

**UNITED STATES
POSTAL REGULATORY COMMISSION
Washington, D.C. 20268-0001**

FORM 10-Q

**QUARTERLY REPORT PURSUANT TO 39 U.S.C. § 3654 AND SECTION 13 OR 15(d) OF
THE SECURITIES EXCHANGE ACT OF 1934**

For the Quarterly Period Ended June 30, 2019



UNITED STATES POSTAL SERVICE
(Exact name of registrant as specified in its charter)

Washington, D.C. 41-0760000
(State or other jurisdiction of incorporation or organization) (I.R.S. Employer Identification No.)

475 L'Enfant Plaza, S.W.
Washington, D.C. 20260
(Address of principal executive offices) (ZIP Code)

(202) 268-2000
(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 Not Applicable

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 (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes No Not Applicable

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

Large accelerated filer Accelerated filer Non-accelerated filer
Smaller reporting company Emerging growth company Not applicable

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.

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

Securities registered pursuant to Section 12(b) of the Act:

<u>Title of each class</u>	<u>Trading Symbol(s)</u>	<u>Name of each exchange on which registered</u>
Not applicable	Not applicable	Not applicable

The number of shares of common stock outstanding as of August 8, 2019: N/A

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PART I. FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

**UNITED STATES POSTAL SERVICE
STATEMENTS OF OPERATIONS
(UNAUDITED)**

<i>(in millions)</i>	Three Months Ended June 30,		Nine Months Ended June 30,	
	2019	2018	2019	2018
Revenue:				
Operating revenue	\$ 17,086	\$ 17,074	\$ 54,289	\$ 53,722
Other revenue	7	3	16	22
Total revenue	17,093	17,077	54,305	53,744
 Operating expenses:				
Compensation and benefits	10,722	10,677	33,415	32,676
Retirement benefits	2,281	2,444	6,927	7,372
Retiree health benefits	873	900	3,423	3,361
Workers' compensation	1,038	206	2,696	172
Transportation	1,968	1,882	6,310	5,940
Other operating expenses	2,451	2,427	7,345	7,487
Total operating expenses	19,333	18,536	60,116	57,008
 Loss from operations	(2,240)	(1,459)	(5,811)	(3,264)
Interest and investment income	36	33	109	82
Interest expense	(52)	(63)	(173)	(182)
Net loss	\$ (2,256)	\$ (1,489)	\$ (5,875)	\$ (3,364)

See accompanying notes to the unaudited financial statements.

**UNITED STATES POSTAL SERVICE
BALANCE SHEETS**

(in millions)

	<u>June 30, 2019</u>	<u>September 30, 2018</u>
	(Unaudited)	
Current Assets:		
Cash and cash equivalents	\$ 7,953	\$ 10,061
Restricted cash	465	275
Receivables, net	1,507	1,094
Supplies, advances and prepayments	180	153
Total current assets	10,105	11,583
Property and equipment, net	14,300	14,616
Other assets	500	489
Total assets	\$ 24,905	\$ 26,688
Current Liabilities:		
Compensation and benefits	\$ 1,815	\$ 1,774
Retirement benefits	7,630	6,011
Retiree health benefits	46,064	42,641
Workers' compensation	1,366	1,383
Payables and accrued expenses	2,053	2,217
Deferred revenue-prepaid postage	2,174	2,066
Customer deposit accounts	1,142	1,198
Other current liabilities	1,154	1,180
Current portion of debt	4,000	11,000
Total current liabilities	67,398	69,470
Workers' compensation costs, noncurrent	16,356	15,026
Employees' accumulated leave, noncurrent	2,025	1,906
Other noncurrent liabilities	720	723
Noncurrent portion of debt	7,000	2,200
Total liabilities	93,499	89,325
Net Deficiency:		
Capital contributions of the U.S. Government	3,132	3,132
Deficit since 1971 reorganization	(71,726)	(65,769)
Total net deficiency	(68,594)	(62,637)
Total liabilities and net deficiency	\$ 24,905	\$ 26,688

See accompanying notes to the unaudited financial statements.

**UNITED STATES POSTAL SERVICE
STATEMENTS OF CHANGES IN NET DEFICIENCY
(UNAUDITED)**

For the nine months ended June 30, 2018

<i>(in millions)</i>	Capital Contributions of U.S. Government	Accumulated Deficit Since Reorganization	Total Net Deficiency
Balance, September 30, 2017	\$ 3,132	\$ (61,856)	\$ (58,724)
Net loss	—	(540)	(540)
Balance, December 31, 2017	\$ 3,132	\$ (62,396)	\$ (59,264)
Net loss	—	(1,335)	(1,335)
Balance, March 31, 2018	\$ 3,132	\$ (63,731)	\$ (60,599)
Net loss	—	(1,489)	(1,489)
Balance, June 30, 2018	<u>\$ 3,132</u>	<u>\$ (65,220)</u>	<u>\$ (62,088)</u>

See accompanying notes to the unaudited financial statements.

For the nine months ended June 30, 2019

<i>(in millions)</i>	Capital Contributions of U.S. Government	Accumulated Deficit Since Reorganization	Total Net Deficiency
Balance, September 30, 2018	\$ 3,132	\$ (65,769)	\$ (62,637)
Cumulative effect adjustments for adoption of ASC 606 and ASC 405-20	—	(82)	(82)
Net loss	—	(1,537)	(1,537)
Balance, December 31, 2018	\$ 3,132	\$ (67,388)	\$ (64,256)
Net loss	—	(2,082)	(2,082)
Balance, March 31, 2019	\$ 3,132	\$ (69,470)	\$ (66,338)
Net loss	—	(2,256)	(2,256)
Balance, June 30, 2019	<u>\$ 3,132</u>	<u>\$ (71,726)</u>	<u>\$ (68,594)</u>

See accompanying notes to the unaudited financial statements.

**UNITED STATES POSTAL SERVICE
STATEMENTS OF CASH FLOWS
(UNAUDITED)**

<i>(in millions)</i>	Nine Months Ended June 30,	
	2019	2018
Cash flows from operating activities:		
Net loss	\$ (5,875)	\$ (3,364)
Adjustments to reconcile net loss to cash provided by operations:		
Depreciation and amortization	1,271	1,247
Gain on disposals of property and equipment, net	(7)	(15)
Increase in other assets	(11)	(46)
Increase (decrease) in noncurrent workers' compensation	1,330	(1,202)
Increase (decrease) in noncurrent deferred appropriations and other revenue	12	(1)
Increase (decrease) in other noncurrent liabilities	110	(32)
Changes in current assets and liabilities:		
Receivables, net	(413)	(136)
Other current assets	(27)	(8)
Retirement benefits	1,619	2,166
Retiree health benefits	3,423	3,361
Payables, accrued expenses and other	(170)	(300)
Deferred revenue-prepaid postage and other deferred revenue	(13)	(46)
Net cash provided by operating activities	1,249	1,624
Cash flows from investing activities:		
Purchases of property and equipment	(953)	(905)
Proceeds from sales of property and equipment	23	14
Net cash used in investing activities	(930)	(891)
Cash flows from financing activities:		
Issuance of notes payable	26,800	52,500
Payments on notes payable	(29,000)	(52,500)
Payments on capital lease obligations and other	(37)	(44)
Net cash used in financing activities	(2,237)	(44)
Net (decrease) increase in cash, cash equivalents and restricted cash	(1,918)	689
Cash, cash equivalents and restricted cash at beginning of period	10,336	10,804
Cash, cash equivalents and restricted cash at end of period	\$ 8,418	\$ 11,493
Supplemental cash flow disclosures:		
Cash paid for interest	\$ 169	\$ 183

See accompanying notes to the unaudited financial statements.

NOTES TO UNAUDITED FINANCIAL STATEMENTS

NOTE 1 - BASIS OF PRESENTATION

Interim Financial Statements

The accompanying unaudited interim financial statements of the United States Postal Service (the "Postal Service") have been prepared in accordance with accounting principles generally accepted in the United States ("GAAP") for interim financial information and with the instructions to Form 10-Q and Rule 10-01 of the U.S. Securities and Exchange Commission ("SEC") Regulation S-X. These financial statements should be read in conjunction with the Postal Service's financial statements for the year ended September 30, 2018, included in its Annual Report on Form 10-K ("Annual Report") filed with the Postal Regulatory Commission ("PRC") on November 14, 2018, and do not include all information and footnotes which are normally included in the Annual Report. Except as otherwise specified, all references to years are to fiscal years beginning October 1 and ending September 30, and quarters are quarters within fiscal years 2019 and 2018.

On August 17, 2018, the SEC adopted amendments to certain disclosure requirements in Securities Act Release No. 33-10532, *Disclosure Update and Simplification*. The amendments became effective on November 5, 2018. Among the amendments is the requirement to present the changes in shareholders' equity in the interim financial statements (either in a separate statement or footnote) in quarterly reports on Form 10-Q. Based on this new requirement, the Postal Service has prepared its *Statements of Changes in Net Deficiency* for the nine months ended June 30, 2019, and 2018, in a separate statement.

In the opinion of management, the accompanying unaudited interim financial statements reflect all material adjustments, including recurring adjustments, necessary to fairly present the financial position as of June 30, 2019, the results of operations for the three and nine months ended June 30, 2019, and 2018, the changes in net deficiency for the nine months ended June 30, 2019, and 2018, and cash flows for the nine months ended June 30, 2019, and 2018. Operating results for the three and nine months ended June 30, 2019, are not necessarily indicative of the results that may be expected for all of 2019. Mail volume and revenue are historically greatest in the first quarter of the year, which includes the holiday mailing season.

Reclassifications

Certain reclassifications have been made to the financial statements as of September 30, 2018, and for the three and nine months ended June 30, 2018, as well as subsequent footnotes, to conform to the current period presentation. Specifically, certain retirement benefit expenses have been reclassified from *Compensation and benefits* and separately identified as *Retirement benefits* within *Operating expenses* in the accompanying unaudited *Statements of Operations*. In addition, unfunded retirement benefits amortization expenses associated with the Civil Service Retirement System ("CSRS") and the Federal Employee Retirement System ("FERS") have been reclassified from *Unfunded retirement benefits amortization* to *Retirement benefits* within *Operating expenses* within the accompanying unaudited *Statements of Operations*.

The liabilities associated with these retirement benefits have also been reclassified from *Compensation and benefits* and separately identified as *Retirement benefits* within *Current liabilities* in the accompanying *Balance Sheets*. In addition, the unfunded retirement benefits liabilities associated with CSRS and FERS have been reclassified from *Unfunded retirement benefits* to *Retirement benefits* within *Current liabilities* in the accompanying *Balance Sheets*. Corresponding reclassifications have been made within *Changes in current assets and liabilities* in the accompanying unaudited *Statements of Cash Flows*.

