Dollars in millions except per share amounts

We enter into foreign currency contracts to minimize our exposure to risk of adverse changes in currency exchange rates. We are subject to foreign exchange risk for foreign currency-denominated transactions, such as debt issued, recognized payables and receivables and forecasted transactions. At December 31, 2007, our foreign currency exposures were principally Euros, British pound sterling, Danish krone and Japanese yen.

QUANTITATIVE INFORMATION ABOUT MARKET RISK

In order to determine the changes in fair value of our various financial instruments, we use certain financial modeling techniques. We apply rate-sensitivity changes directly to our interest rate swap transactions and forward rate sensitivity to our foreign currency-forward contracts.

The changes in fair value, as discussed below, assume the occurrence of certain market conditions, which could have an adverse financial impact on AT&T and do not represent projected gains or losses in fair value that we expect to incur. Future impacts would be based on actual developments in global financial markets. We do not foresee any significant changes in the strategies used to manage interest rate risk, foreign currency rate risk or equity price risk in the near future.

Interest Rate Sensitivity The principal amounts by expected maturity, average interest rate and fair value of our liabilities that are exposed to interest rate risk are described in Notes 8 and 9. Following are our interest rate derivatives, subject to interest rate risk as of December 31, 2007. The interest rates illustrated in the interest rate swaps section of the table below refer to the average expected rates we would receive and the average expected rates we would pay based on the contracts. The notional amount is the principal amount of the debt subject to the interest rate swap contracts. The net fair value asset (liability) represents the amount we would receive or pay if we had exited the contracts as of December 31, 2007.

	Maturity							
	2008	2009	2010	2011	2012	After 2012	Total	Fair Value 12/31/07
Interest Rate Derivatives								
Interest Rate Swaps:								
Receive Fixed/Pay Variable Notional Amount	—	—	—	$1,250	$2,000	—	$3,250	$88
Variable Rate Payable[1]	4.6%	4.4%	5.1%	5.4%	5.3%	—		
Weighted-Average Fixed Rate Receivable	6.0%	6.0%	6.0%	6.0%	5.9%	—		

[1]Interest payable based on current and implied forward rates for Three or Six Month LIBOR plus a spread ranging between approximately 64 and 170 basis points.

We had fair value interest rate swaps with a notional value of $3,250 at December 31, 2007, and $5,050 at December 31, 2006, with a net carrying and fair value asset of $88 and liability of $80, respectively. The net fair value liability at December 31, 2006, was comprised of a liability of $86 and an asset of $6. Included in the fair value interest rate swap notional amount for 2006 were interest rate swaps with a notional value of $1,800, which were acquired as a result of our acquisition of BellSouth on December 29, 2006. These swaps were unwound in January 2007.

Foreign Exchange Forward Contracts The fair value of foreign exchange contracts is subject to changes in foreign currency exchange rates. For the purpose of assessing specific risks, we use a sensitivity analysis to determine the effects that market risk exposures may have on the fair value of our financial instruments and results of operations. To perform the sensitivity analysis, we assess the risk of loss in fair values from the effect of a hypothetical 10% change in the value of foreign currencies (negative change in the value of the U.S. dollar), assuming no change in interest rates. See Note 9 to the consolidated financial statements for additional information relating to notional amounts and fair values of financial instruments.

For foreign exchange forward contracts outstanding at December 31, 2007, assuming a hypothetical 10% depreciation of the U.S. dollar against foreign currencies from the prevailing foreign currency exchange rates, the fair value of the foreign exchange forward contracts (net liability) would have decreased approximately $29. Because our foreign exchange contracts are entered into for hedging purposes, we believe that these losses would be largely offset by gains on the underlying transactions.

The risk of loss in fair values of all other financial instruments resulting from a hypothetical 10% change in market prices was not significant as of December 31, 2007.

QUALITATIVE INFORMATION ABOUT MARKET RISK

Foreign Exchange Risk From time to time, we make investments in businesses in foreign countries, are paid dividends and receive proceeds from sales or borrow funds in foreign currency. Before making an investment, or in anticipation of a foreign currency receipt, we often will enter into forward foreign exchange contracts. The contracts are used to provide currency at a fixed rate. Our policy is to measure the risk of adverse currency fluctuations by calculating the potential dollar losses resulting from changes in exchange rates that have a reasonable probability of occurring. We cover the exposure that results from changes that exceed acceptable amounts. We do not speculate in foreign exchange markets.

Interest Rate Risk We issue debt in fixed and floating rate instruments. Interest rate swaps are used for the purpose of controlling interest expense by managing the mix of fixed and floating rate debt. Interest rate forward contracts are utilized to hedge interest expense related to debt financing. We do not seek to make a profit from changes in interest rates. We manage interest rate sensitivity by measuring potential increases in interest expense that would result from a probable change in interest rates. When the potential increase in interest expense exceeds an acceptable amount, we reduce risk through the issuance of fixed-rate (in lieu of variable-rate) instruments and the purchase of derivatives.

