

WASTE MANAGEMENT INC  
Form 10-Q  
October 31, 2012

**UNITED STATES SECURITIES AND EXCHANGE COMMISSION**

**Washington, D.C. 20549**

**Form 10-Q**

(Mark One)

☒ **QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d)  
OF THE SECURITIES EXCHANGE ACT OF 1934**  
For the Quarterly Period Ended September 30, 2012

☐ **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 1-12154

**Waste Management, Inc.**

*(Exact name of registrant as specified in its charter)*

**Delaware**  
*(State or other jurisdiction of  
incorporation or organization)*

**73-1309529**  
*(I.R.S. Employer  
Identification No.)*

**1001 Fannin**

**Suite 4000**

**Houston, Texas 77002**

*(Address of principal executive offices)*

**(713) 512-6200**

*(Registrant's telephone number, including area code)*

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 ☐

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

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

Large accelerated filer ☐ Accelerated filer ☐ Non-accelerated filer ☐ Smaller reporting company ☐

(Do not check if a smaller reporting company)

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

The number of shares of Common Stock, \$0.01 par value, of the registrant outstanding at October 23, 2012 was 463,899,149 (excluding treasury shares of 166,383,312).

**PART I.****Item 1. Financial Statements.**

**WASTE MANAGEMENT, INC.**  
**CONDENSED CONSOLIDATED BALANCE SHEETS**  
(In Millions, Except Share and Par Value Amounts)

	September 30, 2012 (Unaudited)	December 31, 2011
<b>ASSETS</b>		
Current assets:		
Cash and cash equivalents	\$ 398	\$ 258
Accounts receivable, net of allowance for doubtful accounts of \$37 and \$29, respectively	1,760	1,631
Other receivables	108	144
Parts and supplies	155	153
Deferred income taxes	79	78
Other assets	159	115
Total current assets	2,659	2,379
Property and equipment, net of accumulated depreciation and amortization of \$16,005 and \$15,308, respectively	12,518	12,242
Goodwill	6,259	6,215
Other intangible assets, net	405	457
Investments in unconsolidated entities	652	637
Other assets	580	639
Total assets	\$ 23,073	\$ 22,569
<b>LIABILITIES AND EQUITY</b>		
Current liabilities:		
Accounts payable	\$ 787	\$ 838
Accrued liabilities	1,115	1,129
Deferred revenues	459	470
Current portion of long-term debt	826	631
Total current liabilities	3,187	3,068
Long-term debt, less current portion	9,166	9,125
Deferred income taxes	1,896	1,884
Landfill and environmental remediation liabilities	1,453	1,404
Other liabilities	759	698
Total liabilities	16,461	16,179
Commitments and contingencies		
Equity:		
Waste Management, Inc. stockholders' equity:		
Common stock, \$0.01 par value; 1,500,000,000 shares authorized; 630,282,461 shares issued	6	6
Additional paid-in capital	4,546	4,561
Retained earnings	6,820	6,721
Accumulated other comprehensive income	200	172
Treasury stock at cost, 166,415,015 and 169,749,709 shares, respectively	(5,284)	(5,390)
Total Waste Management, Inc. stockholders' equity	6,288	6,070

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Noncontrolling interests	324	320
Total equity	6,612	6,390
Total liabilities and equity	\$ 23,073	\$ 22,569

See notes to Condensed Consolidated Financial Statements.

## WASTE MANAGEMENT, INC.

## CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

(In Millions, Except per Share Amounts)

(Unaudited)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2012	2011	2012	2011
Operating revenues	\$ 3,461	\$ 3,522	\$ 10,215	\$ 9,972
Costs and expenses:				
Operating	2,229	2,261	6,655	6,396
Selling, general and administrative	335	380	1,116	1,144
Depreciation and amortization	331	317	971	935
Restructuring	44	15	51	15
(Income) expense from divestitures, asset impairments and unusual items	22	6	55	6
	2,961	2,979	8,848	8,496
Income from operations	500	543	1,367	1,476
Other income (expense):				
Interest expense	(123)	(118)	(366)	(358)
Interest income	2	1	4	6
Equity in net losses of unconsolidated entities	(17)	(7)	(35)	(20)
Other, net	(14)	2	(16)	4
	(152)	(122)	(413)	(368)
Income before income taxes	348	421	954	1,108
Provision for income taxes	125	136	329	377
Consolidated net income	223	285	625	731
Less: Net income attributable to noncontrolling interests	9	13	32	36
Net income attributable to Waste Management, Inc.	\$ 214	\$ 272	\$ 593	\$ 695
Basic earnings per common share	\$ 0.46	\$ 0.58	\$ 1.28	\$ 1.47
Diluted earnings per common share	\$ 0.46	\$ 0.58	\$ 1.28	\$ 1.46
Cash dividends declared per common share	\$ 0.355	\$ 0.34	\$ 1.065	\$ 1.02

See notes to Condensed Consolidated Financial Statements.



## WASTE MANAGEMENT, INC.

## CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

(In Millions)

(Unaudited)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2012	2011	2012	2011
Consolidated net income	\$ 223	\$ 285	\$ 625	\$ 731
Other comprehensive income (loss), net of taxes:				
Unrealized gains (losses) on derivative instruments:				
Unrealized losses, resulting from changes in fair value, net of tax benefit of \$(8), \$(8), \$(16) and \$(16), respectively	(13)	(12)	(25)	(25)
Reclassification adjustment for (gains) losses included in net income, net of tax (expense) benefit of \$6, \$(12), \$6 and \$(6), respectively	10	(18)	10	(9)
	(3)	(30)	(15)	(34)
Unrealized gains (losses) on available-for-sale securities, net of tax expense (benefit) of \$0, \$(2), \$1 and \$(3), respectively	1	(3)	2	(4)
Foreign currency translation adjustments	39	(82)	41	(46)
Change in funded status of post-retirement benefit obligation, net of tax benefit of \$0, \$0, \$0 and \$(1), respectively				(2)
Other comprehensive income (loss), net of taxes	37	(115)	28	(86)
Comprehensive income	260	170	653	645
Less: Comprehensive income attributable to noncontrolling interests	9	13	32	36
Comprehensive income attributable to Waste Management, Inc.	\$ 251	\$ 157	\$ 621	\$ 609

See notes to Condensed Consolidated Financial Statements.

## WASTE MANAGEMENT, INC.

## CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(In Millions)

(Unaudited)

	Nine Months Ended September 30,	
	2012	2011
Cash flows from operating activities:		
Consolidated net income	\$ 625	\$ 731
Adjustments to reconcile consolidated net income to net cash provided by operating activities:		
Depreciation and amortization	971	935
Deferred income tax provision	12	48
Interest accretion on landfill liabilities	62	62
Interest accretion on and discount rate adjustments to environmental remediation liabilities and recovery assets	2	21
Provision for bad debts	39	29
Equity-based compensation expense	21	38
Excess tax benefits associated with equity-based transactions	(10)	(7)
Net gain on disposal of assets	(11)	(13)
Effect of (income) expense from divestitures, asset impairments and unusual items and other	69	6
Equity in net losses of unconsolidated entities	35	20
Change in operating assets and liabilities, net of effects of acquisitions and divestitures:		
Receivables	(112)	(146)
Other current assets	(45)	(25)
Other assets	102	35
Accounts payable and accrued liabilities	7	96
Deferred revenues and other liabilities	(49)	(93)
Net cash provided by operating activities	1,718	1,737
Cash flows from investing activities:		
Acquisitions of businesses, net of cash acquired	(178)	(645)
Capital expenditures	(1,132)	(909)
Proceeds from divestitures of businesses (net of cash divested) and other sales of assets	28	22
Net receipts from restricted trust and escrow accounts	15	74
Investments in unconsolidated entities	(61)	(92)
Other	(33)	15
Net cash used in investing activities	(1,361)	(1,535)
Cash flows from financing activities:		
New borrowings	685	1,001
Debt repayments	(473)	(425)
Common stock repurchases		(528)
Cash dividends	(493)	(481)
Exercise of common stock options	39	40
Excess tax benefits associated with equity-based transactions	10	7
Distributions paid to noncontrolling interests	(31)	(30)
Other	44	(43)
Net cash used in financing activities	(219)	(459)
Effect of exchange rate changes on cash and cash equivalents	2	
Increase (decrease) in cash and cash equivalents	140	(257)
Cash and cash equivalents at beginning of period	258	539



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Cash and cash equivalents at end of period	\$	398	\$	282
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See notes to Condensed Consolidated Financial Statements.

## WASTE MANAGEMENT, INC.

## CONDENSED CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

(In Millions, Except Shares in Thousands)

(Unaudited)

	Total	Waste Management, Inc. Stockholders		Equity		Accumulated		Other		Noncontrolling
		Common Stock	Paid-In	Retained	Comprehensive	Treasury Stock	Income	Shares	Amounts	
		Shares	Amounts	Capital	Earnings					Interests
Balance, December 31, 2011	\$ 6,390	630,282	\$ 6	\$ 4,561	\$ 6,721	\$ 172	(169,750)	\$ (5,390)	\$ 320	
Consolidated net income	625				593					32
Other comprehensive income, net of taxes	28					28				
Cash dividends declared	(493)				(493)					
Equity-based compensation transactions, including dividend equivalents, net of taxes	86			(19)	(1)		3,329	106		
Distributions paid to noncontrolling interests	(31)									(31)
Other	7			4			6			3
Balance, September 30, 2012	\$ 6,612	630,282	\$ 6	\$ 4,546	\$ 6,820	\$ 200	(166,415)	\$ (5,284)	\$ 324	

See notes to Condensed Consolidated Financial Statements.

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**WASTE MANAGEMENT, INC.**

**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

**(Unaudited)**

**1. Basis of Presentation**

The financial statements presented in this report represent the consolidation of Waste Management, Inc., a Delaware corporation; Waste Management's wholly-owned and majority-owned subsidiaries; and certain variable interest entities for which Waste Management or its subsidiaries are the primary beneficiary as described in Note 13. Waste Management is a holding company and all operations are conducted by its subsidiaries. When the terms the Company, we, us or our are used in this document, those terms refer to Waste Management, Inc., its consolidated subsidiaries and consolidated variable interest entities. When we use the term WM, we are referring only to Waste Management, Inc., the parent holding company.

