extent to which the market value has been less than cost, the financial condition and near-term prospects of the individual company and our intent and ability to hold the investment. We record

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**SPRINT NEXTEL CORPORATION**

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

impairment losses on investments in equity securities in other income (expense) in the accompanying consolidated statements of operations when our investment's market value declines below our cost basis on an other-than-temporary basis.

***Allowance for Doubtful Accounts***

We establish an allowance for doubtful accounts receivable sufficient to cover probable and reasonably estimable losses. Because it is not practical to review the collectibility of each account individually when we determine the amount of our allowance for doubtful accounts receivable each period, our reserve reflects an estimate of accounts receivable that we believe to be uncollectible. We consider a number of factors in establishing the allowance for our portfolio of customers, including historical collection experience, current economic trends, estimates of forecasted write-offs, agings of the accounts receivable portfolio and other factors.

***Inventories***

Inventories of handsets in Wireless are stated at the lower of cost or market. We determine cost by the first-in, first-out, or FIFO, method. Handset costs in excess of the revenues generated from handset sales, or handset subsidies, are expensed at the time of sale. We do not recognize the expected handset subsidies prior to the time of sale because the promotional discount decision is made at the point of sale and/or because we expect to recover the handset subsidies through service revenues.

Inventories in Long Distance and Local are stated at the lower of cost or market.

***Property, Plant and Equipment***

We record property, plant and equipment, including improvements that extend useful lives, at cost. The cost of property, plant and equipment is generally depreciated on a straight-line basis over estimated economic useful lives. Amortization of assets recorded under capital leases is recorded in depreciation expense. We amortize leasehold improvements over the shorter of the lease terms or the estimated useful lives of the assets. We depreciate buildings and network equipment and software over estimated useful lives of up to 31 years, with approximately 70% being between 5 and 15 years, and office equipment and depreciable property, plant and equipment over estimated useful lives of up to 30 years with approximately 70% being between 3 and 5 years. Repair and maintenance costs are expensed as incurred. We calculate depreciation on certain of our assets using the group life method; accordingly, ordinary asset retirements and disposals are charged against accumulated depreciation with no gain or loss recognized.

We capitalize costs for network and non-network software developed or obtained for internal use during the application development stage. These costs are included in property, plant and equipment, and when the software is placed in service, are amortized over estimated useful lives of up to 10 years. Costs incurred during the preliminary project stage, as well as maintenance and training costs, are expensed as incurred. For those software projects that are under development, we periodically assess the probability of deployment into the business to determine if an impairment charge is required.

Since changes in technology or in our intended use of these assets, as well as changes in broad economic or industry factors, may cause the estimated period of use or the value of these assets to change, we perform annual internal studies to confirm the appropriateness of depreciable lives for most categories of property, plant and equipment. These studies utilize models, which take into account actual usage, physical wear and tear, replacement history, and assumptions about technology evolution, and use in certain instances actuarially determined probabilities to calculate the remaining life of our asset base. When these factors indicate property,

## SPRINT NEXTEL CORPORATION

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

plant and equipment assets may not be useful for as long as originally anticipated, we depreciate the remaining book values over the remaining estimated useful lives. In 2004, we extended the depreciable life of certain high-capacity transmission equipment from eight years to twelve years due to slower anticipated evolution of technology. This extension in life decreased the 2004 depreciation expense in Long Distance by approximately \$74 million.

Network equipment and software includes switching equipment and cell site towers, base transceiver stations, other radio frequency equipment, internal use software, metallic cable and wire facilities, digital fiber-optic cable, conduit, poles, other central office and transport facilities, and transmission-related equipment. Buildings and improvements principally consists of owned general office facilities, leasehold improvements and retail stores.

Non-network internal use software, office equipment and other principally consists of furniture, information technology equipment and vehicles.

Network asset inventory and construction in progress primarily includes materials, transmission and related equipment, labor, engineering, site development, interest and other costs relating to the construction and development of our network. Assets under construction are not depreciated until placed into service.

Our gross property, plant and equipment aggregated by business segment was as follows:

|                                            | December 31,     |                  |
|--------------------------------------------|------------------|------------------|
|                                            | 2005             | 2004             |
|                                            | (in millions)    |                  |
| Wireless                                   | \$ 31,203        | \$ 19,376        |
| Long Distance                              | 2,692            | 2,356            |
| Local                                      | 19,784           | 19,496           |
| Other                                      | 2,180            | 2,334            |
| <b>Gross property, plant and equipment</b> | <b>\$ 55,859</b> | <b>\$ 43,562</b> |

We review our long-lived assets for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. If the total of the expected undiscounted future cash flows is less than the carrying amount of our assets, a loss, if any, is recognized for the difference between the fair value and carrying value of the assets. Impairment analyses, when performed, are based on our current business and technology strategy, our views of growth rates for our business, anticipated future economic and regulatory conditions and expected technological availability.

**Asset Retirement Obligations**

In accordance with SFAS No. 143, *Accounting for Asset Retirement Obligations*, we record an asset retirement obligation and an associated asset retirement cost when we have a legal obligation in connection with the retirement of tangible long-lived assets.

Adoption of SFAS No. 143 on January 1, 2003, affected the cost of removal historically recorded by the Local segment. Consistent with regulatory requirements and industry practice, our Local segment historically accrued costs of removal in its depreciation reserves. These costs of removal do not meet the SFAS No. 143 definition of an asset retirement obligation. Upon adoption of SFAS No. 143, we recorded a reduction in our historical depreciation reserves of approximately \$420 million to remove the accumulated excess cost of removal, resulting in a cumulative effect of change in accounting principle credit, net of tax, in the accompanying consolidated statements of operations of \$258 million.

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**SPRINT NEXTEL CORPORATION**

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

Financial Accounting Standards Board, or FASB, Interpretation No. 47, or FIN 47, *Accounting for Conditional Asset Retirement Obligations* was issued in 2005, interpreting the application of SFAS No. 143. FIN 47 requires the recognition of a liability for legal obligations to perform an asset retirement activity in which the timing and (or) method of the settlement are conditional on a future event. We adopted FIN 47 in the fourth quarter 2005 resulting in the recognition of asset retirement obligations in our Local segment for environmental remediation requirements and contractual obligations for which estimated settlement dates can be determined. The asset retirement obligations are comprised of removal and disposal of the asbestos in company buildings, removal and environmental cleanup of fuel storage tanks used in standby power supply systems and decommissioning of leased building spaces. An asset retirement obligation exists, but will not be recognized, in situations where Local has been granted easements and rights-of-way by municipalities and private landowners to route its cable facilities. Most cable facilities are buried; however, some metallic and fiber cable are above-ground on company-owned poles. Local also contracts with other utilities to connect cable and wire to their poles. An estimated settlement date for these obligations is indeterminate. Upon adoption in the fourth quarter 2005, an asset retirement obligation of \$33 million, a related asset of \$6 million and a cumulative adjustment due to change in accounting principle, net of tax, of \$16 million were recorded.

***Capitalized Interest***

Capitalized interest totaled \$55 million in 2005, \$57 million in 2004, and \$59 million in 2003. Capitalized interest is incurred in connection with the construction of capital assets. SFAS No. 34, *Capitalization of Interest Costs*, requires that assets under construction be incurring interest cost through the payment of cash or incurrence of an interest-bearing liability in order to qualify for interest capitalization.

***Intangible Assets***

***Goodwill and Other Indefinite Life Intangibles***

In conformity with SFAS No. 142, *Goodwill and Other Intangible Assets*, we do not amortize our indefinite life intangibles, which consist of our Federal Communications Commission, or FCC, licenses, goodwill, and the Sprint and Boost Mobile trade names. We are required to test these assets for impairment at least annually or whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. We perform our annual review for impairment in the fourth quarter of each year using the direct value method.

Goodwill represents the excess of the purchase price over the fair value of the net assets acquired in business combinations accounted for as purchases. Virtually all of our goodwill is allocated to the Wireless segment. We determine impairment of goodwill by comparing the net assets of the reporting unit, identified as our operating segments, to their respective fair values. In the event a unit's net assets exceed its fair value, an implied fair value of goodwill must be determined by assigning the unit's fair value to each asset and liability of the unit. The excess of the fair value of the reporting unit over the amounts assigned to its assets and liabilities is the implied fair value of goodwill. An impairment loss is measured by the difference between the goodwill carrying value and the implied fair value.

For FCC licenses and other indefinite lived intangibles, we determine impairment by comparing an asset's respective carrying value to estimates of fair value using the direct value method, which requires the use of estimates, judgments and projections. In the event impairment exists, a loss is recognized based on the amount by which the carrying value exceeds the fair value of the asset. In accordance with EITF Issue No. 02-07, *Unit of Accounting for Testing Impairment of Indefinite-Lived Intangible Assets*, our FCC licenses are combined as a single unit of accounting for impairment testing purposes.

In 2005, we were assisted in our annual impairment review by an independent third party valuation firm and we concluded that as of December 31, 2005, no impairments existed.

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**SPRINT NEXTEL CORPORATION**

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

*Definite Life Intangibles*

Definite life intangibles include the value associated with acquired Wireless subscriber bases, or customer relationships, the Nextel and Direct Connect<sup>SM</sup> trade names and the value of our patents. We evaluate the recoverability of definite life intangible assets when events or circumstances indicate that these assets might be impaired. We determine impairment by comparing an asset's respective carrying value to estimates of the sum of the future cash flows expected to result from our asset, undiscounted and without interest charges. If the carrying amount is more than the recoverable amount, a loss is recognized based on the amount by which the carrying value exceeds the fair value of the asset. Customer relationships are amortized over the estimated customer lives using the sum of the years' digits method, which we believe best reflects the estimated pattern in which the economic benefits will be consumed. All other definite life intangibles are amortized over their estimated useful lives, using the straight line method.

*Derivative Instruments and Hedging Activities*

We recognize derivative instruments as either assets or liabilities in the Consolidated Balance Sheets and measure those instruments at fair value in accordance with SFAS No. 133, *Accounting for Derivative Instruments and Hedging Activities*, as amended. Changes in the fair value of derivatives are recorded each period in current earnings or other comprehensive income (loss) depending on the use of the derivative and whether it qualifies for hedge accounting.

We use derivative instruments only for hedging and risk management purposes. Hedging activity may be done for purposes of mitigating the risks associated with an asset, liability, committed transaction or probable forecasted transaction. We are primarily exposed to the market risk associated with unfavorable movements in interest rates, equity prices and foreign currencies. We do not enter into derivative transactions for speculative or trading purposes.

At inception and on an on-going basis, we assess whether each derivative that qualifies for hedge accounting continues to be highly effective in offsetting changes in the cash flows or fair value of the hedged item. If and when a derivative instrument is no longer expected to be highly effective, hedge accounting is discontinued. Hedge ineffectiveness, if any, is included in current period earnings.

We formally document all hedging relationships between the hedging instrument and the hedged item as well as our risk management objectives and strategies for undertaking various hedge transactions.

*Restructuring and Employee Severance Costs*

In June 2002, the FASB issued SFAS No. 146, *Accounting for Costs Associated with Exit or Disposal Activities*. This standard provides accounting guidance on when a liability for a cost associated with an exit or disposal activity is incurred. We adopted this standard effective January 1, 2003 for restructuring activities occurring after that date.

Employee termination benefits to be paid that are not directly associated with restructuring activities are recorded in accordance with SFAS No. 112, *Employers' Accounting for Postemployment Benefits*. Liabilities for termination benefits to be provided to employees are recognized under SFAS No. 112 when such costs are probable and estimable.

*Debt Financing Costs*

We amortize our debt financing costs as interest expense over the terms of the underlying obligations using the effective interest method.

## SPRINT NEXTEL CORPORATION

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

**Note 2. Business Combinations**

In 2005, we acquired Nextel Communications, US Unwired, Gulf Coast Wireless and IWO Holdings in transactions accounted for under the purchase method as required by SFAS No. 141, *Business Combinations*.

SFAS No. 141 requires that the total purchase price of each of the acquired entities be allocated to the assets acquired and liabilities assumed based on their fair values at the respective merger dates. The allocation process requires an analysis of customer relationships, acquired contractual rights and assumed contractual commitments and legal contingencies to identify and record the fair value of all assets acquired and liabilities assumed. In valuing acquired assets and assumed liabilities, fair values are based on, but are not limited to: quoted market prices, where available; our intent with respect to whether the assets purchased are to be held, sold or abandoned; expected future cash flows; current replacement cost for similar capacity for certain fixed assets; market rate assumptions for contractual obligations; and appropriate discount rates and growth rates.

*Nextel Communications, Inc.*

On August 12, 2005, a subsidiary of Sprint Corporation merged with Nextel and, as a result, Sprint acquired 100% of the outstanding common shares of Nextel. Nextel, now a wholly owned subsidiary of Sprint Nextel, provides wireless voice and data services in the United States. This transaction was consummated as part of our overall strategy to offer the most comprehensive selection of voice, data and multimedia products and services. The results of Nextel's operations have been included in the consolidated financial statements since the merger date.

The aggregate consideration paid for the merger is as follows:

|                                         | Aggregate<br>Consideration<br>(in millions) |
|-----------------------------------------|---------------------------------------------|
| Payment to Nextel shareholders in cash  | \$ 969                                      |
| Payment to Nextel shareholders in stock | 35,645                                      |
| Conversion of Nextel stock-based awards |                                             |
| Vested stock-based awards               | 639                                         |
| Unvested stock-based awards             | 485                                         |
| Direct acquisition costs                | 78                                          |
| <b>Total</b>                            | <b>\$ 37,816</b>                            |

We expect to spin off our local telecommunications business to our shareholders on a tax-free basis. To mitigate the risk that the Sprint Nextel stock that was issued in the merger would preclude this tax-free treatment and to ensure that Sprint Corporation would be treated as the acquiring entity for accounting purposes, the merger agreement provided for an allocation of cash and shares of Sprint Nextel common stock, determined as of the date of the merger, to ensure that former Nextel shareholders would own slightly less than 50% of the equity interests of Sprint Nextel. Pursuant to this allocation, Nextel common shareholders received \$969 million in cash and 1.452 billion shares of Sprint Nextel voting and non-voting common stock in the aggregate, or \$0.84629198 and 1.26750218 shares of our stock in exchange for each share of Nextel stock. In connection with the merger, we amended our articles of incorporation to increase to 6.5 billion the number of shares of common stock authorized for issuance.

The value of the newly issued shares was calculated using the average of the per share closing sales prices of Sprint Corporation Series 1 common stock on the NYSE for the period two business days before and through the two business days after the December 15, 2004 announcement of the merger.

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**SPRINT NEXTEL CORPORATION**

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

In addition, Nextel stock-based awards were converted into Sprint Nextel stock-based awards with the shares issuable under the employee stock option plan and exercise prices of the awards adjusted based on an exchange ratio of 1.3 shares of Sprint Nextel common stock for each share of Nextel common stock, which represents approximately 104 million shares of Sprint Nextel common stock in the aggregate. The value of these awards was calculated by applying the fair value method under SFAS No. 123, as amended by SFAS No. 148, and resulted in \$1.1 billion in stock-based awards. The fair value was calculated on the stock-based awards outstanding on the date of completion of the merger, which include options to purchase our shares and deferred shares.

We incurred approximately \$78 million of direct acquisition costs associated with financial advisory, legal and other services, which were included in the total purchase price.

We paid a premium (i.e., goodwill) over the fair value of the net tangible and identified intangible assets of Nextel for a number of potential strategic and financial benefits that are expected to be realized as a result of the merger, including, but not limited to, the following:

the combination of extensive network and spectrum assets, which enables us to offer consumers, businesses and government agencies a wide array of broadband wireless and integrated communications services;

the combination of Nextel's strength in business and government wireless services with our position in consumer wireless and data services, including services supported by our global IP network, which enables us to serve a broader customer base;

the size and scale of the combined company, which is comparable to that of our two largest competitors, is expected to enable more operating efficiencies than either company could achieve on its own; and,

the ability to position us strategically in the fastest growing areas of the communications industry.

*Allocation of Purchase Price*

The approach to the estimation of the fair values of the Nextel intangible assets was primarily based on the income approach valuation technique and involved the following:

preparation of discounted cash flow analyses;

determination of the fair value of identified significant intangible assets;

reconciliation of the individual assets' returns with the weighted average cost of capital; and

allocation of the excess purchase price over the fair values of the identifiable assets and liabilities acquired to goodwill.

Under the purchase method of accounting, the assets and liabilities of Nextel were recorded at their respective fair values as of the date of the merger. We are in the process of finalizing valuations of assets, including investments, property, plant and equipment, intangible assets, and certain liabilities. Given the size of the merger, the fair values set forth below are based on preliminary valuations and are subject to adjustment as additional information is obtained. Such additional information includes, but may not be limited to, the following: valuations of property,

plant and equipment, plans relative to the disposition of certain assets acquired, exit from

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## SPRINT NEXTEL CORPORATION

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

certain contractual arrangements and the expected involuntary termination of employees in connection with our integration activities and rationalization of the combined work force. When finalized, adjustments to goodwill may result. The following table summarizes the preliminary estimated fair values of the assets acquired and liabilities assumed and related deferred income taxes as of the acquisition date. The amounts reported as of September 30, 2005 reflect the estimated fair values as of the acquisition date of August 12, 2005, plus adjustments made during the third quarter of 2005. The adjustments listed in the table below include purchase price allocation adjustments made during the fourth quarter of 2005.

|                                                                | Preliminary Purchase Price Allocation |                              |                   |
|----------------------------------------------------------------|---------------------------------------|------------------------------|-------------------|
|                                                                | As of                                 |                              | As of             |
|                                                                | September 30, 2005                    | Adjustments<br>(in millions) | December 31, 2005 |
| Current assets, including cash and cash equivalents of \$2,152 | \$ 5,501                              | \$ 4                         | \$ 5,505          |
| Property, plant and equipment                                  | 8,454                                 | (80)                         | 8,374             |
| Goodwill                                                       | 15,549                                | 24                           | 15,573            |
| Spectrum licenses                                              | 14,240                                |                              | 14,240            |
| Other indefinite life intangibles                              | 400                                   |                              | 400               |
| Customer relationships and other definite life intangibles     | 10,448                                |                              | 10,448            |
| Investments                                                    | 2,680                                 | (2)                          | 2,678             |
| Other assets                                                   | 111                                   |                              | 111               |
| Current liabilities                                            | (2,910)                               | (10)                         | (2,920)           |
| Long-term debt                                                 | (8,984)                               |                              | (8,984)           |
| Deferred income taxes, net                                     | (7,865)                               | (70)                         | (7,935)           |
| Other long-term liabilities                                    | (334)                                 | 175                          | (159)             |
| Deferred compensation included in shareholders' equity         | 518                                   | (33)                         | 485               |
| Net assets acquired                                            | \$ 37,808                             | \$ 8                         | \$ 37,816         |

In the fourth quarter 2005, a net increase was made to goodwill in the amount of \$24 million primarily due to adjustments to liabilities in connection with the merger, which includes the recognition of involuntary termination benefits, costs associated with the termination of contracts and exit activities, the rationalization of property plant and equipment, and identification of loss contingencies that were in existence prior to consummation of the merger. Prior to the end of the purchase price allocation period, if information becomes available with respect to any material pre-merger contingencies where the related asset, liability or impairment is probable and the amount can be reasonably estimated, such items will be included in the purchase price allocation.

Management continues to finalize its plans for rationalizing certain redundant assets and activities, such as facilities, software and infrastructure assets, and to integrate the combined companies. These plans affect many areas of the combined company, including sales and marketing, network, information technology, customer care and general and administrative functions. In connection with these activities, we expect to incur significant costs over the next several years associated with dispositions and integration activities. Management is in the process of finalizing these plans and expects to execute these plans over the next few years. We expect that the finalization of certain integration plans will result in adjustments to the purchase price allocation for the acquired assets and assumed liabilities of Nextel and may also result in the need to adjust the useful lives of certain network and other property, plant and equipment.

In 2005, we recorded \$197 million of costs recognized under EITF Issue No. 95-3, *Recognition of Liabilities in Connection with a Purchase Business Combination*, as well as other purchase accounting guidance, as liabilities

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**PRINT NEXTEL CORPORATION**
**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

assumed in the purchase business combination. These costs are primarily associated with Nextel employee retention bonuses earned on the date of the merger and severance benefits for involuntary separations of Nextel employees. Additional liabilities for termination benefits to be provided to involuntarily separated Nextel employees are expected to be recognized as liabilities assumed in the purchase business combination.