These reclassifications had no effect on previously reported total operating expenses, loss from operations or net loss. See *Note 9 - Retirement Plans* for further disclosure pertaining to retirement benefits.

NOTE 2 - RECENT ACCOUNTING PRONOUNCEMENTS

Recently Adopted Accounting Pronouncements

Accounting Standards Update 2014-09 Revenue from Contracts with Customers

In May 2014, the Financial Accounting Standards Board (“FASB”) issued Accounting Standards Update 2014-09 *Revenue from Contracts with Customers*, which has since been codified in Accounting Standards Codification (“ASC”) 606, *Revenue from Contracts with Customers* (“ASC 606”). The new standard outlines a single comprehensive model for entities to use in accounting for revenue arising from contracts with customers and supersedes most current revenue recognition guidance, including industry-specific guidance. The new standard may be adopted either retrospectively or on a modified retrospective basis whereby the standard would be applied to new and existing contracts with remaining performance obligations as of the effective date, with a cumulative catch-up adjustment recorded to beginning retained earnings or net deficiency at the effective date for existing contracts with remaining performance obligations. The Postal Service adopted the standard on October 1, 2018, and applied it to all contracts using the modified retrospective approach with a cumulative catch-up adjustment recorded to net deficiency as of the beginning of fiscal year 2019.

The Postal Service evaluated the impact of the standard utilizing a comprehensive approach. To assess the impact of the guidance on its contracts with customers, the Postal Service reviewed accounting policies and practices to identify potential differences that would result from applying the new requirements to its revenue contracts, including evaluation of transfer of control, multiple-element arrangements, free goods, “breakage” (i.e., the value of prepaid postage that is ultimately not redeemed by the customer) and variable consideration. The Postal Service completed its contract analysis based on the five-step model as outlined in the authoritative literature, and quantified the impact of adopting the new standard on its financial statements.

In adopting the new standard, the Postal Service determined that the October 1, 2018, opening balance of accumulated deficit should increase to account for changes in the recognition of the breakage and mail-in-transit components of deferred revenue associated with prepaid postage. The amount of this increase was considered immaterial to the financial statements taken as a whole. See *Note 4 - Revenue Recognition* for further disclosures pertaining to ASC 606.

Accounting Standards Update 2016-04 Liabilities - Extinguishments of Liabilities

In March 2016, the FASB issued Accounting Standards Update 2016-04 *Liabilities - Extinguishments of Liabilities*, which has since been codified in ASC Subtopic 405-20, *Liabilities - Extinguishments of Liabilities* (“ASC 405-20”). The new standard requires entities that sell prepaid stored-value products redeemable for goods, services or cash at third-party merchants to recognize “breakage” as revenue on a pro-rata basis using an estimate based on past redemption patterns, consistent with how breakage is now recognized under ASC 606, discussed above. The Postal Service adopted the standard on October 1, 2018, using the modified retrospective approach with a cumulative catch-up adjustment recorded to net deficiency as of the beginning of fiscal year 2019. The standard is applicable to the Postal Service’s determinations of revenue from outstanding money orders and related breakage, which are recorded in *Other current liabilities*.

In adopting the new standard, the Postal Service quantified the impact of adopting ASC 405-20 and determined that the October 1, 2018, opening balance of accumulated deficit should decrease to account for the changes in the recognition of breakage revenue related to money orders. The amount of this decrease was considered immaterial to the financial statements taken as a whole. The opening balance of *Other current liabilities* decreased by the same amount.

Cumulative Adjustments

The Postal Service adopted ASC 606 and ASC 405-20 on October 1, 2018. The cumulative effects of changes to its accompanying unaudited *Balance Sheet* as of October 1, 2018, resulting from the adoption were as follows:

(in millions)	Balance as previously reported on September 30, 2018	Adjustments due to adoption of		Balance on October 1, 2018
		ASC 606	ASC 405-20	
Total assets	\$ 26,688	\$ —	\$ —	26,688
Current Liabilities:				
Compensation and benefits*	\$ 1,774	\$ —	\$ —	\$ 1,774
Retirement benefits*	6,011	—	—	6,011
Retiree health benefits	42,641	—	—	42,641
Workers' compensation	1,383	—	—	1,383
Payables and accrued expenses	2,217	—	—	2,217
Deferred revenue-prepaid postage	2,066	164	—	2,230
Customer deposit accounts	1,198	—	—	1,198
Other current liabilities	1,180	—	(82)	1,098
Current portion of debt	11,000	—	—	11,000
Total current liabilities	69,470	164	(82)	69,552
Total noncurrent liabilities	19,855	—	—	19,855
Total liabilities	89,325	164	(82)	89,407
Net Deficiency:				
Capital contributions of the U.S. government	3,132	—	—	3,132
Deficit since 1971 reorganization	(65,769)	(164)	82	(65,851)
Total net deficiency	(62,637)	(164)	82	(62,719)
Total liabilities and net deficiency	\$ 26,688	\$ —	\$ —	\$ 26,688

* Balances previously reported on September 30, 2018, reflect a \$460 million reclassification between *Compensation and benefits* and *Retirement benefits* as further described in Note 1 - *Basis of Presentation, Reclassifications*.

Accounting Pronouncements Issued but not Adopted

Accounting Standards Update 2016-02 Leases

In February 2016, the FASB issued Accounting Standards Update 2016-02 *Leases*, which has since been codified in ASC 842, *Leases* ("ASC 842"). The new standard requires an entity to record most leases on its balance sheets but continue to recognize expenses in the statements of operations in a manner similar to current accounting practices. The new standard states that a lessee will recognize a lease liability for the obligation to make lease payments and a right-of-use asset for the right to use the underlying asset for the lease term. Expenses related to leases determined to be operating leases will be recognized on a straight-line basis, while those determined to be finance leases will generally have higher expense in the earlier periods of the lease and both interest and amortization will be presented separately in the statements of operations.

The Postal Service intends to adopt ASC 842 for its 2020 fiscal year (beginning October 1, 2019) and the quarters therein, with early adoption permitted but not elected by the Postal Service. Entities are required to use a modified retrospective approach for leases that exist or are entered into after the beginning of the earliest comparative period in the financial statements. In July 2018, the FASB approved an additional and optional transition method that would allow adoption of the standard as of the effective date without restating prior periods, and the Postal Service has elected this transition method.

The Postal Service has substantially completed abstracting all of the necessary information to properly account for the portfolio of over 23,000 property leases of Postal Service facilities under the new standard and is continuing its analysis. In addition, the Postal Service has identified service contracts with potential embedded leases and continues the abstraction of the necessary information to properly account for these lease portfolios under ASC 842. The Postal Service is also finalizing changes to its lease accounting policies and procedures and to its related new processes, controls and new lease accounting system.

As of June 30, 2019, the Postal Service had approximately \$2.7 billion of future minimum operating lease commitments that it currently does not recognize on its balance sheet. Therefore, the Postal Service expects that the adoption will have a material effect on its balance sheet and disclosures, but an immaterial effect on its statement of operations and statement of cash flows.

Accounting Standards Update 2016-13 Financial Instruments - Credit Losses

In June 2016, the FASB issued Accounting Standards Update 2016-13 *Financial Instruments - Credit Losses*, which has since been codified in ASC 326, *Financial Instruments - Credit Losses* ("ASC 326"). The new standard requires entities to measure expected credit losses on financial instruments and other commitments by replacing the incurred loss impairment methodology in current GAAP with a methodology that reflects expected credit losses and requires consideration of a broader range of reasonable and supportable information to inform credit loss estimates.

The Postal Service intends to adopt ASC 326 for its 2021 fiscal year (beginning October 1, 2020) and the quarters therein, with early adoption permitted. The standard is applicable to the Postal Service's valuation of its receivables. The Postal Service is currently evaluating the impact of adopting this standard on its financial statements and related disclosures.

Accounting Standards Update 2018-13 Fair Value Measurement

In August 2018, the FASB issued Accounting Standards Update 2018-13 *Fair Value Measurement: Disclosure Framework - Changes to the Disclosure Requirements for Fair Value Measurement*, which has since been codified in ASC 820, *Fair Value Measurement* ("ASC 820"). The new standard modifies the disclosure requirements on fair value measurements by adding, modifying or removing certain disclosures.

The Postal Service intends to adopt ASC 820 for its 2021 fiscal year (beginning October 1, 2020) and the quarters therein, with early adoption permitted. The standard is applicable to the Postal Service's fair value measurements of its revenue forgone installment receivable and its noncurrent portion of debt, as described further in *Note 12 - Fair Value Measurement*. Under ASC 820, certain disclosures are required to be applied on a retrospective basis and others on a prospective basis. The Postal Service is currently evaluating the impact of adopting this standard on its financial statements and related disclosures.

Accounting Standards Update 2018-15 Intangibles - Goodwill and Other - Internal-Use Software

In August 2018, the FASB issued Accounting Standards Update 2018-15 *Intangibles - Goodwill and Other - Internal-Use Software (Subtopic 350-40) - Customer's Accounting for Implementation Costs Incurred in a Cloud Computing Arrangement*, which has since been codified in ASC Subtopic 350-40, *Intangibles - Goodwill and Other - Internal-Use Software* ("ASC 350-40"). This is an update to a standard the FASB issued in April 2015 for entities evaluating the accounting for fees paid by a customer in a cloud computing (hosting) arrangement by providing guidance for determining when such arrangement includes a software license.

If a cloud computing arrangement includes a license for internal-use software, then the software license is accounted for by the customer in accordance with ASC 350-40. This generally means that an intangible asset is recognized for the software license and, to the extent that the payments attributable to the software license are made over time, a liability also is recognized. If a cloud computing arrangement does not include a software license, the entity should account for the arrangement as a service contract. This generally means that the fees associated with the hosting element (service) of the arrangement are expensed as incurred.

The Postal Service intends to adopt ASC 350-40 for its 2021 fiscal year (beginning October 1, 2020) and the quarters therein, with early adoption permitted, including adoption in any interim period. The Postal Service is currently evaluating the impact of adopting this standard on its financial statements and related disclosures.

NOTE 3 - LIQUIDITY

The Postal Service's liquidity consists of unrestricted cash and cash equivalents plus available borrowing capacity.

Cash

The Postal Service generates its cash almost entirely through the sale of postal products and services. The Postal Service holds its cash with the Federal Reserve Bank of New York and invests its excess cash, when available, in highly-liquid, short-term investments issued by the U.S. Department of the Treasury. As of June 30, 2019, and September 30, 2018, the Postal Service held unrestricted cash and cash equivalents of \$8.0 billion and \$10.1 billion, respectively.