Through the third quarter of 2012, we managed and evaluated our operations primarily through our Eastern, Midwest, Southern, Western and Wheelabrator operating Groups. Our four geographic operating Groups provide collection, transfer, disposal (in both solid waste and hazardous waste landfills) and recycling services for residential, commercial, industrial and municipal customers throughout North America. Our Wheelabrator Group provides waste-to-energy services and manages waste-to-energy facilities and independent power production plants. We also provide additional services that are not managed through our five Groups, including the operations of Oakleaf Global Holdings acquired on July 28, 2011 (Oakleaf), which are presented in this report as Other. Additional information related to our segments and to our acquisition of Oakleaf can be found in Note 8 and in Note 9, respectively.

In July 2012, we announced a reorganization of our operations, designed to streamline management and staff support and reduce our cost structure, while not disrupting our front-line operations. We are in the process of implementing the reorganization and we expect it to be completed by the end of 2012. Once the reorganization has been completed, our reportable segments will be realigned to conform with our new management structure. See Note 10 for additional information related to this reorganization.

The Condensed Consolidated Financial Statements as of September 30, 2012 and for the three and nine months ended September 30, 2012 and 2011 are unaudited. In the opinion of management, these financial statements include all adjustments, which, unless otherwise disclosed, are of a normal recurring nature, necessary for a fair presentation of the financial position, results of operations, and cash flows for the periods presented. The results for interim periods are not necessarily indicative of results for the entire year. The financial statements presented herein should be read in connection with the financial statements included in our Annual Report on Form 10-K for the year ended December 31, 2011.

In preparing our financial statements, we make numerous estimates and assumptions that affect the accounting for and recognition and disclosure of assets, liabilities, equity, revenues and expenses. We must make these estimates and assumptions because certain information that we use is dependent on future events, cannot be calculated with a high degree of precision from data available or simply cannot be readily calculated. In some cases, these estimates are particularly difficult to determine and we must exercise significant judgment. In preparing our financial statements, the most difficult, subjective and complex estimates and the assumptions that present the greatest amount of uncertainty relate to our accounting for landfills, environmental remediation liabilities, asset impairments, deferred income taxes and reserves associated with our insured and self-insured claims. Actual results could differ materially from the estimates and assumptions that we use in the preparation of our financial statements.

In the second quarter of 2012, we believed that the fair value of our Wheelabrator Group could potentially be less than its carrying amount because of the negative effect on our revenues of the continued deterioration of electricity commodity prices, coupled with our continued increased exposure to market prices as a result of the expiration of several long-term, fixed-rate electricity commodity contracts at our waste-to-energy and independent power facilities, and the expiration of several long-term disposal contracts at above-market rates. As a result, we performed an interim impairment analysis of our Wheelabrator Group's goodwill balance, which was \$788 million as of June 30, 2012.

## WASTE MANAGEMENT, INC.

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

We performed an interim quantitative assessment using both an income and a market approach, which indicated that the estimated fair value of our Wheelabrator Group exceeded its carrying value; however, the amount by which the fair value exceeded the carrying value declined significantly from the most recent annual impairment test performed at October 1, 2011. At that time, our Wheelabrator Group's estimated fair value exceeded its carrying value by approximately 30%, as compared with slightly greater than 10% as of the interim impairment test performed in the second quarter of 2012. If market prices for electricity worsen or do not recover as we have projected, if our disposal rates continue to decline, or if our costs and capital expenditures exceed our forecasts, the estimated fair value of our Wheelabrator Group could decrease further and potentially result in an impairment charge in a future period. We continue to monitor our Wheelabrator Group for possible impairment of their goodwill balance.

*Adoption of New Accounting Pronouncements*

**Fair Value Measurement** In May 2011, the Financial Accounting Standards Board ( FASB ) amended authoritative guidance associated with fair value measurements. This amended guidance defines certain requirements for measuring fair value and for disclosing information about fair value measurements in accordance with U.S. generally accepted accounting principles. The amendments to authoritative guidance associated with fair value measurements were effective for the Company on January 1, 2012 and have been applied prospectively. The adoption of this guidance did not have a material impact on our consolidated financial statements.

**Comprehensive Income** In June 2011, the FASB issued amended authoritative guidance associated with comprehensive income, which requires companies to present the total of comprehensive income, the components of net income, and the components of other comprehensive income either in a single continuous statement of comprehensive income or in two separate but consecutive statements. This update eliminates the option to present the components of other comprehensive income as part of the statement of changes in equity. In December 2011, the FASB deferred the effective date of the specific requirement to present items that are reclassified out of accumulated other comprehensive income to net income alongside their respective components of net income and other comprehensive income. The amendments to authoritative guidance associated with comprehensive income were effective for the Company on January 1, 2012 and have been applied retrospectively. The adoption of this guidance did not have a material impact on our consolidated financial statements.

**2. Landfill and Environmental Remediation Liabilities**

Liabilities for landfill and environmental remediation costs are presented in the table below (in millions):

	September 30, 2012			December 31, 2011		
	Landfill	Environmental Remediation	Total	Landfill	Environmental Remediation	Total
Current (in accrued liabilities)	\$ 118	\$ 36	\$ 154	\$ 123	\$ 38	\$ 161
Long-term	1,225	228	1,453	1,169	235	1,404
	\$ 1,343	\$ 264	\$ 1,607	\$ 1,292	\$ 273	\$ 1,565

## WASTE MANAGEMENT, INC.

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

The changes to landfill and environmental remediation liabilities for the year ended December 31, 2011 and the nine months ended September 30, 2012 are reflected in the table below (in millions):

	Landfill	Environmental Remediation
December 31, 2010	\$ 1,266	\$ 284
Obligations incurred and capitalized	49	
Obligations settled	(80)	(37)
Interest accretion	84	6
Revisions in cost estimates and interest rate assumptions	(30)	23
Acquisitions, divestitures and other adjustments	3	(3)
December 31, 2011	1,292	273
Obligations incurred and capitalized	43	
Obligations settled	(58)	(19)
Interest accretion	62	3
Revisions in cost estimates and interest rate assumptions	4	7
Acquisitions, divestitures and other adjustments		
September 30, 2012	\$ 1,343	\$ 264

At several of our landfills, we provide financial assurance by depositing cash into restricted trust funds or escrow accounts for purposes of settling final capping, closure, post-closure and environmental remediation obligations. Generally, these trust funds are established to comply with statutory requirements and operating agreements. See Note 13 for additional information related to these trusts.

### 3. Debt

The following table summarizes the major components of debt at each balance sheet date (in millions) and provides the maturities and interest rate ranges of each major category as of September 30, 2012:

	September 30, 2012	December 31, 2011
Revolving credit facility (weighted average interest rate of 1.5% at December 31, 2011)	\$	\$ 150
Letter of credit facilities		
Canadian credit facility (weighted average effective interest rate of 2.0% at September 30, 2012 and 1.8% at December 31, 2011)	117	137
Senior notes and debentures, maturing through 2039, interest rates ranging from 2.6% to 7.75% (weighted average interest rate of 5.8% at September 30, 2012 and 6.0% at December 31, 2011)	6,711	6,228
Tax-exempt bonds maturing through 2041, fixed and variable interest rates ranging from 0.2% to 7.4% (weighted average interest rate of 2.9% at September 30, 2012 and 3.1% at December 31, 2011)	2,680	2,771
Tax-exempt project bonds, maturing through 2029, fixed and variable interest rates ranging from 0.2% to 3.4% (weighted average interest rate of 1.4% at September 30, 2012 and 1.3% at December 31, 2011)	86	86
Capital leases and other, maturing through 2055, interest rates up to 12%	398	384

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	9,992	9,756
Current portion of long-term debt	826	631
	\$ 9,166	\$ 9,125

## WASTE MANAGEMENT, INC.

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

**Debt Classification**

As of September 30, 2012, we had \$708 million of debt maturing within the next twelve months, including U.S. \$117 million of advances outstanding under our Canadian credit facility, \$400 million of 6.375% senior notes that mature in November 2012 and \$141 million of tax-exempt bonds. We also had \$663 million of tax-exempt borrowings subject to repricing within the next twelve months. We have classified \$545 million of these tax-exempt borrowings as long-term based on our intent and ability to fund any failed remarketings with available capacity under our revolving credit facility.

**Revolving Credit and Letter of Credit Facilities**

As of September 30, 2012, we had an aggregate committed capacity of \$2.5 billion for letters of credit under various credit facilities. Our \$2.0 billion revolving credit facility expires in May 2016 and is our primary source of letter of credit capacity. Our remaining letter of credit capacity is provided under facilities with terms that extend from June 2013 to June 2015. As of September 30, 2012, we had an aggregate of \$1.5 billion of letters of credit outstanding under various credit facilities. Approximately \$1.0 billion of these letters of credit have been issued under our revolving credit facility.

**Debt Borrowings and Repayments**

**Revolving credit facility** During the nine months ended September 30, 2012, we have had net repayments under our revolving credit facility of \$150 million.

**Canadian credit facility** We repaid \$27 million of net advances under our Canadian credit facility during the nine months ended September 30, 2012.

**Senior notes** In September 2012, we issued \$500 million of 2.9% senior notes due September 15, 2022. The net proceeds from the debt issuance were \$495 million. We intend to use a portion of these proceeds to repay \$400 million of 6.375% senior notes that mature in November 2012. All remaining proceeds will be used for general corporate purposes. Pending repayment of the senior notes due November 2012, we used a portion of the proceeds to repay borrowings outstanding under our revolving credit facility.

**Tax-exempt bonds** During the nine months ended September 30, 2012, we repaid \$91 million of our tax-exempt bonds with available cash at their scheduled maturities. In addition, we issued \$43 million of tax-exempt bonds, the proceeds of which were used to repay tax-exempt bonds at their scheduled maturities.

**4. Derivative Instruments and Hedging Activities**

The following table summarizes the fair values of derivative instruments recorded in our Condensed Consolidated Balance Sheet (in millions):

		September 30, 2012	December 31, 2011
<b>Derivatives Designated as Hedging Instruments</b>	<b>Balance Sheet Location</b>		
Electricity commodity contracts	Current other assets	\$ 1	\$ 5
Interest rate contracts	Long-term other assets		73
<b>Total derivative assets</b>		<b>\$ 1</b>	<b>\$ 78</b>
Interest rate contracts	Current accrued liabilities	\$	\$ 42
Electricity commodity contracts	Current accrued liabilities	4	
Foreign exchange contracts	Long-term accrued liabilities	16	2
Interest rate contracts	Long-term accrued liabilities	42	32

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Total derivative liabilities	\$	62	\$	76
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## WASTE MANAGEMENT, INC.