*Property, Plant and Equipment Acquired*

The fair values preliminarily allocated to property, plant and equipment acquired in the merger are as follows:

|                                                               | <b>Preliminary</b>                  |
|---------------------------------------------------------------|-------------------------------------|
|                                                               | <b>Fair Value<br/>(in millions)</b> |
| Network equipment and software                                | \$ 7,370                            |
| Buildings and improvements                                    | 239                                 |
| Non-network internal use software, office equipment and other | 765                                 |
| <b>Total</b>                                                  | <b>\$ 8,374</b>                     |

The weighted average remaining useful lives are 6 years for network assets, 3 years for building and improvements and 2 years for non-network internal use software, office equipment and other assets.

*Goodwill and Intangibles Acquired*

Goodwill resulting from the merger with Nextel is allocated to the Wireless segment. Goodwill includes a portion of value for assembled workforce, which is not separately classified from goodwill in accordance with SFAS No. 141. Goodwill, spectrum licenses and the Boost Mobile trademark are considered to have indefinite lives. They are not amortized, but rather are reviewed annually for impairment, or more frequently if indicators of impairment exist.

Definite life intangibles include \$9.5 billion associated with Nextel's customer relationships, which will be amortized over five years using the sum of the years' digits method, which we believe approximately reflects the estimated pattern in which the economic benefits will be consumed. Other definite life intangibles primarily include the Nextel and Direct Connect<sup>SM</sup> trademarks, which will be amortized over 10 years on a straight-line basis. See note 7 for information regarding the amortization expense of these assets.

In accordance with SFAS No. 109, *Accounting for Income Taxes*, a deferred income tax liability was not recorded on the goodwill since it is not tax deductible. Deferred income tax liabilities were recorded on the net assets acquired and will reverse as a tax benefit in the accompanying consolidated statements of operations in proportion to and over the amortization period of the related intangibles or upon their write-off or disposition, if any.

## SPRINT NEXTEL CORPORATION

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

*Long-term Debt Assumed*

The fair value of long-term debt assumed as of the merger date is as follows:

|                                                                                                                   | <b>Preliminary</b>                        |
|-------------------------------------------------------------------------------------------------------------------|-------------------------------------------|
|                                                                                                                   | <b>Fair Value</b><br><i>(in millions)</i> |
| 5.25% convertible senior notes due 2010, principal amount of \$607 including a deferred premium of \$3            | \$ 610                                    |
| 9.5% senior serial redeemable notes due 2011, principal amount of \$85 including a deferred premium of \$5        | 90                                        |
| 6.875% senior serial redeemable notes due 2013, principal amount of \$1,473 including a deferred premium of \$96  | 1,569                                     |
| 5.95% senior serial redeemable notes due 2014, principal amount of \$1,170 including a deferred premium of \$38   | 1,208                                     |
| 7.375% senior serial redeemable notes due 2015, principal amount of \$2,137 including a deferred premium of \$158 | 2,295                                     |
| Bank credit facility, including a deferred premium of \$6                                                         | 3,206                                     |
| Other                                                                                                             | 6                                         |
| <b>Total</b>                                                                                                      | <b>\$ 8,984</b>                           |

*Pro Forma Financial Information*

The following pro forma consolidated results of operations assume that the merger with Nextel was completed as of January 1, 2005 and 2004 for the years ended December 31, 2005 and 2004, respectively.

|                                          | <b>Year Ended</b><br><b>December 31,</b> |             |
|------------------------------------------|------------------------------------------|-------------|
|                                          | <b>2005</b>                              | <b>2004</b> |
|                                          | <i>(in millions except</i>               |             |
|                                          | <b>per share data)</b>                   |             |
| Net operating revenues                   | \$ 44,069                                | \$ 40,902   |
| Net income (loss)                        | \$ 1,593                                 | \$ (1,404)  |
| Diluted earnings (loss) per common share | \$ 0.54                                  | \$ (0.50)   |

The pro forma amounts represent the historical operating results of Sprint and Nextel with adjustments for purchase accounting and to conform accounting policies that affect net operating revenues, costs of services and products, selling, general and administrative expenses, depreciation and amortization, interest expense, other income (expense), income taxes, and the elimination of intercompany activity.

*Affiliate Acquisitions*

During 2005, we acquired three PCS Affiliates. We believe that the acquisitions of Nextel Partners and the PCS Affiliates we have acquired to date will give us control of the distribution of services under our Sprint and Nextel brands, and provide us with the strategic and financial benefits associated with a larger customer base and expanded network coverage, which include a number of markets with favorable growth and competitive characteristics.



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**SPRINT NEXTEL CORPORATION**

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

*US Unwired Inc.*

On August 12, 2005, we acquired US Unwired, a PCS Affiliate, for a purchase price of \$968 million in cash. As of December 31, 2005, the majority of the purchase price has been preliminarily allocated to goodwill in the amount of \$872 million and customer relationships in the amount of \$276 million. See note 7 for information regarding amortization expense for customer relationships. We are in the process of completing our valuation of US Unwired's assets and liabilities, as well as internal studies of assets, property, plant and equipment, intangible assets, certain liabilities, and commercial contracts, which when final, may result in additional adjustments to the purchase price allocation for the acquired assets and assumed liabilities of US Unwired.

*Gulf Coast Wireless, Limited Partnership*

On October 3, 2005, we acquired Gulf Coast Wireless, a PCS Affiliate, for \$211 million in cash, net of the 13.4% ownership interest held by US Unwired, Inc. As of December 31, 2005, the majority of the purchase price has been preliminarily allocated to intangible assets including goodwill in the amount of \$220 million and customer relationships of \$48 million. See note 7 for information regarding the amortization expense for customer relationships. We are in the process of completing our valuation of Gulf Coast Wireless' assets and liabilities, as well as internal studies of assets, property, plant and equipment, intangible assets, certain liabilities, and commercial contracts, which when final, may result in additional adjustments to the purchase price allocation for the acquired assets and assumed liabilities of Gulf Coast Wireless.

*IWO Holdings, Inc.*

On October 20, 2005, we acquired IWO Holdings, a PCS Affiliate, for \$192 million in cash. As of December 31, 2005, the excess purchase price over the fair value of the net assets acquired has been preliminarily allocated to intangible assets including goodwill in the amount of \$249 million and customer relationships of \$94 million. See note 7 for information regarding the amortization expense for customer relationships. We are in the process of completing our valuation of IWO Holdings' assets and liabilities, as well as internal studies of assets, property, plant and equipment, intangible assets, certain liabilities, and commercial contracts, which when final, may result in additional adjustments to the purchase price allocation for the acquired assets and assumed liabilities of IWO Holdings.

The results of operations of these 2005 affiliate purchase acquisitions are included in our consolidated financial statements from the respective dates of acquisition. Pro forma information has not been provided for any of the 2005 affiliate acquisitions, as the impact to prior periods would have been immaterial.

***Acquisitions Subsequent to December 31, 2005***

On January 31, 2006, we completed the acquisition of Enterprise Communications Partnership, a PCS Affiliate, for \$77 million in cash.

On February 1, 2006, we completed the acquisition of Alamosa Holdings Inc., the largest PCS Affiliate, for \$3.4 billion in cash.

On February 21, 2006, we acquired 94% of the voting stock of Velocita Wireless Holding Corporation for \$157 million in cash. We expect to acquire the remaining 6% of Velocita Wireless in May 2006 for an additional \$7 million in cash. Velocita Wireless owns and operates a nationwide digital packet-switched wireless data network in the 900 MHz frequency band.

## SPRINT NEXTEL CORPORATION

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

**Note 3. Recombination of Tracking Stock**

On April 23, 2004, we recombined our two tracking stocks. Each share of PCS common stock automatically converted into 0.50 shares of FON common stock. The conversion of PCS common stock into FON common stock resulted in an increase in FON common stock outstanding of 518.5 million shares as of April 23, 2004. As of April 23, 2004, the FON Group and the PCS Group ceased to exist. Our common stock now represents all of our operations and assets, including Wireless, Long Distance and Local operations. The financial statements are shown as if the recombination had occurred as of the earliest period presented.

**Earnings Per Common Share**

For 2003, all per share amounts have been restated to reflect the recombination of the FON common stock and PCS common stock at an identical conversion ratio of 0.50. The conversion ratio was also applied to dilutive PCS securities (mainly stock options, employee stock purchase plan shares, convertible preferred stock and restricted stock units) to determine diluted weighted average shares on a consolidated basis.

Following is previously reported earnings per common share information for the FON Group and the PCS Group:

|                                                                  | 2003                                     |           |
|------------------------------------------------------------------|------------------------------------------|-----------|
|                                                                  | FON                                      | PCS       |
|                                                                  | Group                                    |           |
|                                                                  | <i>(in millions, except earnings and</i> |           |
|                                                                  | <i>dividends per common share)</i>       |           |
| <b>Income (loss) from continuing operations</b>                  | \$ 360                                   | \$ (652)  |
| Discontinued operations, net                                     | 1,324                                    |           |
| Cumulative effect of change in accounting principle, net         | 258                                      |           |
| <b>Net income (loss)</b>                                         | 1,942                                    | (652)     |
| Preferred stock dividends received (paid)                        | 8                                        | (15)      |
| <b>Income (loss) available to common shareholders</b>            | \$ 1,950                                 | \$ (667)  |
| <b>Basic earnings (loss) per common share<sup>(2)</sup></b>      |                                          |           |
| Continuing operations                                            | \$ 0.41                                  | \$ (0.65) |
| Discontinued operations, net                                     | 1.47                                     |           |
| Cumulative effect of change in accounting principle, net         | 0.29                                     |           |
| <b>Total</b>                                                     | \$ 2.16                                  | \$ (0.65) |
| Basic weighted average common shares                             | 901                                      | 1,029     |
| <b>Diluted earnings (loss) per common share<sup>(1)(2)</sup></b> |                                          |           |
| Continuing operations                                            | \$ 0.41                                  | \$ (0.65) |
| Discontinued operations, net                                     | 1.47                                     |           |
| Cumulative effect of change in accounting principle, net         | 0.29                                     |           |
| <b>Total</b>                                                     | \$ 2.16                                  | \$ (0.65) |

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|                                        |     |       |
|----------------------------------------|-----|-------|
| Diluted weighted average common shares | 903 | 1,029 |
|----------------------------------------|-----|-------|

**Dividends per common share**

|                  |         |    |
|------------------|---------|----|
| FON common stock | \$ 0.50 | \$ |
|------------------|---------|----|

*(1) As the effects of including potentially dilutive PCS securities were antidilutive, they were not included in the diluted weighted average common shares outstanding for the PCS Group, nor were they included in the calculation of diluted earnings per common share.*

*(2) Earnings per common share amounts may not add due to rounding.*

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## SPRINT NEXTEL CORPORATION

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

## Note 4. Supplemental Balance Sheet Information

|                                                               | December 31,         |           |
|---------------------------------------------------------------|----------------------|-----------|
|                                                               | 2005                 | 2004      |
|                                                               | <i>(in millions)</i> |           |
| <b>Accounts receivable, net</b>                               |                      |           |
| Trade                                                         | \$ 5,065             | \$ 3,372  |
| Other                                                         | 78                   | 28        |
| Less allowance for doubtful accounts                          | (316)                | (293)     |
|                                                               | \$ 4,827             | \$ 3,107  |
| <b>Prepaid expenses and other current assets</b>              |                      |           |
| Prepaid expenses                                              | \$ 484               | \$ 303    |
| Deferred charges                                              | 103                  | 106       |
| Other                                                         | 252                  | 138       |
|                                                               | \$ 839               | \$ 547    |
| <b>Property, plant and equipment, net</b>                     |                      |           |
| Land                                                          | \$ 333               | \$ 334    |
| Network equipment and software                                | 41,192               | 32,138    |
| Buildings and improvements                                    | 6,873                | 6,182     |
| Non-network internal use software, office equipment and other | 3,785                | 3,120     |
| Less accumulated depreciation and amortization                | (24,726)             | (20,934)  |
|                                                               | 27,457               | 20,840    |
| Network asset inventory and construction in progress          | 3,676                | 1,788     |
|                                                               | \$ 31,133            | \$ 22,628 |
| <b>Accounts payable</b>                                       |                      |           |
| Trade                                                         | \$ 2,558             | \$ 1,535  |
| Accrued interconnection costs                                 | 449                  | 410       |
| Construction obligations                                      | 407                  | 361       |
| Other                                                         | 413                  | 365       |
|                                                               | \$ 3,827             | \$ 2,671  |
| <b>Accrued expenses and other</b>                             |                      |           |
| Deferred revenues                                             | \$ 1,439             | \$ 737    |
| Payroll and related                                           | 814                  | 428       |
| Accrued taxes                                                 | 695                  | 404       |
| Accrued interest                                              | 448                  | 335       |
| Other                                                         | 1,780                | 1,039     |
|                                                               | \$ 5,176             | \$ 2,943  |
| <b>Other liabilities</b>                                      |                      |           |



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|                                             |    |       |    |       |
|---------------------------------------------|----|-------|----|-------|
| Deferred rental income-communication towers | \$ | 1,097 | \$ |       |
| Deferred revenue                            |    | 95    |    | 52    |
| Other                                       |    | 1,450 |    | 1,062 |
|                                             | \$ | 2,642 | \$ | 1,114 |

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## SPRINT NEXTEL CORPORATION

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

**Note 5. Investments**

Specific investment types and the related carrying amounts include:

|                                                | December 31,         |        |
|------------------------------------------------|----------------------|--------|
|                                                | 2005                 | 2004   |
|                                                | <i>(in millions)</i> |        |
| Investments in debt securities                 | \$ 1,172             | \$ 536 |
| Investments in equity securities               | 734                  | 157    |
| Equity method investments                      |                      |        |
| Nextel Partners                                | 2,346                |        |
| Virgin Mobile USA, LLC                         | (180)                | 20     |
| Other investments                              | 60                   | 9      |
|                                                | 4,132                | \$ 722 |
| Less amounts included as marketable securities | (1,763)              | (445)  |
|                                                | \$ 2,369             | \$ 277 |

***Investments in Debt Securities***

Our investments in debt securities, including auction rate securities, with original or remaining maturities at purchase of greater than 90 days but less than one year, are classified in current assets as marketable securities on the accompanying consolidated balance sheets. We also invested in debt securities with original or remaining maturities at purchase of 90 days or less. These securities were included in cash and cash equivalents on the accompanying consolidated balance sheets.

Interest on debt securities is reinvested and recognized in interest income in the accompanying consolidated statements of operations. We recognized approximately \$96 million of interest income on these investments in 2005 compared to \$11 million in 2004. Accumulated unrealized holding gains and losses were immaterial in both 2005 and 2004.

***Investments in Equity Securities***

As of December 31, 2005, \$617 million of our marketable equity securities relates to our investment in NII Holdings Inc. common stock and is reflected in current assets as marketable securities on the accompanying consolidated balance sheets. We acquired this investment as part of the merger with Nextel in the third quarter 2005 at a fair value of \$892 million. In 2005, we received approximately \$376 million in cash and recognized a \$15 million gain on the sale of a portion of our holdings in NII Holdings common stock. We continue to hold 14.7 million shares, following a two-for-one stock split in November 2005, or less than 10% of the outstanding common stock of NII Holdings. We have entered into a series of option contracts associated with the planned sale of our remaining investment in NII Holdings, which will mature during the fourth quarter 2006. See note 12 for additional information.

In 2005, in connection with the maturity of the remaining EarthLink variable prepaid forward contracts, 10.5 million shares of EarthLink common stock were used to settle approximately \$90 million of the forward contracts recorded in outstanding long-term debt. We recognized a \$9 million gain on these transactions. In 2004, in connection with the maturity of certain EarthLink variable prepaid forward contracts, 5.6 million shares were used to settle approximately \$48 million of the forward contracts recorded in outstanding long-term debt. We sold an additional 1.0 million shares in the open market upon settlement of the contracts. We recognized an \$11 million gain on these transactions. As of December 31, 2005, we held 1.8 million shares of EarthLink common stock, valued at \$20 million. See note 12 for additional information.



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**SPRINT NEXTEL CORPORATION**

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

We hold approximately \$97 million in other investments at December 31, 2005 which are included in investments on the accompanying consolidated balance sheets.

Accumulated unrealized holding gains, net of tax, resulting from our investments in equity securities of \$90 million as of December 31, 2005 and \$42 million as of December 31, 2004 were included in accumulated other comprehensive loss on the accompanying consolidated balance sheets.

***Equity Method Investments***

As of December 31, 2005, investments accounted for using the equity method consisted primarily of our investments in Nextel Partners and Virgin Mobile USA, LLC. These investments were reflected in investments on the accompanying consolidated balance sheets.

***Nextel Partners, Inc.***

We owned approximately 30% of the outstanding common stock of Nextel Partners with a carrying value of \$2.3 billion as of December 31, 2005. In 2005, we recorded \$137 million of equity in earnings associated with our ownership interest in Nextel Partners, the majority of which related to a release by Nextel Partners of a significant portion of its deferred tax valuation allowance.

As a result of the merger with Nextel, the shareholders of Nextel Partners in October 2005, exercised their right to require us to purchase, at fair market value, the 70% of the outstanding shares of Nextel Partners stock that we do not already own. In December 2005, we and Nextel Partners announced that the purchase price for each share of Nextel Partners stock under this right had been determined to be \$28.50. As a result, the aggregate amount payable to shareholders of Nextel Partners at closing will be about \$6.5 billion including amounts payable upon conversion of debt securities and settlement of options. The purchase is subject to customary regulatory approvals and is currently expected to be completed by the end of the second quarter 2006.

***Virgin Mobile USA, LLC***

As of December 31, 2005, we held a 49% ownership interest in Virgin Mobile USA. Since Virgin Mobile USA's inception, we have contributed approximately \$180 million to the venture in the form of cash and discounted network services, thereby satisfying 100% of our original commitments. In 2004, we advanced \$10 million to Virgin Mobile USA in the form of a loan to be repaid in 2005. An additional \$10 million was advanced in the form of a loan in January 2005. Applying equity method accounting, we have recognized losses to the extent of our investment, except that under the terms of the joint venture agreement, we were guaranteed a \$20 million distribution in the event of liquidation.

In July 2005, we received approximately \$200 million from Virgin Mobile USA representing a loan repayment of \$20 million and a return of capital of \$180 million resulting in a negative investment balance of \$180 million as of December 31, 2005. Virgin Mobile USA funded the distribution with proceeds from a loan. Although we have no obligation to provide future funding to the joint venture or to return the distribution, we have accounted for the return of capital as a negative investment. As a result of this repayment, under the terms of the joint venture agreement, we no longer hold any right to a guaranteed distribution in liquidation. Our investment in Virgin Mobile USA was \$20 million as of December 31, 2004.

***Rogers Communications, Inc.***

In July 2005, Rogers Communications, Inc., or RCI, acquired Call-Net Enterprises, Inc. in a stock for stock transaction, including the common shares and Class B shares of Call-Net owned by us. Prior to Call-Net's

## SPRINT NEXTEL CORPORATION

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

acquisition by RCI, we accounted for our investment in Call-Net as an equity method investment carried at a zero basis with previously recognized carry-over losses. The RCI stock received in exchange was recorded at fair value as an equity security investment and a gain of \$18 million was recognized. Subsequent changes in the value of this investment have been recorded in other comprehensive income.

Combined, unaudited, summarized financial information as reported by the investees accounted for using the equity method was as follows:

|                                                                   | Year Ended December 31, |          |         |
|-------------------------------------------------------------------|-------------------------|----------|---------|
|                                                                   | 2005                    | 2004     | 2003    |
|                                                                   | <i>(in millions)</i>    |          |         |
| <b>Results of operations</b>                                      |                         |          |         |
| Net operating revenues                                            | \$ 3,238                | \$ 1,244 | \$ 831  |
| Operating income (loss)                                           | 349                     | (181)    | (279)   |
| Net income (loss)                                                 | 502                     | (206)    | (255)   |
| <b>Equity in earnings (losses) of unconsolidated subsidiaries</b> | \$ 110                  | \$ (39)  | \$ (77) |
| <b>Financial position</b>                                         |                         |          |         |
| Current assets                                                    | \$ 845                  | \$ 239   | \$ 260  |
| Other assets                                                      | 1,712                   | 465      | 480     |
| <b>Total assets</b>                                               | \$ 2,557                | \$ 704   | \$ 740  |
| Current liabilities                                               | \$ 568                  | \$ 448   | \$ 294  |
| Other liabilities                                                 | 1,742                   | 267      | 337     |
| <b>Total liabilities</b>                                          | \$ 2,310                | \$ 715   | \$ 631  |

The carrying amount of our investment in Nextel Partners exceeds the amount of the underlying equity in net assets by \$2.1 billion due to purchase price accounting applied at the time of the Sprint-Nextel merger. This difference is principally related to customer relationships, spectrum licenses and goodwill. The customer relationship portion is being amortized over seven years, using the sum of the years digits method. The portion related to spectrum licenses and goodwill is not being amortized.