Issuer Equity Repurchases

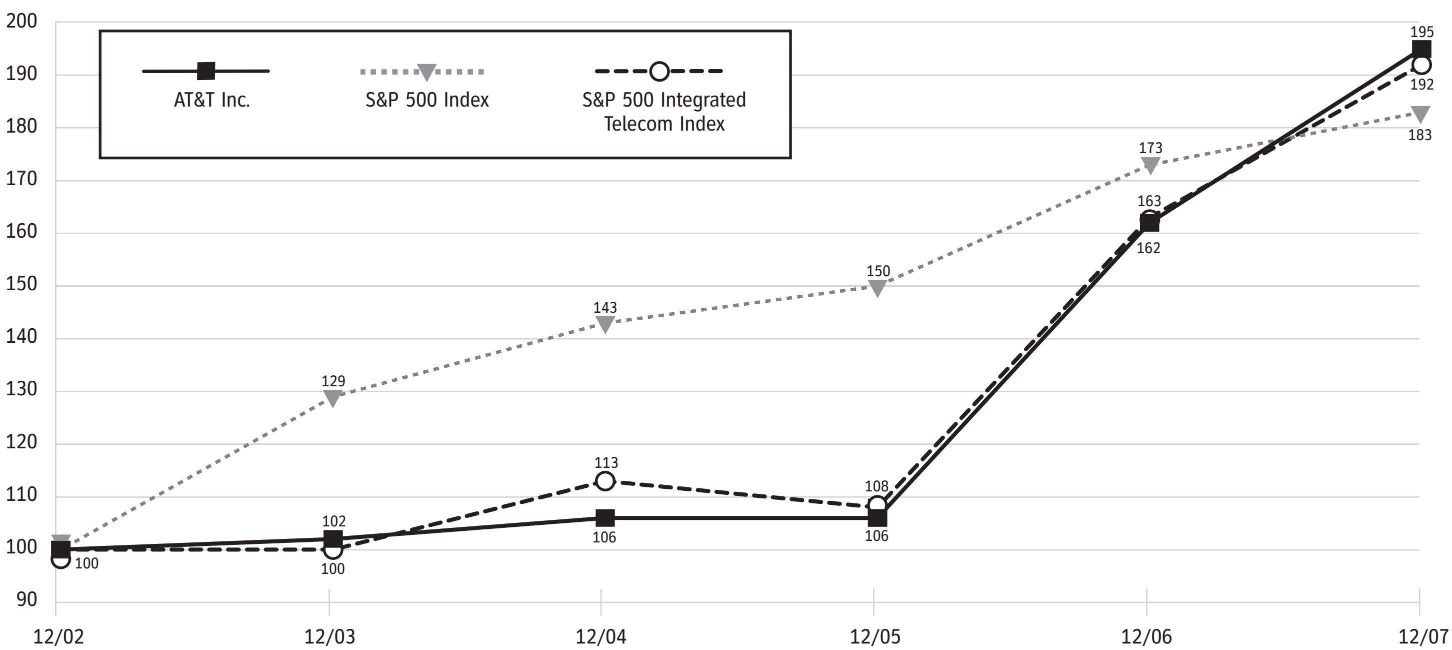
On March 4, 2006, our Board of Directors authorized the repurchase of up to 400 million shares of AT&T common stock. During the fourth quarter of 2007, we repurchased 37 million shares at a cost of $1,478. Share repurchases under this plan totaled approximately 351 million shares at a cost of $13,068. On December 10, 2007, our Board of Directors authorized a new share repurchase plan of 400 million shares, which replaces our previous share repurchase authorization. This new authorization represents approximately 6.6% of AT&T's shares outstanding at December 31, 2007 and expires at the end of 2009.
We have repurchased, and intend to continue to repurchase, a portion of the shares pursuant to plans that comply with the requirements of Rule 10b5-1(c) under the Securities Exchange Act of 1934. We will fund our share repurchases through a combination of cash from operations, borrowings dependent upon market conditions, and cash from the disposition of certain non-strategic investments.

Purchase Period	Total Number of Shares Purchased	Average Price Paid per Share[1]	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs	Maximum Number of Shares that May Yet Be Purchased Under the Plans or Programs[2]
October 1, 2007 – October 31, 2007	11,500,000	$41.94	11,500,000	74,708,783
November 1, 2007 – November 30, 2007	23,500,000	$39.13	23,500,000	51,208,783
December 3, 2007 – December 5, 2007	2,000,000	$37.81	2,000,000	49,208,783
Total	37,000,000	$39.93	37,000,000	49,208,783

[1]Average Price Paid per Share excludes transaction costs.
[2]Replaced by new authorization on December 10, 2007.