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

We have not offset fair value amounts recognized for our derivative instruments. For information related to the inputs used to measure our derivative assets and liabilities at fair value, refer to Note 12.

*Interest Rate Derivatives**Interest Rate Swaps*

We have used interest rate swaps to maintain a portion of our debt obligations at variable market interest rates. As of September 30, 2012 and December 31, 2011, we had approximately \$6.6 billion and \$6.1 billion in fixed-rate senior notes outstanding, respectively. As of December 31, 2011, the interest payments on \$1 billion, or 16%, of these senior notes were swapped to variable interest rates to protect the debt against changes in fair value due to changes in benchmark interest rates. In April 2012, we elected to terminate our interest rate swaps and, upon termination, we received \$76 million in cash for their fair value plus accrued interest receivable. The terminated interest rate swaps were associated with senior notes that are scheduled to mature from November 2012 to March 2018. The associated fair value adjustments to long-term debt are being amortized as a reduction to interest expense over the remaining terms of the underlying debt using the effective interest method. The cash proceeds received from our termination of the swaps have been classified as a change in Other assets within Net cash provided by operating activities in the Condensed Consolidated Statement of Cash Flows.

We designated our interest rate swaps as fair value hedges of our fixed-rate senior notes. Fair value hedge accounting for interest rate swap contracts increased the carrying value of our debt instruments by \$85 million as of September 30, 2012 and \$102 million as of December 31, 2011. Gains or losses on the derivatives as well as the offsetting losses or gains on the hedged items attributable to our interest rate swaps are recognized in current earnings. We include gains and losses on our interest rate swaps as adjustments to interest expense, which is the same financial statement line item where offsetting gains and losses on the related hedged items are recorded. The following table summarizes the fair value adjustments from active interest rate swaps and the underlying hedged items on our results of operations (in millions):

Three Months Ended September 30,	Statement of Operations Classification	Gain (Loss) on Swap	Gain (Loss)
			on Fixed-Rate Debt
2012	Interest expense	\$	\$
2011	Interest expense	\$ 25	\$ (25)
Nine Months Ended September 30,	Statement of Operations Classification	Gain (Loss) on Swap	Gain (Loss)
			on Fixed-Rate Debt
2012	Interest expense	\$ (1)	\$ 1
2011	Interest expense	\$ 37	\$ (37)

We also recognize the impacts of (i) net periodic settlements of current interest on our active interest rate swaps and (ii) the amortization of previously terminated interest rate swap agreements as adjustments to interest expense. The following table summarizes the impact of periodic settlements of active swap agreements and the impact of terminated swap agreements on our results of operations (in millions):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2012	2011	2012	2011
<b>Decrease to Interest Expense Due to Hedge Accounting for Interest Rate Swaps</b>				
Periodic settlements of active swap agreements(a)(b)	\$	\$ 7	\$ 7	\$ 18
Terminated swap agreements(b)	7	2	16	8
	\$ 7	\$ 9	\$ 23	\$ 26

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- (a) These amounts represent the net of our periodic variable-rate interest obligations and the swap counterparties' fixed-rate interest obligations. Our variable-rate obligations were based on a spread from the three-month LIBOR.

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WASTE MANAGEMENT, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

- (b) Due to our election to terminate our interest rate swap portfolio with a notional amount of \$1 billion in April 2012, periodic settlements of active swap agreements have decreased and amortization to interest expense of terminated swap agreements has increased.

*Forward-Starting Interest Rate Swaps*

In 2009, we entered into forward-starting interest rate swaps with a total notional value of \$525 million to hedge the risk of changes in semi-annual interest payments due to fluctuations in the forward ten-year LIBOR swap rate for anticipated fixed-rate debt issuances in 2011, 2012 and 2014. We designated these forward-starting interest rate swaps as cash flow hedges.

During the first quarter of 2011 and the third quarter of 2012, \$150 million and \$200 million, respectively, of these forward-starting interest rate swaps were terminated contemporaneously with the actual issuance of senior notes in February 2011 and September 2012, respectively, and we paid cash of \$9 million and \$59 million, respectively, to settle the liabilities related to these swap agreements. The ineffectiveness recognized upon termination of these hedges was immaterial and the related deferred losses continue to be recognized as a component of Accumulated other comprehensive income. The deferred losses are being amortized as an increase to interest expense over the ten-year life of the related senior note issuances using the effective interest method.

The active forward-starting interest rate swaps outstanding as of September 30, 2012 relate to an anticipated debt issuance in March 2014. As of September 30, 2012, the fair value of these active interest rate derivatives was comprised of \$42 million of long-term liabilities compared with \$32 million of long-term liabilities as of December 31, 2011.

We recognized pre-tax and after-tax losses of \$3 million and \$2 million, respectively, to other comprehensive income for changes in the fair value of our forward-starting interest rate swaps during the three months ended September 30, 2012 and pre-tax and after-tax losses of \$28 million and \$17 million, respectively, during the nine months ended September 30, 2012. We recognized pre-tax and after-tax losses of \$46 million and \$28 million, respectively, to other comprehensive income for changes in the fair value of our forward-starting interest rate swaps during the three months ended September 30, 2011 and \$53 million and \$33 million, respectively, during the nine months ended September 30, 2011. Pre-tax and after-tax losses of \$2 million and \$1 million, respectively, for the three and nine months ended September 30, 2012 were reclassified out of accumulated other comprehensive income and into interest expense. The losses reclassified to interest expense were immaterial for the three and nine months ended September 30, 2011. As of September 30, 2012, \$7 million (on a pre-tax basis) is scheduled to be reclassified as an increase to interest expense over the next twelve months. There was no significant ineffectiveness associated with these hedges during the three and nine months ended September 30, 2012 or 2011.

*Treasury Rate Locks*

In prior years, we used Treasury rate locks to secure underlying interest rates in anticipation of senior note issuances. The deferred losses, net of taxes, associated with these cash flow hedges were \$8 million at September 30, 2012 and \$12 million at December 31, 2011, which are included in Accumulated other comprehensive income. These deferred losses are reclassified as an increase to interest expense over the life of the related senior note issuances, which extend through 2032. Pre-tax and after-tax losses of \$2 million for the three-month period ended September 30, 2012 and pre-tax and after-tax losses of \$6 million and \$4 million, respectively, for the nine-month period ended September 30, 2012, were reclassified out of accumulated other comprehensive income and into interest expense. Pre-tax and after-tax losses of \$2 million and \$1 million, respectively, for the three-month period ended September 30, 2011, and pre-tax and after-tax losses of \$6 million and \$3 million, respectively, for the nine-month period ended September 30, 2011, were reclassified out of accumulated other comprehensive income and into interest expense. As of September 30, 2012, \$2 million (on a pre-tax basis) is scheduled to be reclassified as an increase to interest expense over the next twelve months.

## WASTE MANAGEMENT, INC.

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

*Credit-Risk-Related Contingent Features*

Our interest rate derivative instruments have in the past and may in the future contain provisions related to the Company's credit rating. These provisions generally provide that if the Company's credit rating were to fall to specified levels below investment grade, the counterparties have the ability to terminate the derivative agreements, resulting in settlement of all affected transactions. As of September 30, 2012, we did not have any interest rate derivatives outstanding that contained these credit-risk related provisions.

*Foreign Currency Derivatives*

We use foreign currency exchange rate derivatives to hedge our exposure to fluctuations in exchange rates for anticipated intercompany cash transactions between Waste Management Holdings, Inc., a wholly-owned subsidiary ( WM Holdings ), and its Canadian subsidiaries. As of September 30, 2012, we had foreign currency forward contracts outstanding for all of the anticipated cash flows associated with a debt arrangement between these wholly-owned subsidiaries. The hedged cash flows as of September 30, 2012 include C\$370 million of principal, which is scheduled for payment on October 31, 2013, and scheduled interest payments of C\$11 million on November 30, 2012 and C\$10 million on October 31, 2013. We designated the forward contracts as cash flow hedges.

Gains or losses on the underlying hedged items attributable to foreign currency exchange risk are recognized in current earnings. The gains or losses on our foreign currency forward contracts that are reclassified out of accumulated other comprehensive income are recognized as adjustments to other income and expense, which is the same financial statement line item where offsetting gains or losses on the related hedged items are recorded. The following table summarizes the pre-tax impacts of our foreign currency cash flow derivatives on our comprehensive income and results of operations (in millions):

Three Months	Derivative Gain or (Loss) Recognized in OCI (Effective Portion)	Statement of Operations Classification	Derivative Gain or (Loss) Reclassified from AOCI into Income (Effective Portion)
Ended September 30,			
2012	\$ (15)	Other income (expense)	\$ (14)
2011	\$ 25	Other income (expense)	\$ 33

Nine Months	Derivative Gain or (Loss) Recognized in OCI (Effective Portion)	Statement of Operations Classification	Derivative Gain or (Loss) Reclassified from AOCI into Income (Effective Portion)
Ended September 30,			
2012	\$ (14)	Other income (expense)	\$ (17)
2011	\$ 11	Other income (expense)	\$ 21

Amounts reported in other comprehensive income and accumulated other comprehensive income are reported net of tax. Adjustments to other comprehensive income for changes in the fair value of our foreign currency cash flow hedges resulted in the recognition of after-tax losses of \$9 million and \$8 million during the three and nine months ended September 30, 2012, respectively, and after-tax gains of \$15 million and \$7

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million during the three and nine months ended September 30, 2011, respectively. After-tax adjustments for the reclassification of losses from accumulated other comprehensive income into income were \$8 million and \$10 million during the three and nine months ended September 30, 2012, respectively. After-tax adjustments for the reclassification of gains from accumulated other comprehensive income into income were \$20 million and \$13 million during the three and nine months ended September 30, 2011, respectively. Ineffectiveness has been included in other income and expense during each of the reported periods. There was no significant ineffectiveness associated with these hedges during the three and nine months ended September 30, 2012 or 2011.

## WASTE MANAGEMENT, INC.

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

*Electricity Commodity Derivatives*

We use short-term receive fixed, pay variable electricity commodity swaps to reduce the variability in our revenues and cash flows caused by fluctuations in the market prices for electricity. We hedged 1.55 million megawatt hours, or approximately 50%, of our Wheelabrator Group's full year 2011 merchant electricity sales, and the swaps executed through September 30, 2012 are expected to hedge about 628,800 megawatt hours, or 20%, of the Wheelabrator Group's full year 2012 merchant electricity sales. For the three-month periods ended September 30, 2012 and 2011, we hedged 16% and 46%, respectively, of our merchant electricity sales. For the nine-month periods ended September 30, 2012 and 2011, we hedged 21% and 49%, respectively, of our merchant electricity sales.