**Note 6. Fair Value of Financial Instruments**

We have determined the estimated fair values of financial instruments using available market information and appropriate valuation methodologies. However, considerable judgment is required in interpreting market data to develop fair value estimates. As a result, the estimates presented below are not necessarily indicative of the amounts that we could realize or be required to pay in a current market exchange. The use of different market assumptions, as well as estimation methodologies, may have a material effect on the estimated fair value amounts.

The carrying amounts and estimated fair values of our financial instruments at year-end were as follows:

|                           | December 31,         |            |          |            |
|---------------------------|----------------------|------------|----------|------------|
|                           | 2005                 |            | 2004     |            |
|                           | Carrying             | Estimated  | Carrying | Estimated  |
|                           | Amount               | Fair Value | Amount   | Fair Value |
|                           | <i>(in millions)</i> |            |          |            |
| Cash and cash equivalents | \$ 8,902             | \$ 8,902   | \$ 4,176 | \$ 4,176   |
| Investments in securities | 1,906                | 1,906      | 693      | 693        |

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|                                       |        |        |        |        |
|---------------------------------------|--------|--------|--------|--------|
| Restricted cash and deposits          | 174    | 174    | 148    | 148    |
| Total debt, including current portion | 25,679 | 27,999 | 17,204 | 19,568 |
| Redeemable preferred stock            | 247    | 261    | 247    | 284    |

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## SPRINT NEXTEL CORPORATION

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

*Cash and Cash Equivalents, Marketable Securities, Restricted Cash, Accounts Receivable, Deposits, Accounts Payable and Accrued Expenses*

Due to the short term nature of these items, the carrying amounts are reasonable estimates of fair value.

*Marketable Debt and Equity Securities*

We estimate the fair value of these securities based on quoted market prices. As of December 31, 2005 and 2004, marketable debt and equity securities included within marketable securities and investments consist of the following:

|                                                          | Amortized            | Gross<br>Unrealized | Gross<br>Unrealized | Fair     |
|----------------------------------------------------------|----------------------|---------------------|---------------------|----------|
|                                                          | Cost                 | Gain                | Loss                | Value    |
|                                                          | <i>(in millions)</i> |                     |                     |          |
| <b>2005</b>                                              |                      |                     |                     |          |
| Available-for-sale marketable debt and equity securities | \$ 1,763             | \$ 143              | \$                  | \$ 1,906 |
| <b>2004</b>                                              |                      |                     |                     |          |
| Available-for-sale marketable debt and equity securities | \$ 627               | \$ 67               | \$ 1                | \$ 693   |

*Long-Term Debt*

The fair value of our long-term debt, including the current portion, is estimated based on available market prices of our senior notes and loans under our bank credit facility.

*Derivative Instruments*

The fair value of these instruments is based on estimates using available market information and appropriate valuation methodologies. See note 12 for additional information.

*Redeemable Preferred Stock*

We estimate the fair value of these securities by using available market data to value a debt instrument with embedded optionality.

*Letters of Credit*

Outstanding letters of credit totaled \$2.6 billion as of December 31, 2005 and \$123 million as of December 31, 2004. Pursuant to the terms of the Report and Order described in note 15 below, we were required to establish a letter of credit in the amount of \$2.5 billion to provide assurance that funds will be available to pay the relocation costs of the incumbent users of the 800 MHz spectrum in connection with the band reconfiguration process. We obtained the letter of credit using borrowing capacity under Nextel's then existing revolving credit facility and it continues to be supported by the new credit facility entered into in December 2005. The letter of credit reflects fair value as a condition of its underlying purpose and is subject to fees competitively determined in the market place. We also use letters of credit to provide credit support for various financial obligations.

*Concentrations of Risk*

Our accounts receivable are not subject to any concentration of credit risk. We are exposed to the risk of loss that would occur if a counterparty defaults on a derivative transaction used for hedging and risk management purposes. This exposure is controlled through credit approvals, continual review and monitoring of all

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## SPRINT NEXTEL CORPORATION

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

counterparties and legal review of contracts. In the event of nonperformance by the counterparties, our accounting loss would be limited to the net amount we would be entitled to receive under the terms of the applicable interest rate swap agreement or foreign currency contract. However, we do not anticipate nonperformance by any of the counterparties to these contracts.

We rely on Motorola, Inc. to provide us with technology improvements designed to expand our iDEN-based wireless voice capacity and improve our services. Motorola provides all of the iDEN infrastructure equipment used in the iDEN network, and substantially all iDEN handset devices. Motorola is and is expected to continue to be our sole source supplier of iDEN infrastructure and iDEN handsets, except BlackBerry® devices, which are manufactured by Research in Motion, or RIM. Further, our ability to timely and efficiently implement the spectrum reconfiguration plan in connection with the FCC's Report and Order is dependent, in part, on Motorola.

**Note 7. Intangible Assets**

|                                          | Useful Lives  | December 31, 2005 |                   |                  | December 31, 2004 |                |                 |
|------------------------------------------|---------------|-------------------|-------------------|------------------|-------------------|----------------|-----------------|
|                                          |               | Gross             |                   | Net              | Gross             |                | Net             |
|                                          |               | Carrying          | Accumulated       | Carrying         | Carrying          | Accumulated    | Carrying        |
|                                          |               | Value             | Amortization      | Value            | Value             | Amortization   | Value           |
| <i>(in millions)</i>                     |               |                   |                   |                  |                   |                |                 |
| <b>Indefinite life intangible assets</b> |               |                   |                   |                  |                   |                |                 |
| Goodwill                                 | Indefinite    | \$ 21,315         | \$                | \$ 21,315        | \$ 4,401          | \$             | \$ 4,401        |
| FCC licenses                             | Indefinite    | 18,023            |                   | 18,023           | 3,376             |                | 3,376           |
| Trademarks                               | Indefinite    | 416               |                   | 416              | 16                |                | 16              |
|                                          |               | 39,754            |                   | 39,754           | 7,793             |                | 7,793           |
| <b>Definite life intangible assets</b>   |               |                   |                   |                  |                   |                |                 |
| Customer relationships                   | 3 to 5 years  | \$ 9,953          | \$ (1,302)        | \$ 8,651         | \$ 35             | \$ (6)         | \$ 29           |
| Trademarks                               | 10 years      | 900               | (34)              | 866              |                   |                |                 |
| Other                                    | Up to 5 years | 73                | (10)              | 63               | 19                | (5)            | 14              |
|                                          |               | 10,926            | (1,346)           | 9,580            | 54                | (11)           | 43              |
| <b>Total intangible assets</b>           |               | <b>\$ 50,680</b>  | <b>\$ (1,346)</b> | <b>\$ 49,334</b> | <b>\$ 7,847</b>   | <b>\$ (11)</b> | <b>\$ 7,836</b> |

*Indefinite Life Intangibles*

We have identified goodwill, spectrum licenses and our Sprint and Boost Mobile trademarks as indefinite life intangibles after considering the expected use of the assets, the regulatory and economic environment within which they are being used, and the effects of obsolescence on their use.

Substantially all of the goodwill is allocated to the wireless segment. Goodwill includes a portion of value for assembled workforce, which is not separately classified from goodwill in accordance with SFAS No. 141.

The changes in the carrying value of goodwill are as follows:

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|                                                      | (in millions) |
|------------------------------------------------------|---------------|
| Balance, December 31, 2004                           | \$ 4,401      |
| Goodwill acquired through Nextel merger              | 15,573        |
| Goodwill acquired through PCS Affiliate acquisitions | 1,341         |
| Balance, December 31, 2005                           | \$ 21,315     |

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**SPRINT NEXTEL CORPORATION**

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

We hold several kinds of licenses to deploy our services: 1.9 gigahertz, or GHz, PCS licenses utilized in our CDMA network, 800 megahertz, or MHz, and 900 MHz licenses utilized in our iDEN network, and 2.5 GHz licenses that we use for first generation wireless internet access services. We also hold 2.5 GHz, 1.9 GHz and other FCC licenses that we currently do not utilize in our networks or operations. As long as we act within the requirements and constraints of the regulatory authorities, the renewal and extension of our licenses is reasonably certain at minimal cost. Spectrum licenses authorize wireless carriers to use radio frequency spectrum. That spectrum is a renewable, reusable resource that does not deplete or exhaust over time. At present there is no competing technology on the horizon that would render spectrum obsolete. Currently, there are no changes in the competitive or legislative environments that would put in question the future need for spectrum licenses.

The Sprint and Boost Mobile trademarks are highly respected brands with positive connotations. We have no legal, regulatory or contractual limitations associated with our trademarks. We cultivate and protect the use of our brands.

*Definite Life Intangibles*

Definite life intangibles consist primarily of customer relationships of which \$9.5 billion was acquired through our merger with Nextel. Customer relationships are amortized over three to five years using the sum of the years' digits method, which we believe best reflects the estimated pattern in which the economic benefits will be consumed. Other definite life intangibles primarily include the Nextel and Direct Connect<sup>SM</sup> trade names, which will be amortized over 10 years on a straight-line basis. Based on the definite life intangibles as of December 31, 2005, amortization expense will be \$3.2 billion in 2006, \$2.5 billion in 2007, \$1.8 billion in 2008, \$1.1 billion in 2009 and \$0.5 billion in 2010.

**Spectrum Reconfiguration Obligations**

On February 7, 2005, Nextel accepted the terms and conditions of the Report and Order of the FCC, which implemented a spectrum reconfiguration plan designed to eliminate interference with public safety operators in the 800 MHz band. Under the terms of the Report and Order, prior to the August 12, 2005 merger date, Nextel surrendered its spectrum rights in the 700 MHz spectrum band and certain portions of its spectrum rights in the 800 MHz band, and received spectrum rights in the 1.9 GHz band and spectrum rights in a different part of the 800 MHz band and undertook to pay the costs incurred by Nextel and third parties in connection with the reconfiguration plan. Based on the FCC's determination of the values of the spectrum rights received and relinquished by Nextel, the minimum obligation incurred under the Report and Order is \$2.8 billion. The Report and Order also provides that qualifying costs we incur as part of the reconfiguration plan, including costs to reconfigure our own infrastructure and spectrum positions, can be used to offset the minimum obligation of \$2.8 billion; however, we are obligated to pay the full amount of the costs relating to the reconfiguration plan, even if those costs exceed that amount.

The Report and Order requires us to complete the reconfiguration plan within a 36-month period, subject to certain exceptions particularly with respect to markets that border Mexico and Canada. If, as a result of events within our control we fail to complete the reconfiguration plan within the 36-month period, we could be subject to actions, which could be material. In addition, a financial reconciliation is required to be completed in 2008 at the end of the reconfiguration implementation, at which time we are required to make a payment to the U.S. Department of the Treasury to the extent that the value of the spectrum rights received exceeds the total of (i) the value of spectrum rights that are surrendered and (ii) the qualifying costs referred to above.

At August 12, 2005, we had recorded a liability of \$403 million associated with the then-estimated portion of the reconfiguration costs that represented our best estimate of amounts to be paid under the Report and Order that

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**SPRINT NEXTEL CORPORATION**

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

would not benefit our infrastructure or spectrum positions. As of December 31, 2005, we reduced that estimate by \$137 million, through a reduction in goodwill, to reflect updated estimates of these costs. All other costs incurred pursuant to the Report and Order that relate to the spectrum and infrastructure, when expended, are accounted for either as property, plant and equipment or as additions to the spectrum license intangible asset, consistent with our accounting and capitalization policy.

Certain of our reconfiguration costs which we will submit to an FCC appointed Transition Administrator seeking credit against our \$2.8 billion obligation are based on estimated allocations between reconfiguration activity and our normal network growth. These estimated allocations may vary depending on key assumptions including subscribers, call volumes and other factors over the life of the reconfiguration program. As a result, the amount allocated to reconfiguration activity is subject to change based on final assessments made at the conclusion of the reconfiguration program process. Since we, the Transition Administrator and the FCC have not yet reached an agreement on our methodology for calculating the amount to be submitted for credit, we cannot provide assurance that we will be granted full credit for certain of these network costs.

**Note 8. Restructuring and Asset Impairments**

***Organizational Realignment***

In late 2003, we initiated a company-wide effort to create a more efficient cost structure by realigning internal resources to enhance our focus on the needs and preferences of two distinct consumer types – businesses and individuals. In conjunction with the market-facing realignment, we also undertook initiatives to improve productivity.

We recognized related pre-tax charges of \$59 million in 2003 and \$130 million in 2004 primarily associated with severance benefits associated with the involuntary employee separation of approximately 5,400 employees. We have completed substantially all activities related to this realignment, and in the fourth quarter 2005, we completed an analysis to finalize original estimates. This analysis resulted in an \$11 million reduction in liabilities. The remaining \$6 million commitment has been reclassified as other current liabilities.

***Web Hosting Wind-down***

In 2003, we announced the wind-down of web hosting services offered by Long Distance. This decision resulted in a \$316 million pre-tax charge for asset impairments. This wind-down, along with related restructurings in other Long Distance operations, also resulted in pre-tax charges of \$60 million in 2003, \$63 million in 2004 and \$9 million in 2005, primarily related to facility lease terminations. As of December 31, 2005, substantially all activities associated with this wind-down have been completed; however, we continue to be obligated under facility leases that expire from 2007 through 2014.

***Wireless Billing Platform Termination***

In 2003, we announced the termination of the development of a new billing platform in Wireless. This decision resulted in pre-tax charges of \$351 million, consisting of \$339 million for asset impairments and \$12 million for other contractual obligations. In 2004, we recorded an expense reduction of \$2 million as a result of finalizing the contractual obligations associated with this action.

## SPRINT NEXTEL CORPORATION

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

The 2005, 2004 and 2003 restructuring activity is summarized as follows:

|                             | December 31, 2004<br>Liability<br>Balance | Total<br>Restructuring<br>Charge | 2005 Activity                     |                                      | December 31, 2005<br>Liability<br>Balance |
|-----------------------------|-------------------------------------------|----------------------------------|-----------------------------------|--------------------------------------|-------------------------------------------|
|                             |                                           |                                  | Cash<br>Payments<br>(in millions) | Reclasses to<br>Other<br>Liabilities |                                           |
| <b>Restructuring Events</b> |                                           |                                  |                                   |                                      |                                           |
| Organizational Realignment  |                                           |                                  |                                   |                                      |                                           |
| Severance                   | \$ 67                                     | \$ (8)                           | \$ (55)                           | \$ (4)                               | \$                                        |
| Other exit costs            | 8                                         | (3)                              | (3)                               | (2)                                  |                                           |
| Web Hosting Wind-down       |                                           |                                  |                                   |                                      |                                           |
| Other exit costs            | 93                                        | 9                                | (24)                              |                                      | 78                                        |
| Total                       | \$ 168                                    | \$ (2)                           | \$ (82)                           | \$ (6)                               | \$ 78                                     |

|                                       | December 31, 2003<br>Liability<br>Balance | Total<br>Restructuring<br>Charge | 2004 Activity                     |  | December 31, 2004<br>Liability<br>Balance |
|---------------------------------------|-------------------------------------------|----------------------------------|-----------------------------------|--|-------------------------------------------|
|                                       |                                           |                                  | Cash<br>Payments<br>(in millions) |  |                                           |
| <b>Restructuring Events</b>           |                                           |                                  |                                   |  |                                           |
| Organizational Realignment            |                                           |                                  |                                   |  |                                           |
| Severance                             | \$ 54                                     | \$ 122                           | \$ (109)                          |  | \$ 67                                     |
| Other exit costs                      |                                           | 8                                |                                   |  | 8                                         |
| Web Hosting Wind-down                 |                                           |                                  |                                   |  |                                           |
| Severance                             | 6                                         | (2)                              | (4)                               |  |                                           |
| Other exit costs                      | 45                                        | 65                               | (17)                              |  | 93                                        |
| Wireless Billing Platform Termination |                                           |                                  |                                   |  |                                           |
| Other exit costs                      | 12                                        | (2)                              | (10)                              |  |                                           |
| Total                                 | \$ 117                                    | \$ 191                           | \$ (140)                          |  | \$ 168                                    |

|                             | December 31, 2002<br>Liability<br>Balance | Total<br>Restructuring<br>Charge | 2003 Activity                     |  | December 31, 2003<br>Liability<br>Balance |
|-----------------------------|-------------------------------------------|----------------------------------|-----------------------------------|--|-------------------------------------------|
|                             |                                           |                                  | Cash<br>Payments<br>(in millions) |  |                                           |
| <b>Restructuring Events</b> |                                           |                                  |                                   |  |                                           |
| Organizational Realignment  |                                           |                                  |                                   |  |                                           |
| Severance                   | \$                                        | \$ 59                            | \$ (5)                            |  | \$ 54                                     |
| Web Hosting Wind-down       |                                           |                                  |                                   |  |                                           |
| Severance                   |                                           | 15                               | (9)                               |  | 6                                         |

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|                                       |           |           |            |                |               |
|---------------------------------------|-----------|-----------|------------|----------------|---------------|
| Other exit costs                      |           |           | 45         |                | 45            |
| Wireless Billing Platform Termination |           |           |            |                |               |
| Other exit costs                      |           |           | 12         |                | 12            |
| <b>Total</b>                          | <b>\$</b> | <b>\$</b> | <b>131</b> | <b>\$ (14)</b> | <b>\$ 117</b> |

Note during 2003, we also finalized estimates related to prior years restructuring activities, resulting in a \$52 million reduction in liabilities, and reclassification of remaining liabilities to other current liabilities.

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SPRINT NEXTEL CORPORATION

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

*Other Asset Impairments*

In 2005, we incurred a \$77 million asset impairment related to the write-off and removal from service of certain internal-use software systems that are no longer being utilized by Local. We also incurred \$19 million in asset impairments related to hurricane damage, which were substantially recovered from insurance carriers. Also in 2005, we recorded \$50 million in asset impairments related to the write-down of various software applications.

In 2004, we determined that business conditions and events occurring in 2004 and impacting our Long Distance operations constituted a triggering event requiring an evaluation of the recoverability of the Long Distance long-lived assets pursuant to SFAS No. 144, *Accounting for the Impairment or Disposal of Long-Lived Assets*.

The industry-wide business conditions and events included the continuing impacts of the highly-competitive Long Distance market, the related aggressive pricing, recent changes in the regulatory climate negatively impacting the long-term ability of Long Distance to bridge the last mile in the consumer and small business market segments, product substitution and customers' accelerated demands for cost-effective, advanced, IP-driven telecommunications solutions requiring transparent wireline and wireless connectivity. In light of these industry-wide business conditions and events, we reevaluated our strategy and financial forecasts in 2004.

Evaluations of asset recoverability are performed at the lowest asset or asset group level for which identifiable cash flows are largely independent of the cash flows of other assets or asset groups. Due to the integrated nature of the long distance network, we conducted our testing of the asset group at the Long Distance entity level (excluding assets held for sale), as this is the lowest level for which identifiable cash flows are available. Further, it was concluded that the fiber-optic backbone constituted the primary asset of the Long Distance asset group. Accordingly, cash flows were projected over the remaining useful life of the fiber-optic backbone. These cash flow projections reflect estimated future operating results, considering all relevant circumstances and events, and estimated capital expenditures required to maintain, but not to increase, the service potential of the asset group. The resulting undiscounted future cash flows were less than the carrying value of the Long Distance asset group, requiring that the asset group be reduced to fair value.

The fair value of the asset group was determined by discounting the cash flow projections at a 10% discount rate, reflecting a risk-adjusted weighted average cost of capital. The resulting fair value of the asset group required a \$3.52 billion pre-tax non-cash impairment charge, reducing the net carrying value of Long Distance property, plant and equipment by about 60%, to \$2.29 billion at September 30, 2004.