STOCK PERFORMANCE GRAPH

Comparison of Five-Year Cumulative Total Return
AT&T Inc., S&P 500 Index and S&P 500 Integrated Telecom Index



The comparison above assumes $100 invested on December 31, 2002, in AT&T common stock, Standard & Poor's 500 Index (S&P 500), and Standard & Poor's 500 Integrated Telecom Index (Telecom Index). Total return equals stock price appreciation plus reinvestment of dividends on a quarterly basis.

CERTIFICATION BY THE CHIEF EXECUTIVE OFFICER

As required under the rules of the New York Stock Exchange (NYSE), our chief executive officer has timely submitted to the NYSE his annual certification that he is not aware of any violation by the company of NYSE corporate governance standards. Also as required under the rules of the NYSE, readers are advised that the certifications required under Section 302 of the Sarbanes-Oxley Act of 2002 are not included in this report but instead are included as exhibits to our Annual Report on Form 10-K for 2007.

RISK FACTORS

In addition to the other information set forth in this document, including the matters contained under the caption "Cautionary Language Concerning Forward-Looking Statements," you should carefully read the matters described below. We believe that each of these matters could materially affect our business. We recognize that most of these factors are beyond our ability to control and therefore to predict an outcome. Accordingly, we have organized them by first addressing general factors, then industry factors and, finally, items specifically applicable to us.

Adverse changes in the U.S. economy could materially hamper our customers' abilities to purchase our products and services.

We provide services and products to consumers and large and small businesses in the United States and to larger businesses throughout the world. While our wireless customers are located throughout the United States, our wireline consumer and small business customers are located in the 22 states in which we provide local exchange services. Adverse changes in the U.S. economy are likely to adversely affect these customers' ability to pay for existing services and to decrease their interest in purchasing new services. Should this customer pullback occur, we likely would experience both a decrease in revenues and an increase in certain expenses, including expenses relating to bad debt. We are also likely to experience pressure on pricing and margins as we continue to compete for customers who would have less discretionary income. While our large-business customers are less likely to be affected by adverse changes in any particular economy, a lengthy U.S. or a global recession would tend to affect them in a similar manner.

Adverse changes in medical costs and the U.S. securities markets and interest rates could materially increase our benefit plan costs.

Our pension and postretirement costs are subject to increases, primarily due to continuing increases in medical and prescription drug costs and can be affected by lower returns in prior years on funds held by our pension and other benefit plans, which are reflected in our financial statements over several years. Investment returns on these funds depend largely on trends in the U.S. securities markets and the U.S. economy. In calculating the annual costs included on our financial statements of providing benefits under our plans, we have made certain assumptions regarding future investment returns, medical costs and interest rates. If actual investment returns, medical costs and interest rates are worse than those previously assumed, our annual costs will increase.

The FASB required companies to recognize the funded status of defined benefit pension and postretirement plans as an asset or liability in our statement of financial position and to recognize changes in that funded status in the year in which the changes occur through comprehensive income. Therefore, an increase in our costs will have a negative effect on our balance sheet.

Changes in available technology could increase competition and our capital costs.

The telecommunications industry has experienced rapid changes in the last several years. The development of wireless, cable and IP technologies has significantly increased the commercial viability of alternatives to traditional wireline telephone service and enhanced the capabilities of wireless networks. In order to remain competitive, we have begun to deploy a more sophisticated wireline network and continue to deploy a more sophisticated wireless network, as well as research other new technologies. If the new technologies we have adopted or on which we have focused our research efforts fail to be cost-effective and accepted by customers, our ability to remain competitive could be materially adversely affected.

Changes to federal, state and foreign government regulations and decisions in regulatory proceedings could materially adversely affect us.

Our wireline subsidiaries are subject to significant federal and state regulation while many of our competitors are not. In addition, our subsidiaries and affiliates operating outside the U.S. are also subject to the jurisdiction of national and supranational regulatory authorities in the market where service is provided. Our wireless subsidiaries are regulated to varying degrees by the FCC and some state and local agencies. The adoption of new regulations or changes to existing regulations could significantly increase our costs, which either would reduce our operating margins or potentially increase customer turnover should we attempt to increase prices to cover our increased costs. In addition, the development of new technologies, such as IP-based services, has created or potentially could create conflicting regulation between the FCC and various state and local authorities, which may involve lengthy litigation to resolve and may result in outcomes unfavorable to us.

Increasing competition in our wireline markets could adversely affect wireline operating margins.

We expect competition in the telecommunications industry to continue to intensify. We expect this competition will continue to put pressure on pricing, margins and customer retention. A number of our competitors that rely on alternative technologies (e.g., wireless, cable and VoIP) are typically subject to less (or no) regulation than our wireline and ATTC subsidiaries and therefore are able to operate with lower costs. These competitors also have cost advantages compared to us, due in part to a nonunionized workforce, lower employee benefits and fewer retirees (as most of the competitors are relatively new companies). We believe such advantages can be offset by continuing to increase the efficiency of our operating systems and by improving employee training and productivity; however, there can be no guarantee that our efforts in these areas will be successful.