Debt

Under the *Postal Reorganization Act*, as amended by Public Laws 101-227 and 109-435 (the "PRA"), the Postal Service can issue debt obligations. Per the PRA, the Postal Service is limited by statute to net annual debt increases of \$3.0 billion, and total debt may not exceed \$15.0 billion.

In 1974, the Postal Service began issuing debt through individual debt agreements to the Federal Financing Bank ("FFB"), a government-owned corporation under the general supervision of the Secretary of the Treasury. The FFB holds all of the Postal Service's debt. In 1999, the Postal Service entered into a Note Purchase Agreement ("NPA") with the FFB to establish standardized procedures for the Postal Service to issue its debt. Under the NPA, the Postal Service can issue a series of notes with established terms and conditions by providing two days prior notice. Also under the NPA, the Postal Service can make borrowings against two annually renewable revolving credit line facilities totaling up to \$4.0 billion with interest rates determined by the U.S. Department of the Treasury each business day.

As of June 30, 2019, excluding revolving facilities, the Postal Service had a combination of fixed-rate and floating-rate notes outstanding with various maturities totaling \$7.0 billion. As of September 30, 2018, the Postal Service had fixed-rate notes outstanding with various maturities totaling \$9.2 billion.

As of both June 30, 2019, and September 30, 2018, the revolving facilities were fully drawn to \$4.0 billion and were included in the current portion of debt. These annually renewable revolving facilities were renewed on April 22, 2019, and are scheduled to expire in April 2020.

As of June 30, 2019, and September 30, 2018, the aggregate principal balance of all debt outstanding was \$11.0 billion and \$13.2 billion, respectively, which is \$4.0 billion and \$1.8 billion, respectively, below the \$15.0 billion maximum borrowing amount allowed under the Postal Service's statutory debt ceiling.

The NPA must be periodically extended through an amendment jointly with the FFB so that the Postal Service may continue to issue debt to the FFB pursuant to the standardized procedures and terms and conditions established by the NPA. Prior to September 28, 2018, the FFB's standard practice was to provide the Postal Service with extensions for a full year. Since September 28, 2018, the FFB has provided amendments extending the agreement with the Postal Service for shorter two-to-three-month intervals. These amendments did not affect the terms of any of the Postal Service's outstanding debt as of June 30, 2019, and September 30, 2018.

On June 30, 2019, the FFB amended the NPA agreement by extending it until August 31, 2019. If the Postal Service is unable to extend the NPA beyond August 31, 2019, it has no assurance that it could obtain alternative debt financing after that date on comparable terms. However, the Postal Service believes that should the NPA not be renewed, the Postal Service would be able to maintain adequate liquidity through existing and new financing arrangements, as necessary and allowed by statute, to fund its operations for the foreseeable future.

Liquidity Concerns

The Postal Service is constrained by laws and regulations, including the *Postal Accountability and Enhancement Act*, Public Law 109-435 ("PAEA"), which restrict revenue sources and mandate certain expenses. These expenses include prefunding requirements for retiree health benefits, and amortization schedules to provide full funding of retiree health and pension benefits that are unlike those imposed on most other U.S. government entities or private sector businesses.

Statutorily mandated expenses include amortization payments to provide full funding of retirement benefits under CSRS and FERS, described in greater detail below and in *Note 9 - Retirement Plans*. Additionally, the PAEA established the Postal Service Retiree Health Benefits Fund (“PSRHBF”) and mandated certain obligations for paying the normal costs and amortization payments for full prefunding of retiree health benefits. Normal costs are the present value of the estimated retiree health benefits attributable to active employees’ current year of service. These prefunding obligations are described in greater detail below and in *Note 10 - Health Benefits Plans*.

Absent legislative and regulatory change, the Postal Service projects continuing annual net losses in the future. As a result of these losses and its liquidity concerns, the Postal Service will be unlikely to have sufficient liquidity to meet all of its existing legal obligations when due while also paying down its debt and making the critical infrastructure investments that have been deferred in recent years.

In the event that circumstances leave the Postal Service with insufficient liquidity, it would likely be required to implement additional contingency plans to ensure that its primary mission is fulfilled and that mail deliveries continue. These measures may require the Postal Service to prioritize payments to the FFB, employees and suppliers ahead of some payments to other U.S. government entities, as has been done in the past.

Past Due Obligations

The Postal Service reported operating expenses of approximately \$74 billion in 2018 and has incurred cumulative net losses of \$74.9 billion from 2007 through June 30, 2019. The Postal Service defaulted on \$33.9 billion in statutorily specified PSRHBF prefunding payments to the U.S. Office of Personnel Management (“OPM”) for the years 2012 through 2016. The Postal Service also did not make payments totaling \$13.8 billion to OPM over the last two years (approximately \$6.9 billion in payments were each due September 30, 2018, and September 30, 2017), for normal cost of retiree health benefits and amortization payments for PSRHBF, CSRS and FERS unfunded liabilities, in order to preserve liquidity and to ensure that the Postal Service’s ability to fulfill its primary universal service mission was not placed at undue risk.

The following table presents the total expenses related to past due obligations for retiree health benefits, CSRS and FERS by the Postal Service and the years in which the accruals were recorded:

<i>(in millions)</i>	2018	2017	2012 to 2016	Total as of September 30, 2018
PSRHBF prefunding fixed amount ¹	\$ —	\$ —	\$ 33,900	\$ 33,900
PSRHBF unfunded benefits amortization	815	955	—	1,770
Normal cost of retiree health benefits	3,666	3,305	—	6,971
CSRS unfunded retirement benefits amortization	1,440	1,741	—	3,181
FERS unfunded retirement benefits amortization ²	958	917	495	2,370
Total expenses related to past due obligations	\$ 6,879	\$ 6,918	\$ 34,395	\$ 48,192

¹ The 2012 to 2016 period amount includes \$5.8 billion for 2016, \$5.7 billion for 2015, \$5.7 billion for 2014, \$5.6 billion for 2013, and \$11.1 billion for 2012.

² The 2012 to 2016 period amount includes \$247.6 million for 2016, \$240.9 million for 2015, and \$6.7 million for 2014.

Business Model Challenges/Constraints

Market-Dominant services, which accounted for approximately 67% of the Postal Service’s annual operating revenue in 2018, are currently subject to a price cap as measured by the Consumer Price Index for All Urban Consumers (“CPI-U”). However, the Postal Service’s costs are not similarly constrained. A large portion of the Postal Service’s cost structure cannot be altered expeditiously due to the universal service obligation, which currently includes a legal requirement to deliver mail six days per week, while the number of delivery points continues to grow by approximately one million per year, further driving up delivery costs. When combined with the reduction in mail volume, this has resulted in a drop in the average number of pieces delivered per delivery point per day from approximately 5.5 pieces in 2007 to 3.5 pieces in 2018, a decline of approximately 37%.

As described above, certain employee and retiree benefit costs are mandated by law and cannot be altered without legislative change. Under current law, the Postal Service is generally unable to increase prices sufficiently to offset increased costs, and is likewise constrained by law from reducing many of its costs or from pursuing many alternate sources of revenue.

Aside from its universal service obligation, a significant factor contributing to Postal Service losses is the ongoing decline in the volume of Market-Dominant products and services. Specifically, declines in *First-Class Mail* are largely the result of changes in consumers' and businesses' use of mail resulting from the continuing migration to electronic communication and transactional alternatives, which have taken place over the last decade and are expected to continue. After experiencing relatively flat volume between 2009 and 2016, beginning in 2017, *Marketing Mail* volume has been challenged by commercial mailers' increasing use of digital advertising, although it has benefited from strong political and election mail volumes, particularly in the second half of 2018 and the first quarter of 2019.

The Postal Service's Shipping and Packages category has historically shown revenue and volume growth as a result of its successful efforts to compete in shipping services, including last-mile e-commerce fulfillment markets and Sunday delivery as well as end-to-end markets. However, this service category is subject to intense competition which significantly impacts both revenue and volume. Certain major customers of the Postal Service have recently begun diverting additional volume from the Postal Service's network by in-sourcing the last-mile delivery. These customers are also aggressively pricing their products and services in order to fill their networks and grow package density.

Because the Postal Service provides its services primarily through its employees, its costs are heavily concentrated in wages and benefits for both current employees and retirees. These costs are significantly impacted by contractual wage increases, employee health benefit premium increases, and statutorily mandated retirement and workers' compensation programs. Some of these costs have historically increased at a higher rate than inflation.

Mitigating Circumstances

The Postal Service continues to pursue strategies within its control to increase operational efficiency and improve liquidity. The Postal Service has managed capital in recent years by spending only what it believed was essential to maintain its existing facilities and service levels, and to increase efficiencies. However, continued increases in capital investment are necessary to upgrade its facilities, fleet of vehicles and processing equipment in order to remain operationally viable. Aggressive management of the business operations, as well as legislative and regulatory reforms that will enable it to increase revenue and reduce costs, will all be necessary to restore the Postal Service to financial health.

The Postal Service's status as an independent establishment of the executive branch that does not receive tax dollars for its operations presents unique requirements and restrictions, but also potentially mitigates some of the financial risk that would otherwise be associated with a cash shortfall. With annual total revenue in 2018 of approximately \$71 billion, a financially sound Postal Service continues to be vital to U.S. commerce.

The U.S. economy benefits greatly from the Postal Service and the many businesses that provide the printing and mailing services that it supports. Disruption of the mail would cause undue hardship to businesses and consumers as it would significantly inhibit the remittance of payments through the mail, and in the event of a cash shortfall, the U.S. government would likely prevent the Postal Service from significantly curtailing or ceasing operations. The Postal Service continues to inform the Executive Branch, Congress, the PRC and other stakeholders of the immediate and long-term financial challenges it faces and the legislative and regulatory changes that are required to restore its financial stability.

NOTE 4 - REVENUE RECOGNITION

The Postal Service generates the majority of its revenue from contracts associated with the processing and delivery of different types of mail and packages, both domestically and internationally, which generally occurs over a relatively short period of time (e.g., several days).

Practical Expedients

The Postal Service elected to apply the *Incremental cost to obtain a contract* practical expedient under the ASC 606 adoption. As such, the Postal Service recognizes the incremental costs to obtain a contract as expenses when incurred since the amortization period if capitalized would be less than one year and the Postal Service fulfills the majority of its contract obligations within that time frame.