We recognized pre-tax and after-tax losses of \$3 million and \$2 million, respectively, in other comprehensive income for changes in the fair value of our electricity commodity derivatives during the three months ended September 30, 2012 and pre-tax and after-tax gains of \$1 million and less than \$1 million, respectively, for the nine months ended September 30, 2012. We recognized pre-tax and after-tax adjustments of \$2 million and \$1 million, respectively, for the reclassification of gains from accumulated other comprehensive income into income as a component of Operating revenues during the three months ended September 30, 2012 and \$9 million and \$5 million, respectively, for the nine months ended September 30, 2012. All financial statement impacts associated with these derivatives were immaterial for the three and nine months ended September 30, 2011. There was no significant ineffectiveness associated with these cash flow hedges during the three and nine months periods ended September 30, 2012 or 2011.

**5. Income Taxes**

Our effective income tax rate for the three and nine months ended September 30, 2012 was 36.1% and 34.5%, respectively, compared with 32.3% and 34.0% for the comparable prior year periods. We evaluate our effective income tax rate at each interim period and adjust it accordingly as facts and circumstances warrant. The differences between federal income taxes computed at the federal statutory rate and reported income taxes for the three and nine months ended September 30, 2012 were primarily due to the favorable impact of federal tax credits, audit settlements and the realization of additional acquired federal net operating losses. These favorable items were more than offset during the third quarter and almost entirely offset during the nine months by the unfavorable impacts of adjustments to our accruals and related deferred taxes due to the filing of our 2011 income tax returns, state and local income taxes, a Canadian provincial tax rate increase and the tax implications of impairments of unconsolidated investments. The differences between federal income taxes computed at the federal statutory rate and reported income taxes for the three and nine months ended September 30, 2011 were primarily due to the favorable impact of federal tax credits, audit settlements and adjustments to our accruals due to the filing of our 2010 income tax returns, offset in part by the unfavorable impact of state and local income taxes.

*Investment in Refined Coal Facility* In January 2011, we acquired a noncontrolling interest in a limited liability company, which was established to invest in and manage a refined coal facility in North Dakota. The facility's refinement processes qualify for federal tax credits that are expected to be realized through 2019 in accordance with Section 45 of the Internal Revenue Code. Our initial consideration for this investment consisted of a cash payment of \$48 million.

We account for our investment in this entity using the equity method of accounting, recognizing our share of the entity's results and other reductions in Equity in net losses of unconsolidated entities, within our Condensed Consolidated Statement of Operations. During the three and nine months ended September 30, 2012 and 2011, we recognized less than \$1 million and \$2 million, respectively, of net losses resulting from our share of the entity's operating losses. Our tax provision for the three and nine months ended September 30, 2012 and 2011 was reduced, primarily as a result of tax credits realized from this investment, by \$6 million and \$14 million and by \$4 million and \$11 million, respectively. See Note 13 for additional information related to this investment.

## WASTE MANAGEMENT, INC.

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

*Investment in Federal Low-income Housing Tax Credits* In April 2010, we acquired a noncontrolling interest in a limited liability company established to invest in and manage low-income housing properties. The entity's low-income housing investments qualify for federal tax credits that are expected to be realized through 2020 in accordance with Section 42 of the Internal Revenue Code.

We account for our investment in this entity using the equity method of accounting. We recognize our share of the entity's results and reductions in the value of our investment in Equity in net losses of unconsolidated entities, within our Condensed Consolidated Statement of Operations. The value of our investment decreases as the tax credits are generated and utilized. During the three and nine months ended September 30, 2012, we recognized \$6 million and \$18 million of losses relating to our equity investment in this entity, \$2 million and \$5 million of interest expense, and a reduction in our tax provision of \$11 million (including \$8 million of tax credits) and \$27 million (including \$18 million of tax credits), respectively. During the three and nine months ended September 30, 2011, we recognized \$5 million and \$17 million of losses associated with our equity investment, \$2 million and \$6 million of interest expense, and a reduction in our tax provision of \$9 million (including \$7 million of tax credits) and \$27 million (including \$18 million of tax credits), respectively.

*Recent Legislation* The Tax Relief, Unemployment Insurance Reauthorization, and Job Creation Act, signed into law on December 17, 2010, included an extension of the bonus depreciation allowance through the end of 2012 and increased the amount of qualifying capital expenditures that can be depreciated immediately from 50% to 100%. The 100% depreciation deduction applied to qualifying property placed in service from September 8, 2010 through December 31, 2011. The depreciation deduction for qualifying property placed in service in 2012 has been reduced to 50%. The acceleration of deductions on capital expenditures resulting from the bonus depreciation provisions has no impact on our effective tax rate, but reduces our cash taxes in the periods in which the deductions are taken.

The acceleration of depreciation deductions related to qualifying property additions in 2011 decreased our full year 2011 cash taxes by approximately \$190 million and, based on our current forecast of 2012 capital expenditures, we estimate a reduction in our full year 2012 cash taxes of approximately \$90 million related to qualifying property additions in 2012. However, taking accelerated deductions results in increased cash taxes in subsequent periods when the deductions for these capital expenditures would have otherwise been taken.

## 6. Earnings Per Share

Basic and diluted earnings per share were computed using the following common share data (shares in millions):

	Three Months		Nine Months	
	Ended September 30,		Ended September 30,	
	2012	2011	2012	2011
Number of common shares outstanding at end of period	463.9	461.2	463.9	461.2
Effect of using weighted average common shares outstanding	0.2	7.1	(0.6)	11.5
Weighted average basic common shares outstanding	464.1	468.3	463.3	472.7
Dilutive effect of equity-based compensation awards and other contingently issuable shares	0.8	1.4	0.9	1.8
Weighted average diluted common shares outstanding	464.9	469.7	464.2	474.5
Potentially issuable shares	16.5	17.3	16.5	17.3
Number of anti-dilutive potentially issuable shares excluded from diluted common shares outstanding	8.1	9.9	8.1	6.4

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WASTE MANAGEMENT, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

**7. Commitments and Contingencies**

*Financial Instruments* We have obtained letters of credit, performance bonds and insurance policies and have established trust funds and issued financial guarantees to support tax-exempt bonds, contracts, performance of landfill final capping, closure and post-closure requirements, environmental remediation, and other obligations. Letters of credit generally are supported by our revolving credit facility and other credit facilities established for that purpose. We obtain surety bonds and insurance policies from an entity in which we have a noncontrolling financial interest. We also obtain insurance from a wholly-owned insurance company, the sole business of which is to issue policies for us. In those instances where our use of financial assurance from entities we own or have financial interests in is not allowed, we have available alternative financial assurance mechanisms.

Management does not expect that any claims against or draws on these instruments would have a material adverse effect on our consolidated financial statements. We have not experienced any unmanageable difficulty in obtaining the required financial assurance instruments for our current operations. In an ongoing effort to mitigate risks of future cost increases and reductions in available capacity, we continue to evaluate various options to access cost-effective sources of financial assurance.

*Insurance* We carry insurance coverage for protection of our assets and operations from certain risks including automobile liability, general liability, real and personal property, workers compensation, directors and officers liability, pollution legal liability and other coverages we believe are customary to the industry. Our exposure to loss for insurance claims is generally limited to the per incident deductible under the related insurance policy. Our exposure, however, could increase if our insurers are unable to meet their commitments on a timely basis.

We have retained a significant portion of the risks related to our automobile, general liability and workers compensation claims programs.

General liability refers to the self-insured portion of specific third party claims made against us that may be covered under our commercial General Liability Insurance Policy. For our self-insured retentions, the exposure for unpaid claims and associated expenses, including incurred but not reported losses, is based on an actuarial valuation and internal estimates. The accruals for these liabilities could be revised if future occurrences or loss development significantly differ from our assumptions used. We do not expect the impact of any known casualty, property, environmental or other contingency to have a material impact on our financial condition, results of operations or cash flows.

*Guarantees* In the ordinary course of our business, WM and WM Holdings enter into guarantee agreements associated with their subsidiaries operations. Additionally, WM and WM Holdings have each guaranteed all of the senior debt of the other entity. No additional liabilities have been recorded for these intercompany guarantees because all of the underlying obligations are reflected in our Condensed Consolidated Balance Sheets.

We also have guaranteed the obligations and certain performance requirements of, and provided indemnification to, third parties in the ordinary course of business for both consolidated and unconsolidated entities. Guarantee agreements outstanding as of September 30, 2012 include (i) guarantees of unconsolidated entities financial obligations maturing through 2020 for maximum future payments of \$10 million; and (ii) agreements guaranteeing certain market value losses for approximately 850 homeowners properties adjacent to or near 20 of our landfills. Our indemnification obligations generally arise from divestitures and provide that we will be responsible for liabilities associated with our operations for events that occurred prior to the sale of the operations. Additionally, under certain of our acquisition agreements, we have provided for additional consideration to be paid to the sellers if established financial targets are achieved post-closing, and we have recognized liabilities for these contingent obligations based on an estimate of the fair value of these contingencies at the time of acquisition. Contingent obligations related to indemnifications arising from our divestitures and contingent consideration provided for by our acquisitions are not expected to be material to our financial position, results of operations or cash flows.



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WASTE MANAGEMENT, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

*Environmental Matters* A significant portion of our operating costs and capital expenditures could be characterized as costs of environmental protection as we are subject to an array of laws and regulations relating to the protection of the environment. Under current laws and regulations, we may have liabilities for environmental damage caused by our operations, or for damage caused by conditions that existed before we acquired a site. In addition to remediation activity required by state or local authorities, such liabilities include potentially responsible party, or PRP, investigations. The costs associated with these liabilities can include settlements and certain legal and consultant fees, as well as incremental internal and external costs directly associated with site investigation and clean-up.