Increasing competition in the wireless industry could adversely affect our operating results.

On average, we have three to four other wireless competitors in each of our service areas and compete for customers based principally on price, service offerings, call quality, coverage area and customer service. In addition, we are likely to experience growing competition from providers offering services using alternative wireless technologies and IP-based networks as well as traditional wireline networks. We expect intense industry competition and market saturation may cause the wireless industry's customer growth rate to moderate in comparison with historical growth rates. We expect that the availability of additional 700 MHz spectrum to be licensed through the FCC's ongoing spectrum auction could increase competition, the effectiveness of existing competition, or result in new entrants in the wireless arena. This competition will continue to put pressure on pricing and margins as companies compete for potential customers. Our ability to respond will depend, among other things, on continued improvement in network quality and customer service and effective marketing of attractive products and services, and cost management. These efforts will involve significant expenses and require strategic management decisions on, and timely implementation of equipment choices, marketing plans and financial budgets.

Equipment failures, natural disasters and terrorist attacks may materially adversely affect our operations.

Major equipment failures or natural disasters, including severe weather, terrorist acts or other breaches of network or IT security that affect our wireline and wireless networks, including telephone switching offices, microwave links, third-party owned local and long-distance networks on which we rely, our cell sites or other equipment, could have a material adverse effect on our operations. While we have insurance coverage for some of these events, our inability to operate our wireline or wireless systems, even for a limited time period, may result in significant expenses, a loss of customers or impair our ability to attract new customers, which could have a material adverse effect on our business, results of operations and financial condition.

The success of our U-verse services initiative will depend on the timing, extent and cost of deployment; the development of attractive and profitable service offerings; the extent to which regulatory, franchise fees and build-out requirements apply to this initiative; and the availability and reliability of the various technologies required to provide such offerings.

The trend in telecommunications technology is to shift from the traditional circuit- and wire-based technology to IP-based technology. IP-based technology can transport voice and data, as well as video, from both wired and wireless networks. IP-based networks also potentially cost less to operate than traditional networks. Our competitors, many of which are newer companies, are deploying this IP-based technology. In order to continue to offer attractive and competitively priced services, we are deploying a new broadband network to offer IP-based voice, data and video services. Using a new and sophisticated technology on a very large scale entails risks but also presents opportunities to expand service offerings to customers. Should deployment of our network be delayed or costs exceed expected amounts, our margins would be adversely affected and such effects could be material. Should regulatory requirements be different than we anticipated, our deployment could be delayed, perhaps significantly, or limited to only those geographical areas where regulation is not burdensome. In addition, should the delivery of services expected to be deployed on our network be delayed due to technological or regulatory constraints, performance of suppliers, or other reasons, or the cost of providing such services becomes higher than expected, customers may decide to purchase services from our competitors, which would adversely affect our revenues and margins, and such effects could be material.

The impact of our year-end 2006 acquisition of BellSouth, including the risk that the businesses will not be integrated successfully; the risk that the cost-savings and any other synergies from the acquisition may take longer to realize than expected or may not be fully realized; and disruption from the acquisition may make it more difficult to maintain relationships with customers, employees or suppliers.

We acquired BellSouth in order to streamline the ownership and operations of AT&T Mobility and to combine the AT&T Mobility, BellSouth and AT&T IP networks into a single IP network; to speed the deployment, and at lower cost, of next-generation IP video and other services; to provide business customers with the benefits of combining AT&T's national and international networks and services with BellSouth's local exchange and broadband services; and to create potential cost-savings, technological development and other benefits. Achieving these results will depend in part on successfully integrating three large corporations, which could involve significant management attention and create uncertainties for employees. To date, this integration has proceeded on schedule and within our budget assumptions. We have not experienced any significant customer or supplier disruptions. However, this process is lengthy and we expect that it will continue to involve significant management attention. We also expect to incur substantial expenses related to the integration of these companies. We must integrate a large number of systems, both operational and administrative. These integration expenses may result in our taking significant charges against earnings, both cash and noncash, primarily from the amortization of intangibles. Delays in this process could have a material adverse effect on our revenues, expenses, operating results and financial condition. In addition, events outside of our control, including changes in state and federal regulation and laws as well as economic trends, also could adversely affect our ability to realize the expected benefits from this acquisition.

CAUTIONARY LANGUAGE CONCERNING FORWARD-LOOKING STATEMENTS

Information set forth in this report contains forward-looking statements that are subject to risks and uncertainties, and actual results could differ materially. Many of these factors are discussed in more detail in the "Risk Factors" section. We claim the protection of the safe harbor for forward-looking statements provided by the Private Securities Litigation Reform Act of 1995.