Disaggregation of Revenue

The following table summarizes the Postal Service's disaggregated operating revenue for the three and nine months ended June 30, 2019, and 2018, by each service category:

<i>(in millions)</i>	Three Months Ended June 30,		Nine Months Ended June 30,	
	2019	2018	2019	2018
Operating revenue:				
First-Class Mail	\$ 5,859	\$ 5,957	\$ 18,758	\$ 19,153
Marketing Mail	3,861	3,982	12,359	12,418
Shipping and Packages	5,416	5,166	17,319	16,299
International	615	617	1,922	2,050
Periodicals	302	340	910	980
Other	1,033	1,012	3,021	2,822
Total operating revenue	\$ 17,086	\$ 17,074	\$ 54,289	\$ 53,722

Satisfaction of Performance Obligations

ASC 606 defines a performance obligation as a promise in a contract to transfer a distinct good or service to the customer. A contract's transaction price is allocated to each distinct performance obligation and recognized as revenue when, or as, the performance obligation is satisfied.

First-Class Mail, Marketing Mail, Shipping and Packages, International Mail and Periodicals are categorized as Mailing and Shipping services for purposes of satisfying performance obligations. The Postal Service recognizes revenue for Mailing and Shipping services as it fulfills its obligation to process and deliver each mailpiece and the customer mail sender/recipient receives and consumes the benefits of these services.

Other revenue includes *PO Box services, Return Receipts, Insurance, Other Ancillary Services, Shipping and Mailing Supplies, Collect on Delivery, Registered Mail, Stamped Envelopes and Cards, Money Orders, and other goods and services.* The Postal Service recognizes revenue for the majority of these services over time as the customer receives and consumes the benefits of the service. The revenue for a small portion of certain goods or services in this service category is recognized at a point in time when the goods or service are provided to the customer.

The vast majority of the Postal Service's contracts include only one performance obligation. However, if a contract is separated into more than one performance obligation, the total transaction price for each performance obligation is allocated in an amount based on the estimated relative stand-alone selling prices of the promised goods or services underlying each performance obligation. The majority of the goods or services sold by the Postal Service services have observable stand-alone sales prices.

If the Postal Service were unable to complete delivery to the destination point, another entity would not need to re-perform the entire portion of delivery already performed by the Postal Service. Accordingly, control from the Postal Service to the customer transfers over time for the vast majority of services the Postal Service offers, and revenue is recognized based on the progress of the completion of the performance obligations.

Variable Consideration

The Postal Service offers certain contracts to its customers that contain various types of customer incentives or other provisions that can either increase or decrease the transaction price. Customer incentives include discounts, money back guarantees, rebates, refunds or incentive payments. The other provisions include performance penalties. The Postal Service uses the expected value approach to estimate variable consideration to which it expects to be entitled.

Contract Modifications

The Postal Service considers contract modifications to exist when the modification either creates new enforceable rights and obligations or alters the existing arrangement. Contract modifications do not add distinct services; they are typically used to change the prices that the Postal Service charges its customer for existing services. These contract modifications are accounted for prospectively as the remaining performance obligations are executed.

Principal vs. Agent Consideration

The Postal Service utilizes third parties to assist with the transportation of mailpieces between different points as part of the delivery process. Based on its evaluation of the transfer of control model, the Postal Service has determined that it acts as the principal rather than the agent within these arrangements.

Contract Liabilities

The vast majority of the Postal Service's contract liabilities consist of *Deferred revenue-prepaid postage* and prepaid *PO Box* and Caller Service fees. *Deferred revenue-prepaid postage* is an estimate of postage that has been sold, but not yet used by customers. The Postal Service recognizes revenue over time as the Postal Service delivers mailpieces. Because payments for postage are collected in advance of the satisfaction of related performance obligations, the Postal Service defers and reports this unearned revenue as *Deferred revenue-prepaid postage* in its balance sheet. Stamp sales and metered postage account for the majority of *Deferred revenue-prepaid postage*. The liability also includes an estimate for mail that is in-transit within the Postal Service network.

The prepaid *PO Box* and Caller Service fees consist of the payments received from customers for *PO Box* fees at the beginning of their contracts. The Postal Service defers and reflects this unearned revenue as prepaid *PO Box* and Caller Service fees within *Other current liabilities* in the accompanying *Balance Sheets*. Revenue is recognized over time as customers use the *PO Box* and Caller Services over the terms of their contracts.

The following table establishes the opening balances of the Postal Service's contract liabilities, including *Deferred revenue-prepaid postage* and prepaid *PO Box* and Caller Service fees, as of April 1, 2019, and October 1, 2018, respectively:

<i>(in millions)</i>	<u>April 1, 2019</u>	<u>October 1, 2018</u>
Deferred revenue-prepaid postage:		
Forever stamps	\$ 1,444	\$ 1,229
Mail-in-transit	570	569
Metered postage	283	302
Other prepaid postage	124	130
Total deferred revenue-prepaid postage	2,421	2,230
Prepaid PO Box and Caller Service fees	447	438
Total deferred revenue	\$ 2,868	\$ 2,668

The following table provides details of revenue recognized for the three months ended June 30, 2019, that was reported in the opening balances of the Postal Service's contract liabilities for deferred revenue as of April 1, 2019, and for the nine months ended June 30, 2019, that was reported in the opening balances of the Postal Service's contract liabilities for deferred revenue as of October 1, 2018:

<i>(in millions)</i>	Three Months Ended June 30, 2019	Nine Months Ended June 30, 2019
Revenue recognized in the period from deferred revenue:		
Forever stamps	\$ 609	\$ 864
Mail-in-transit	570	569
Metered postage	283	302
Other prepaid postage	51	97
PO Box and Caller Service fees	230	419

NOTE 5 - RELATED PARTIES

As disclosed throughout this report, the Postal Service has significant transactions with other U.S. government entities, which are considered related parties for accounting purposes.

The following table presents related-party assets and liabilities as of June 30, 2019, and September 30, 2018:

<i>(in millions)</i>	June 30, 2019	September 30, 2018
Related-party assets:		
Receivables and advances ¹	\$ 54	\$ 61
Carrying amount of revenue forgone installment receivable ²	461	446
Related-party liabilities:		
Current portion of debt	\$ 4,000	\$ 11,000
Other current liabilities ³	55,076	50,312
Noncurrent portion of debt	7,000	2,200
Other noncurrent liabilities ⁴	16,394	15,047

¹ Current portion within *Receivables, net* and noncurrent portion within *Other assets* in the accompanying *Balance Sheets*.
² Included within *Other assets* in the accompanying *Balance Sheets*. See further discussion in *Note 12 - Fair Value Measurement*.
³ Amounts include CSRS, FERS, PSRHBFB and current workers' compensation obligations as well as payables to other agencies.
⁴ Amounts include noncurrent workers' compensation obligations.

The following table presents related-party revenue and expenses for the three and nine months ended June 30, 2019, and 2018:

(in millions)	Three Months Ended June 30,		Nine Months Ended June 30,	
	2019	2018	2019	2018
Related-party operating revenue ¹	\$ 238	\$ 244	\$ 724	\$ 744
Related-party operating expenses ²	\$ 3,815	\$ 4,099	\$ 12,293	\$ 12,852
Related-party interest income ³	\$ 36	\$ 33	\$ 109	\$ 82
Related-party interest expense ⁴	\$ 50	\$ 60	\$ 163	\$ 170

¹ Included within *Operating revenue* in the accompanying unaudited *Statements of Operations*.
² Included within *Operating expenses* in the accompanying unaudited *Statements of Operations*.
³ Represents interest imputed on the revenue forgone installment receivable as well as interest generated on U.S. Treasury instruments and other cash equivalents held with the Federal Reserve Bank of New York. Included within *Interest and investment income* in the accompanying unaudited *Statements of Operations*.
⁴ Incurred on debt issued to the FFB, and included within *Interest expense* in the accompanying unaudited *Statements of Operations*.

NOTE 6 - CASH, CASH EQUIVALENTS AND RESTRICTED CASH

The following table provides a reconciliation of *Cash and cash equivalents* and *Restricted cash* reported in the accompanying *Balance Sheets* as of June 30, 2019, and 2018, respectively, and as of September 30, 2018, and 2017, respectively (to disclose the opening balances), that sum to the totals of the same such amounts shown in the accompanying unaudited *Statements of Cash Flows* for the nine months ended June 30, 2019, and 2018:

(in millions)	June 30,		September 30,	
	2019	2018	2018	2017
Cash and cash equivalents	\$ 7,953	\$ 11,152	\$ 10,061	\$ 10,513
Restricted cash	465	341	275	291
Total cash, cash equivalents and restricted cash	\$ 8,418	\$ 11,493	\$ 10,336	\$ 10,804

Restricted cash represents Postal Service cash that is not available for general use. This includes cash originated from forfeitures or seizures related to consumer fraud or other criminal activity related to the mail and either held for third-party beneficiaries or awaiting disposition. *Restricted cash* also includes funds designated for specific use due to congressional appropriation for Postal Service obligations to the PRC and the United States Postal Service Office of Inspector General, or that are otherwise restricted.

The Postal Service holds its *Cash and cash equivalents* and *Restricted cash* with the Federal Reserve Bank of New York and invests its excess cash, when available, in highly-liquid, short-term investments issued by the U.S. Department of the Treasury.

NOTE 7 - PROPERTY AND EQUIPMENT, NET

Assets within *Property and equipment, net* in the accompanying *Balance Sheets* are recorded at cost, which includes the interest on borrowings used to finance construction of major capital additions, less allowances for depreciation and amortization. Interest capitalized during both the three and nine months ended June 30, 2019, and 2018, was not significant. Fixed assets are depreciated over estimated useful lives ranging from 3 to 40 years using the straight-line method.

The net book values of assets classified as held for sale were approximately \$4 million and \$13 million as of June 30, 2019, and September 30, 2018, respectively, and are included within *Property and equipment, net* in the accompanying *Balance Sheets*.

For the three months ended June 30, 2019, and 2018, depreciation and amortization expense was \$430 million and \$421 million, respectively, and impairment charges were de minimis. For the nine months ended June 30, 2019, and 2018, depreciation and amortization expense was \$1.3 billion and \$1.2 billion, respectively, and impairment charges were de minimis. These items are included within *Other operating expenses* in the accompanying unaudited *Statements of Operations*.

NOTE 8 - COMMITMENTS AND CONTINGENCIES

Commitments

In May 2019, the Postal Service reached a new collective bargaining agreement with the National Rural Letter Carriers' Association ("NRLCA") which was subsequently ratified by NRLCA membership in August 2019. The previous contract with the NRLCA expired on May 20, 2018. The new contract includes general wage increases totaling 3.4% over the three-year term of the contract (1.3% of which is retroactive to November 2018) with a Cost of Living Allowance ("COLA") base of April 2018 (the first COLA payment is retroactive to September 1, 2018), the introduction of proportional COLA for new career hires, a reduction in the Postal Service's share of health insurance premiums, no increase in the Equipment Maintenance Allowance base rate, additional operational flexibility to use Rural Carrier Associates, administrative cost savings from elimination of mail counts over the contract term, enhanced health benefits for non-career rural employees, and a comprehensive Memorandum of Understanding on implementation of the rural standards study. The new contract will expire on May 20, 2021.