Also in 2004, we completed the sale of our wholesale Dial IP business for \$34 million, resulting in a pre-tax non-cash charge of \$21 million.

In 2003, we recorded a pre-tax, non-cash charge of \$1.2 billion related to the write-down in the carrying value of our BRS spectrum. Our evaluation of our business use for this asset resulted in a decision to end pursuit of a residential fixed wireless strategy. This decision required an impairment analysis of the asset. As a result of our merger, we have increased our BRS spectrum holdings, and intend to use this spectrum in combination with other spectrum holdings to offer wireless interactive multimedia services.

## SPRINT NEXTEL CORPORATION

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

**Note 9. Long-term Debt and Capital Lease Obligations**

Our long-term debt and capital lease obligations at year-end were as follows:

|                                                                                                                                                                 | December 31, 2004 | Acquired Debt<br>and<br>Borrowings | Retirements and<br>Repayments of<br>Principal<br>and Other | December 31, 2005 |
|-----------------------------------------------------------------------------------------------------------------------------------------------------------------|-------------------|------------------------------------|------------------------------------------------------------|-------------------|
|                                                                                                                                                                 |                   |                                    | <i>(in millions)</i>                                       |                   |
| <b>Senior notes due 2007 to 2032</b>                                                                                                                            |                   |                                    |                                                            |                   |
| 4.78% to 9.50%, including fair value hedge adjustments of \$19 and \$(17), and deferred premiums of \$0 and \$332 net of unamortized discounts of \$31 and \$65 | \$ 15,919         | \$ 6,559                           | \$ (1,039)                                                 | \$ 21,439         |
| <b>Bank credit facilities due 2006 and 2010</b>                                                                                                                 |                   |                                    |                                                            |                   |
| 4.775%, including deferred premium of \$0 and \$15 net of an unamortized discount of \$0 and \$9                                                                |                   | 6,406                              | (3,200)                                                    | 3,206             |
| <b>Debentures and notes due 2013 to 2022</b>                                                                                                                    |                   |                                    |                                                            |                   |
| 6.75% to 9.25%                                                                                                                                                  | 400               |                                    |                                                            | 400               |
| <b>First mortgage bonds due 2008 to 2025</b>                                                                                                                    |                   |                                    |                                                            |                   |
| 6.75% to 9.79%, net of unamortized discounts of \$2 and \$2                                                                                                     | 579               |                                    | (114)                                                      | 465               |
| <b>Capital lease obligations</b>                                                                                                                                |                   |                                    |                                                            |                   |
| 4.11% to 11.174%                                                                                                                                                | 215               | 43                                 | (95)                                                       | 163               |
| <b>Other</b>                                                                                                                                                    | 91                | 6                                  | (91)                                                       | 6                 |
|                                                                                                                                                                 | 17,204            | \$ 13,014                          | \$ (4,539)                                                 | 25,679            |
| <b>Current maturities of long-term debt</b>                                                                                                                     | (1,288)           |                                    |                                                            | (5,047)           |
| <b>Long-term debt and capital lease obligations</b>                                                                                                             | \$ 15,916         |                                    |                                                            | \$ 20,632         |

**Senior Notes**

As of December 31, 2005, we have \$21.4 billion in principal amount of convertible and senior serial redeemable notes. This balance primarily consists of newly acquired debt from the merger with Nextel of \$5.8 billion, the acquisition of PCS Affiliates of \$659 million and the existing debt of one of our subsidiaries of \$14.9 billion. Cash interest on these notes is payable semiannually in arrears. We may choose to redeem some or all of these notes at the then applicable redemption price, plus accrued and unpaid interest. The \$607 million in aggregate principal amount of our 5.25% notes are convertible at the option of the holders into our Series 1 common stock at any time prior to redemption, repurchase or maturity at an effective conversion price of \$57.23 per share. As of December 31, 2005, senior notes also included \$130 million of debt associated with a consolidated variable interest entity.

Our weighted average effective interest rate related to these borrowings was 7.0% for the year-ended December 31, 2005 and 7.1% for the year-ended 2004. The effective interest rate includes the effect of interest rate swap agreements accounted for as fair value hedges. See note 12 for more details regarding interest rate swaps.





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**SPRINT NEXTEL CORPORATION**

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

In February 2006, we completed the redemption of all of our outstanding 9.5% senior redeemable notes due 2011, of which \$85 million in aggregate principal amount was outstanding as of December 31, 2005. As of December 31, 2005, we have recorded \$93 million of restricted cash in prepaid expenses and other current assets to satisfy this obligation.

***Bank Credit Facilities***

As of December 31, 2005, our bank credit facilities provide for total unsecured financing capacity of \$10.2 billion, of which we have borrowed \$3.2 billion and have \$2.5 billion of outstanding letters of credit, resulting in \$4.5 billion of available revolving credit.

On December 19, 2005, we entered into a new bank credit facility, consisting of a five year \$6.0 billion revolving credit facility and a 364 day \$3.2 billion term loan, for a total unsecured financing capacity of \$9.2 billion. Under the terms of this new loan, the interest rate equates to the London Interbank Offered Rate, or LIBOR, or the prime rate plus a spread that varies depending on the applicable borrower's or guarantor's credit ratings. The \$6.0 billion revolving credit facility is also subject to a facility fee on the total facility which is payable quarterly. Facility fees can vary between 4 to 15 basis points based upon our credit ratings. This facility replaces the existing Nextel credit agreement, which included a \$4.0 billion revolving credit facility and a \$2.2 billion term loan. In connection with the execution of the new credit agreement, the \$3.2 billion term loan was used to refinance the outstanding term loan and revolving credit loans under the existing Nextel credit agreement, which was terminated in connection with entering into the new credit agreement.

The transaction related to the term loan was accounted for as a modification of debt in accordance with EITF Issue No. 96-19, *Debtors Accounting for a Modification or Exchange of Debt Instruments*, because the terms of the new loan were not substantially different from the terms of the original loan. Thus, the \$15 million unamortized premium associated with the original \$2.2 billion loan will be amortized over the remaining life of the new loan.

The refinancing of the revolving credit facility was accounted for in accordance with EITF Issue No. 98-14, *Debtors Accounting for Changes in Line-of-Credit or Revolving-Debt Arrangements*. Because the borrowing capacity of the new facility is greater than the borrowing capacity of the original facility, any unamortized discount plus any debt issue costs are deferred and amortized over the remaining term of the new facility. Thus, \$9 million of unamortized discount and \$4 million of debt issue costs will be amortized over the remaining life of the new facility.

The \$2.5 billion of letters of credit that were outstanding under the Nextel credit agreement remain outstanding under the new \$6.0 billion revolving credit facility. We also have an additional \$118 million of outstanding letters of credit as of December 31, 2005 used for various financial obligations.

Our credit facility requires compliance with a financial ratio test as defined under the credit agreement. The maturity dates of the loans may accelerate if we do not comply with the financial ratio test. As of December 31, 2005, we were in compliance with the financial ratio test under our credit facility. We are also obligated to repay the loans if certain change of control events occur. Borrowings under the facility are unsecured.

Our ability to borrow additional amounts under the credit facility may be restricted by provisions included in some of our public notes that limit the incurrence of additional indebtedness in certain circumstances. The availability of borrowings under this facility also is subject to the satisfaction or waiver of specified borrowing conditions. As of December 31, 2005, we have satisfied the conditions under this facility.

The credit facility also contains covenants which limit our ability and the ability of some of our subsidiaries to incur additional indebtedness, including guaranteeing obligations of other entities, creating liens, consolidating,

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**SPRINT NEXTEL CORPORATION**

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

merging or selling all or substantially all of our and their assets and entering into transactions with affiliates. Although these covenants are similar to those contained in our previous credit facility, they have been revised under the new credit facility to provide us with greater operating flexibility.

In June 2005, we entered into a revolving credit facility of \$1.0 billion. This facility is unsecured and is structured as a 364-day credit line with a subsequent one-year, \$1.0 billion term-out option. In connection with the execution of the new credit agreement, on December 16, 2005, we amended this facility to allow Nextel to participate in the new facility. We had no outstanding borrowings against this facility as of December 31, 2005.

***Debentures***

As of December 31, 2005, we have \$400 million in principal amount of debentures. This balance is comprised of \$50 million in principal amount of our 6.75% debentures due 2013, \$150 million in principal amount of our 9.00% debentures due 2019 and \$200 million in principal amount of our 9.25% debentures due 2022. Cash interest on these debentures is payable semiannually in arrears. These debentures are not redeemable prior to maturity.

***Mortgage Bonds***

As of December 31, 2005, we have \$465 million in first mortgage bonds. Cash interest on these bonds is payable semiannually in arrears. These bonds are made up of redeemable and non-redeemable bonds and are secured by \$13.6 billion of gross property, plant and equipment.

***Capital Lease Obligations***

As of December 31, 2005, we have \$163 million in capital lease obligations primarily for the use of communication switches, which are secured by \$415 million of gross property, plant and equipment.

***Other***

In December 2005, we terminated two accounts receivable asset securitization facilities that provided us with up to \$1.2 billion of additional liquidity. Neither facility had an outstanding balance when it was terminated, and both were scheduled to expire during 2006.

The indentures and financing agreements of certain of our subsidiaries contain provisions limiting cash dividend payments on subsidiary common stock held by us. As a result, \$432 million of those subsidiaries' \$2.7 billion total retained earnings were restricted as of December 31, 2005. The flow of cash in the form of advances from the subsidiaries to us is generally not restricted.

We are currently in compliance with all restrictive and financial covenants associated with our borrowings. There is no provision under any of our indebtedness that requires repayment in the event of a downgrade by any ratings service.

***2004 Retirements***

In 2004, we purchased and retired a total of \$1.4 billion of our senior notes before their scheduled maturities in exchange for cash. As a result, we recorded a loss due to the premium paid of \$60 million and wrote-off \$12 million of unamortized debt costs associated with this repayment. We also paid \$13 million in cash to complete an early buy out on certain capital lease obligations.

## SPRINT NEXTEL CORPORATION

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

**2003 Retirements**

In 2003, we purchased and retired \$1.5 billion of our long-term debt before scheduled maturities. The prepayments consisted of current maturities of a \$300 million Export Development Canada loan with an interest rate of 2.8% and \$34 million of our senior notes with interest rates ranging from 5.7% to 5.9%. The prepayments also included \$84 million of Local's first mortgage bonds with interest rates ranging from 9.1% to 9.3% and maturity dates ranging from 2019 to 2021. We recorded a loss due to a premium paid of \$2 million associated with these prepayments. We also completed a tender offer to purchase \$1.1 billion principal amount of our senior notes before their scheduled maturities. The notes had interest rates ranging from 5.7% to 5.9% and maturity dates ranging from 2003 to 2004. A loss was recorded due to a premium paid of \$19 million associated with these prepayments.

**Future Maturities of Long-term Debt and Capital Lease Obligations**

For the years subsequent to December 31, 2005, scheduled annual principal payments of long-term debt, including our bank credit facility and capital lease obligations outstanding, as of December 31, 2005 are as follows:

|                          | <i>(in millions)</i> |
|--------------------------|----------------------|
| 2006                     | \$ 5,027             |
| 2007                     | 1,650                |
| 2008                     | 1,368                |
| 2009                     | 608                  |
| 2010                     | 748                  |
| Thereafter               | 16,007               |
|                          | 25,408               |
| Add net deferred premium | 271                  |
|                          | <b>\$ 25,679</b>     |

Included in the above schedule are payments to be made in connection with various capital lease obligations. A substantial portion of the capital lease payments will be in Japanese yen and we already satisfied this obligation by depositing the present value of the future yen payment obligations at various banks. These amounts are included on the accompanying consolidated balance sheet in other assets.

**Note 10. Equity Unit Notes**

In 2001, we completed a registered offering of 69 million equity units, each with a stated amount of \$25. Each equity unit initially consisted of a corporate unit. Each corporate unit consisted of a forward purchase contract and \$25 principal amount of senior notes, or Notes, of our wholly-owned subsidiary, Sprint Capital Corporation. The corporate unit could be converted by the holder into a treasury unit consisting of the forward purchase contract and a treasury portfolio of zero-coupon U.S. treasury securities by substituting the treasury securities for the Notes. The underlying Notes, or treasury portfolio, were pledged to us to secure the holder's obligations under the forward purchase contract.

*Forward Purchase Contract*

As a component of the equity units, the forward purchase contracts originally obligated the holders to purchase, and obligated us to sell, on August 17, 2004, a variable number of newly issued shares of PCS common stock,



## SPRINT NEXTEL CORPORATION

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

which became FON common stock as a result of the recombination. These forward purchase contracts included a provision permitting the equity unit holders to benefit from or participate in any dividends declared on the common stock during the contract period. On August 17, 2004 the forward purchase contracts were settled by the issuance of approximately 35 million shares of FON common stock in exchange for \$1.7 billion in cash.

*Notes*

The Notes were originally issued as part of the equity units and had an interest rate of 6.0% for a notional amount of \$1.7 billion. In May 2004, we purchased \$750 million principal amount of the Notes before their scheduled maturity. As a result, we recognized a \$29 million loss in other income due to the premium paid and the write-off of unamortized debt issuance costs.

The interest rate on the Notes was reset to 4.8% on May 24, 2004, after a successful remarketing, and after the remarketing the Notes were no longer pledged to secure the obligations under the original forward purchase contracts.

As of December 31, 2005, \$880 million of the remarketed Notes, which are due in August 2006, are included in current portion of long-term debt and capital lease obligations on the accompanying consolidated balance sheets.

**Note 11. Seventh Series Redeemable Preferred Stock**

The redeemable preferred stock outstanding at year-end is as follows:

|                                                                                                                                                                         | December 31,         |        |
|-------------------------------------------------------------------------------------------------------------------------------------------------------------------------|----------------------|--------|
|                                                                                                                                                                         | 2005                 | 2004   |
|                                                                                                                                                                         | <i>(in millions)</i> |        |
| Seventh series preferred stock stated value \$1,000 per share, 300,000 shares authorized, 246,766 shares outstanding, voting, cumulative \$6.73 quarterly dividend rate | \$ 247               | \$ 247 |

The Seventh series preferred stock is currently convertible into approximately 32.5 shares of voting common stock for each Seventh series share. The Seventh series preferred stock is mandatorily redeemable in November 2008 at the stated value plus any accrued but unpaid dividends. On February 28, 2006, notices were sent out to holders of our Seventh series preferred stock with our intent to redeem the preferred stock. We expect to close on March 31, 2006 for a redemption price of \$1,000 per outstanding share plus accumulated unpaid dividends.

**Note 12. Derivative Instruments and Hedging Activities***Risk Management Policies*

Our derivative instruments typically include interest rate swaps, stock warrants, option contracts, and foreign currency forward and option contracts. We primarily use our derivative transactions to hedge our exposure to the market risks associated with unfavorable movements in interest rates, equity prices, and foreign currencies. Our board of directors has authorized us to enter into derivative transactions, and all transactions comply with our risk management policies.

Interest rate risk is the risk that changes in interest rates could adversely affect earnings or cash flows. Specific interest rate risks include the risk of increasing interest rates on short-term debt, the risk of increasing interest rates for planned new fixed rate long-term financing and the risk of increasing interest rates for planned refinancings using long-term fixed rate debt.

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**SPRINT NEXTEL CORPORATION**

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

Exposure to strategic investments in other companies includes the risk that unfavorable changes in market prices could adversely affect earnings and cash flows. We may also obtain equity rights in other companies, usually in the form of warrants to purchase common stock of the companies. These equity rights are typically obtained in connection with commercial agreements or strategic investments.

Our foreign exchange risk management program focuses on reducing transaction exposure to optimize consolidated cash flow. We enter into forward and option contracts in foreign currencies to reduce the impact of changes in foreign exchange rates. Our primary transaction exposure results from net payments made to and received from overseas telecommunications companies for completing international calls made by our domestic customers and the operations of our international subsidiaries.

***Interest Rate Swaps***

As of December 31, 2005, we held fair value interest rate swaps with a notional value of \$1 billion. These swaps were entered into as hedges of the fair value of a portion of our senior notes. These interest rate swaps have maturities ranging from 2008 to 2012. On a semiannual basis, we pay a floating rate of interest equal to the six-month LIBOR plus a fixed spread and receive an average interest rate equal to the coupon rates stated on the underlying senior notes. On December 31, 2005, the rate we would pay averaged 7.0% and the rate we would receive was 7.2%.

Our interest rate swaps meet all the required criteria under SFAS No. 133, *Accounting for Derivative Instruments and Hedging Activities*, as amended, in order to apply the shortcut method in accounting for these instruments. Under the shortcut method we can assume that our interest rate swaps are perfectly effective in hedging our interest rate risk. As a result, we recognize all changes in the fair values of these instruments in accumulated other comprehensive loss on the Consolidated Balance Sheets, with no impact on earnings during the life of the swap. We held only fair-value hedges during 2005 and 2004.

Our interest rate swap activity generated a net liability of \$18 million at December 31, 2005 compared to a net asset of \$19 million as of December 31, 2004, resulting from changes in the fair value of the interest rate swaps. As the swaps have been deemed perfectly effective, an offset was recorded to the underlying long-term debt.

During the fourth quarter 2005 we entered into a series of interest rate collars associated with the anticipated issuance of debt by Local at the time of its expected spin-off in 2006. These collars have been designated as cash flow hedges in Local's standalone financial statements against the variability in interest payments that would result from a change in interest rates before the debt is issued at the time of the spin-off. However, because the forecasted interest payments of debt will occur after the subsidiary is spun-off, the derivative instruments do not qualify for hedge accounting treatment in our consolidated financial statements, and so changes in the fair value of these instruments are recognized in earnings during the period of change. During the fourth quarter 2005, the fair value of these derivatives decreased, resulting in a pre-tax loss of \$18 million as of December 31, 2005.

***Stock Warrants***

The stock warrants are not designated as hedging instruments and changes in the fair value of these derivative instruments are recognized in earnings during the period of change. Our net derivative gains on stock warrants were immaterial in all periods presented.

***Equity Options***

We have also entered into a series of option contracts associated with our investment in NII Holdings, Inc. The first of these contracts was not designated as a hedging instrument, and changes in the fair value of the derivative instrument are recognized in earnings during the period of change. The change in fair value of this instrument

## SPRINT NEXTEL CORPORATION

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

resulted in a pre-tax loss of \$9 million as of December 31, 2005. The remaining instruments are designated as cash flow hedges and meet all the required criteria under SFAS No. 133 and the Derivative Implementation Group Issue No. G-20, *Assessing and Measuring the Effectiveness of a Purchased Option Used in a Cash Flow Hedge*, in order to assume that these option contracts are perfectly effective in hedging the market risk associated with our investment in NII Holdings. As a result, we recognize all changes in the fair values of these remaining instruments in accumulated other comprehensive loss on the Consolidated Balance Sheets, with no impact on earnings during the life of the hedging relationship. Changes in fair value of these instruments resulted in an unrealized loss of \$16 million at December 31, 2005. These unrealized losses were included in accumulated other comprehensive loss on the Consolidated Balance Sheets. These derivative instruments will be settled by December 31, 2006.

The net purchased equity options embedded in variable prepaid forward contracts are designated as cash flow hedges. During 2005, we used 10.5 million shares of EarthLink common stock to settle the prepaid forward contracts, which resulted in a \$9 million pre-tax gain. There are no variable prepaid forward contracts outstanding at December 31, 2005.

**Foreign Currency Forward and Option Contracts**

Foreign currency forward and option contracts held during 2005 and 2004 were not designated as hedges as defined in SFAS No. 133, *Accounting for Derivative Instruments and Hedging Activities*, as amended, and changes in the fair value of these derivative instruments are recognized in earnings during the period of change. The activity associated with these contracts was immaterial in all periods presented.