The following factors could cause our future results to differ materially from those expressed in the forward-looking statements:

- Adverse economic changes in the markets served by us or in countries in which we have significant investments.
- Changes in available technology and the effects of such changes including product substitutions and deployment costs.
- Increases in our benefit plans' costs including increases due to adverse changes in the U.S. and foreign securities markets, resulting in worse-than-assumed investment returns and discount rates, and adverse medical cost trends.
- The final outcome of Federal Communications Commission proceedings and reopenings of such proceedings and judicial review, if any, of such proceedings, including issues relating to access charges, broadband deployment, unbundled loop and transport elements and wireless services.
- The final outcome of regulatory proceedings in the states in which we operate and reopenings of such proceedings, and judicial review, if any, of such proceedings, including proceedings relating to interconnection terms, access charges, universal service, unbundled network elements and resale and wholesale rates, broadband deployment including our U-verse services, performance measurement plans, service standards and traffic compensation.
- Enactment of additional state, federal and/or foreign regulatory and tax laws and regulations pertaining to our subsidiaries and foreign investments.
- Our ability to absorb revenue losses caused by increasing competition, including offerings using alternative technologies (e.g., cable, wireless and VoIP), and our ability to maintain capital expenditures.
- The extent of competition and the resulting pressure on access line totals and wireline and wireless operating margins.
- Our ability to develop attractive and profitable product/service offerings to offset increasing competition in our wireless and wireline markets.
- The ability of our competitors to offer product/service offerings at lower prices due to lower cost structures and regulatory and legislative actions adverse to us, including state regulatory proceedings relating to unbundled network elements and nonregulation of comparable alternative technologies (e.g., VoIP).
- The timing, extent and cost of deployment of our U-verse services (our Lightspeed initiative); the development of attractive and profitable service offerings; the extent to which regulatory, franchise fees and build-out requirements apply to this initiative; and the availability, cost and/or reliability of the various technologies and/or content required to provide such offerings.
- The outcome of pending or threatened litigation including patent claims by or against third parties.
- The impact on our networks and business of major equipment failures, severe weather conditions, natural disasters or terrorist attacks.
- The issuance by the Financial Accounting Standards Board or other accounting oversight bodies of new accounting standards or changes to existing standards.
- The issuance by the Internal Revenue Service and/or state tax authorities of new tax regulations or changes to existing standards and actions by federal, state or local tax agencies and judicial authorities with respect to applying applicable tax laws and regulations; and the resolution of disputes with any taxing jurisdictions.
- Our ability to adequately fund our wireless operations, including access to additional spectrum; network upgrades and technological advancements.
- The impact of our acquisition of BellSouth, including the risk that the businesses will not be integrated successfully; the risk that the cost savings and any other synergies from the acquisition may take longer to realize than expected or may not be fully realized; and disruption from the acquisition may make it more difficult to maintain relationships with customers, employees or suppliers.
- Changes in our corporate strategies, such as changing network requirements or acquisitions and dispositions, to respond to competition and regulatory, legislative and technological developments.

Readers are cautioned that other factors discussed in this report, although not enumerated here, also could materially affect our future earnings.

Consolidated Statements of Income

Dollars in millions except per share amounts

	2007	2006	2005
Operating Revenues			
Voice	**$ 40,798**	$33,714	$24,180
Data	**23,206**	18,317	10,783
Wireless service	**38,568**	223	35
Directory	**4,806**	3,634	3,625
Other	**11,550**	7,167	5,141
Total operating revenues	**118,928**	63,055	43,764
Operating Expenses			
Cost of services and sales (exclusive of depreciation and amortization shown separately below)	**46,055**	28,542	19,173
Selling, general and administrative	**30,892**	14,318	10,780
Depreciation and amortization	**21,577**	9,907	7,643
Total operating expenses	**98,524**	52,767	37,596
Operating Income	**20,404**	10,288	6,168
Other Income (Expense)			
Interest expense	**(3,507)**	(1,843)	(1,456)
Equity in net income of affiliates	**692**	2,043	609
Other income (expense) – net	**615**	393	397
Total other income (expense)	**(2,200)**	593	(450)
Income Before Income Taxes	**18,204**	10,881	5,718
Income taxes	**6,253**	3,525	932
Net Income	**$ 11,951**	$ 7,356	$ 4,786
Basic Earnings Per Share	**$ 1.95**	$ 1.89	$ 1.42
Diluted Earnings Per Share	**$ 1.94**	$ 1.89	$ 1.42

The accompanying notes are an integral part of the consolidated financial statements.