In September 2018, the Postal Service agreed to extend contract negotiations relating to a new collective bargaining agreement with the American Postal Workers Union, AFL-CIO ("APWU"). The contract with the APWU expired on September 20, 2018, and the respective parties mutually agreed to extend negotiations beyond the deadline. On December 21, 2018, negotiations between the Postal Service and the APWU came to an impasse. On April 3, 2019, the APWU invoked mediation. On June 7, 2019, the mediation process concluded and the parties have moved forward with interest arbitration, during which a three-member arbitration panel will decide the terms of the successor collective bargaining agreement. The respective parties will continue to follow the current agreement until a new contract is reached through the interest arbitration process. No new agreement has been reached as of the date of this report.

Contingent Liabilities

The Postal Service's contingent liabilities consist primarily of claims resulting from labor and employment matters; asset retirement obligations and environmental matters; property damage and injuries on Postal Service properties; and issues arising from Postal Service contracts, personal claims and traffic accidents. Each quarter, the Postal Service evaluates each claim to determine its potential liability. If the Postal Service determines that an unfavorable outcome from a new claim is both probable and reasonably estimable, it records a liability for the amount. Preexisting claims are also reviewed and adjusted quarterly for resolutions or revisions to prior estimates based on new facts and circumstances.

The Postal Service is from time to time involved in other litigation incidental to the conduct of its business, none of which is expected to be material to its financial condition or operations.

Provision for Losses

The Postal Service has made adequate provision for probable losses arising from all claims. The following table presents contingent liabilities by current and noncurrent portions and by category, as of June 30, 2019, and September 30, 2018:

<i>(in millions)</i>	<u>June 30, 2019</u>	<u>September 30, 2018</u>
Current/noncurrent portions of contingent liabilities:		
Current portion ¹	\$ 185	\$ 244
Noncurrent portion ²	183	193
Total contingent liabilities	<u>\$ 368</u>	<u>\$ 437</u>
Contingent liabilities by category:		
Labor and employment matters	\$ 238	\$ 297
Asset retirement obligations	57	67
Tort matters	73	67
Contractual matters	—	6
Total contingent liabilities	<u>\$ 368</u>	<u>\$ 437</u>

¹ Included within *Payables and accrued expenses* in the accompanying *Balance Sheets*.
² Included within *Other noncurrent liabilities* in the accompanying *Balance Sheets*.

Reasonably Possible Contingencies

The Postal Service does not accrue for contingencies which it deems reasonably possible of an unfavorable outcome. These ranged in amount from approximately \$150 million to \$1.0 billion at June 30, 2019, and from approximately \$225 million to \$1.1 billion at September 30, 2018.

Class Action Litigation

As previously reported, on January 14, 2010, the Equal Employment Opportunity Commission's ("EEOC") Office of Federal Operations ("OFO") certified the case *McConnell v. Brennan* (first instituted in 2006 as *McConnell v. Potter*) as a class action against the Postal Service, with the class consisting of permanent-rehabilitation and limited-duty Postal Service employees who the Postal Service assessed under the National Reassessment Process ("NRP") between the dates of May 5, 2006, and July 1, 2011. The Postal Service utilized the NRP to ensure employees receiving workers' compensation benefits were placed in jobs consistent with their abilities, and that records regarding employees injured on the job were correct.

The *McConnell* case alleges violations of the Rehabilitation Act of 1973 resulting from the NRP's failure to provide a reasonable accommodation, the NRP's wrongful disclosure of medical information, the NRP's creation of a hostile work environment, and the NRP's adverse impact on disabled employees. The class is seeking injunctive relief and damages of an uncertain amount. If the plaintiffs are able to prove their allegations in this matter and to establish the damages they assert, an adverse ruling could have a material impact on the Postal Service.

In 2015, the Administrative Judge assigned to handle the *McConnell* case granted in-part both the Class Agent's and the Postal Service's motions for summary judgment. In her decision, the Administrative Judge found that the NRP violated the Rehabilitation Act. The Postal Service appealed this decision to the OFO, and the OFO denied this appeal in 2018. The Postal Service implemented the OFO's order, and notified all class members of their right to file an individual claim for relief. Class members were allowed thirty days to submit claims to the Postal Service's National Equal Employment Opportunity Investigative Services Office. The claims submission deadline has now passed and the dispute process for individual claims is currently underway before a newly assigned EEOC Administrative Judge.

The ultimate outcome of the individual claims dispute process may result in a liability amount that is greater or less than the amount accrued as of June 30, 2019.

NOTE 9 - RETIREMENT PLANS

The majority of career employees participate in one of two U.S. government defined benefit pension programs, CSRS and FERS, which OPM administers. These plans provide retirement, death and termination benefits for eligible employees based on specific eligibility and participation requirements, vesting periods and benefit formulas. Each employee’s participation in either plan is based on the starting date of employment with the Postal Service or another U.S. government entity.

As government-sponsored benefit plans, CSRS and FERS are not subject to the provisions of the *Employee Retirement Income Security Act of 1974*, as amended. Likewise, because the Postal Service cannot direct the costs, benefits or funding requirements of these plans, it accounts for program expenses under multiemployer plan accounting rules. As such, the Postal Service records contributions to the plans as an expense in the period in which each contribution is due. For FERS, the Postal Service contributes to the plan an amount established by OPM as the employer portion of retirement benefits for participating employees and their qualifying survivors, upon retirement, for each employee’s current year service (normal cost). As further discussed below, the Postal Service is not required to pay the normal cost for those employees who participate in CSRS. The Postal Service is also required to contribute amounts sufficient to fully amortize the unfunded CSRS and FERS liabilities.

Career employees may also participate in the Thrift Savings Plan (“TSP”), a defined contribution retirement savings and investment plan administered by the Federal Retirement Thrift Investment Board. The Postal Service’s TSP expenses are related only to its contributions for FERS employees who participate in the TSP.

CSRS provides a basic annuity plan benefit to employees hired before January 1, 1984. CSRS Offset provides Social Security benefits in addition to its basic annuity plan for employees hired between January 1, 1984, and January 1, 1987. CSRS and CSRS Offset employees may also participate in the TSP, although the Postal Service does not match contributions for these participants.

The PAEA suspended the Postal Service’s employer contributions to CSRS that would otherwise have been required under *Title 5, Section 8334(a)(1)* of the U.S. Code, although CSRS employees continue to contribute to the plan. By law, the Postal Service does not pay normal costs for participating employees for CSRS retirement benefits; however, in 2017 the Postal Service was required to begin making annual payments to amortize the unfunded CSRS liability. Employee contributions for both 2018 and 2019, as a percentage of employee basic pay, are 7.0% for CSRS.

Effective January 1, 1987, FERS covers employees hired since December 31, 1983, and FERS employees are covered by an annuity, Social Security and TSP benefits. For FERS employees who participate in TSP, the Postal Service contributes 1% of basic pay and matches voluntary employee contributions up to an additional 4% of basic pay.

FERS employees are further categorized as either FERS, FERS - Revised Annuity Employees (“FERS-RAE”), or FERS - Further Revised Annuity Employees (“FERS-FRAE”) depending on whether their date of hire was before, during, or after calendar year 2013, respectively. The following table presents the employee and employer contributions, as a percentage of employee basic pay, for both 2018 and 2019:

	Employee Contributions	Postal Service Contributions
FERS	0.8%	13.7%
FERS-RAE	3.1%	11.9%
FERS-FRAE	4.4%	10.7%

Aside from these different contribution rates, the Postal Service uses the term "FERS employees" to apply to all of the FERS employee categories.

FERS Employees' Current Year Service

The Postal Service records expenses for FERS employees' current year service consisting of employer contributions for FERS normal cost, Social Security and TSP, each of which is included within *Retirement benefits* in the accompanying unaudited *Statements of Operations*.

The following table presents the details of FERS employees' current year service expenses for the three and nine months ended June 30, 2019, and 2018:

<i>(in millions)</i>	Three Months Ended June 30,		Nine Months Ended June 30,	
	2019	2018	2019	2018
FERS normal costs	\$ 878	\$ 871	\$ 2,635	\$ 2,609
Social Security	522	519	1,640	1,599
TSP	282	276	854	829
Total FERS employees' current year service	\$ 1,682	\$ 1,666	\$ 5,129	\$ 5,037

The Postal Service makes payments for FERS employees' current year service costs in accordance with its bi-weekly payroll cycle. Any unpaid employer amounts at the end of a period, along with any employee amounts withheld but not remitted at the end of a period, are recorded as a current liability within *Retirement benefits* in the accompanying *Balance Sheets*. Those accrued amounts were \$280 million and \$460 million at June 30, 2019, and September 30, 2018, respectively.

CSRS and FERS Unfunded Retirement Benefits Amortization

OPM periodically notifies the Postal Service regarding its revaluation of unfunded CSRS and FERS liabilities. The Postal Service records these expenses as *Retirement benefits* in the accompanying unaudited *Statements of Operations*. These amounts may be significantly impacted by changes in actuarial assumptions used to revalue the unfunded liabilities.

OPM historically calculated these obligations using government-wide economic and demographic data. In October 2017, OPM issued a new rule announcing its intent to calculate future unfunded CSRS and FERS obligations using Postal Service-specific demographic assumptions.

In October 2018, OPM provided the Postal Service with an actuarial report using these new rules indicating the projected annual amortization payments due September 30, 2019, would be \$1.4 billion for the CSRS obligation and \$958 million for the FERS obligation. The Postal Service expects to receive invoices from OPM for the actual amounts due September 30, 2019, during the fourth quarter of 2019, and these invoices may differ from OPM's original projections due to changes in experience, discount rates and/or actuarial assumptions as of the calculation date.

The following table presents the expense recorded for CSRS and FERS unfunded retirement benefits amortization for the three and nine months ended June 30, 2019, and 2018:

<i>(in millions)</i>	Three Months Ended June 30,		Nine Months Ended June 30,	
	2019	2018	2019	2018
CSRS unfunded retirement benefits amortization ¹	\$ 360	\$ 456	\$ 1,080	\$ 1,369
FERS unfunded retirement benefits amortization ²	239	322	718	966
Total CSRS and FERS unfunded retirement benefits amortization	\$ 599	\$ 778	\$ 1,798	\$ 2,335

¹ Expense for the accrual for the annual payment due to OPM by September 30 of the respective year, based on information provided by OPM, to amortize the unfunded CSRS retirement obligation. Payments are to be made through 2043 based on OPM invoices.