**Note 13. Income Taxes**

Income tax expense (benefit) allocated to continuing operations consists of the following:

|                                              | Year Ended December 31, |          |          |
|----------------------------------------------|-------------------------|----------|----------|
|                                              | 2005                    | 2004     | 2003     |
|                                              | <i>(in millions)</i>    |          |          |
| <b>Current income tax expense (benefit)</b>  |                         |          |          |
| Federal                                      | \$ 115                  | \$ 15    | \$ (672) |
| State                                        | 160                     | (30)     | 21       |
| Total current                                | 275                     | (15)     | (651)    |
| <b>Deferred income tax expense (benefit)</b> |                         |          |          |
| Federal                                      | 856                     | (562)    | 494      |
| State                                        | (26)                    | (14)     | (55)     |
| Total deferred                               | 830                     | (576)    | 439      |
| <b>Foreign income tax expense</b>            |                         |          |          |
| Total                                        | \$ 1,105                | \$ (591) | \$ (212) |



## SPRINT NEXTEL CORPORATION

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

The differences that caused our effective income tax rates to vary from the 35% federal statutory rate for income taxes related to continuing operations were as follows:

|                                                            | Year Ended December 31, |          |          |
|------------------------------------------------------------|-------------------------|----------|----------|
|                                                            | 2005                    | 2004     | 2003     |
|                                                            | <i>(in millions)</i>    |          |          |
| Income tax expense (benefit) at the federal statutory rate | \$ 1,017                | \$ (562) | \$ (176) |
| Effect of:                                                 |                         |          |          |
| State income taxes, net of federal income tax effect       | 88                      | (28)     | (23)     |
| Credit for research activities                             | (8)                     | (2)      | (27)     |
| Other, net                                                 | 8                       | 1        | 14       |
| Income tax expense (benefit)                               | \$ 1,105                | \$ (591) | \$ (212) |
| Effective income tax rate                                  | 38.0%                   | 36.9%    | 42.1%    |

Income tax expense (benefit) allocated to other items was as follows:

|                                                                  | Year Ended December 31, |      |        |
|------------------------------------------------------------------|-------------------------|------|--------|
|                                                                  | 2005                    | 2004 | 2003   |
|                                                                  | <i>(in millions)</i>    |      |        |
| Discontinued operations                                          | \$                      | \$   | \$ 820 |
| Cumulative effect of change in accounting principle              | (10)                    |      | 162    |
| Additional minimum pension liability <sup>(1)</sup>              | (39)                    | (17) | (12)   |
| Gains on securities <sup>(1)</sup>                               | 27                      | 2    | 27     |
| Gains (losses) on qualifying cash flow hedges <sup>(1)</sup>     | 7                       | 1    | (23)   |
| Stock ownership, purchase and option arrangements <sup>(2)</sup> | (38)                    | (25) | (4)    |

(1) These amounts have been recorded directly to shareholders' equity accumulated other comprehensive income (loss) on the accompanying consolidated balance sheets.

(2) These amounts have been recorded directly to shareholders' equity paid-in capital on the accompanying consolidated balance sheets. We recognize deferred income taxes for the temporary differences between the carrying amounts of our assets and liabilities for financial statement purposes and their tax bases. The sources of the differences that give rise to the deferred income tax assets and liabilities at year-end 2005 and 2004, along with the income tax effect of each, were as follows:

|                                  | December 31, 2005    |           | December 31, 2004 |           |
|----------------------------------|----------------------|-----------|-------------------|-----------|
|                                  | Current              | Long-Term | Current           | Long-Term |
|                                  | <i>(in millions)</i> |           |                   |           |
| <b>Deferred tax assets</b>       |                      |           |                   |           |
| Net operating loss carryforwards | \$ 1,835             | \$ 1,186  | \$ 1,050          | \$ 1,269  |
| Capital loss carryforwards       | 354                  | 77        |                   |           |

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|                                   |       |       |       |       |
|-----------------------------------|-------|-------|-------|-------|
| Accruals and other liabilities    | 473   | 335   | 219   | 150   |
| Tax credit carryforwards          |       | 556   |       | 397   |
| Postretirement and other benefits |       | 871   |       | 842   |
|                                   | 2,662 | 3,025 | 1,269 | 2,658 |
| <b>Valuation allowance</b>        | (556) | (515) | (220) | (450) |
|                                   | 2,106 | 2,510 | 1,049 | 2,208 |

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## SPRINT NEXTEL CORPORATION

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

|                                         | December 31, 2005    |           | December 31, 2004 |           |
|-----------------------------------------|----------------------|-----------|-------------------|-----------|
|                                         | Current              | Long-Term | Current           | Long-Term |
|                                         | <i>(in millions)</i> |           |                   |           |
| <b>Deferred tax liabilities</b>         |                      |           |                   |           |
| Property, plant and equipment           |                      | 3,769     |                   | 3,735     |
| Intangibles                             |                      | 9,594     |                   | 649       |
| Investments                             | 225                  | 834       |                   |           |
| Other                                   | 70                   |           |                   |           |
|                                         | 295                  | 14,197    |                   | 4,384     |
| <b>Current deferred tax asset</b>       | \$ 1,811             |           | \$ 1,049          |           |
| <b>Long-term deferred tax liability</b> |                      | \$ 11,687 |                   | \$ 2,176  |

The foreign income (loss) included in income (loss) from continuing operations totaled \$27 million in 2005, \$(203) million in 2004 and \$(141) million in 2003. We have no material un-remitted earnings of foreign subsidiaries.

In 2005, we acquired approximately \$2.8 billion of potential income tax benefits related to net operating loss carryforwards, capital loss carryforwards and tax credit carryforwards in the Nextel and PCS Affiliates acquisitions. In 1999 we acquired approximately \$193 million of potential tax benefits related to net operating loss carryforwards in the acquisitions of broadband fixed wireless companies. In 1998, we acquired approximately \$229 million of potential tax benefits related to net operating loss carryforwards in the controlling interest acquisition of our wireless joint venture, which we call the PCS Restructuring. The benefits from these acquisitions are subject to certain realization restrictions under various tax laws. As of December 31, 2005, a valuation allowance of \$820 million remains on these deferred tax benefits. If the benefits for which a valuation allowance has been provided are subsequently recognized, they will first reduce goodwill or intangibles resulting from the application of the purchase method of accounting for these transactions. If goodwill and intangibles related to the acquisition are reduced to zero, any additional tax benefits recognized would reduce tax expense.

In connection with the PCS Restructuring, we are required to reimburse the former cable company partners of the joint venture for net operating loss and tax credit carryforward benefits generated before the PCS Restructuring if realization by us produces a cash benefit that would not otherwise have been realized. The reimbursement will equal 60% of the net cash benefit received by us and will be made to the former cable company partners in shares of our stock. The unexpired carryforward benefits subject to this requirement total \$202 million.

As of December 31, 2005, we had federal operating loss carryforwards of approximately \$7.0 billion and state operating loss carryforwards of approximately \$12.7 billion. Related to these loss carryforwards are federal tax benefits of \$2.5 billion and state tax benefits of \$872 million. In addition, we had available, for income tax purposes, federal alternative minimum tax net operating loss carryforwards of \$5.5 billion and state alternative minimum tax net operating loss carryforwards of \$1.1 billion. The loss carryforwards expire in varying amounts through 2025. We also had available capital loss carryforwards of approximately \$1.2 billion. Related to these capital loss carryforwards are tax benefits of \$431 million. Included in the capital loss carryforward amount is \$966 million which expires in 2006. The remaining capital loss carryforward expires in varying amounts through 2009.

We also had available \$556 million of federal and state income tax credit carryforwards as of December 31, 2005. Included in this amount are \$350 million of income tax credits which expire in varying amounts through 2025. The remaining \$206 million do not expire.

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**SPRINT NEXTEL CORPORATION**
**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

The valuation allowance related to deferred income tax assets increased \$401 million in 2005 and increased \$50 million in 2004. The 2005 increase is primarily related to the Nextel and PCS Affiliate acquisitions.

Management believes it is more likely than not that these deferred income tax assets, net of the valuation allowance, will be realized based on current income tax laws and expectations of future taxable income stemming from the reversal of existing deferred tax liabilities or ordinary operations. Uncertainties surrounding income tax law changes, shifts in operations between state taxing jurisdictions and future operating income levels may, however, affect the ultimate realization of all or some of these deferred income tax assets. When we evaluated these and other qualitative factors and uncertainties concerning our industry, we found that they provide continuing evidence requiring the valuation allowance which we currently recognize related to the realization of the tax benefit of our net operating loss and tax credit carryforwards as of December 31, 2005. Additionally, we establish reserves when, despite our belief that our tax return positions are fully supportable, certain positions could be challenged, and the positions may not be fully sustained.

**Note 14. Discontinued Operations**

In 2002, we reached a definitive agreement to sell our directory publishing business, held in the Local segment, to R.H. Donnelley for \$2.2 billion in cash. The sale closed on January 3, 2003. The pretax gain recognized in 2003 was \$2.1 billion, \$1.3 billion after tax. In accordance with SFAS No. 144, *Accounting for the Impairment or Disposal of Long-Lived Assets*, we have presented the results of operations of the directory publishing business as a discontinued operation in the accompanying consolidated financial statements. Summary financial information is as follows:

|                            | <b>Year Ended</b>    |
|----------------------------|----------------------|
|                            | <b>December 31,</b>  |
|                            | <b>2003</b>          |
|                            | <b>(in millions)</b> |
| Net operating revenues     | \$ 5                 |
| Income before income taxes | 5                    |

In prior years, we reported the cash flows attributable to these discontinued operations on a combined basis as a single amount. In 2005, these cash flows are no longer reported as a single amount, and have been combined with the cash flows of our continuing operations.

**Note 15. Commitments and Contingencies***Litigation, Claims and Assessments*

In 2005, several PCS Affiliates filed lawsuits in various courts, alleging that the merger between Sprint and Nextel would result in breaches of exclusivity provisions in their management agreements with our subsidiaries. Suits were brought by UbiquiTel and UbiquiTel Operating Company, iPCS Wireless, Inc., Horizon Personal Communications Inc. and Bright Personal Communications Services LLC, which are both subsidiaries of iPCS Wireless and Northern PCS Services, LLC. The lawsuits seek, among other things, to enjoin us from engaging in certain post-merger business conduct in the respective service areas of the PCS Affiliates, and unspecified damages caused by the alleged breach. UbiquiTel, Horizon Personal Communications and Bright Personal Communications Services have all entered into forbearance agreements with us governing certain business practices addressed by the litigation until a decision is rendered by the trial court in the lawsuits. We and our subsidiaries intend to defend all of these lawsuits vigorously.

In March 2004, eight purported class action lawsuits relating to the recombination of the tracking stocks were filed against us and our directors by holders of PCS common stock. Seven of the lawsuits were consolidated in

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**SPRINT NEXTEL CORPORATION**

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

the District Court of Johnson County, Kansas. The eighth, pending in New York, has been voluntarily stayed. The consolidated lawsuit alleges breach of fiduciary duty in connection with allocations between the wireline operations and the wireless operations before the recombination of the tracking stocks and breach of fiduciary duty in the recombination. The lawsuit seeks to rescind the recombination and monetary damages. In early 2005, the court denied defendants' motion to dismiss the complaint and discovery is proceeding. All defendants have denied plaintiffs' allegations and intend to defend this matter vigorously.

In 2003, certain participants in the Sprint Nextel Retirement Savings Plan and the Sprint Nextel and Centel Retirement Savings Plans for Bargaining Unit Employees filed suit in the U.S. District Court for the District of Kansas against us, the committees that administer the plans, the plan trustee, and various current and former directors and officers. The consolidated lawsuit alleges that defendants breached their fiduciary duties to the plans and violated the Employee Retirement Income Security Act of 1974, or ERISA, statutes by making the company matching contribution in company stock and by including company stock among the thirty investment options offered to plan participants. The lawsuit seeks to recover any decline in the value of our tracking stocks during the class period. A settlement agreement has been filed with the court and is subject to final court approval. The settlement calls for us to make certain changes to the savings plans, to allow for vesting of certain Sprint Nextel stock in the accounts of certain former employees, and to distribute \$4 million in cash to former employees who no longer have accounts in the savings plans. We have insurance coverage for the cash component of this settlement.

In September 2004, the U.S. District Court for the District of Kansas denied a motion to dismiss a shareholder lawsuit alleging that our 2001 and 2002 proxy statements were false and misleading in violation of federal securities laws to the extent they described new employment agreements with certain senior executives without disclosing that, according to the allegations, replacement of those executives was inevitable. These allegations, made in an amended complaint in a lawsuit originally filed in 2003, are asserted against us and certain current and former officers and directors, and seek to recover any decline in the value of our tracking stocks during the class period. The parties have stipulated that the case can proceed as a class action. All defendants have denied plaintiffs' allegations and intend to defend this matter vigorously. Allegations in the original complaint, which asserted claims against the same defendants and our former independent auditor, were dismissed by the court in April 2004.

A number of putative class action cases that allege Sprint Communications Company LP failed to obtain easements from property owners during the installation of its fiber optic network in the 1980's have been filed in various courts. Several of these cases sought certification of nationwide classes, and in one case, a nationwide class has been certified. In 2002, a nationwide settlement of these claims was approved by the U.S. District Court for the Northern District of Illinois, but objectors appealed the preliminary approval order to the Seventh Circuit Court of Appeals, which overturned the settlement and remanded the case to the trial court for further proceedings. The parties now are proceeding with litigation and/or settlement negotiations on a state by state basis. In 2001, we accrued an expense reflecting the estimated settlement costs of these suits.

Various other suits, proceedings and claims, including purported class actions, typical for a business enterprise, are pending against us or our subsidiaries. While it is not possible to determine the ultimate disposition of each of these proceedings and whether they will be resolved consistent with our beliefs, we expect that the outcome of such proceedings, individually or in the aggregate, will not have a material adverse effect on our financial condition or results of operations or our business segments.

***Spectrum Reconfiguration Obligations***

On February 7, 2005, Nextel accepted the terms and conditions of the Report and Order of the FCC which implemented a spectrum reconfiguration plan designed to eliminate interference with public safety operators in

## SPRINT NEXTEL CORPORATION

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

the 800 MHz band. Under the terms of the Report and Order, prior to the August 12, 2005 merger date, Nextel surrendered its spectrum rights in the 700 MHz spectrum band and certain portions of its spectrum rights in the 800 MHz band, and received spectrum rights in the 1.9 GHz band and spectrum rights in a different part of the 800 MHz band and undertook to pay the costs incurred by Nextel and third parties in connection with the reconfiguration plan. Based on the FCC's determination of the values of the spectrum rights received and relinquished by Nextel, the minimum obligation incurred under the Report and Order will be \$2.8 billion. The Report and Order also provides that qualifying costs we incur as part of the reconfiguration plan, including costs to reconfigure our own infrastructure and spectrum positions, can be used to offset the minimum obligation of \$2.8 billion; however, we are obligated to pay the full amount of the costs relating to the reconfiguration plan, even if those costs exceed that amount. See note 7 for further information.

**Operating Leases**

We lease various equipment, office facilities, retail outlets and kiosks, switching facilities, transmitter and receiver sites and spectrum under operating leases. The non-cancelable portion of these leases ranges from monthly up to 25 years. These leases, with few exceptions, provide for automatic renewal options and escalations that are either fixed or based on the consumer price index. Any rent abatements, along with rent escalations, are included in the computation of rent expense calculated on a straight-line basis over the lease term. Our lease term for most leases includes the initial non-cancelable term plus at least one renewal period, as the exercise of the related renewal option or options is reasonably assured. Our cell site leases generally provide for an initial non-cancelable term of 5 to 7 years with up to 5 renewal options for 5 years each.

As of December 31, 2005, our rental commitments for operating leases, including lease renewals that are reasonably assured, consisted mainly of leases for cell and switch sites, real estate, data processing equipment and office space were as follows (in millions):

|            |          |
|------------|----------|
| 2006       | \$ 1,475 |
| 2007       | 1,423    |
| 2008       | 1,325    |
| 2009       | 1,237    |
| 2010       | 1,105    |
| Thereafter | 9,814    |

Total rental expense was \$1.4 billion in 2005, \$1.1 billion in 2004, and \$1.2 billion in 2003.

Leasehold improvements are depreciated over the lesser of the estimated useful life of the asset or the lease term, including renewal option periods that are reasonably assured.

**Commitments**

We are a party to service and other contracts in connection with conducting our business. Minimum amounts due under some of the more significant agreements are \$2,427 million in 2006, \$1,885 million in 2007, \$1,412 million in 2008, \$1,180 million in 2009, \$603 million in 2010 and \$577 million thereafter. Amounts actually paid under some of these agreements will likely be higher due to variable components of these agreements. The more significant variable components that determine the ultimate obligation owed include such items as hours contracted, subscribers and other factors. In addition, we are party to various arrangements that are conditional in nature and obligate us to make payments only upon the occurrence of certain events, such as the delivery of functioning software or a product.

We had about \$5 billion of open purchase orders for goods or services as of December 31, 2005 that are enforceable and legally binding and that specify all significant terms, but were not recorded as liabilities as of

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**SPRINT NEXTEL CORPORATION**

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

December 31, 2005. These outstanding commitments consist primarily of network equipment and maintenance, access commitments, advertising and marketing, information technology services and customer support provided by third parties, handset purchases and other expenses related to normal business operations. We expect substantially all of these commitments to become due in the next twelve months as services are rendered or goods are received. Certain of these service and other contracts are in the process of being re-negotiated as a result of our merger with Nextel, and could result in changes to these minimum commitments, which could be material.

***Environmental Compliance***

We have identified seven sites, not currently owned or operated by us, that formerly contained manufactured gas plants that may have been owned or operated by entities acquired by one of our subsidiaries before we acquired it. We and the current land owner of the site in Columbus, Nebraska are working with the Environmental Protection Agency, or EPA, pursuant to an administrative consent order. Amounts expended pursuant to the order are not expected to be material. We are negotiating with the EPA as to whether clean up is required at two additional sites. In addition, our subsidiary has entered into agreements with another potentially responsible party to share costs in connection with four of the sites, including two of those where the EPA is involved. We are working to assess the scope and nature of these sites and our potential responsibility. Other environmental compliance and remediation expenditures result mainly from the operation of standby power generators for our telecommunications equipment. These expenditures arise in connection with standards compliance, permits or occasional remediation, which are usually related to generators, batteries or fuel storage. Although we cannot assess with certainty the impact of any future compliance and remediation obligations, we do not believe that future environmental compliance and remediation expenditures will have a material adverse effect on our financial condition or results of operations.

**Note 16. Capital Stock and Stock Rights**

We have the authority to issue 6,620,000,000 shares of capital stock as follows:

6,000,000,000 shares of Series 1 voting common stock, par value \$2.00 per share;

500,000,000 shares of Series 2 voting common stock, par value \$2.00 per share;

100,000,000 shares of non-voting common stock, par value \$0.01 per share; and

20,000,000 shares of preferred stock, no par value per share

***Classes of Common Stock***

***Series 1 Common Stock***

The holders of our Series 1 common stock are entitled to one vote per share on all matters submitted for action by the shareholders.

***Series 2 Common stock***

The holders of our Series 2 common stock are entitled to 10% of one vote per share, but otherwise have rights that are substantially identical to those of the Series 1 common stock.

We paid a dividend of \$0.025 per share on the common stock, Series 1, the common stock, Series 2, and the non-voting common stock in the third and fourth quarters 2005. The non-voting common stock was issued in the





## SPRINT NEXTEL CORPORATION

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Sprint-Nextel merger in August 2005. We paid a dividend of \$0.125 per share on the common stock, Series 1 in the first two quarters of 2005 and in each of the quarters of 2004 and 2003 and a dividend of \$0.125 per share on the common stock, Series 2 in the first two quarters of 2005 and in each of the last three quarters of 2004. The common stock, Series 2 was issued at the time of the recombination of the PCS common stock and the FON common stock in April 2004.

***Common Stock Reserved for Future Grants***

As of December 31, 2005, Series 1 common stock reserved for future grants under plans providing for the grant of stock options and other equity-based awards, future grants under the employees stock purchase plan or future issuances under various other arrangements included:

|                                                                                     | Shares<br>(in millions) |
|-------------------------------------------------------------------------------------|-------------------------|
| Employee stock purchase plan                                                        | 25.6                    |
| Employee savings plans                                                              | 22.4                    |
| Automatic dividend reinvestment plan                                                | 2.3                     |
| Officer and key employees and directors stock options and other equity-based awards | 109.5                   |
| Conversion of mandatorily redeemable preferred stock                                | 8.0                     |
| 5.25% convertible debt conversion rights                                            | 10.3                    |
| Conversion of non-voting common stock                                               | 37.6                    |
| Other                                                                               | 0.1                     |
|                                                                                     | 215.8                   |

**Note 17. Stock Plans*****Management Incentive Stock Option Plan***

Under the Management Incentive Stock Option Plan, or MISOP, before 2003 we granted stock options to employees eligible to receive annual incentive compensation. Eligible employees could elect to receive stock options in lieu of a portion of their target incentive under our annual incentive compensation plans. The options generally became exercisable on December 31 of the year granted and have a maximum term of 10 years. Under the MISOP, we also granted stock options to executives in lieu of long-term incentive compensation, or LTIP-MISOP options. The LTIP-MISOP options generally became exercisable on the third December 31 following the grant date and have a maximum term of 10 years. MISOP options were granted with exercise prices equal to the market price of the underlying common stock on the grant date. No new options may be granted under this plan after April 2005. As of December 31, 2005, options to buy approximately 40.0 million common shares were outstanding.