Estimating our degree of responsibility for remediation is inherently difficult. We recognize and accrue for an estimated remediation liability when we determine that such liability is both probable and reasonably estimable. Determining the method and ultimate cost of remediation requires that a number of assumptions be made. There can sometimes be a range of reasonable estimates of the costs associated with the likely site remediation alternatives identified in the investigation of the extent of environmental impact. In these cases, we use the amount within the range that constitutes our best estimate. If no amount within a range appears to be a better estimate than any other, we use the amount that is the low end of such range. If we used the high ends of such ranges, our aggregate potential liability would be approximately \$150 million higher than the \$264 million recorded in the Condensed Consolidated Financial Statements as of September 30, 2012. Our ultimate responsibility may differ materially from current estimates. It is possible that technological, regulatory or enforcement developments, the results of environmental studies, the inability to identify other PRPs, the inability of other PRPs to contribute to the settlements of such liabilities, or other factors could require us to record additional liabilities. Our ongoing review of our remediation liabilities, in light of relevant internal and external facts and circumstances, could result in revisions to our accruals that could cause upward or downward adjustments to income from operations. These adjustments could be material in any given period.

As of September 30, 2012, we had been notified that we are a PRP in connection with 80 locations listed on the EPA's Superfund National Priorities List, or NPL. Of the 80 sites at which claims have been made against us, 16 are sites we own. Each of the NPL sites we own was initially developed as a landfill disposal facility by one or more other parties. At each of these facilities, we are working in conjunction with the government to characterize or remediate identified site problems, and we have either agreed with other legally liable parties on an arrangement for sharing the costs of remediation or are working toward a cost-sharing agreement. We generally expect to receive any amounts due from other participating parties at or near the time that we make the remedial expenditures. The other 64 NPL sites, which we do not own, are at various procedural stages under the Comprehensive Environmental Response, Compensation and Liability Act of 1980, as amended, known as CERCLA or Superfund.

The majority of these proceedings involving NPL sites that we do not own are based on allegations that certain of our subsidiaries (or their predecessors) transported hazardous substances to the sites, often prior to our acquisition of these subsidiaries. CERCLA generally provides for liability for those parties owning, operating, transporting to or disposing at the sites. Proceedings arising under Superfund typically involve numerous waste generators and other waste transportation and disposal companies and seek to allocate or recover costs associated with site investigation and remediation, which costs could be substantial and could have a material adverse effect on our consolidated financial statements. At some of the sites at which we have been identified as a PRP, our liability is well defined as a consequence of a governmental decision and an agreement among liable parties as to the share each will pay for implementing that remedy. At other sites, where no remedy has been selected or the liable parties have been unable to agree on an appropriate allocation, our future costs are uncertain.

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WASTE MANAGEMENT, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Item 103 of the SEC's Regulation S-K requires disclosure of certain environmental matters when a governmental authority is a party to the proceedings, or such proceedings are known to be contemplated, unless we reasonably believe that the matter will result in no monetary sanctions, or in monetary sanctions, exclusive of interest and costs, of less than \$100,000. The following matters are disclosed in accordance with that requirement. We do not currently believe that the eventual outcome of any such matters, individually or in the aggregate, could have a material adverse effect on the Company's business, financial condition, results of operations or cash flows.

On April 4, 2006, the EPA issued a Notice of Violation (NOV) to Waste Management of Hawaii, Inc., an indirect wholly-owned subsidiary of WM, and to the City and County of Honolulu for alleged violations of the federal Clean Air Act, based on alleged failure to submit certain reports and design plans required by the EPA, and the failure to begin and timely complete the installation of a gas collection and control system (GCCS) for the Waimanalo Gulch Sanitary Landfill on Oahu. The EPA has also indicated that it will seek penalties and injunctive relief as part of the NOV enforcement for elevated landfill temperatures that were recorded after installation of the GCCS. The parties have been in confidential settlement negotiations. Pursuant to an indemnity agreement, any penalty assessed will be paid by the Company, and not by the City and County of Honolulu.

On December 22, 2011, the Harris County Attorney in Houston, Texas filed suit against McGinnes Industrial Maintenance Corporation (MIMC), WM and Waste Management of Texas, Inc., et al, seeking civil penalties and attorneys' fees for alleged violations of the Texas Water Code and the Texas Health and Safety Code. The County's Original Petition pending in the District Court of Harris County, Texas alleges the mismanagement of certain waste pits that were operated from 1965 to 1966 by MIMC. In 1998, a predecessor of WM acquired the stock of the parent entity of MIMC.

On April 20, 2012, the Pennsylvania Department of Environmental Protection (PADEP) transmitted a proposed Consent Order and Agreement to Waste Management of Pennsylvania, Inc., an indirect wholly-owned subsidiary of WM, for alleged violations of Pennsylvania solid waste regulations, including certain operations failures, at the Northwest Sanitary Landfill. PADEP has indicated that it is seeking penalties and corrective action.

Additionally, the United States Attorney's Office for the District of Hawaii has commenced an investigation prompted by allegations of violations of the federal Clean Water Act involving discharge of stormwater at the Waimanalo Gulch Sanitary Landfill, located on Oahu, in connection with three major storm events in December 2010 and January 2011. No formal enforcement action has been brought against the Company. While we could potentially be subject to sanctions, including requirements to pay monetary penalties, in connection with a future proceeding that may arise from the investigation, a range of loss cannot currently be estimated because no proceeding has yet commenced and significant factual and legal issues remain. We are cooperating with the U.S. Attorney's Office.

*Litigation* In April 2002, certain former participants in the ERISA plans of WM Holdings filed a lawsuit in the U.S. District Court for the District of Columbia in a case entitled *William S. Harris, et al. v. James E. Koenig, et al.* The lawsuit attempts to increase the recovery of a class of ERISA plan participants on behalf of the plan based on allegations related to both the events alleged in, and the settlements relating to, the securities class action against WM Holdings that was settled in 1998, the litigation against WM in Texas that was settled in 2002, as well as the decision to offer WM common stock as an investment option within the plan beginning in 1990, despite alleged knowledge by at least two members of the investment committee of financial misstatement by WM during the relevant time period.

During the second quarter of 2010, the Court dismissed certain claims against individual defendants, including all claims against each of the current members of our Board of Directors. Previously, plaintiffs dismissed all claims related to the settlement of the securities class action against WM that was settled in 2002,

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**WASTE MANAGEMENT, INC.**

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

and the court certified a limited class of participants who may bring claims on behalf of the plan, but not individually. During the third quarter of 2011, the Court ruled in favor of WM and two former employees dismissing all claims brought by the plaintiffs related to the decision to offer WM stock as an investment option within the plan. We have reached a settlement with the plaintiffs on this matter, with a proposed class settlement agreement submitted to the Court on October 17, 2012. We anticipate all the details with respect to the settlement will be resolved and finally approved by the Court within the next few months. We do not believe the settlement could have a material adverse effect on the Company's business, financial condition, results of operations, or cash flows.

In October 2011 and January 2012, we were named as a defendant in a purported class action in the Circuit Court of Sarasota County, Florida and the Circuit Court of Lawrence County Alabama, respectively. These cases primarily pertain to our fuel and environmental charges included on our invoices, generally alleging that such charges were not properly disclosed, were unfair and were contrary to the customer service contracts. The law firm that filed these lawsuits had filed, in 2008, a purported class action against subsidiaries of WM in Bullock County, Alabama, making similar allegations. The prior Alabama suit was removed to federal court, where the federal court ultimately dismissed the plaintiffs' national class action claims. The plaintiffs then elected to dismiss the case without prejudice. We will vigorously defend against these pending lawsuits. Given the inherent uncertainties of litigation, including the early stage of these cases, the unknown size of any potential class, and legal and factual issues in dispute, the outcome of these cases cannot be predicted and a range of loss cannot currently be estimated.

From time to time, we are also named as defendants in personal injury and property damage lawsuits, including purported class actions, on the basis of having owned, operated or transported waste to a disposal facility that is alleged to have contaminated the environment or, in certain cases, on the basis of having conducted environmental remediation activities at sites. Some of the lawsuits may seek to have us pay the costs of monitoring of allegedly affected sites and health care examinations of allegedly affected persons for a substantial period of time even where no actual damage is proven. While we believe we have meritorious defenses to these lawsuits, the ultimate resolution is often substantially uncertain due to the difficulty of determining the cause, extent and impact of alleged contamination (which may have occurred over a long period of time), the potential for successive groups of complainants to emerge, the diversity of the individual plaintiffs' circumstances, and the potential contribution or indemnification obligations of co-defendants or other third parties, among other factors. Additionally, we often enter into contractual arrangements with landowners imposing obligations on us to meet certain regulatory or contractual conditions upon site closure or upon termination of the agreements. Compliance with these arrangements is inherently subject to subjective determinations and may result in disputes, including litigation.

As a large company with operations across the United States and Canada, we are subject to various proceedings, lawsuits, disputes and claims arising in the ordinary course of our business. Many of these actions raise complex factual and legal issues and are subject to uncertainties. Actions filed against us include commercial, customer, and employment-related claims, including purported class action lawsuits related to our sales and marketing practices and our customer service agreements and purported class actions involving federal and state wage and hour and other laws. The plaintiffs in some actions seek unspecified damages or injunctive relief, or both. These actions are in various procedural stages, and some are covered in part by insurance. We currently do not believe that the eventual outcome of any such actions could have a material adverse effect on the Company's business, financial condition, results of operations, or cash flows.

WM's charter and bylaws provide that WM shall indemnify against all liabilities and expenses, and upon request shall advance expenses to, any person who is subject to a pending or threatened proceeding because such person is a director or officer of the Company. Such indemnification is required to the maximum extent permitted under Delaware law. Accordingly, the director or officer must reimburse the Company for any fees advanced if it is later determined that the director or officer was not entitled to have such fees advanced under Delaware law. Additionally, WM has entered into separate indemnification agreements with each of the members of its Board.

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WASTE MANAGEMENT, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

of Directors, and the employment agreements between WM and its Chief Executive Officer, Chief Financial Officer and other executive and senior vice presidents contain a direct contractual obligation of the Company to provide indemnification to the executive. The Company may incur substantial expenses in connection with the fulfillment of its advancement of costs and indemnification obligations in connection with current actions involving former officers of the Company or its subsidiaries or other actions or proceedings that may be brought against its former or current officers, directors and employees.

*Multiemployer Defined Benefit Pension Plans* About 20% of our workforce is covered by collective bargaining agreements with various union locals across the United States and Canada. As a result of some of these agreements, certain of our subsidiaries are participating employers in a number of trustee-managed multiemployer, defined benefit pension plans for the affected employees. In connection with our ongoing renegotiation of various collective bargaining agreements, we may discuss and negotiate for the complete or partial withdrawal from one or more of these pension plans. A complete or partial withdrawal from a multiemployer pension plan may also occur if employees covered by a collective bargaining agreement vote to decertify a union from continuing to represent them.