² Expense for the accrual for the annual payment due to OPM by September 30 of the respective year, based on information provided by OPM, to amortize the unfunded FERS retirement obligation. Payments are to be made over a 30-year rolling period based on OPM invoices.

The amounts the Postal Service has accrued for CSRS and FERS unfunded retirement benefits but has not yet paid are recorded as a current liability within *Retirement benefits* in the accompanying *Balance Sheets*. Those accrued unpaid amounts were approximately \$7.3 billion and \$5.6 billion at June 30, 2019, and September 30, 2018, respectively.

Total expenses related to multiemployer retirement plans, which includes the CSRS and FERS unfunded liability amortization, and FERS normal costs, were \$1.5 billion and \$1.6 billion, for the three months ended June 30, 2019, and 2018, respectively. For the nine months ended June 30, 2019, and 2018, these multiemployer retirement plans expenses totaled \$4.4 billion and \$4.9 billion, respectively.

NOTE 10 - HEALTH BENEFITS PLANS

The Federal Employees Health Benefits (“FEHB”) Program covers nearly all career employees and also covers non-career employees and retirees who meet certain eligibility requirements. OPM administers FEHB and allocates the cost of funding the program to participating U.S. government employers. The Postal Service cannot direct the costs, benefits or funding requirements of the plans. Therefore, it accounts for program expenses using multiemployer plan accounting rules by recording contributions to the plans that will be required by OPM as an expense in the period in which the contributions are due. Although OPM determines the actual health benefits premium costs, the allocation of these costs between the Postal Service and most of its employees is determined through agreements with Postal Service labor unions. Separate from FEHB, the Postal Service offers its own healthcare plan to certain non-career employees who are ineligible for FEHB.

Active Employees

The Postal Service paid 71.8% and 72.5% of FEHB premium costs during the three months ended June 30, 2019, and 2018, respectively. The Postal Service paid 72.1% and 72.9% of FEHB premium costs during the nine months ended June 30, 2019, and 2018, respectively.

Postal Service employee health benefits expense (which includes the employer portion of Medicare taxes) is most significantly impacted by the number of employees electing coverage and the premium costs of the selected plans. Postal Service employee health benefits expense was approximately \$1.3 billion for each of the three-month periods ended June 30, 2019, and 2018. Postal Service employee health benefits expense was approximately \$3.8 billion and \$3.9 billion for the nine-month periods ended June 30, 2019, and 2018, respectively. These expenses are included within *Compensation and benefits* in the accompanying unaudited *Statements of Operations*.

Retirees

Postal Service retirees who participated in FEHB for the five years immediately preceding their retirement may continue to participate in the plan during retirement. Qualifying survivors of retirees are also eligible to receive benefits. The Postal Service is required to contribute to the PSRHBFB an amount estimated to be equal to the employer portion of FEHB insurance premiums for participating employees and their qualifying survivors, upon retirement, for each employee’s current year of service (normal cost). The Postal Service is also required to contribute an amount sufficient to fully amortize the unfunded liability of the PSRHBFB by 2056. These amounts are based, in part, on each current and prospective retiree’s length of federal civilian service occurring on or after July 1, 1971. Each participant’s share of premium costs is set by law and is not subject to negotiation with Postal Service labor unions. The Postal Service expenses what it is billed by OPM for both normal cost and amortization of the unfunded liability.

The PAEA required the Postal Service to prefund retiree health benefits during years 2007 through 2016 by paying statutorily specified annual amounts ranging from \$1.4 billion to \$5.8 billion, totaling \$54.8 billion, into the PSRHBFB, which began paying the Postal Service’s share of retiree health benefit premiums in 2017. The Postal Service remains obligated to fund the \$33.9 billion in statutorily required PSRHBFB prefunding payments that it defaulted on for the years 2012 through 2016, as well as the amortization and normal cost payments of \$955 million and \$3.3 billion, respectively, that it did not pay at the end of 2017, and the amortization and normal cost payments of \$815 million and \$3.7 billion, respectively, that it did not pay at the end of 2018. As of the date of this report, the Postal Service has not been assessed any penalties associated with these non-payments.

As required by PAEA, OPM annually performs an actuarial valuation for the purpose of developing a payment schedule for the Postal Service to fund the remaining unfunded PSRHBF obligation in annual payments through the year 2056. Based on preliminary calculations provided by OPM using updated discount rate assumptions, the Postal Service originally estimated the amortization payment due September 30, 2019, to be \$1.1 billion, and therefore accrued an expense of \$550 million for the first six months of 2019. On July 2, 2019, the Postal Service received OPM's invoice for 2019, which indicated the year-end amortization payment amount due is \$789 million. This amount was lower than the Postal Service's original estimate largely due to OPM's use of revised discount rates. Due to the lower-than-estimated invoiced amount, the Postal Service has adjusted its accrual for the amortization payment, resulting in expenses of \$42 million and \$592 million for the three and nine months ended June 30, 2019, respectively. These amounts are included within *Retiree health benefits* in the accompanying unaudited *Statements of Operations*.

Furthermore, the Postal Service is obligated to pay the estimated normal cost of retiree health benefits attributable to the service of its employees during the most recently ended year. Based on preliminary calculations provided by OPM using updated discount rate assumptions, the Postal Service originally estimated the normal cost payment, also due by September 30, 2019, to be \$4.0 billion, and therefore accrued an expense of \$2.0 billion for the first six months of 2019. OPM's July 2, 2019, invoice indicated the normal cost payment amount due is approximately \$3.8 billion. This amount was lower than the Postal Service's original estimate largely due to OPM's use of revised discount rates. Due to the lower-than-estimated invoiced amount, the Postal Service has adjusted its accrual for the normal cost payment, resulting in expenses of \$831 million and \$2.8 billion for the three and nine months ended June 30, 2019, respectively. These amounts are included within *Retiree health benefits* in the accompanying unaudited *Statements of Operations*.

The cumulative amount of statutorily specified, normal cost and amortization PSRHBF payments the Postal Service has accrued is \$46.1 billion as of June 30, 2019, inclusive of the \$42.6 billion that was unpaid as of September 30, 2018. Given that OPM considers these amounts to be due and payable, the Postal Service reflects the cumulative unpaid amount as a current liability within *Retiree health benefits* in the accompanying *Balance Sheets*.

The following table details retiree health benefits expenses for the three and nine months ended June 30, 2019, and 2018:

<i>(in millions)</i>	Three Months Ended June 30,		Nine Months Ended June 30,	
	2019	2018	2019	2018
PSRHBF unfunded liability amortization ¹	\$ 42	\$ 16	\$ 592	\$ 611
Normal cost of retiree health benefits ²	831	884	2,831	2,750
Total retiree health benefits expense	\$ 873	\$ 900	\$ 3,423	\$ 3,361

¹ Expense for the accrual for the annual payment due to PSRHBF by September 30 of the respective year, for the amortization of the unfunded liability. The 2019 amounts are based on OPM's invoice received July 2, 2019, with updated discount rate assumptions. The 2018 amounts are based on OPM's invoice received July 19, 2018, with updated discount rate assumptions.

² Expense for the accrual for the annual payment due to the PSRHBF by September 30 of the respective year, for actuarially determined normal cost of retiree health benefits for current employees. The 2019 amounts are based on OPM's invoice received July 2, 2019, with updated discount rate assumptions. The 2018 amounts are based on OPM's invoice received July 19, 2018, with updated discount rate assumptions.

NOTE 11 - WORKERS' COMPENSATION

Postal Service employees injured on the job are covered by the Federal Employees' Compensation Act ("FECA"), administered by the U.S. Department of Labor's ("DOL") Office of Workers' Compensation Programs, which makes all decisions regarding injured workers' eligibility for benefits. The Postal Service reimburses DOL for all workers' compensation benefits paid to or on behalf of Postal Service employees, plus an administrative fee.

Workers' Compensation Liability

The Postal Service records a liability for its workers' compensation obligations for employees who have been injured on the job and are eligible for benefits, or their qualified survivors. Both the current and noncurrent portions of the workers' compensation liability are recorded in the accompanying *Balance Sheets*. The Postal Service uses

an estimation model that combines four generally-accepted actuarial valuation techniques based upon past claim-payment experience and exposure to claims as measured by total employee hours worked.

Changes in the liability are primarily attributable to the combined impacts of routine changes in actuarial assumptions, new compensation and medical cases, the progression of existing cases and changes in discount (interest) and inflation rates, including long-term cost-of-living-adjustment (“COLA”) rates for compensation claims, and medical rates for medical claims. These rates are updated as of the balance sheet date and factored into the model in accordance with GAAP.

To determine the fair value of the liability each quarter, the Postal Service first estimates the future total cost of workers’ compensation claims based on the dates of claim-related injuries, frequency or severity of the injuries, the pattern of historical payments to beneficiaries and the expected trend in future costs. The Postal Service then calculates the amount that would need to be invested at current discount (interest) rates to fully fund the future total cost of claims, and this calculated present value is the recorded value of the workers’ compensation liability.

This liability calculation is highly sensitive to changes in discount rates. For example, a 1% increase in the discount rate would decrease the June 30, 2019, liability and related expense by approximately \$1.9 billion. Likewise, a 1% decrease in the discount rate would increase the June 30, 2019, liability and related expense by approximately \$2.3 billion.

The following table details the applicable inflation and discount rates for compensation and medical claims used to estimate the workers’ compensation liability as of June 30, 2019, and September 30, 2018:

	<u>June 30, 2019</u>	<u>September 30, 2018</u>
Compensation claims liability:		
Discount rate	2.23%	3.10%
Long-term wage inflation rate	2.60%	2.60%
Medical claims liability:		
Discount rate	2.25%	3.10%
Medical inflation rate	3.00%	3.00%

As of June 30, 2019, and September 30, 2018, the Postal Service’s total liability for workers’ compensation was approximately \$17.7 billion and \$16.4 billion, respectively. As of June 30, 2019, and September 30, 2018, the current portion of the liability was approximately \$1.4 billion and \$1.4 billion, respectively, and the noncurrent portion of the liability was approximately \$16.3 billion and \$15.0 billion, respectively, as reflected in the accompanying *Balance Sheets*.

Workers’ Compensation Expense

The impacts of changes in discount rates and inflation rates, as well as the actuarial valuation of new cases and revaluation of existing cases, are components of total workers’ compensation expense as recorded in the accompanying unaudited *Statements of Operations*. In addition, the Postal Service pays an administrative fee to DOL, which is considered a component of workers’ compensation expense.