***Long-Term Stock Incentive Program***

Under the 1997 Long-Term Stock Incentive Program, or the 1997 Program, we can grant stock options, restricted stock and restricted stock units and other equity based awards to directors and employees. In the 1997 Program the number of shares available for grant increases each year until 2007. No awards may be granted under the plan after April 2007. On January 1, 2006, the number of shares authorized by the 1997 Program increased by approximately 43.8 million shares. As of December 31, 2005, this plan authorized equity-based awards for approximately 146.0 million common shares, and 61.0 million common shares remained available.

Employees and directors who are granted restricted stock units are not required to pay for the shares but must remain employed with us, or continue to serve as a member of our board of directors, until the restrictions on the shares lapse. In addition, beginning with the 2005 awards, the number of restricted stock units granted is based on performance criteria as well. The 2005 awards vest 100% three years from the date of grant.



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**SPRINT NEXTEL CORPORATION**

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

The 2005 stock option awards for executives holding titles of Senior Vice President or above, including our Chief Executive Officer, have a strike price equal to 110% of the market value of the underlying stock on the grant date. All other executives received stock options with a strike price equal to 100% of fair market value on the grant date. The 2005 stock option award for all participants will vest 25% per year on each of the anniversaries of the date of grant and will have a maximum term of 10 years.

Under our Restricted Stock Plan, we granted restricted stock to officers and key employees. Employees granted restricted stock are not required to pay for the shares but must remain employed with us until the restrictions on the shares lapse. The restricted stock vests at a rate of 33.3% per year on each of the first three anniversaries of the grant date. No restricted stock was granted in 2005.

Under the Sprint Retention Program, if the employment of a holder of an equity award is involuntarily terminated other than for cause within one year of the Nextel merger, then unvested equity awards held by that holder for at least one year at the end of the holders' severance period will fully vest at that time.

***Nextel Incentive Equity Plan***

As a result of the Sprint-Nextel merger, outstanding Nextel deferred shares, which constitute an agreement to transfer shares upon the performance of service over a defined period of time, and grants of options to purchase shares of Nextel common stock were converted into Sprint Nextel Series 1 deferred shares or options to purchase a number of shares of Sprint Nextel Series 1 common stock equal to the number of shares of Nextel common stock subject to the corresponding Nextel options or deferred shares multiplied by 1.3, with a corresponding adjustment to the option strike price.

The Nextel Incentive Equity Plan, or Nextel Equity Plan, was approved by Nextel's shareholders before the Nextel merger. This plan provides for the issuance to directors, officers, employees and consultants of our common stock (giving effect to the conversion ratio in the merger) upon the exercise or issuance of a variety of forms of equity rights, including grants of options to purchase stock and deferred shares. As of December 31, 2005, this plan authorized equity-based awards for approximately 132.9 million common shares and 48.5 million common shares remained available. Typically, nonqualified stock options to purchase stock were granted under the Nextel Equity Plan, and such options that currently are outstanding generally:

have been granted at prices equal to or exceeding the market value of the stock on the grant date;

vest on a monthly basis over periods up to four years; and

expire ten years from date of grant.

If an option holder's employment is involuntarily terminated within one year after the effective date of a change of control of Nextel, or, in the case of specified executives, if the employee terminates their employment for good reason as defined in the plan, then that holder's unvested options immediately vest or otherwise become payable, subject to some limits. A change of control was deemed to have occurred as a result of the Sprint-Nextel merger.

The Nextel Equity Plan also provides for the grant of deferred shares at no cost to selected employees generally in consideration of future services. These deferred shares generally vest over a service period ranging from several months to four years. An accelerated vesting schedule may be triggered in the event of a change in control. Accelerated vesting was triggered with respect to certain deferred shares granted prior to the Sprint-Nextel merger as a result of the Sprint-Nextel merger.

## SPRINT NEXTEL CORPORATION

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

*Employee Stock Purchase Plan*

Under our Employees Stock Purchase Plan, or ESPP, eligible employees may subscribe quarterly to purchase shares of Series 1 common stock through payroll deductions of up to 20% of eligible compensation. The purchase price is equal to 90% of market value on the last trading day of each quarter. The aggregate number of shares purchased by an employee may not exceed 9,000 shares or \$25,000 of fair market value in any calendar year, subject to limitations imposed by Section 423 of the Internal Revenue Code.

As of December 31, 2005, this plan authorized for purchase approximately 25.6 million shares, net of elections made in 2005 by employees participating in the fourth quarter 2005 offering under the ESPP to purchase approximately 720,000 common shares in the first quarter 2006. Employees purchased these shares for \$21.11.

*Fair Value Disclosures*

In connection with the Nextel merger, Nextel stock options were converted into Sprint Nextel stock options with the shares issuable and exercise prices of the options adjusted based on an exchange ratio of 1.3 shares of Sprint Nextel common stock for each share of Nextel common stock. The value of these awards was calculated by applying the fair value method under SFAS No. 123, as amended by SFAS No. 148. The fair value was calculated on the stock options outstanding on the date of completion of the merger.

The following table reflects the weighted average fair value per option granted, as well as the significant weighted average assumptions used in determining those fair values using the Black-Scholes pricing model for the converted Nextel stock options, as well as the stock options issued under the 1997 Program. The following information related to PCS common stock has not been adjusted to reflect the recombination of our tracking stocks.

|                            | 2005             |         | Year Ended December 31, 2004 |            | 2003       |            |
|----------------------------|------------------|---------|------------------------------|------------|------------|------------|
|                            | Issued in Nextel |         | FON Common                   | PCS Common | FON Common | PCS Common |
|                            | Merger           | Other   | Stock                        | Stock      | Stock      | Stock      |
| Fair value on grant date   | \$ 12.60         | \$ 9.28 | \$ 6.43                      | \$ 6.56    | \$ 3.58    | \$ 3.16    |
| Risk-free interest rate    | 4.07%            | 3.70%   | 3.13%                        | 3.13%      | 2.93%      | 2.93%      |
| Expected volatility        | 44.8%            | 44.9%   | 45.1%                        | 83.30%     | 45.0%      | 87.20%     |
| Expected dividend yield    | 0.40%            | 2.06%   | 2.78%                        |            | 4.23%      |            |
| Expected life (years)      | 3.4              | 6       | 6                            | 6          | 6          | 6          |
| Options granted (millions) | 102.8            | 7.1     | 5.1                          | 5.1        | 10.5       | 10.5       |

*Restricted Stock Units*

We granted 3.5 million restricted stock units in 2005, which vest after three years, and 1.1 million of these restricted stock units are performance based. The weighted average fair value per unit was \$24.76.

*Employees Stock Purchase Plan*

Prior to the Sprint-Nextel merger, Nextel employees elected, under the Nextel Associate Stock Purchase Plan, to purchase approximately 244,000 shares of common stock. As a result of the Sprint-Nextel merger, we issued these shares to the former Nextel employees. Using the Black-Scholes pricing model, the weighted average fair value was \$3.42 per share.

During the 2004 ESPP offering that ended in June 2005, employees elected to purchase approximately 3.6 million common shares. Using the Black-Scholes pricing model, the weighted average fair value was \$3.19 per share.



## SPRINT NEXTEL CORPORATION

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

During the 2003 ESPP offering that ended in June 2004, employees elected to purchase approximately 1.8 million FON and 7.2 million PCS shares. Using the Black-Scholes pricing model, the weighted average fair value was \$4.11 per share for each FON election and \$2.52 per share for each PCS election. Because of the recombination of the tracking stocks, the elections to purchase PCS shares were converted into elections to purchase FON shares.

**Stock Options**

Activity under our stock option plans was as follows:

|                               | Shares<br>Under<br>Option<br><i>(in millions)</i> | Weighted<br>Average per<br>Share<br>Exercise<br>Price |
|-------------------------------|---------------------------------------------------|-------------------------------------------------------|
| Outstanding December 31, 2002 | 135.2                                             | \$ 28.04                                              |
| Granted                       | 15.8                                              | 10.73                                                 |
| Exercised                     | (1.2)                                             | 12.38                                                 |
| Forfeited/expired             | (9.2)                                             | 27.84                                                 |
| Outstanding December 31, 2003 | 140.6                                             | 26.25                                                 |
| Granted                       | 7.7                                               | 18.08                                                 |
| Exercised                     | (10.9)                                            | 14.43                                                 |
| Forfeited/expired             | (10.0)                                            | 31.39                                                 |
| Outstanding December 31, 2004 | 127.4                                             | 26.35                                                 |
| Nextel option exchange        | 102.8                                             | 21.08                                                 |
| Granted                       | 7.1                                               | 25.30                                                 |
| Exercised                     | (28.6)                                            | 15.32                                                 |
| Forfeited/expired             | (9.5)                                             | 34.74                                                 |
| Outstanding December 31, 2005 | 199.2                                             | 24.75                                                 |

The following is a summary of the status of employees' stock options outstanding and exercisable as of December 31, 2005:

| Range of Exercise Prices | Option Outstanding             |                                                                           |                                       | Option Exercisable             |                                       |
|--------------------------|--------------------------------|---------------------------------------------------------------------------|---------------------------------------|--------------------------------|---------------------------------------|
|                          | Shares<br><i>(in millions)</i> | Weighted<br>Average<br>Remaining<br>Contractual<br>Life<br><i>(years)</i> | Weighted<br>Average<br>Exercise Price | Shares<br><i>(in millions)</i> | Weighted<br>Average<br>Exercise Price |
| \$2.00 - \$9.99          | 20.2                           | 5.98                                                                      | \$ 6.79                               | 14.4                           | \$ 6.41                               |
| 10.00 - 19.99            | 58.3                           | 6.36                                                                      | 15.47                                 | 36.3                           | 15.20                                 |
| 20.00 - 29.99            | 74.0                           | 6.17                                                                      | 22.98                                 | 48.3                           | 23.02                                 |
| 30.00 - 39.99            | 15.4                           | 3.08                                                                      | 36.84                                 | 15.3                           | 36.84                                 |
| 40.00 - 49.99            | 24.9                           | 4.22                                                                      | 47.93                                 | 24.9                           | 47.93                                 |
| 50.00 - 79.99            | 5.3                            | 3.70                                                                      | 58.92                                 | 5.3                            | 58.92                                 |
| 80.00 - 139.99           | 1.1                            | 2.99                                                                      | 107.22                                | 1.1                            | 107.22                                |

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The number of shares exercisable and their weighted average exercise prices were 145.6 million shares at \$27.10 in 2005, 101.4 million shares at \$29.04 in 2004, and 103.3 million shares at \$29.36 in 2003.

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## SPRINT NEXTEL CORPORATION

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

**Note 18. Employee Benefit Plans*****Defined Benefit Pension Plan***

Most of our legacy Sprint employees are participants in a noncontributory defined benefit pension plan. Benefits for plan participants belonging to unions are based on negotiated schedules. For non-union participants, pension benefits are based on years of service and the participants compensation.

At the time of the merger with Nextel, we did not extend plan participation to former Nextel employees. Additionally, as of December 31, 2005, the pension plan was amended to freeze benefit accruals for plan participants not designated to work for Embarq. This amendment was treated as a curtailment under SFAS No. 88, *Employers' Accounting for Settlements and Curtailments of Defined Benefit Pension Plans and for Termination Benefits*. We recognized a \$4 million curtailment loss. This amendment also resulted in a \$233 million reduction in the projected benefit obligation, which is offset against existing unrecognized losses.

We use a December 31 measurement date for our pension plan.

The following table shows the changes in the projected benefit obligation:

|                                         | Year Ended December 31, |          |
|-----------------------------------------|-------------------------|----------|
|                                         | 2005                    | 2004     |
|                                         | <i>(in millions)</i>    |          |
| Benefit obligation at beginning of year | \$ 4,466                | \$ 4,038 |
| Service cost                            | 134                     | 133      |
| Interest cost                           | 264                     | 250      |
| Amendments                              | 8                       | 12       |
| Curtailment                             | (233)                   |          |
| Actuarial loss                          | 252                     | 223      |
| Benefits paid                           | (208)                   | (190)    |
| Benefit obligation at end of year       | \$ 4,683                | \$ 4,466 |

The plan's accumulated benefit obligation was \$4.6 billion as of December 31, 2005 and \$4.1 billion as of December 31, 2004.

The following table shows the changes in plan assets:

|                        | Year Ended December 31, |          |
|------------------------|-------------------------|----------|
|                        | 2005                    | 2004     |
|                        | <i>(in millions)</i>    |          |
| Beginning balance      | \$ 3,678                | \$ 3,176 |
| Employer contributions | 300                     | 300      |
| Investment return      | 363                     | 392      |
| Benefits paid          | (208)                   | (190)    |
| Ending balance         | \$ 4,133                | \$ 3,678 |





## SPRINT NEXTEL CORPORATION

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

The funded status and amounts recognized on the accompanying consolidated balance sheets for the plan were as follows:

|                                                       | As of December 31, |          |
|-------------------------------------------------------|--------------------|----------|
|                                                       | 2005               | 2004     |
|                                                       | (in millions)      |          |
| Projected benefit obligation in excess of plan assets | \$ (550)           | \$ (788) |
| Unrecognized net losses                               | 1,424              | 1,551    |
| Unrecognized prior service cost                       | 80                 | 92       |
| Unamortized transition asset                          | (1)                | (2)      |
| Net amount recognized                                 | \$ 953             | \$ 853   |

Amounts recognized on the accompanying consolidated balance sheets consist of:

|                                      | As of December 31, |          |
|--------------------------------------|--------------------|----------|
|                                      | 2005               | 2004     |
|                                      | (in millions)      |          |
| Pension benefit obligations          | \$ (435)           | \$ (451) |
| Intangible asset                     | 80                 | 92       |
| Accumulated other comprehensive loss | 1,308              | 1,212    |
| Net amount recognized                | \$ 953             | \$ 853   |

In accordance with SFAS No. 87, *Employers Accounting for Pensions*, as of December 31, 2005 and 2004 we recorded an additional minimum pension liability representing the excess of the unfunded accumulated benefit obligation over plan assets and accrued pension costs. Recognition of the additional pension liability also resulted in an intangible asset equal to the unrecognized prior service costs and a charge to equity through other comprehensive income (loss).

The following table sets forth these amounts:

|                                      | Year Ended December 31, |          |          |
|--------------------------------------|-------------------------|----------|----------|
|                                      | 2005                    | 2004     | 2003     |
|                                      | (in millions)           |          |          |
| Additional minimum liability         | \$ 1,388                | \$ 1,304 | \$ 1,289 |
| Intangible asset                     | 80                      | 92       | 95       |
| Accumulated other comprehensive loss | \$ 1,308                | \$ 1,212 | \$ 1,194 |

The tax effect for the charge to accumulated other comprehensive income (loss) was \$38 million for 2005, \$10 million for 2004, and \$12 million for 2003.

This resulted in a net charge to accumulated other comprehensive income (loss) of \$58 million for 2005, \$8 million for 2004, and \$25 million for 2003.

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We also maintain a nonqualified defined benefit plan to provide supplemental retirement benefits for certain executives in addition to the benefits provided under the qualified pension plan.

For 2005, an additional minimum pension liability of \$2 million was recognized for the nonqualified defined benefit plan with a charge to accumulated other comprehensive income (loss) of \$1 million, net of taxes.

For 2004, an additional minimum pension liability of \$20 million was recognized for the nonqualified defined benefit plan with a charge to accumulated other comprehensive income (loss) of \$13 million, net of taxes.

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## SPRINT NEXTEL CORPORATION

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

The net pension expense consisted of the following:

|                                                     | Year Ended December 31, |        |        |
|-----------------------------------------------------|-------------------------|--------|--------|
|                                                     | 2005                    | 2004   | 2003   |
|                                                     | <i>(in millions)</i>    |        |        |
| Service cost benefits earned during the year        | \$ 134                  | \$ 133 | \$ 119 |
| Interest on projected benefit obligation            | 264                     | 250    | 234    |
| Expected return on plan assets                      | (328)                   | (303)  | (290)  |
| Amortization of unrecognized transition asset       |                         | (2)    | (3)    |
| Recognition of prior service cost                   | 16                      | 16     | 15     |
| Recognition of actuarial losses                     | 110                     | 89     | 33     |
| Curtailment loss partial freeze of benefit accruals | 4                       |        |        |
| Net pension expense                                 | \$ 200                  | \$ 183 | \$ 108 |

Weighted-average assumptions used to determine net periodic pension costs:

|                                                  | Year Ended December 31, |       |       |
|--------------------------------------------------|-------------------------|-------|-------|
|                                                  | 2005                    | 2004  | 2003  |
| Discount rate                                    | 6.00%                   | 6.25% | 6.75% |
| Expected long-term rate of return on plan assets | 8.75%                   | 8.75% | 9.00% |
| Expected blended rate of future pay raises       | 4.25%                   | 4.25% | 4.25% |

Weighted average assumptions used to determine benefit obligations:

|                                            | As of December 31, |       |
|--------------------------------------------|--------------------|-------|
|                                            | 2005               | 2004  |
| Discount rate                              | 5.75%              | 6.00% |
| Expected blended rate of future pay raises | 4.25%              | 4.25% |

In choosing the discount rate, our actuaries construct a hypothetical portfolio of bonds rated AA- or better that produces a cash flow matching the projected benefit payments of the plan. The average yield of this portfolio is used as the discount rate benchmark. For the December 31, 2005 measurement date, this exercise produced a range of yields between 5.67% and 5.87%, and our discount rate was set at 5.75%. For the December 31, 2004 measurement date, the bond matching described above produced a range of yields between 5.86% and 6.04%, guiding us to set the discount rate at 6.0%.

During 2005, the assumption regarding the expected long-term return on plan assets was 8.75%, unchanged from the prior year. After revising the target asset allocation policy in the second half of 2003 to reduce the pension trust's exposure to equities, we obtained from two investment consulting firms forward-looking estimates of the expected long-term returns for a portfolio invested according to the revised target policy. The average of the two firms' estimates was 8.77%, guiding a reduction in the assumed long-term return from the prior year's 9.0% to 8.75%. We validate this assumption each year against estimates provided by our third party actuaries.

The plan's asset allocations by asset category, are as follows:

As of December 31,

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|                   | 2005 | 2004 |
|-------------------|------|------|
| Equity securities | 65%  | 66%  |
| Debt securities   | 14%  | 17%  |
| Real estate       | 11%  | 9%   |
| Alternatives      | 10%  | 8%   |
| Total             | 100% | 100% |

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**SPRINT NEXTEL CORPORATION**
**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

The pension trust is invested in a well-diversified portfolio of securities. The Employee Benefits Committee has established an investment policy that specifies asset allocation targets and ranges for the trust of: Equities 65% (+/-10%), Debt 15% (+/-5%), Real Estate 10% (+/-5%), and Alternatives 10% (+/-5%). The pension trust holds no Sprint Nextel securities.

The following benefit payments, which reflect expected future service, as appropriate, are expected to be paid (in millions):

|             |        |
|-------------|--------|
| 2006        | \$ 190 |
| 2007        | 194    |
| 2008        | 199    |
| 2009        | 206    |
| 2010        | 214    |
| 2011 - 2015 | 1,223  |

The plan is expected to be split into two plans in connection with the spin-off of Embarq. No contributions are expected to be made until after the spin-off. Preliminary estimates of these contributions are \$100 million for Sprint Nextel. Pension trust asset performance and changes in interest rates in the period leading to the anticipated plan spin-off could significantly affect these estimates.