One of the most significant multiemployer pension plans in which we have participated is the Central States Southeast and Southwest Areas Pension Plan ( Central States Pension Plan ). The Central States Pension Plan is in critical status as defined by the Pension Protection Act of 2006. Since 2008, certain of our affiliates have bargained to remove covered employees from the Central States Pension Plan, resulting in a series of withdrawals. In October 2011, employees at the last of our affiliates with active participants in the Central States Pension Plan voted to decertify the union that represented them, withdrawing themselves from the Central States Pension Plan.

We are still negotiating and litigating final resolutions of our withdrawal liability for previous withdrawals, including our recent final withdrawal mentioned above, but we do not believe any additional liability above the charges we have already recognized for such previous withdrawals could be material to the Company's business, financial condition, results of operations or cash flows. We also do not believe that any future withdrawals, individually or in the aggregate, from the multiemployer plans to which we contribute, could have a material adverse effect on our business, financial condition or liquidity. However, such withdrawals could have a material adverse effect on our results of operations for a particular reporting period, depending on the number of employees withdrawn in any future period and the financial condition of the multiemployer plan(s) at the time of such withdrawal(s).

*Tax Matters* We are currently in the examination phase of IRS audits for the tax years 2011 and 2012 and expect these audits to be completed within the next three and 15 months, respectively. We participate in the IRS's Compliance Assurance Program, which means we work with the IRS throughout the year in order to resolve any material issues prior to the filing of our year-end tax return. We are also currently undergoing audits by various state and local jurisdictions that date back to 2000. We have finalized audits in Canada through the 2005 tax year and are not currently under audit for any subsequent tax years in Canada. On July 28, 2011, we acquired Oakleaf, which is subject to IRS examinations for years dating back to 2009 and state income tax examinations for years dating back to 2002. Pursuant to the terms of our acquisition of Oakleaf, we are entitled to indemnification for Oakleaf's pre-acquisition tax liabilities. We maintain a liability for uncertain tax positions, the balance of which management believes is adequate. Results of audit assessments by taxing authorities are not currently expected to have a material adverse impact on our results of operations or cash flows.

## 8. Segment and Related Information

Through the third quarter of 2012, we managed and evaluated our operations primarily through our Eastern, Midwest, Southern, Western and Wheelabrator operating Groups. These five Groups are presented below as our reportable segments. Our four geographic operating Groups provide collection, transfer, disposal (in both solid waste and hazardous waste landfills) and recycling services for residential, commercial, industrial and municipal

**WASTE MANAGEMENT, INC.**

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

customers throughout North America. Our fifth Group is the Wheelabrator Group, which provides waste-to-energy services and manages waste-to-energy facilities and independent power production plants in the United States and participates in the design, construction, operation and management of waste-to-energy facilities through investments and consolidated entities in China and Europe. In addition, the Oakleaf operations we acquired on July 28, 2011 represent a separate operating segment; however, they do not meet the criteria to be presented as a separate reportable segment. The operations not managed through our five operating Groups, including the Oakleaf operations, are presented herein as Other. See Note 9 for additional information related to our acquisition of Oakleaf.

In July 2012, we announced a reorganization of our operations, designed to streamline management and staff support and reduce our cost structure, while not disrupting our front-line operations. We are in the process of implementing the reorganization, which includes the elimination of our four existing geographic Groups, and we expect it to be completed by the end of 2012. Once the reorganization has been completed, our reportable segments will be realigned to conform with our new management structure. See Note 10 for additional information related to this reorganization.

## WASTE MANAGEMENT, INC.

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Summarized financial information concerning our reportable segments for the three and nine months ended September 30 is shown in the following table (in millions):

	Gross Operating Revenues	Intercompany Operating Revenues	Net Operating Revenues	Income from Operations
<b>Three Months Ended:</b>				
<b>September 30, 2012</b>				
Eastern	\$ 778	\$ (158)	\$ 620	\$ 142
Midwest	833	(141)	692	175
Southern	862	(140)	722	180
Western	840	(127)	713	129
Wheelabrator	218	(30)	188	43
Other	552	(26)	526	(22)
	4,083	(622)	3,461	647
Corporate and Other				(147)
Total	\$ 4,083	\$ (622)	\$ 3,461	\$ 500
<b>September 30, 2011</b>				
Eastern	\$ 822	\$ (139)	\$ 683	\$ 146
Midwest	847	(123)	724	175
Southern	853	(104)	749	194
Western	841	(114)	727	154
Wheelabrator	228	(28)	200	57
Other	462	(23)	439	(40)
	4,053	(531)	3,522	686
Corporate and Other				(143)
Total	\$ 4,053	\$ (531)	\$ 3,522	\$ 543
<b>Nine Months Ended:</b>				
<b>September 30, 2012</b>				
Eastern	\$ 2,294	\$ (434)	\$ 1,860	\$ 416
Midwest	2,412	(388)	2,024	504
Southern	2,575	(386)	2,189	567
Western	2,472	(365)	2,107	405
Wheelabrator	631	(92)	539	62
Other	1,564	(68)	1,496	(94)
	11,948	(1,733)	10,215	1,860
Corporate and Other				(493)
Total	\$ 11,948	\$ (1,733)	\$ 10,215	\$ 1,367
<b>September 30, 2011</b>				
Eastern	\$ 2,326	\$ (387)	\$ 1,939	\$ 407

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Midwest	2,403	(355)	2,048	460
Southern	2,553	(307)	2,246	579
Western	2,456	(336)	2,120	436
Wheelabrator	664	(89)	575	112
Other	1,085	(41)	1,044	(75)
	11,487	(1,515)	9,972	1,919
Corporate and Other				(443)
Total	\$ 11,487	\$ (1,515)	\$ 9,972	\$ 1,476

## WASTE MANAGEMENT, INC.

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Fluctuations in our operating results may be caused by many factors, including period-to-period changes in the relative contribution of revenue by each line of business and operating segment, changes in commodity prices and by general economic conditions. In addition, our revenues and income from operations typically reflect seasonal patterns. Our operating revenues normally tend to be somewhat higher in the summer months, primarily due to the traditional seasonal increase in the volume of construction and demolition waste. Historically, the volumes of industrial and residential waste in certain regions in which we operate have tended to increase during the summer months. Our second and third quarter revenues and results of operations typically reflect these seasonal trends.

Additionally, certain destructive weather conditions that tend to occur during the second half of the year, such as hurricanes that most often impact our Southern Group, can actually increase our revenues in the areas affected. While weather-related and other one-time occurrences can boost revenues through additional work, as a result of significant start-up costs and other factors, such revenue sometimes generates earnings at comparatively lower margins. Certain weather conditions, including severe winter storms, may result in the temporary suspension of our operations, which can significantly affect the operating results of the affected regions. The operating results of our first quarter also often reflect higher repair and maintenance expenses because we rely on the slower winter months, when waste flows are generally lower, to perform scheduled maintenance at our waste-to-energy facilities.

## 9. Acquisitions

*Oakleaf* On July 28, 2011, we paid \$432 million, net of cash received of \$4 million and inclusive of certain adjustments, to acquire Oakleaf. Oakleaf provides outsourced waste and recycling services principally through a nationwide network of third-party haulers. The operations we acquired generated approximately \$580 million in revenues in 2010. We acquired Oakleaf to advance our growth and transformation strategies and increase our national accounts customer base while enhancing our ability to provide comprehensive environmental solutions. For the year ended December 31, 2011, we incurred \$1 million of acquisition-related costs, which were classified as Selling, general and administrative expenses. For the three- and nine-month periods ended September 30, 2012, Oakleaf recognized revenues of \$143 million and \$438 million, respectively, and net losses of \$4 million and \$8 million, respectively. These amounts are included in our Condensed Consolidated Statement of Operations.

The following table shows adjustments since December 31, 2011 to the allocation of the purchase price of Oakleaf to the assets acquired and liabilities assumed based on their estimated fair value and is final as of September 30, 2012 (in millions):

	December 31, 2011	Adjustments	September 30, 2012
Accounts and other receivables	\$ 70	\$ 1	\$ 71
Other current assets	28		28
Property and equipment	72	(2)	70
Goodwill	327	1	328
Other intangible assets	87		87
Accounts payable	(82)		(82)
Accrued liabilities	(48)		(48)
Deferred income taxes, net	(10)	1	(9)
Other liabilities	(12)	(1)	(13)
Total purchase price	\$ 432	\$	\$ 432



## WASTE MANAGEMENT, INC.

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

The following table presents the final allocation of the purchase price to other intangible assets (amounts in millions, except for amortization periods):

	Amount	Weighted Average Amortization Periods (In Years)
Customer relationships	\$ 74	10.0
Vendor relationships	4	10.0
Trademarks	9	15.0
	\$ 87	10.5

Goodwill of \$328 million was calculated as the excess of the consideration paid over the net assets recognized and represents the future economic benefits arising from other assets acquired that could not be individually identified and separately recognized. Goodwill is a result of expected synergies from combining the Company's operations with Oakleaf's national accounts customer base and vendor network. The vendor-hauler network expands our partnership with third-party service providers. In many cases we can provide vendor-haulers with opportunities to maintain and increase their business by utilizing our extensive post-collection network. We believe this will generate significant benefits for the Company and for the vendor-haulers. Goodwill has been assigned to our four geographic Groups as they are expected to benefit from the synergies of the combination. Goodwill related to this acquisition is not deductible for income tax purposes.

The following pro forma consolidated results of operations for the three and nine months ended September 30, 2011 have been prepared as if the acquisition of Oakleaf occurred at January 1, 2011 (in millions, except per share amounts):

	Three Months Ended September 30, 2011	Nine Months Ended September 30, 2011
Operating revenues	\$ 3,566	\$ 10,287
Net income attributable to Waste Management, Inc.	272	689
Basic earnings per common share	0.58	1.46
Diluted earnings per common share	0.58	1.45

*Other* During the nine months ended September 30, 2012, we paid \$94 million for interests in oil and gas producing properties through two transactions. The purchase price was allocated primarily to Property and equipment. Additionally, during the nine months ended September 30, 2012 we acquired 21 other businesses related to our collection and recycling operations.