The following table presents the components of workers' compensation expense for the three and nine months ended June 30, 2019, and 2018:

<i>(in millions)</i>	Three Months Ended June 30,		Nine Months Ended June 30,	
	2019	2018	2019	2018
Impact of discount rate changes	\$ 697	\$ (137)	\$ 1,656	\$ (694)
Actuarial revaluation of existing cases	28	49	80	(112)
Cost of new cases	291	275	893	920
Administrative fee	22	19	67	58
Total workers' compensation expense	\$ 1,038	\$ 206	\$ 2,696	\$ 172

NOTE 12 - FAIR VALUE MEASUREMENT

The Postal Service defines fair value as the price that would be received upon sale of an asset or the price that would be paid to transfer a liability between unrelated parties.

The carrying amounts of certain current assets and liabilities, including cash, accounts receivable, accounts payable, accrued expenses and the current portion of debt, approximate fair value due to their short-term nature. Assets within *Property and equipment, net* are recorded at cost and measured at fair value on a nonrecurring basis if they are determined to be impaired or classified as assets held for sale.

Noncurrent receivables and noncurrent debt are measured using a fair value hierarchy model. This model prioritizes observable and unobservable inputs used to measure fair value, and consists of three broad levels, as defined in authoritative literature.

For the periods ended June 30, 2019, and September 30, 2018, no significant transfers between *Level 1* and *Level 2* assets or liabilities transpired. The carrying amount and fair value of the revenue forgone installment receivable and the noncurrent portion of debt are presented for disclosure purposes only in the following table:

<i>(in millions)</i>	June 30, 2019		September 30, 2018	
	Carrying Amount	Fair Value	Carrying Amount	Fair Value
Revenue forgone installment receivable*	\$ 461	\$ 498	\$ 446	\$ 475
Noncurrent portion of debt	\$ 7,000	\$ 7,345	\$ 2,200	\$ 2,295

* The carrying amount is included within *Other assets* (which includes items in addition to the revenue forgone installment receivable) in the accompanying *Balance Sheets*.

The revenue forgone installment receivable qualifies as a financial instrument in accordance with authoritative literature. To calculate its fair value, the Postal Service recognizes the imputed interest it is owed as interest income and estimates the value of this receivable using the interest method, which converts future cash flows to a single discounted amount using interest rates for similar assets, which are considered *Level 2* inputs. The Postal Service then calculates the net present value of anticipated annual installment payments to be received, discounted by the 20-year U.S. Treasury Constant Maturity Rate, which was 2.31% and 3.13% as of June 30, 2019, and September 30, 2018, respectively.

The noncurrent portion of debt also qualifies as a financial instrument. Because no active market exists for its debt with the FFB, the Postal Service estimates the fair value of the noncurrent portion of this liability using expected future payments at discount rates provided by the FFB, considered *Level 3* inputs. The weighted averages of the FFB discount rates, based on U.S. Treasury Yield Curve Rates, were 1.99% and 3.02% as of June 30, 2019, and September 30, 2018, respectively.

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

CAUTIONARY STATEMENTS

The following *Management's Discussion and Analysis of Financial Condition and Results of Operations* and other parts of this report describe the principal factors affecting the financial results, liquidity, capital resources and critical accounting estimates of the United States Postal Service ("Postal Service," "USPS," "we," "our" and "us"). Our results of operations may be impacted by risks and uncertainties discussed here and in our Annual Report on Form 10-K for the year ended September 30, 2018, ("Annual Report") filed with the Postal Regulatory Commission ("PRC") on November 14, 2018. Such factors, many of which we cannot control or influence, may cause actual results to differ materially from those currently contemplated.

Our operating results for the three and nine months ended June 30, 2019, are presented in accordance with accounting principles generally accepted in the United States ("GAAP"). These results are not necessarily indicative of the results to be expected for the year ended September 30, 2019, and should be read in conjunction with our Annual Report. All references to years in this report, unless otherwise stated, refer to fiscal years beginning October 1 and ending September 30. All references to quarters, unless otherwise stated, refer to quarters within fiscal years 2019 and 2018.

Forward-looking statements contained in this report represent our best estimates of known and anticipated trends believed relevant to future operations. However, actual results may differ significantly from current estimates. Certain forward-looking statements included in this report use such words as "may," "will," "could," "expect," "believe," "plan," "estimate," "project" or other similar terminology. These forward-looking statements, which involve a number of risks and uncertainties, reflect current expectations regarding future events and operating performance as of the date of this report. We have no obligation to publicly update or revise any forward-looking statements, whether as a result of new information, future events or otherwise.

OVERVIEW

With our mandate to provide universal postal services to the nation, we serve retail and commercial customers in the U.S., as well as internationally. Our operations include an extensive and integrated retail, distribution, transportation and delivery network, and we operate throughout the U.S., its possessions and territories.

The *Postal Accountability and Enhancement Act* ("PAEA") classifies our products into two broad categories: Market-Dominant and Competitive "products," however, we use the term "services" in this document for consistency with other descriptions of services offered. The statutes under which we operate also establish certain requirements that affect our financial results, including obligations for retirement benefits within the Civil Service Retirement System ("CSRS") and the Federal Employee Retirement System ("FERS"), and obligations for retiree health benefits including funding of the Postal Service Retiree Health Benefits Fund ("PSRHBF"). We must coordinate with the U.S. Office of Personnel Management ("OPM") to address these obligations.

We have successfully implemented initiatives that have reduced the growth in certain costs by billions of dollars while offering new features for customers such as *Informed Delivery*. However, legal restrictions on pricing, service diversification and operations restrict our ability to cover our costs to provide prompt, reliable and efficient postal services to the nation while meeting all legally mandated payment obligations.

We have established a core set of goals that drive our strategic initiatives and continuous improvement efforts:

1. Deliver a world-class customer experience;
2. Equip, empower and engage employees;
3. Innovate faster to deliver value; and
4. Invest in our future platforms.

As part of these efforts, we aim to achieve long-term financial stability, as well as a reduction in our debt. Our focus on maintaining liquidity and reducing operating expenses reflects current trends, as well as projected future volume of mail and packages. We believe that financial stability is within reach with legislative and regulatory reform to address our overall cost structure and enhance our revenue-generating opportunities as we continue to identify and create innovative and affordable services, and deliver high levels of performance and service.

RESULTS OF OPERATIONS

SUMMARY

The major factors that impact our operating results include overall customer demand, the mix of postal services and contribution associated with those services, volume of mail and packages processed through our network and our ability to manage our cost structure in line with declining levels of mail volume, increased competition in the more labor-intensive Shipping and Packages business and an increasing number of delivery points. We operate as a single segment and report our performance as such.

Three Months Ended June 30, 2019

As more fully described below in *Operating Revenue and Volume*, our operating revenue for the three months ended June 30, 2019, increased \$12 million, or was essentially flat, compared to the same period last year.

The slight increase in operating revenue was primarily due to a Shipping and Packages revenue increase of \$250 million, or 4.8%, despite a volume decline of 47 million pieces, or 3.2%. We continued to see revenue growth in this service category during the three-month period, driven largely by the January 2019 price increases applicable to certain Competitive services.

The above increase in operating revenue was partially offset by the following:

- *First-Class Mail* revenue decrease of \$98 million, or 1.6%, with a volume decline of 361 million pieces, or 2.7%, reflecting the continuing migration from mail to electronic communication and transaction alternatives;
- *Marketing Mail* revenue decrease of \$121 million, or 3.0%, with a volume decline of 878 million pieces, or 4.7%, largely driven by customers transitioning to alternatives such as digital advertising. Also contributing to this decrease, revenue and volume from political and election mail decreased by approximately \$70 million and over 350 million pieces, compared to the same period last year, reflective of the election cycles; and
- *Periodicals* revenue decrease of \$38 million, or 11.2%, with a volume decline of 173 million pieces, driven by the continuing migration to electronic communication and digital advertising.

As more fully described below in *Operating Expenses*, our operating expenses for the three months ended June 30, 2019, increased \$797 million, or 4.3%, compared to the same period last year. The increase in operating expenses was primarily due to the following:

- Compensation and benefits expense increase of \$45 million, or 0.4%, due primarily to contractual wage adjustments, partially offset by a decrease in total work hours;
- Workers' compensation expense increase of \$832 million, nearly all of which was the result of changes in discount rates, which are outside of management's control; and
- Transportation expenses increase of \$86 million, or 4.6%, due to higher air transportation costs largely driven by higher air rates and volumes for certain carriers, as well as higher average jet fuel prices.

The above increases in operating expenses were partially offset by a decrease in retirement benefits expense of \$163 million, or 6.7%, primarily due to revised actuarial assumptions outside of management's control for CSRS and FERS unfunded retirement benefits amortization.

Overall, we reported a net loss of nearly \$2.3 billion for the three months ended June 30, 2019, compared to a net loss of nearly \$1.5 billion for the same period last year.

Nine Months Ended June 30, 2019

As more fully described below in *Operating Revenue and Volume*, our operating revenue for the nine months ended June 30, 2019, increased \$567 million, or 1.1%, compared to the same period last year. The increase in operating revenue was primarily due to the following:

- Shipping and Packages revenue increase of \$1.0 billion, or 6.3%, on volume growth of 52 million pieces, or 1.1%, as we continued to see growth in this service category during the nine-month period driven largely by the January 2019 price increases applicable to certain Competitive services and the expansion of e-commerce, particularly during the 2018 holiday season; and
- Other services revenue increase of \$199 million, or 7.1%, with the January 2019 price increases applicable to various Market-Dominant and Competitive services contributing to this increase, with *PO Box* services among the larger revenue increases in the category. Passport services also experienced a large revenue increase resulting from an April 2018 price increase.

The above increases in operating revenue were partially offset by the following:

- *First-Class Mail* revenue decrease of \$395 million, or 2.1%, with a volume decline of approximately 1.4 billion pieces, or 3.1%, reflecting the continuing migration from mail to electronic communication and transaction alternatives;
- *Marketing Mail* revenue decrease of \$59 million, or 0.5%, with a volume decline of 837 million pieces, or 1.4%, largely driven by customers transitioning to alternatives such as digital advertising;
- *International Mail* revenue decrease of \$128 million, or 6.2%, with a volume decline of 82 million pieces, due to declines in both inbound and outbound volume due to various pricing, political and economic factors; and
- *Periodicals* revenue decrease of \$70 million, or 7.1%, with a volume decline of 311 million pieces, driven by the continuing migration to electronic communication and digital advertising.