Consolidated Balance Sheets

Dollars in millions except per share amounts

	December 31,	
	2007	2006
Assets		
Current Assets		
Cash and cash equivalents	**$ 1,970**	$ 2,418
Accounts receivable – net of allowances for uncollectibles of $1,364 and $1,276	**16,185**	16,194
Prepaid expenses	**1,524**	1,477
Deferred income taxes	**2,044**	3,034
Other current assets	**2,963**	2,430
Total current assets	**24,686**	25,553
Property, Plant and Equipment – Net	**95,890**	94,596
Goodwill	**70,713**	67,657
Licenses	**37,985**	34,252
Customer Lists and Relationships – Net	**14,505**	18,922
Other Intangible Assets – Net	**5,912**	6,566
Investments in Equity Affiliates	**2,270**	1,995
Postemployment Benefit	**17,291**	14,228
Other Assets	**6,392**	6,865
Total Assets	**$275,644**	$270,634
Liabilities and Stockholders' Equity		
Current Liabilities		
Debt maturing within one year	**$ 6,860**	$ 9,733
Accounts payable and accrued liabilities	**21,399**	22,106
Advanced billing and customer deposits	**3,571**	3,402
Accrued taxes	**5,027**	3,026
Dividends payable	**2,417**	2,215
Total current liabilities	**39,274**	40,482
Long-Term Debt	**57,255**	50,063
Deferred Credits and Other Noncurrent Liabilities		
Deferred income taxes	**24,939**	27,406
Postemployment benefit obligation	**24,011**	28,901
Unamortized investment tax credits	**150**	181
Other noncurrent liabilities	**14,648**	8,061
Total deferred credits and other noncurrent liabilities	**63,748**	64,549
Stockholders' Equity		
Common shares ($1 par value, 7,000,000,000 authorized: issued 6,495,231,088 at December 31, 2007 and 2006)	**6,495**	6,495
Capital in excess of par value	**91,638**	91,352
Retained earnings	**33,297**	30,375
Treasury shares (451,685,839 at December 31, 2007 and 256,484,793 at December 31, 2006, at cost)	**(15,683)**	(7,368)
Accumulated other comprehensive loss	**(380)**	(5,314)
Total stockholders' equity	**115,367**	115,540
Total Liabilities and Stockholders' Equity	**$275,644**	$270,634

The accompanying notes are an integral part of the consolidated financial statements.

Consolidated Statements of Cash Flows

Dollars in millions, increase (decrease) in cash and cash equivalents

	2007	2006	2005
Operating Activities			
Net income	**$ 11,951**	$ 7,356	$ 4,786
Adjustments to reconcile net income to net cash provided by operating activities:			
Depreciation and amortization	**21,577**	9,907	7,643
Undistributed earnings from investments in equity affiliates	**(297)**	(1,946)	(451)
Provision for uncollectible accounts	**1,617**	586	744
Amortization of investment tax credits	**(31)**	(28)	(21)
Deferred income tax benefit	**(240)**	(87)	(658)
Net gain on sales of investments	**(11)**	(10)	(135)
Gain on license exchange	**(409)**	—	—
Changes in operating assets and liabilities:			
Accounts receivable	**(1,491)**	519	(94)
Other current assets	**(1,020)**	30	34
Accounts payable and accrued liabilities	**672**	(2,213)	74
Stock-based compensation tax benefit	**(173)**	(18)	(3)
Other – net	**1,927**	1,519	1,055
Total adjustments	**22,121**	8,259	8,188
Net Cash Provided by Operating Activities	**34,072**	15,615	12,974
Investing Activities			
Construction and capital expenditures	**(17,717)**	(8,320)	(5,576)
Net investments in affiliates	**—**	(1,104)	2,436
Dispositions	**1,594**	756	526
Acquisitions, net of cash acquired	**(2,873)**	368	1,504
Proceeds from sale of marketable securities	**471**	—	—
Proceeds from sale of debt and equity securities	**562**	—	—
Investments in debt and equity securities	**(579)**	—	—
Maturities of held-to-maturity securities	**—**	—	99
Proceeds from note repayment	**—**	—	37
Other	**36**	7	—
Net Cash Used in Investing Activities	**(18,506)**	(8,293)	(974)
Financing Activities			
Net change in short-term borrowings with original maturities of three months or less	**(3,411)**	3,649	(4,119)
Issuance of long-term debt	**11,367**	1,491	1,973
Repayment of long-term debt	**(6,772)**	(4,242)	(2,682)
Purchase of treasury shares	**(10,390)**	(2,678)	(1,843)
Issuance of treasury shares	**1,986**	589	432
Repurchase of preferred shares of subsidiaries	**—**	—	(728)
Dividends paid	**(8,743)**	(5,153)	(4,256)
Stock-based compensation tax benefit	**173**	18	3
Other	**(224)**	198	(6)
Net Cash Used in Financing Activities	**(16,014)**	(6,128)	(11,226)
Net increase (decrease) in cash and cash equivalents from continuing operations	**(448)**	1,194	774
Net Cash Used in Operating Activities From Discontinued Operations	**—**	—	(310)
Net increase (decrease) in cash and cash equivalents	**(448)**	1,194	464
Cash and cash equivalents beginning of year	**2,418**	1,224	760
Cash and Cash Equivalents End of Year	**$ 1,970**	$ 2,418	$ 1,224

The accompanying notes are an integral part of the consolidated financial statements.