## 10. Restructuring

*2012 Restructurings* In July 2012, we announced a reorganization of operations, designed to streamline management and staff support and reduce our cost structure, while not disrupting our front-line operations. Principal organizational changes being implemented include removal of the management layer consisting of our four existing geographic Groups; consolidation and reduction of the number of Areas managing the core collection, disposal and recycling businesses from 22 to 17; and reduction of corporate support staff in an effort to better align support with the needs of the operating units.

We are in the process of implementing this restructuring plan and we expect it to be completed by the end of 2012. We currently estimate that approximately 700 employee positions throughout the Company, including positions at both the management and support levels, will be

eliminated. Voluntary separation arrangements were offered to many in certain levels of management.

## WASTE MANAGEMENT, INC.

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Additionally, during the first nine months of 2012, we recognized employee severance and benefits restructuring charges associated with the reorganization of Oakleaf that began in 2011 and certain other actions taken by the Company in early 2012.

During the third quarter of 2012, we recognized pre-tax charges of \$44 million associated with these restructuring activities, \$39 million of which related to employee severance and benefit costs. The remainder of the charge was primarily related to abandoned operating leases. We currently expect to incur additional restructuring charges in the fourth quarter of 2012, consisting of employee severance and benefits expenses and facility, lease and other related expenses, in the range of \$20 million to \$30 million. The additional restructuring charges are an estimate, and actual charges may vary materially based on various factors, including the number of employee terminations; facility, lease or other restructuring charges that are not yet estimable; and changes in management's objectives.

The following table summarizes the employee severance and benefit costs and other charges recognized for these restructuring activities by each of our current reportable segments and our Corporate and Other organizations for the three and nine months ended September 30, 2012 (in millions):

	Three Months Ended September 30, 2012	Nine Months Ended September 30, 2012
Eastern	\$ 3	\$ 4
Midwest	5	5
Southern	5	7
Western	9	9
Wheelabrator	1	1
Corporate and Other	21	25
<b>Total</b>	<b>\$ 44</b>	<b>\$ 51</b>

**2011 Restructurings** Beginning in July 2011, we took steps to streamline our organization as part of our cost savings programs. This reorganization eliminated over 700 employee positions throughout the Company, including approximately 300 open positions. Additionally, subsequent to our acquisition of Oakleaf, we incurred charges in connection with restructuring that organization. During the year ended December 31, 2011, we recognized a total of \$19 million of pre-tax restructuring charges, of which \$18 million were related to employee severance and benefit costs. The remaining charges were primarily related to operating lease obligations for property that will no longer be utilized.

Through September 30, 2012, we have paid a total of approximately \$29 million of the employee severance and benefit costs incurred as a result of these combined 2012 and 2011 restructuring efforts.

# 11. Asset Impairments and Unusual Items

*(Income) expense from divestitures, asset impairments and unusual items* During the third quarter of 2012, we recognized impairment charges aggregating \$21 million, relating in large part to (i) the impairment of a note receivable from an entity that we invested in that is now being liquidated (see *Equity in net losses of unconsolidated entities* discussion below), (ii) the impairment of certain related assets due to our decision not to use or develop those assets and (iii) the impairment of an oil and gas well as a result of projected operating losses that caused us to write-down the carrying value of the oil and gas well to its estimated fair value. These charges are included in our Other operations in Note 8.

During the second quarter of 2012, we recognized impairment charges of \$34 million, relating primarily to two facilities in our medical waste services business as a result of projected operating losses at each of these facilities. We wrote down the carrying values of the facilities' operating permits and property, plant and equipment to their estimated fair values. Our medical waste services business is included in our Other operations in Note 8.



## WASTE MANAGEMENT, INC.

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

During the third quarter of 2011, we recognized impairment charges relating to two facilities in our medical waste services business, in addition to the two facilities impaired in the second quarter and discussed above, as a result of the closure of one site and as a result of continuing operating losses at the other site. We wrote down the net book values of the sites to their estimated fair values.

*Equity in net losses of unconsolidated entities* During the third quarter of 2012, we recognized a charge of \$10 million related to a payment we made under a guarantee on behalf of an unconsolidated entity accounted for under the equity method.

*Other income (expense)* During the third quarter of 2012, we recognized an impairment charge of \$14 million relating to an other-than-temporary decline in the value of an investment accounted for under the cost method. We wrote down the carrying value of our investment to its fair value based on other third-party investors' recent transactions in these securities, which are considered to be the best evidence of fair value currently available. This charge is recorded in Other, net in our Condensed Consolidated Statement of Operations.

**12. Fair Value Measurements***Assets and Liabilities Accounted for at Fair Value*

Our assets and liabilities that are measured at fair value on a recurring basis include the following (in millions):

Fair Value Measurements at September 30, 2012 Using				
	Total	Quoted Prices in Active Markets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
<b>Assets:</b>				
Cash equivalents	\$ 270	\$ 270	\$	\$
Available-for-sale securities	164	139		25
Electricity commodity derivatives	1		1	
<b>Total assets</b>	<b>\$ 435</b>	<b>\$ 409</b>	<b>\$ 1</b>	<b>\$ 25</b>
<b>Liabilities:</b>				
Electricity commodity derivatives	\$ 4	\$	\$ 4	\$
Foreign exchange derivatives	16		16	
Interest rate derivatives	42		42	
<b>Total liabilities</b>	<b>\$ 62</b>	<b>\$</b>	<b>\$ 62</b>	<b>\$</b>

## WASTE MANAGEMENT, INC.

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Fair Value Measurements at December 31, 2011 Using				
	Total	Quoted Prices in Active Markets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
<b>Assets:</b>				
Cash equivalents	\$ 120	\$ 120	\$	\$
Available-for-sale securities	179	154		25
Interest rate derivatives	73		73	
Electricity commodity derivatives	5		5	
Total assets	\$ 377	\$ 274	\$ 78	\$ 25
<b>Liabilities:</b>				
Interest rate derivatives	\$ 74	\$	\$ 74	\$
Foreign exchange derivatives	2		2	
Total liabilities	\$ 76	\$	\$ 76	\$

**Fair Value of Available-for-sale Securities** The available-for-sale securities measured using Level 1 inputs are primarily included in long-term Other assets in our Condensed Consolidated Balance Sheets. The fair value of available-for-sale securities measured using Level 3 inputs consists of redeemable preferred stock that was acquired in November 2011 and is included in Investments in unconsolidated entities in our Condensed Consolidated Balance Sheets. The redeemable preferred stock is recorded at fair value based on other third-party investors' recent or pending transactions in these securities, which are considered to be the best evidence of fair value currently available. When this evidence is not available, we use other valuation techniques as appropriate and available. These valuation methodologies may include transactions in similar instruments, discounted cash flow techniques, third-party appraisals or industry multiples and public comparables.

**Fair Value of Debt**

At September 30, 2012, the carrying value of our debt was approximately \$10.0 billion compared with \$9.8 billion at December 31, 2011. The carrying value of our debt includes adjustments associated with fair value hedge accounting related to our interest rate swaps as discussed in Note 4.

The estimated fair value of our debt was approximately \$11.5 billion at September 30, 2012 and approximately \$10.8 billion at December 31, 2011. The estimated fair value of our senior notes is based on quoted market prices. The carrying value of remarketable debt and borrowings under our revolving credit facilities approximates fair value due to the short-term nature of the interest rates. The fair value of our other debt is estimated using discounted cash flow analysis, based on current market rates for similar types of instruments. The increase in the fair value of our debt when comparing September 30, 2012 with December 31, 2011 is attributable to net borrowings during 2012, increases in market prices for corporate debt securities and decreases in current market rates on fixed-rate tax-exempt bonds.

Although we have determined the estimated fair value amounts using available market information and commonly accepted valuation methodologies, considerable judgment is required in interpreting market data to develop the estimates of fair value. Accordingly, our estimates are not necessarily indicative of the amounts that we, or holders of the instruments, could realize in a current market exchange. The use of different assumptions and/or estimation methodologies could have a material effect on the estimated fair values. The fair value estimates are based on Level 2 inputs of the fair value hierarchy available as of September 30, 2012 and December 31, 2011. These amounts have not been revalued since those dates, and current estimates of fair value could differ significantly from the amounts presented.



WASTE MANAGEMENT, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

**13. Variable Interest Entities**

Following is a description of our financial interests in variable interest entities that we consider significant, including (i) those for which we have determined that we are the primary beneficiary of the entity and, therefore, have consolidated the entities into our financial statements; and (ii) those that represent a significant interest in an unconsolidated entity.

*Consolidated Variable Interest Entities*

*Waste-to-Energy LLCs* In June 2000, two limited liability companies were established to purchase interests in existing leveraged lease financings at three waste-to-energy facilities that we lease, operate and maintain. We own a 0.5% interest in one of the LLCs ( *LLC I* ) and a 0.25% interest in the second LLC ( *LLC II* ). John Hancock Life Insurance Company ( *Hancock* ) owns 99.5% of *LLC I* and 99.75% of *LLC II* is owned by *LLC I* and the CIT Group ( *CIT* ). In 2000, Hancock and CIT made an initial investment of \$167 million in the LLCs, which was used to purchase the three waste-to-energy facilities and assume the seller's indebtedness. Under the LLC agreements, the LLCs shall be dissolved upon the occurrence of any of the following events: (i) a written decision of all members of the LLCs; (ii) December 31, 2063; (iii) a court's dissolution of the LLCs; or (iv) the LLCs ceasing to own any interest in the waste-to-energy facilities.

Income, losses and cash flows of the LLCs are allocated to the members based on their initial capital account balances until Hancock and CIT achieve targeted returns; thereafter, we will receive 80% of the earnings of each of the LLCs and Hancock and CIT will be allocated the remaining 20% proportionate to their respective equity interests. All capital allocations made through September 30, 2012 have been based on initial capital account balances as the target returns have not yet been achieved.

Our obligations associated with our interests in the LLCs are primarily related to the lease of the facilities. In addition to our minimum lease payment obligations, we are required to make cash payments to the LLCs for differences between fair market rents and our minimum lease payments. These payments are subject to adjustment based on factors that include the fair market value of rents for the facilities and lease payments made through the re-measurement dates. In addition, we may also be required under certain circumstances to make capital contributions to the LLCs based on differences between the fair market value of the facilities and defined termination values as provided for in the underlying lease agreements, although we believe the likelihood of the occurrence of these circumstances is remote.