***Defined Contribution Plans***

We sponsor defined contribution savings plans covering most employees. Participants may contribute portions of their pay to the plans. For union employees, we match contributions based on negotiated amounts. Through December 31, 2005, we matched contributions of non-union pre-merger Sprint employees in shares of company stock. The matching contribution was equal to 30% of participants' contributions up to 6% of their pay for 2005 and 25% of participants' contributions during 2004 and the second half of 2003. The matching contribution for the first half of 2003 was 75%. From the merger date through December 31, 2005, we matched contributions of pre-merger Nextel employees up to 4% of their pay. Our total matching contributions were \$56 million in 2005, \$29 million in 2004, and \$72 million in 2003. In 2006, the pre-merger Nextel plan will be terminated and participants covered by that plan will be eligible to enroll in the amended Sprint Nextel plan. The amended plan will no longer match contributions with company stock, but we will match participants' contributions up to 5% of their pay.

***Postretirement Benefits***

We provide postretirement medical benefits to certain employees. We also provide postretirement life insurance to employees who retired before certain dates. Employees who retired before certain dates were eligible for medical benefits at no cost, or at a reduced cost. Employees who retire after certain dates are eligible for medical benefits on a shared-cost basis. We fund the accrued costs as benefits are paid. We use a December 31 measurement date for our postretirement benefit plans.

Because prescription drug coverage is available through Medicare beginning in 2006, we amended the retiree medical plans in the third quarter 2005 to largely eliminate prescription drug coverage for Medicare-eligible retirees. This amendment precipitated a remeasurement of retiree medical expense, using a 5.25% discount rate as of the July 1, 2005 remeasurement date. The amendment decreased the accumulated postretirement benefit obligation, or APBO, by \$250 million, and decreased 2005 benefit expense by \$13 million.

At the time of the Nextel merger, we did not extend plan participation in the retiree medical plan to former Nextel employees and we amended the plan to only include employees designated to work for Embarq and legacy Sprint employees born prior to 1956. Because the attribution period used to accrue retiree medical benefits begins at age 50, this amendment had no immediate impact on the APBO or expense.

## SPRINT NEXTEL CORPORATION

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

In 2004, we amended certain retiree medical plans to standardize the plan design effective January 1, 2005, eliminating differences in benefit levels. These amendments decreased the accumulated postretirement benefit obligation, or APBO, related to other postretirement benefits by approximately \$35 million, and decreased the 2004 net benefit expense by \$5 million.

As a result of these amendments, we also recognized the then-anticipated effects of the 2003 Medicare Prescription Drug, Improvement and Modernization Act, or the Act. The Act contains a subsidy to employers who provide prescription drug coverage to retirees that is actuarially equivalent to Medicare Part D. In 2004, we planned to provide such coverage. Analysis of our retiree prescription drug claims data determined that our retiree prescription drug benefit was actuarially equivalent. In estimating the effects of the Act, estimates of participation rates and per capita claims costs were not changed. The effect of recognizing the federal subsidy related to the Act in 2004 was a \$67 million reduction in the APBO, and an \$11 million reduction in the 2004 net benefit cost. We have accounted for our retiree medical benefit plan in accordance with FASB Staff Position No. 106-2.

The following table shows the changes in the accumulated postretirement benefit obligation:

|                          | Year Ended December 31, |          |
|--------------------------|-------------------------|----------|
|                          | 2005                    | 2004     |
|                          | <i>(in millions)</i>    |          |
| Beginning balance        | \$ 967                  | \$ 1,116 |
| Service cost             | 13                      | 13       |
| Interest cost            | 48                      | 56       |
| Plan amendments          | (250)                   | (35)     |
| Actuarial losses (gains) | 3                       | (125)    |
| Benefits paid            | (62)                    | (58)     |
| Ending balance           | \$ 719                  | \$ 967   |

Amounts included on the accompanying consolidated balance sheets were as follows:

|                                               | As of December 31,   |        |
|-----------------------------------------------|----------------------|--------|
|                                               | 2005                 | 2004   |
|                                               | <i>(in millions)</i> |        |
| Accumulated postretirement benefit obligation | \$ 719               | \$ 967 |
| Plan assets                                   | (42)                 | (43)   |
| Unrecognized transition obligation            | 7                    | 8      |
| Unrecognized prior service benefit            | 397                  | 204    |
| Unrecognized net loss                         | (243)                | (264)  |
| Accrued postretirement benefits cost          | \$ 838               | \$ 872 |
| Discount rate                                 | 5.75%                | 6.0%   |

The net postretirement benefits cost consisted of the following:

|  | Year Ended December 31, |      |      |
|--|-------------------------|------|------|
|  | 2005                    | 2004 | 2003 |

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|                                                           | <i>(in millions)</i> |       |       |
|-----------------------------------------------------------|----------------------|-------|-------|
| Service cost benefits earned during the year              | \$ 13                | \$ 13 | \$ 14 |
| Interest on accumulated postretirement benefit obligation | 48                   | 56    | 62    |
| Expected return on assets                                 | (3)                  | (3)   | (3)   |
| Recognition of transition obligation                      | (1)                  | (1)   | (1)   |
| Recognition of prior service cost                         | (57)                 | (49)  | (45)  |
| Recognition of actuarial losses                           | 28                   | 28    | 27    |
| Net periodic postretirement benefits cost                 | \$ 28                | \$ 44 | \$ 54 |

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## SPRINT NEXTEL CORPORATION

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Weighted-average assumptions used to determine net periodic postretirement benefit costs:

|                                       | Year Ended December 31, |       |       |
|---------------------------------------|-------------------------|-------|-------|
|                                       | 2005                    | 2004  | 2003  |
| Discount rate                         | 6.00%                   | 6.25% | 6.75% |
| Assumed return on assets              | 8.75%                   | 8.75% | 9.00% |
| Assumed health care cost trend rates: |                         |       |       |

|                                                                                   | As of December 31, |       |
|-----------------------------------------------------------------------------------|--------------------|-------|
|                                                                                   | 2005               | 2004  |
| Health care cost increases assumed for next year                                  | 9.3%               | 10.0% |
| Rate to which the cost trend rate is assumed to decline (the ultimate trend rate) | 5.0%               | 5.0%  |
| Year that the rate reaches the ultimate trend rate                                | 2012               | 2012  |

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

|                                              | One-percentage-point |          |
|----------------------------------------------|----------------------|----------|
|                                              | Increase             | Decrease |
| Effect on total of service and interest cost | \$ 2                 | \$ (2)   |
| Effect on postretirement benefit obligation  | 37                   | (32)     |

Plan assets totaled \$42 million and \$43 million as of December 31, 2005 and 2004. We target a 60% allocation to equities and a 40% allocation to debt. The plans hold no Sprint Nextel securities.

We plan to contribute to the postretirement benefit plan an amount equal to the value of benefits and premiums paid.

The expected benefit payments, which reflect expected future service, as appropriate are as follows (in millions):

|             |       |
|-------------|-------|
| 2006        | \$ 66 |
| 2007        | 63    |
| 2008        | 63    |
| 2009        | 64    |
| 2010        | 65    |
| 2011 - 2015 | 323   |

**Note 19. Communication Towers Lease Transaction**

In May 2005, we closed a transaction with Global Signal, Inc. under which Global Signal acquired exclusive rights to lease or operate approximately 6,560 communications towers owned by us for a negotiated lease term, which is the greater of the remaining terms of the underlying ground leases, approximately 17 years at present, or up to 32 years, assuming successful renegotiation of the underlying ground leases at the end of their current lease terms.

We have subleased space on approximately 6,350 of the towers from Global Signal. This sublease arrangement is accounted for as an operating lease. See note 15 for additional information. We will maintain ownership of the towers, and we will continue to reflect the towers on our

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accompanying consolidated balance sheet.

At closing, we received proceeds of approximately \$1.2 billion, which we recorded in other liabilities on our accompanying consolidated balance sheet. The deferred rental income is being recognized as a reduction of lease expense related to our subleasing arrangement on a straight-line basis over the remaining terms of the underlying ground leases.

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## SPRINT NEXTEL CORPORATION

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

**Note 20. Segment Footnote**

We are divided into three main lines of business: Wireless, Long Distance and Local.

We generally manage our segments to the operating income (loss) level of reporting. Items below operating income (loss) are managed at a corporate level. The reconciliation from operating income to net income is shown on the face of the accompanying consolidated statements of operations.

We generally account for transactions between segments based on fully distributed costs, which we believe approximate fair value. In certain transactions, pricing is set using market rates.

Segment financial information was as follows:

|                                                    | Wireless  | Long<br>Distance | Local <sup>(1)</sup><br><i>(in millions)</i> | Corporate<br>and<br>Eliminations <sup>(2)</sup> | Consolidated |
|----------------------------------------------------|-----------|------------------|----------------------------------------------|-------------------------------------------------|--------------|
| <b>2005</b>                                        |           |                  |                                              |                                                 |              |
| Net operating revenues                             | \$ 22,328 | \$ 6,834         | \$ 6,527                                     | \$ (1,009)                                      | \$ 34,680    |
| Inter-company revenues                             | 29        | 710              | 270                                          | (1,009)                                         |              |
| Restructuring and asset impairments <sup>(3)</sup> | 20        | 15               | 82                                           | 8                                               | 125          |
| Depreciation                                       | 3,358     | 488              | 1,090                                        | (3)                                             | 4,933        |
| Amortization                                       | 1,335     | 1                |                                              |                                                 | 1,336        |
| Operating expenses                                 | 20,155    | 6,322            | 4,769                                        | (392) <sup>(4)</sup>                            | 30,854       |
| Operating income                                   | 2,173     | 512              | 1,758                                        | (617)                                           | 3,826        |
| Operating margin                                   | 9.7%      | 7.5%             | 26.9%                                        | NM                                              | 11.0%        |
| Capital expenditures                               | 3,545     | 384              | 857                                          | 271                                             | 5,057        |
| Total assets                                       | 67,090    | 3,437            | 8,848                                        | 23,205                                          | 102,580      |
| <b>2004</b>                                        |           |                  |                                              |                                                 |              |
| Net operating revenues                             | \$ 14,647 | \$ 7,327         | \$ 6,421                                     | \$ (967)                                        | \$ 27,428    |
| Inter-company revenues                             | 27        | 678              | 262                                          | (967)                                           |              |
| Restructuring and asset impairments <sup>(3)</sup> | 30        | 3,661            | 40                                           |                                                 | 3,731        |
| Depreciation                                       | 2,557     | 1,070            | 1,089                                        | (3)                                             | 4,713        |
| Amortization                                       | 6         | 1                |                                              |                                                 | 7            |
| Operating expenses                                 | 13,095    | 10,916           | 4,685                                        | (965)                                           | 27,731       |
| Operating income (loss)                            | 1,552     | (3,589)          | 1,736                                        | (2)                                             | (303)        |
| Operating margin                                   | 10.6%     | NM               | 27.0%                                        | NM                                              | NM           |
| Capital expenditures                               | 2,559     | 282              | 1,018                                        | 121                                             | 3,980        |
| Total assets                                       | 21,417    | 3,695            | 8,999                                        | 7,210                                           | 41,321       |
| <b>2003</b>                                        |           |                  |                                              |                                                 |              |
| Net operating revenues                             | \$ 12,690 | \$ 8,005         | \$ 6,486                                     | \$ (984)                                        | \$ 26,197    |
| Inter-company revenues                             | 25        | 693              | 266                                          | (984)                                           |              |
| Restructuring and asset impairments <sup>(3)</sup> | 362       | 1,564            | 25                                           |                                                 | 1,951        |
| Depreciation                                       | 2,454     | 1,431            | 1,089                                        | (2)                                             | 4,972        |
| Amortization                                       |           | 1                |                                              |                                                 | 1            |
| Operating expenses                                 | 12,056    | 9,447            | 4,666                                        | (979)                                           | 25,190       |
| Operating income (loss)                            | 634       | (1,442)          | 1,820                                        | (5)                                             | 1,007        |

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|                      |        |           |       |           |        |
|----------------------|--------|-----------|-------|-----------|--------|
| Operating margin     | 5.0%   | <i>NM</i> | 28.1% | <i>NM</i> | 3.8%   |
| Capital expenditures | 2,123  | 339       | 1,201 | 134       | 3,797  |
| Total assets         | 21,671 | 8,232     | 9,075 | 3,696     | 42,674 |

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## SPRINT NEXTEL CORPORATION

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

NM = Not meaningful

(1) Includes North Supply, which in prior years had been included in the Other segment for segment reporting purposes. However, due to the planned spin off of Embarq, which is expected to include North Supply, the North Supply operations have been reclassified to the Local segment for all periods presented.

(2) Revenues eliminated in consolidation consist primarily of local access charged to Long Distance by Local, Long Distance services provided to Wireless for resale to Wireless customers and for internal business use, caller ID services provided by Local to Wireless, handset purchases from Wireless and access to the Wireless network.

Corporate assets are not allocated to the operating segments, and consist primarily of cash and cash equivalents, the operational headquarters campus and other assets managed at a corporate level. Corporate capital expenditures were incurred mainly for various administrative assets and improvements at our operational headquarters campus. Operating expenses related to corporate assets are allocated to each segment.

(3) See note 8 for additional information.

(4) Operating expenses include \$608 million of merger and integration costs primarily associated with the Nextel merger and PCS Affiliate acquisitions and the anticipated spin-off of Embarq and have been reflected as unallocated corporate selling, general and administrative expense.

In 2005, 2004 and 2003, more than 95% of our revenues was from services and equipment provided within the United States.

More than 99% of our property, plant, and equipment are in the United States.

Net operating revenues by services and products were as follows:

|                                     | Wireless             | Long<br>Distance | Local <sup>(1)</sup> | Corporate<br>and<br>Eliminations <sup>(2)</sup> | Consolidated     |
|-------------------------------------|----------------------|------------------|----------------------|-------------------------------------------------|------------------|
|                                     | <i>(in millions)</i> |                  |                      |                                                 |                  |
| <b>2005</b>                         |                      |                  |                      |                                                 |                  |
| Wireless services                   | \$ 19,289            | \$               | \$                   | \$ (29)                                         | \$ 19,260        |
| Wireless equipment                  | 2,147                |                  |                      |                                                 | 2,147            |
| Voice                               |                      | 4,213            | 4,335                | (829)                                           | 7,719            |
| Data                                |                      | 1,632            | 983                  | (63)                                            | 2,552            |
| Internet                            |                      | 736              |                      | (9)                                             | 727              |
| Other                               | 892                  | 253              | 1,209                | (79)                                            | 2,275            |
| <b>Total net operating revenues</b> | <b>\$ 22,328</b>     | <b>\$ 6,834</b>  | <b>\$ 6,527</b>      | <b>\$ (1,009)</b>                               | <b>\$ 34,680</b> |

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| <b>2004</b>                         |                  |                 |                 |           |              |                  |
|-------------------------------------|------------------|-----------------|-----------------|-----------|--------------|------------------|
| Wireless services                   | \$ 12,529        | \$              | \$              | \$        | (27)         | \$ 12,502        |
| Wireless equipment                  | 1,510            |                 |                 |           |              | 1,510            |
| Voice                               |                  | 4,560           | 4,498           |           | (768)        | 8,290            |
| Data                                |                  | 1,722           | 833             |           | (71)         | 2,484            |
| Internet                            |                  | 793             |                 |           | (12)         | 781              |
| Other                               | 608              | 252             | 1,090           |           | (89)         | 1,861            |
| <b>Total net operating revenues</b> | <b>\$ 14,647</b> | <b>\$ 7,327</b> | <b>\$ 6,421</b> | <b>\$</b> | <b>(967)</b> | <b>\$ 27,428</b> |

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## SPRINT NEXTEL CORPORATION

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

|                                     | Wireless         | Long<br>Distance | Local <sup>(1)</sup><br>(in millions) | Corporate<br>and<br>Eliminations <sup>(2)</sup> | Consolidated     |
|-------------------------------------|------------------|------------------|---------------------------------------|-------------------------------------------------|------------------|
| <b>2003</b>                         |                  |                  |                                       |                                                 |                  |
| Wireless services                   | \$ 11,217        | \$               | \$                                    | \$ (17)                                         | \$ 11,200        |
| Wireless equipment                  | 1,143            |                  |                                       | (8)                                             | 1,135            |
| Voice                               |                  | 4,999            | 4,654                                 | (757)                                           | 8,896            |
| Data                                |                  | 1,853            | 730                                   | (81)                                            | 2,502            |
| Internet                            |                  | 973              |                                       | (29)                                            | 944              |
| Other                               | 330              | 180              | 1,102                                 | (92)                                            | 1,520            |
| <b>Total net operating revenues</b> | <b>\$ 12,690</b> | <b>\$ 8,005</b>  | <b>\$ 6,486</b>                       | <b>\$ (984)</b>                                 | <b>\$ 26,197</b> |

<sup>(1)</sup> Includes North Supply, which in prior years had been included in the Other segment for segment reporting purposes. However, due to the planned spin-off of Embarq, which is expected to include North Supply, the North Supply operations have been reclassified to the Local segment for all periods presented.

<sup>(2)</sup> Revenues eliminated in consolidation consist primarily of local access charged to Long Distance by Local, Long Distance services provided to Wireless for resale to Wireless customers and for internal business use, caller ID services provided by Local to Wireless, handset purchases from Wireless and access to the Wireless network.

**Note 21. Recently Issued Accounting Pronouncements***SFAS No. 123R*

In December 2004, the FASB issued SFAS No. 123R, *Share-Based Payment*. This statement requires an entity to recognize the cost of employee services received in share-based payment transactions, through the use of fair-value-based methods of recognizing cost. This statement is effective for us as of January 1, 2006.

We voluntarily adopted fair value accounting for share-based payments effective January 1, 2003, under SFAS No. 123 as amended by SFAS No. 148, using the prospective method. Upon adoption, we began expensing the fair value of stock-based compensation for all grants, modifications or settlements made on or after January 1, 2003. In connection with the tracking stock recombination, as required by SFAS No. 123, we accounted for the conversion of PCS stock options to FON stock options as a modification and accordingly applied stock option expensing to FON stock options resulting from the conversion of PCS stock options granted before January 1, 2003. Further, in connection with the Nextel merger, we accounted for the conversion of Nextel stock options to Sprint Nextel stock options as a modification and accordingly applied stock option expensing to the unvested stock options beginning on the merger date.

The revised standard will require us to begin to recognize compensation cost for unvested common stock options granted to our employees before January 1, 2003, which are outstanding as of January 1, 2006. This requirement to recognize expense on these unvested grants is expected to be immaterial to us.

*SFAS No. 151*

In November 2004, the FASB issued SFAS No. 151, *Inventory Costs - an amendment of ARB No. 43, Chapter 4*. This statement requires that items such as idle facility expense, excessive spoilage, double freight, and rehandling costs be recognized as current-period charges regardless of whether they meet the definition of abnormal provided in ARB No. 43, Chapter 4, *Inventory Pricing*. The statement is effective for inventory

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costs incurred during fiscal years beginning after June 15, 2005. We do not expect the adoption of this standard to have a material impact on our financial statements.

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## SPRINT NEXTEL CORPORATION

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

## Note 22. Quarterly Financial Data (Unaudited)

|                                                              | Quarter                                     |                 |                 |                 |
|--------------------------------------------------------------|---------------------------------------------|-----------------|-----------------|-----------------|
|                                                              | 1 <sup>st</sup>                             | 2 <sup>nd</sup> | 3 <sup>rd</sup> | 4 <sup>th</sup> |
|                                                              | <i>(in millions, except per share data)</i> |                 |                 |                 |
| <b>2005</b>                                                  |                                             |                 |                 |                 |
| Net operating revenues                                       | \$ 6,936                                    | \$ 7,113        | \$ 9,335        | \$ 11,296       |
| Operating income                                             | 1,036                                       | 1,196           | 923             | 671             |
| Income from continuing operations                            | 472                                         | 600             | 516             | 213             |
| Net income                                                   | 472                                         | 600             | 516             | 197             |
| Basic earnings per common share from continuing operations   | 0.32                                        | 0.40            | 0.23            | 0.07            |
| Diluted earnings per common share from continuing operations | 0.31                                        | 0.40            | 0.23            | 0.07            |

|                                                                                       | Quarter                                     |                 |                 |                 |
|---------------------------------------------------------------------------------------|---------------------------------------------|-----------------|-----------------|-----------------|
|                                                                                       | 1 <sup>st</sup>                             | 2 <sup>nd</sup> | 3 <sup>rd</sup> | 4 <sup>th</sup> |
|                                                                                       | <i>(in millions, except per share data)</i> |                 |                 |                 |
| <b>2004</b>                                                                           |                                             |                 |                 |                 |
| Net operating revenues                                                                | \$ 6,707                                    | \$ 6,869        | \$ 6,922        | \$ 6,930        |
| Operating income (loss)                                                               | 724                                         | 718             | (2,715)         | 970             |
| Income (loss) from continuing operations                                              | 225                                         | 236             | (1,910)         | 437             |
| Net income (loss)                                                                     | 225                                         | 236             | (1,910)         | 437             |
| Basic earnings (loss) per common share from continuing operations <sup>(1)</sup>      | 0.16                                        | 0.16            | (1.32)          | 0.30            |
| Diluted earnings (loss) per common share from continuing operations <sup>(1)(2)</sup> | 0.16                                        | 0.16            | (1.32)          | 0.29            |

<sup>(1)</sup> On April 23, 2004, we recombined our two tracking stocks. Each share of PCS common stock automatically converted into 0.5 shares of FON common stock. All per share amounts had been restated to reflect the recombination of the FON common stock and the PCS common stock as of the earliest period presented at an identical conversion ratio (0.5). The conversion ratio was also applied to dilutive PCS securities (mainly stock options, employee stock purchase plan shares, convertible preferred stock and restricted stock units) to determine diluted weighted average shares on a consolidated basis.