Consolidated Statements of Stockholders' Equity

Dollars and shares in millions except per share amounts

	2007		2006		2005	
	Shares	**Amount**	Shares	Amount	Shares	Amount
Common Stock						
Balance at beginning of year	**6,495**	**$ 6,495**	4,065	$ 4,065	3,433	$ 3,433
Issuance of shares	**—**	**—**	2,430	2,430	632	632
Balance at end of year	**6,495**	**$ 6,495**	6,495	$ 6,495	4,065	$ 4,065
Capital in Excess of Par Value						
Balance at beginning of year		**$ 91,352**		$27,499		$13,350
Issuance of shares		**225**		63,637		14,087
Stock-based compensation		**61**		216		62
Balance at end of year		**$ 91,638**		$91,352		$27,499
Retained Earnings						
Balance at beginning of year		**$ 30,375**		$29,106		$28,806
Net income ($1.94, $1.89 and $1.42 per share)		**11,951**		7,356		4,786
Dividends to stockholders ($1.47, $1.35 and $1.30 per share)		**(8,945)**		(6,079)		(4,480)
Adoption of FIN 48		**(50)**		—		—
Other		**(34)**		(8)		(6)
Balance at end of year		**$ 33,297**		$30,375		$29,106
Treasury Shares						
Balance at beginning of year	**(256)**	**$ (7,368)**	(188)	$ (5,406)	(132)	$ (4,535)
Purchase of shares	**(267)**	**(10,390)**	(84)	(2,678)	(76)	(1,843)
Issuance of shares	**72**	**2,075**	16	716	20	972
Balance at end of year	**(451)**	**$(15,683)**	(256)	$ (7,368)	(188)	$ (5,406)
Additional Minimum Pension Liability Adjustment						
Balance at beginning of year		**$ —**		$ (218)		$ (190)
Required adjustments, net of tax $6 and $(17)		**—**		10		(28)
Adoption of FAS 158		**—**		208		—
Balance at end of year		**$ —**		$ —		$ (218)
Accumulated Other Comprehensive Income (Loss), net of tax						
Balance at beginning of year		**$ (5,314)**		$ (356)		$ (360)
Foreign currency translation adjustments, net of taxes of $10, $9 and $27		**19**		17		50
Net unrealized gains (losses) on securities:						
Unrealized gains, net of taxes of $35, $7 and $3		**65**		13		5
Less reclassification adjustment realized in net income, net of taxes of $(19), $(4) and $(30)		**(35)**		(8)		(56)
Net unrealized gains (losses) on cash flow hedges:						
Unrealized gains (losses), net of taxes of $(38), $2 and $(1)		**(71)**		2		(1)
Less reclassification adjustment realized in net income, net of taxes of $9, $8 and $3		**17**		15		7
Defined benefit postretirement plans (see Note 11):						
Net actuarial gains and prior service cost arising during period, net of taxes of $3,411		**4,734**		—		—
Amortization of net actuarial loss and prior service benefit included in net income, net of taxes of $125		**206**		—		—
Other		**(1)**		2		(1)
Other comprehensive income		**4,934**		41		4
Adoption of FAS 158, net of tax		**—**		(4,999)		—
Balance at end of year		**$ (380)**		$ (5,314)		$ (356)
Total Comprehensive Income						
Net income		**$ 11,951**		$ 7,356		$ 4,786
Additional minimum pension liability adjustments per above		**—**		10		(28)
Other comprehensive income per above		**4,934**		41		4
Total Comprehensive Income		**$ 16,885**		$ 7,407		$ 4,762

The accompanying notes are an integral part of the consolidated financial statements.

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of Presentation Throughout this document, AT&T Inc. is referred to as “AT&T,” “we” or the “Company.” The consolidated financial statements include the accounts of the Company and our majority-owned subsidiaries and affiliates. Our subsidiaries and affiliates operate in the communications services industry throughout the U.S. and internationally, providing wireless and wireline telecommunications services and equipment as well as directory advertising and publishing services. On December 29, 2006, we acquired 100% of the outstanding common shares of BellSouth Corporation (BellSouth). BellSouth is a wholly-owned subsidiary, and the results of BellSouth’s operations have been included in our consolidated financial statements after the December 29, 2006 acquisition date. For a detailed discussion of our acquisition, see Note 2.