We have determined that we are the primary beneficiary of the LLCs and consolidate these entities in our Consolidated Financial Statements because (i) all of the equity owners of the LLCs are considered related parties for purposes of applying this accounting guidance; (ii) the equity owners share power over the significant activities of the LLCs; and (iii) we are the entity within the related party group whose activities are most closely associated with the LLCs.

As of September 30, 2012 and December 31, 2011, our Condensed Consolidated Balance Sheets included \$299 million and \$308 million, respectively, of net property and equipment associated with the LLCs' waste-to-energy facilities and \$250 million and \$246 million, respectively, in noncontrolling interests associated with Hancock's and CIT's interests in the LLCs. As of September 30, 2012 and December 31, 2011, all debt obligations of the LLCs had been paid in full and, therefore, the LLCs had no liabilities. We recognized reductions in earnings of \$9 million and \$34 million for the three and nine months ended September 30, 2012 respectively, and \$13 million and \$38 million for the three and nine months ended September 30, 2011, respectively, for Hancock's and CIT's noncontrolling interests in the LLCs' earnings. The LLCs' earnings relate to the rental income generated from leasing the facilities to our subsidiaries, reduced by depreciation expense. The LLCs' rental income is eliminated in WM's consolidation.



WASTE MANAGEMENT, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

*Significant Unconsolidated Variable Interest Entities*

*Investment in U.K. Waste-to-Energy and Recycling Entity* In the first quarter of 2012, we established a U.K. limited liability company (the Ltd. ) along with our joint venture partner, a commercial entity in the waste management industry, to develop, construct, operate and maintain a waste-to-energy and recycling facility in England. We own a 50% interest in this joint venture. The total cost of constructing this facility is expected to be £200 million, or \$323 million based on the exchange rate as of September 30, 2012. The Ltd. will be funded primarily through loans from the joint venture partners and loans under the Ltd. 's credit facility agreements with third-party financial institutions. The funds loaned under the credit facility agreements will be used for the development and construction of the facility. We are committed to provide up to £57 million, or \$92 million based on the exchange rate as of September 30, 2012, of funding to the Ltd. Our actual commitment may be more or less depending on the actual cost of the facility. Through September 30, 2012, we had funded approximately £7 million, or \$11 million, through loans and less than \$1 million through equity contributions. These amounts are included in our Condensed Consolidated Balance Sheet as long-term Other assets and Investments in unconsolidated entities, respectively. In addition to the funding commitments described above, the Ltd. has entered into certain foreign currency and interest rate derivatives at the direction of the authority. The impacts of gains or losses incurred on these derivatives will ultimately be remitted to or recoverable from the authority under the terms of the project, and accordingly, are not reflected in our equity in net losses of unconsolidated entities. We also have guaranteed the performance of certain management services for the project for which our maximum exposure under the guarantee is not material.

In addition, a wholly-owned subsidiary of the Company will be responsible for constructing the waste-to-energy facility for the Ltd. under a fixed-price construction contract. Once the facility is constructed, a majority-owned subsidiary of the Company will be responsible for operating and maintaining the facility for the Ltd. under a substantially fixed-price operating and maintenance contract. Under the operating and maintenance contract, we have guaranteed our ability to operate this facility at certain performance levels that we believe are within our control to achieve. We also will be jointly responsible, along with our Ltd. joint venture partner, for the performance of sales and marketing services for the Ltd. through a 50%-owned and unconsolidated entity. The fixed-price components of the above-mentioned contracts were established based on estimates of expected construction, operation and maintenance costs. However, we are subject to variation in our expected profits or potential losses if the actual costs differ from the costs established in the contracts. Our maximum exposure to loss under these contracts cannot be quantified.

We determined that we are not the primary beneficiary of the Ltd. as all decision-making responsibility is shared jointly with our joint venture partner. As such, we do not have the power to individually direct the entity 's activities. Accordingly, we account for this investment under the equity method of accounting and do not consolidate this entity.

*Investment in Refined Coal Facility* In January 2011, we acquired a noncontrolling interest in a limited liability company, which was established to invest in and manage a refined coal facility. Along with the other equity investor, we support the operations of the entity in exchange for a pro-rata share of the tax credits it generates. Our initial consideration for this investment consisted of a cash payment of \$48 million. As of September 30, 2012 and December 31, 2011, our investment balance was \$27 million and \$35 million, respectively, representing our current maximum pre-tax exposure to loss. Under the terms and conditions of the transaction, we do not believe that we have any material exposure to loss. Future contributions will commence once certain levels of tax credits have been generated and will continue through the expiration of the tax credits under Section 45 of the Internal Revenue Code, which occurs at the end of 2019. We are only obligated to make future contributions to the extent tax credits are generated. We determined that we are not the primary beneficiary of this entity as we do not have the power to individually direct the entity 's activities. Accordingly, we account for this investment under the equity method of accounting and do not consolidate the entity. Additional information related to this investment is discussed in Note 5.

**WASTE MANAGEMENT, INC.**

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

*Investment in Federal Low-income Housing Tax Credits* In April 2010, we acquired a noncontrolling interest in a limited liability company established to invest in and manage low-income housing properties. We support the operations of the entity in exchange for a pro-rata share of the tax credits it generates. Our target return on the investment is guaranteed and, therefore, we do not believe that we have any material exposure to loss. Our consideration for this investment totaled \$221 million, which was comprised of a \$215 million note payable and an initial cash payment of \$6 million. As of September 30, 2012 and December 31, 2011, our investment balance was \$160 million and \$178 million, respectively, and our debt balance was \$158 million and \$176 million, respectively. We determined that we are not the primary beneficiary of this entity as we do not have the power to individually direct the entity's activities. Accordingly, we account for this investment under the equity method of accounting and do not consolidate the entity. Additional information related to this investment is discussed in Note 5.

*Trusts for Final Capping, Closure, Post-Closure or Environmental Remediation Obligations* We have significant financial interests in trust funds that were created to settle certain of our final capping, closure, post-closure or environmental remediation obligations. Generally, we are the sole beneficiary of these restricted balances; however, certain of the funds have been established for the benefit of both the Company and the host community in which we operate. We have determined that these trust funds are variable interest entities; however, we are not the primary beneficiary of these entities because either (i) we do not have the power to direct the significant activities of the trusts or (ii) power over the trusts' significant activities is shared.

We account for the trusts for which we are the sole beneficiary as long-term Other assets in our Condensed Consolidated Balance Sheet. These trusts had a fair value of \$121 million at September 30, 2012 and \$123 million at December 31, 2011. Our interests in the trusts that have been established for the benefit of both the Company and the host community in which we operate are accounted for as investments in unconsolidated entities and receivables. These amounts are recorded in Other receivables, Investments in unconsolidated entities and long-term Other assets in our Condensed Consolidated Balance Sheet, as appropriate. Our investments and receivables related to these trusts had an aggregate carrying value of \$111 million as of September 30, 2012 and \$107 million as of December 31, 2011. We reflect our interests in the unrealized gains and losses on available-for-sale securities held by these trusts as a component of Accumulated other comprehensive income.

As the party with primary responsibility to fund the related final capping, closure, post-closure or environmental remediation activities, we are exposed to risk of loss as a result of potential changes in the fair value of the assets of the trust. The fair value of trust assets can fluctuate due to (i) changes in the market value of the investments held by the trusts and (ii) credit risk associated with trust receivables. Although we are exposed to changes in the fair value of the trust assets, we currently expect the trust funds to continue to meet the statutory requirements for which they were established.

**14. Condensed Consolidating Financial Statements**

WM Holdings has fully and unconditionally guaranteed all of WM's senior indebtedness. WM has fully and unconditionally guaranteed all of WM Holdings' senior indebtedness. None of WM's other subsidiaries have guaranteed any of WM's or WM Holdings' debt. As a result of these guarantee arrangements, we are required to present the following condensed consolidating financial information (in millions):

## WASTE MANAGEMENT, INC.

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

## CONDENSED CONSOLIDATING BALANCE SHEETS

September 30, 2012

(Unaudited)

	WM	WM Holdings	Non-Guarantor Subsidiaries	Eliminations	Consolidated
<b>ASSETS</b>					
Current assets:					
Cash and cash equivalents	\$ 270	\$	\$ 128	\$	\$ 398
Other current assets			2,261		2,261
	270		2,389		2,659
Property and equipment, net			12,518		12,518
Investments in and advances to affiliates	12,412	16,417	3,446	(32,275)	
Other assets	47	12	7,837		7,896
Total assets	\$ 12,729	\$ 16,429	\$ 26,190	\$ (32,275)	\$ 23,073
<b>LIABILITIES AND EQUITY</b>					
Current liabilities:					
Current portion of long-term debt	\$ 401	\$	\$ 425	\$	\$ 826
Accounts payable and other current liabilities	75	5	2,281		2,361
	476	5	2,706		3,187
Long-term debt, less current portion	5,923	449	2,794		9,166
Other liabilities	42		4,066		4,108
Total liabilities	6,441	454	9,566		16,461
Equity:					
Stockholders' equity	6,288	15,975	16,300	(32,275)	6,288
Noncontrolling interests			324		324
	6,288	15,975	16,624	(32,275)	6,612
Total liabilities and equity	\$ 12,729	\$ 16,429	\$ 26,190	\$ (32,275)	\$ 23,073

## WASTE MANAGEMENT, INC.

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

## CONDENSED CONSOLIDATING BALANCE SHEETS (Continued)

December 31, 2011

	WM	WM Holdings	Non-Guarantor Subsidiaries	Eliminations	Consolidated
<b>ASSETS</b>					
Current assets:					
Cash and cash equivalents	\$ 119	\$	\$ 139	\$	\$ 258
Other current assets	6		2,115		2,121
	125		2,254		2,379
Property and equipment, net			12,242		12,242
Investments in and advances to affiliates	12,006	14,905	3,033	(29,944)	
Other assets	120	12	7,816		7,948
Total assets	\$ 12,251	\$ 14,917	\$ 25,345	\$ (29,944)	\$ 22,569
<b>LIABILITIES AND EQUITY</b>					
Current liabilities:					
Current portion of long-term debt	\$ 298	\$	\$ 333	\$	\$ 631
Accounts payable and other current liabilities	124	13	2,300		2,437
	422	13	2,633		3,068
Long-term debt, less current portion	5,727	449	2,949		9,125
Other liabilities	32		3,954		3,986
Total liabilities	6,181	462	9,536		16,179
Equity:					
Stockholders' equity	6,070	14,455			20,525