<sup>(2)</sup> As the effects of including the incremental shares associated with options, restricted stock units and ESPP shares are antidilutive, both basic earnings per common share and diluted earnings per common share reflect the same calculation for the third quarter 2004.

## Note 23. Restatements of Previously Issued Financial Statements

In November 2004, we restated previously issued financial statements to correct an error related to the calculation of interest capitalized during construction. The financial statements were also restated to apply an adjustment previously recorded and disclosed in the 2003 fourth quarter related to the liability for medical coverage for participants in our long-term disability plan to the appropriate pre-2003 periods.

## Note 24. Subsequent Event

In February 2006, our board of directors declared dividends of 2.5 cents on our common stock to shareholders of record at the close of business on March 10, 2006. The dividends are payable March 31, 2006.



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**SPRINT NEXTEL CORPORATION**

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

**Note 25. Pending Transaction**

*Spin-off of Local Telecommunications Business*

We have decided to spin-off our local communications business to our shareholders as Embarq Corporation. On the date of the spin-off, the assets, liabilities and historical financial results which we have reported as our local segment in our financial statements will be removed from our financial statements and reported in Embarq's separate company financial statements. We are currently in the process of identifying the assets and liabilities that will be transferred to the new company, for which we expect to receive approximately \$6.6 billion in the form of cash and senior notes. We will present Embarq's results of operations for the periods in which it was a wholly owned subsidiary as a discontinued operation when the spin-off occurs. We anticipate that the spin-off will be completed in the second quarter 2006.

**Note 26. Guarantor Financial Information**

Presented below is consolidating financial information of:

Sprint Nextel Corporation on a stand alone basis, as of and for the year ended December 31, 2005;

IWO Holdings, Inc., a wholly owned subsidiary of Sprint Nextel, together with its subsidiary guarantors (collectively, IWO Holdings), as of and for the period from acquisition (October 20, 2005) to December 31, 2005; and

Sprint Nextel's other subsidiaries on a combined basis, and Sprint Nextel and all of its subsidiaries on a consolidated basis, as of and for the year ended December 31, 2005.

Sprint Nextel is the guarantor of certain indebtedness of IWO Holdings. Specifically, Sprint Nextel entered into a guarantee, dated March 22, 2006, in favor of the holders of Senior Secured Floating Rate Notes due 2012 of IWO Holdings, and a guarantee, dated March 22, 2006, in favor of the holders of 10.75% Senior Discount Notes due 2015 of IWO Holdings. Each guarantee represents the full and unconditional guarantee by Sprint Nextel of the obligations under the applicable notes, and other obligations under the respective indentures under which the notes were issued. No subsidiary of Sprint Nextel, other than the subsidiary guarantors of IWO Holdings, Inc., guarantees these securities.

IWO Holdings, Inc. has no independent assets, other than its investment in its subsidiary guarantors, or operations and the guarantees of its subsidiary guarantors are full and unconditional and joint and several.

## SPRINT NEXTEL CORPORATION

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

## CONSOLIDATING STATEMENT OF OPERATIONS

|                                                                          | For the<br>Year<br>Ended<br>December 31,<br>2005 | For the<br>Period<br>from<br>Acquisition to<br>December 31,<br>2005 | For the Year<br>Ended<br>December 31,<br>2005             |              | For the<br>Year<br>Ended<br>December 31,<br>2005 |
|--------------------------------------------------------------------------|--------------------------------------------------|---------------------------------------------------------------------|-----------------------------------------------------------|--------------|--------------------------------------------------|
|                                                                          | Sprint<br>Nextel<br>Corporation                  | IWO Holdings                                                        | Sprint Nextel s<br>Other<br>Subsidiaries<br>(in millions) | Eliminations | Consolidated                                     |
| <b>Net operating revenues</b>                                            | \$ 1                                             | \$ 40                                                               | \$ 34,661                                                 | \$ (22)      | \$ 34,680                                        |
| <b>Operating expenses</b>                                                |                                                  |                                                                     |                                                           |              |                                                  |
| Cost of services and products (exclusive of depreciation included below) | 1                                                | 25                                                                  | 14,378                                                    | (20)         | 14,384                                           |
| Selling, general and administrative                                      |                                                  | 2                                                                   | 10,076                                                    | (2)          | 10,076                                           |
| Restructuring and asset impairments                                      |                                                  |                                                                     | 125                                                       |              | 125                                              |
| Depreciation and amortization                                            | 32                                               | 13                                                                  | 6,224                                                     |              | 6,269                                            |
|                                                                          | 33                                               | 40                                                                  | 30,803                                                    | (22)         | 30,854                                           |
| <b>Operating income (loss)</b>                                           | (32)                                             |                                                                     | 3,858                                                     |              | 3,826                                            |
| <b>Other income (expense)</b>                                            |                                                  |                                                                     |                                                           |              |                                                  |
| Equity in earnings of unconsolidated subsidiaries, net                   |                                                  |                                                                     | 110                                                       |              | 110                                              |
| Equity in earnings of consolidated subsidiaries, net                     | 1,560                                            |                                                                     |                                                           | (1,560)      |                                                  |
| Interest and other, net                                                  | 321                                              | (3)                                                                 | (1,348)                                                   |              | (1,030)                                          |
|                                                                          | 1,881                                            | (3)                                                                 | (1,238)                                                   | (1,560)      | (920)                                            |
| <b>Income (loss) from continuing operations before income taxes</b>      | 1,849                                            | (3)                                                                 | 2,620                                                     | (1,560)      | 2,906                                            |
| <b>Income tax benefit (expense)</b>                                      | (64)                                             | 1                                                                   | (1,042)                                                   |              | (1,105)                                          |
| <b>Income (loss) from continuing operations</b>                          | 1,785                                            | (2)                                                                 | 1,578                                                     | (1,560)      | 1,801                                            |
| Cumulative effect of change in accounting principle, net                 |                                                  |                                                                     | (16)                                                      |              | (16)                                             |
| <b>Net income (loss)</b>                                                 | \$ 1,785                                         | \$ (2)                                                              | \$ 1,562                                                  | \$ (1,560)   | \$ 1,785                                         |

## SPRINT NEXTEL CORPORATION

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

## CONSOLIDATING BALANCE SHEET

As of December 31, 2005

|                                           | Sprint Nextel s           |              |                                     |              | Consolidated |
|-------------------------------------------|---------------------------|--------------|-------------------------------------|--------------|--------------|
|                                           | Sprint Nextel Corporation | IWO Holdings | Other Subsidiaries<br>(in millions) | Eliminations |              |
| <b>ASSETS</b>                             |                           |              |                                     |              |              |
| <b>Current assets</b>                     |                           |              |                                     |              |              |
| Cash and cash equivalents                 | \$ 4,770                  | \$ 63        | \$ 4,069                            | \$           | \$ 8,902     |
| Marketable securities                     | 570                       |              | 1,193                               |              | 1,763        |
| Accounts receivable, net                  |                           | 32           | 4,795                               |              | 4,827        |
| Intercompany receivable                   |                           |              | 148                                 | (148)        |              |
| Inventories                               |                           | 3            | 947                                 |              | 950          |
| Deferred tax asset                        |                           |              | 1,811                               |              | 1,811        |
| Prepaid expenses and other current assets | 78                        | 3            | 758                                 |              | 839          |
| Total current assets                      | 5,418                     | 101          | 13,721                              | (148)        | 19,092       |
| <b>Investments</b>                        |                           |              | 2,369                               |              | 2,369        |
| <b>Investment in subsidiaries</b>         | 46,378                    |              |                                     | (46,378)     |              |
| <b>Property, plant and equipment, net</b> | 35                        | 110          | 30,988                              |              | 31,133       |
| <b>Intangible assets</b>                  |                           |              |                                     |              |              |
| Goodwill                                  |                           | 249          | 21,066                              |              | 21,315       |
| Other intangible assets, net              | 48                        | 86           | 27,885                              |              | 28,019       |
| <b>Intercompany notes receivable</b>      | 13,029                    |              | 12,574                              | (25,603)     |              |
| <b>Other assets</b>                       | 1,163                     | 4            | 513                                 | (1,028)      | 652          |
|                                           | \$ 66,071                 | \$ 550       | \$ 109,116                          | \$ (73,157)  | \$ 102,580   |

## LIABILITIES AND SHAREHOLDERS EQUITY

|                                                                 |        |     |          |          |          |
|-----------------------------------------------------------------|--------|-----|----------|----------|----------|
| <b>Current liabilities</b>                                      |        |     |          |          |          |
| Accounts payable                                                | \$ 2   | \$  | \$ 3,825 | \$       | \$ 3,827 |
| Accrued expenses and other                                      | 369    | 19  | 4,788    |          | 5,176    |
| Intercompany payable                                            | 98     | 50  |          | (148)    |          |
| Current portion of long-term debt and capital lease obligations |        |     | 5,047    |          | 5,047    |
| Total current liabilities                                       | 469    | 69  | 13,660   | (148)    | 14,050   |
| <b>Long-term debt and capital lease obligations</b>             | 200    | 259 | 20,173   |          | 20,632   |
| <b>Intercompany notes payable</b>                               | 12,574 |     | 13,029   | (25,603) |          |
| <b>Deferred income taxes</b>                                    | 321    | 9   | 11,357   |          | 11,687   |
| <b>Postretirement and other benefit obligations</b>             | 323    |     | 1,062    |          | 1,385    |
| <b>Other liabilities</b>                                        |        | 1   | 3,669    | (1,028)  | 2,642    |
| Total liabilities                                               | 13,887 | 338 | 62,950   | (26,779) | 50,396   |

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|                                                  |               |            |               |                 |               |
|--------------------------------------------------|---------------|------------|---------------|-----------------|---------------|
| <b>Seventh series redeemable preferred stock</b> | 247           |            |               |                 | 247           |
| <b>Shareholders' equity</b>                      |               |            |               |                 |               |
| Common stock                                     | 5,846         |            | 2,829         | (2,829)         | 5,846         |
| Paid-in capital                                  | 46,136        | 214        | 41,775        | (41,989)        | 46,136        |
| Retained (deficit) earnings                      | 681           | (2)        | 1,562         | (1,560)         | 681           |
| Accumulated other comprehensive loss             | (726)         |            |               |                 | (726)         |
| <b>Total shareholders' equity</b>                | <b>51,937</b> | <b>212</b> | <b>46,166</b> | <b>(46,378)</b> | <b>51,937</b> |
|                                                  | \$ 66,071     | \$ 550     | \$ 109,116    | \$ (73,157)     | \$ 102,580    |

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## SPRINT NEXTEL CORPORATION

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

## CONSOLIDATING STATEMENT OF CASH FLOWS

|                                                                                          | For the<br>Year Ended<br>December 31,<br>2005 | For the<br>Period<br>from<br>Acquisition to<br>December 31,<br>2005<br>IWO<br>Holdings | For the<br>Year Ended<br>December 31,<br>2005<br>Sprint Nextel<br>Other<br>Subsidiaries<br>(in millions) | Eliminations | For the<br>Year Ended<br>December 31,<br>2005<br>Consolidated |
|------------------------------------------------------------------------------------------|-----------------------------------------------|----------------------------------------------------------------------------------------|----------------------------------------------------------------------------------------------------------|--------------|---------------------------------------------------------------|
| <b>Cash flows from operating activities</b>                                              |                                               |                                                                                        |                                                                                                          |              |                                                               |
| Net income (loss)                                                                        | \$ 1,785                                      | \$ (2)                                                                                 | \$ 1,562                                                                                                 | \$ (1,560)   | \$ 1,785                                                      |
| Adjustments to reconcile net income (loss) to net cash provided by operating activities: |                                               |                                                                                        |                                                                                                          |              |                                                               |
| Cumulative effect of change in accounting principle, net                                 |                                               |                                                                                        | 16                                                                                                       |              | 16                                                            |
| Provision for losses on accounts receivable                                              |                                               |                                                                                        | 441                                                                                                      |              | 441                                                           |
| Depreciation and amortization                                                            | 32                                            | 13                                                                                     | 6,224                                                                                                    |              | 6,269                                                         |
| Equity in earnings of unconsolidated subsidiaries, net                                   |                                               |                                                                                        | (110)                                                                                                    |              | (110)                                                         |
| Equity in earnings of consolidated subsidiaries, net                                     | (1,560)                                       |                                                                                        |                                                                                                          | 1,560        |                                                               |
| Deferred income taxes                                                                    | 44                                            | (3)                                                                                    | 789                                                                                                      |              | 830                                                           |
| Gain on sale of assets, net                                                              |                                               |                                                                                        | (43)                                                                                                     |              | (43)                                                          |
| Losses on impairment of assets                                                           |                                               |                                                                                        | 127                                                                                                      |              | 127                                                           |
| Other, net                                                                               | 302                                           | 1                                                                                      | 133                                                                                                      |              | 436                                                           |
| Changes in assets and liabilities, net of effects of acquisitions:                       |                                               |                                                                                        |                                                                                                          |              |                                                               |
| Receivables, including intercompany                                                      | 1,980                                         | (30)                                                                                   | (2,392)                                                                                                  |              | (442)                                                         |
| Inventories and other current assets                                                     |                                               | (1)                                                                                    | 12                                                                                                       |              | 11                                                            |
| Accounts payable and other current liabilities                                           | (24)                                          | 64                                                                                     | 259                                                                                                      |              | 299                                                           |
| Proceeds from communications towers lease transaction                                    |                                               |                                                                                        | 1,195                                                                                                    |              | 1,195                                                         |
| Noncurrent assets and liabilities, net                                                   | 37                                            |                                                                                        | (173)                                                                                                    |              | (136)                                                         |
| Net cash provided by operating activities                                                | 2,596                                         | 42                                                                                     | 8,040                                                                                                    |              | 10,678                                                        |
| <b>Cash flows from investing activities</b>                                              |                                               |                                                                                        |                                                                                                          |              |                                                               |
| Capital expenditures                                                                     |                                               | (1)                                                                                    | (5,056)                                                                                                  |              | (5,057)                                                       |
| Cash acquired in Nextel merger, net of cash paid                                         | (969)                                         |                                                                                        | 2,152                                                                                                    |              | 1,183                                                         |
| Purchase of PCS Affiliates, net of cash acquired                                         | (1,371)                                       |                                                                                        |                                                                                                          |              | (1,371)                                                       |
| Purchases of marketable securities                                                       | (468)                                         |                                                                                        | (353)                                                                                                    |              | (821)                                                         |
| Proceeds from maturities and sales of marketable securities                              | 434                                           |                                                                                        | 374                                                                                                      |              | 808                                                           |
| Proceeds from sales of assets and investments                                            | 272                                           |                                                                                        | 376                                                                                                      |              | 648                                                           |
| Investments in consolidated subsidiaries                                                 | 304                                           |                                                                                        |                                                                                                          | (304)        |                                                               |

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|                                                                     |                 |              |                 |              |                 |
|---------------------------------------------------------------------|-----------------|--------------|-----------------|--------------|-----------------|
| Distributions from (investment in) unconsolidated subsidiaries, net | 176             |              | (9)             |              | 167             |
| Other, net                                                          |                 |              | (281)           |              | (281)           |
| <b>Net cash used in investing activities</b>                        | <b>(1,622)</b>  | <b>(1)</b>   | <b>(2,797)</b>  | <b>(304)</b> | <b>(4,724)</b>  |
| <b>Cash flows from financing activities</b>                         |                 |              |                 |              |                 |
| Borrowings under bank credit facility                               |                 |              | 3,200           |              | 3,200           |
| Repayments under bank credit facility                               |                 |              | (3,200)         |              | (3,200)         |
| Purchase and retirements of debt securities                         | (50)            |              | (1,120)         |              | (1,170)         |
| Proceeds from issuance of common stock                              | 432             |              |                 |              | 432             |
| Equity distribution to parent                                       |                 |              | (304)           | 304          |                 |
| Dividends paid                                                      | (525)           |              |                 |              | (525)           |
| Other, net                                                          |                 |              | 35              |              | 35              |
| <b>Net cash used in financing activities</b>                        | <b>(143)</b>    |              | <b>(1,389)</b>  | <b>304</b>   | <b>(1,228)</b>  |
| <b>Net increase in cash and cash equivalents</b>                    | <b>831</b>      | <b>41</b>    | <b>3,854</b>    |              | <b>4,726</b>    |
| <b>Cash and cash equivalents, beginning of period</b>               | <b>3,939</b>    | <b>22</b>    | <b>215</b>      |              | <b>4,176</b>    |
| <b>Cash and cash equivalents, end of period</b>                     | <b>\$ 4,770</b> | <b>\$ 63</b> | <b>\$ 4,069</b> |              | <b>\$ 8,902</b> |

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## SPRINT NEXTEL CORPORATION

## SCHEDULE II

## CONSOLIDATED VALUATION AND QUALIFYING ACCOUNTS

Years Ended December 31, 2005, 2004, and 2003

|                                                  | Balance<br>Beginning<br>of Year | Additions (Deductions)         |                                                         |                         | Balance<br>End<br>of Year |
|--------------------------------------------------|---------------------------------|--------------------------------|---------------------------------------------------------|-------------------------|---------------------------|
|                                                  |                                 | Charged<br>to Income<br>(Loss) | Charged<br>to Other<br>Accounts<br><i>(in millions)</i> | Other<br>Deductions     |                           |
| <b>2005</b>                                      |                                 |                                |                                                         |                         |                           |
| Allowance for doubtful accounts                  | \$ 293                          | \$ 441                         | \$ 160 <sup>(1)</sup>                                   | \$ (578) <sup>(2)</sup> | \$ 316                    |
| Valuation allowance - deferred income tax assets | \$ 670                          | \$ 15                          | \$ 386 <sup>(3)</sup>                                   | \$                      | \$ 1,071                  |
| <b>2004</b>                                      |                                 |                                |                                                         |                         |                           |
| Allowance for doubtful accounts                  | \$ 276                          | \$ 386                         | \$ 124 <sup>(1)</sup>                                   | \$ (493) <sup>(2)</sup> | \$ 293                    |
| Valuation allowance - deferred income tax assets | \$ 620                          | \$ 50                          | \$                                                      | \$                      | \$ 670                    |
| <b>2003</b>                                      |                                 |                                |                                                         |                         |                           |
| Allowance for doubtful accounts                  | \$ 414                          | \$ 422                         | \$ 137 <sup>(1)</sup>                                   | \$ (697) <sup>(2)</sup> | \$ 276                    |
| Valuation allowance - deferred income tax assets | \$ 573                          | \$ 47                          | \$                                                      | \$                      | \$ 620                    |

<sup>(1)</sup> Amounts charged to other accounts consist of receivable reserves for billing and collection services we provide for certain PCS Affiliates. Uncollectible accounts are recovered from affiliates. In 2005, the amount includes the allowance recorded in the merger of Nextel and the PCS Affiliate acquisitions.

<sup>(2)</sup> Accounts written off, net of recoveries.

<sup>(3)</sup> Amount represents increases in valuation allowance for deferred income tax assets related primarily to the purchase price allocations for the Nextel merger and PCS Affiliate acquisitions.