All significant intercompany transactions are eliminated in the consolidation process. Investments in partnerships, joint ventures, and less-than-majority-owned subsidiaries where we have significant influence are accounted for under the equity method. Prior to the closing of the BellSouth acquisition on December 29, 2006, we accounted for our joint ventures with BellSouth under the equity method since we shared control equally. Thus, for 2006 we recorded as equity income our proportionate share of economic ownership in these joint ventures, namely, 60% of AT&T Mobility LLC (AT&T Mobility), formerly Cingular Wireless LLC, and 66% of YELLOWPAGES.COM (YPC). AT&T Mobility and YPC became wholly-owned subsidiaries of AT&T on December 29, 2006. Earnings from certain foreign equity investments accounted for using the equity method are included for periods ended within up to one month of our year end (see Note 7).

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

FAS 159 In February 2007, the Financial Accounting Standards Board (FASB) issued Statement of Financial Accounting Standards No. 159, “The Fair Value Option for Financial Assets and Financial Liabilities” (FAS 159). FAS 159 permits companies to choose to measure many financial instruments and certain other items at fair value, providing the opportunity to mitigate volatility in reported earnings caused by measuring related assets and liabilities differently without having to apply complex hedge accounting provisions. FAS 159 is effective for fiscal years beginning after November 15, 2007. We elected not to adopt the fair value option for valuation of those assets and liabilities which are eligible, therefore there is no impact on our financial position and results of operations.

FAS 160 In December 2007, the FASB issued Statement of Financial Accounting Standards No. 160, “Noncontrolling Interests in Consolidated Financial Statements – an amendment of ARB No. 51” (FAS 160). FAS 160 requires noncontrolling interests held by parties other than the parent in subsidiaries be clearly identified, labeled, and presented in the consolidated statement of financial position within equity, but separate from the parent’s equity. FAS 160 is effective for fiscal years beginning after December 15, 2008. We are currently evaluating the impact FAS 160 will have on our financial position and results of operations.

FAS 141(R) In December 2007, the FASB issued Statement of Financial Accounting Standards No. 141 (revised 2007), “Business Combinations” (FAS 141(R)). FAS 141(R) is a revision of FAS 141 and requires that costs incurred to effect the acquisition (i.e., acquisition-related costs) be recognized separately from the acquisition. In addition, in accordance with Statement of Financial Accounting Standards No. 141, “Business Combinations” (FAS 141), restructuring costs that the acquirer expected but was not obligated to incur, which included changes to benefit plans, were recognized as if they were a liability assumed at the acquisition date. FAS 141(R) requires the acquirer to recognize those costs separately from the business combination. We are currently evaluating the impact that FAS 141(R) will have on our accounting for acquisitions prior to the effective date of the first fiscal year beginning after December 15, 2008.

FIN 48 We adopted FASB Interpretation No. 48, “Accounting for Uncertainty in Income Taxes” (FIN 48) on January 1, 2007. FIN 48 clarifies the accounting for uncertainty in income taxes recognized in an enterprise’s financial statements in accordance with Statement of Financial Accounting Standards No. 109, “Accounting for Income Taxes.” The interpretation prescribes a threshold for the financial statement recognition and measurement of a tax position taken or expected to be taken within an income tax return. For each tax position, the enterprise must determine whether it is more likely than not that the position will be sustained upon examination based on the technical merits of the position, including resolution of any related appeals or litigation. A tax position that meets the more likely than not recognition threshold is then measured to determine the amount of benefit to recognize within the financial statements. No benefits may be recognized for tax positions that do not meet the more likely than not threshold. As required by FIN 48, on January 1, 2007, we reclassified deferred income tax liabilities of $6,225 from our “Deferred income taxes” for unrecognized tax benefits, of which $6,100 was included in “Other noncurrent liabilities” and $175 was included in “Accrued taxes” on our consolidated balance sheets and the remaining $50 was recorded as a reduction to the beginning-of-year retained earnings to reflect the cumulative effect of adoption of FIN 48 in the first quarter. In May 2007, the FASB issued further guidance on whether a tax position is effectively settled, the adoption of which did not have a material impact on our financial position.

EITF 06-11 In June 2007, the Emerging Issues Task Force (EITF) ratified the consensus on EITF 06-11, “Accounting for Income Tax Benefits of Dividends on Share-Based Payment Awards.” EITF 06-11 provides that a realized income tax benefit from dividends or dividend equivalents that are charged to retained earnings and are paid to employees for nonvested equity-classified share-based awards and equity-classified outstanding share options should be recognized as an increase to additional paid-in capital rather than a reduction of income tax expense. EITF 06-11 applies prospectively to the income tax benefits that result from dividends on equity-classified employee share-based payment awards that are declared in fiscal periods beginning after December 15, 2007. EITF 06-11 will not have a material impact on our financial position and results of operations.

Reclassifications We have reclassified certain amounts in prior-period financial statements to conform to the current period’s presentation. Included among these, as a result of