As more fully described below in *Operating Expenses*, our operating expenses for the nine months ended June 30, 2019, increased \$3.1 billion, or 5.5%, compared to the same period last year. The increase in operating expenses was primarily due to the following:

- Compensation and benefits expense increase of \$739 million, or 2.3%, due primarily to contractual wage adjustments, as well as overtime hours incurred during the 2018 holiday period;
- Workers' compensation expense increase of approximately \$2.5 billion, of which nearly \$2.4 billion was the result of changes in discount rates, which are outside of management's control; and
- Transportation expenses increase of \$370 million, or 6.2%, due to higher air and ground transportation costs. The increase in air transportation costs was largely driven by higher air rates and volumes for certain carriers, as well as higher average jet fuel prices. The increase in ground transportation costs was largely driven by higher unit costs per mile due to supplier cost pressures resulting in part from a national shortage of truck drivers, as well as higher average fuel costs.

The above increases in operating expenses were partially offset by the following decreases in operating expenses:

- Retirement benefits expense decrease of \$445 million, or 6.0%, due to revised actuarial assumptions for CSRS and FERS unfunded retirement benefits amortization, which are outside of management's control; and
- Other operating expenses decrease of \$142 million, or 1.9%, due to spending reductions in various categories.

Overall, we reported a net loss of nearly \$5.9 billion for the nine months ended June 30, 2019, compared to a net loss of nearly \$3.4 billion for the same period last year.

Non-GAAP Controllable Loss

In the day-to-day operation of our business, we focus on costs that can be managed in the course of normal business operations, such as salaries and transportation. We calculate controllable loss, a non-GAAP measure, by excluding items over which we have no control, such as PSRHBF actuarial revaluation and amortization expenses, workers' compensation expenses caused by actuarial revaluation and discount rate changes, and

retirement expenses caused by actuarial revaluation. Controllable loss should not be considered a substitute for net loss and other GAAP reporting measures.

The following table reconciles our GAAP net loss to controllable loss for the three and nine months ended June 30, 2019, and 2018:

(in millions)	Three Months Ended June 30,		Nine Months Ended June 30,	
	2019	2018	2019	2018
Net loss	\$ (2,256)	\$ (1,489)	\$ (5,875)	\$ (3,364)
PSRHBf unfunded liability amortization expense ¹	42	16	592	611
Change in workers' compensation liability resulting from fluctuations in discount rates	697	(137)	1,656	(694)
Other change in workers' compensation liability ²	9	(59)	11	(184)
CSRS unfunded liability amortization expense ³	360	456	1,080	1,369
FERS unfunded liability amortization expense ⁴	239	322	718	966
Change in normal cost of retiree health benefits due to revised actuarial assumptions ⁵	(168)	2	(168)	104
Controllable loss	<u>\$ (1,077)</u>	<u>\$ (889)</u>	<u>\$ (1,986)</u>	<u>\$ (1,192)</u>

¹ Expense for the accrual for the annual payment due to PSRHBf by September 30 of the respective year, for the amortization of the unfunded liability. The 2019 amounts are based on OPM's invoice received July 2, 2019, with updated discount rate assumptions. The 2018 amounts are based on OPM's invoice received July 19, 2018, with updated discount rate assumptions.

² Net amounts include changes in assumptions, valuation of new claims and revaluation of existing claims, less current year claim payments.

³ Expense for the accrual for the annual payment due to OPM by September 30 of the respective year, based on information provided by OPM, to amortize the unfunded CSRS retirement obligation. Payments are to be made through 2043 based on OPM invoices.

⁴ Expense for the accrual for the annual payment due to OPM by September 30 of the respective year, based on information provided by OPM, to amortize the unfunded FERS retirement obligation. Payments are to be made over a 30-year rolling period based on OPM invoices.

⁵ Represents the accrual for the portion of the increase in the annual normal cost payments due September 30, 2019, and 2018, attributable to revised actuarial assumptions and discount rate changes, based on OPM's invoices for the respective year. This amount represents the noncontrollable portion of the expense recorded for normal cost of retiree health benefits.

Our controllable loss increased \$188 million for the three months ended June 30, 2019, compared to the same period last year. This increase was largely driven by higher compensation and benefits expenses of \$45 million, higher transportation expenses of \$86 million, a \$24 million increase in other operating expenses, and the higher controllable portion of the normal cost of retiree health benefits expenses of \$117 million, partially offset by the lower controllable portion of workers' compensation of \$70 million.

Our controllable loss increased \$794 million for the nine months ended June 30, 2019, compared to the same period last year. This increase was largely driven by higher compensation and benefits expenses of \$739 million, higher transportation expenses of \$370 million, and the higher controllable portion of the normal cost of retiree health benefits expenses of \$353 million, partially offset by the \$567 million increase in operating revenue and the decrease in other operating expenses of \$142 million.

These items are discussed in greater detail in *Operating Revenue and Volume* and *Operating Expenses* below.

OPERATING REVENUE AND VOLUME

The combined categories of *First-Class Mail* and *Marketing Mail* continued to provide the majority of our revenue, despite long-term trends away from traditional paper communication and correspondence to electronic media. Although this migration to electronic media has resulted in significant volume declines in *First-Class Mail* over the last decade, *Marketing Mail* volume remained relatively steady between 2009 and 2016. However, *Marketing Mail* volume began to decline at a greater rate beginning in 2017 and continued to decline through the first half of 2018. Aside from a volume rebound between the second half of 2018 through the first quarter of 2019 that was driven by increases in political and election mail associated with the 2018 mid-term elections, *Marketing Mail* resumed its volume decline in the second and third quarters of 2019.

The following table summarizes our operating revenue and volume for the three and nine months ended June 30, 2019, and 2018, by each service category:

<i>(in millions)</i>	Three Months Ended June 30,		Nine Months Ended June 30,	
	2019	2018	2019	2018
Operating Revenue:				
First-Class Mail ¹	\$ 5,859	\$ 5,957	\$ 18,758	\$ 19,153
Marketing Mail ²	3,861	3,982	12,359	12,418
Shipping and Packages ³	5,416	5,166	17,319	16,299
International	615	617	1,922	2,050
Periodicals	302	340	910	980
Other ⁴	1,033	1,012	3,021	2,822
Total operating revenue	\$ 17,086	\$ 17,074	\$ 54,289	\$ 53,722
Volume:				
First-Class Mail ¹	13,098	13,459	42,155	43,519
Marketing Mail ²	17,668	18,546	57,356	58,193
Shipping and Packages ³	1,423	1,470	4,711	4,659
International	204	222	662	744
Periodicals	1,182	1,355	3,543	3,854
Other ⁵	85	96	240	257
Total volume	33,660	35,148	108,667	111,226
¹ Excludes <i>First-Class Package Service - Retail</i> .				
² Excludes <i>Marketing Mail Parcels</i> .				
³ Includes <i>Priority Mail, USPS Retail Ground, Parcel Select Mail, Parcel Return Service Mail, Marketing Mail Parcels, Package Service Mail, First-Class Package Service - Retail, First-Class Package Service - Commercial and Priority Mail Express</i> .				
⁴ Revenue includes <i>PO Box services, Certified Mail, Return Receipts, Insurance, Other Ancillary Services, Shipping and Mailing Supplies, Collect on Delivery, Registered Mail, Stamped Envelopes and Cards, Money Orders and Other services</i> .				
⁵ Volume includes Postal Service internal mail and free mail provided to certain congressionally-mandated groups.				

For the three months ended June 30, 2019, *First-Class Mail* generated approximately 34% of operating revenue, a 1% decrease from the same period last year, and approximately 39% of our volume, a 1% increase compared to the same period last year. *Marketing Mail* generated approximately 23% of operating revenue, which was essentially unchanged compared to the same period last year, and approximately 52% of our volume, a 1% decrease from the same period last year.

For the nine months ended June 30, 2019, *First-Class Mail* generated approximately 35% of operating revenue, and approximately 39% of our volume, both essentially unchanged compared to the same period last year. *Marketing Mail* generated approximately 23% of operating revenue, which was essentially unchanged compared to the same period last year, and approximately 53% of our volume, a 1% increase from the same period last year.

We continued to experience positive overall results in our Shipping and Packages category, and it represented approximately 32% of our revenue for both the three and nine months ended June 30, 2019, a 2% increase from the same periods last year. Shipping and Packages generated approximately 4% of our volume for both the three and nine months ended June 30, 2019, which was essentially unchanged compared to the same periods last year.

Although revenue and volume are closely linked to the strength of the U.S. economy and changes in how our customers use the mail, we have proactively targeted opportunities to grow our business. We continue to focus on our customers' needs and have increased our marketing investment in mail and package innovation. However, we also recognize that revenue growth is constrained by laws and regulations restricting the types of products, services and pricing we may offer to our customers and the speed with which we can bring new products to market.

We anticipate that *First-Class Mail* will continue to lose volume in future years with the migration to electronic communication and transactional alternatives resulting from technological changes. To address the long-term trend that such changes have had on our *First-Class Mail* revenue and volume, we have been working with the mailing industry to slow the decline through mailing promotions and leveraging the high open-and-read rates of, for example, bills and statements for additional customer engagement and education.

We have also focused on providing new services and innovating with *Marketing Mail*. We have expanded service offerings such as *Informed Delivery*, which enables customers to preview mail and manage packages scheduled to arrive as a means of merging digital and physical mail, and we believe these service offerings will further improve the value of *Marketing Mail*.

Our Shipping and Packages category has historically shown revenue and volume growth as a result of our successful efforts to compete in shipping services, including last-mile e-commerce fulfillment markets and Sunday delivery as well as end-to-end markets. We have also focused on implementing marketing campaigns and developed strategic business partnerships that help us capitalize on the growing e-commerce business. By offering day-specific delivery on *Priority Mail Express* packages, improved tracking and text alerts, and up to \$50 of free insurance on most *Priority Mail* packages, we have demonstrated our responsiveness to our customers.

However, our Shipping and Packages category is subject to intense competition which significantly impacts both revenue and volume. Certain major customers have recently begun diverting additional volume from our network by in-sourcing the last-mile delivery. These customers are also aggressively pricing their products and services in order to fill their networks and grow package density.

In January 2018, we implemented price increases on certain Market-Dominant and Competitive services by an average of 1.9% and 4.1%, respectively. In January 2019, we implemented price increases for certain Market-Dominant and Competitive services by an average of 2.5% and 7.4%, respectively. In late June 2019, we implemented dimensional weighting provisions that amount to price increases for certain Shipping and Packages subcategories.

First-Class Mail

First-Class Mail, presented in this report as a mail class and a Market-Dominant service category, includes cards, letters and flats. Prices of *First-Class Mail*, our most profitable service category, are the same regardless of how far the mail travels. Because *First-Class Mail* is classified by law as Market-Dominant, price increases are currently generally subject to a price cap based on the Consumer Price Index for All Urban Consumers ("CPI-U").

For the three months ended June 30, 2019, *First-Class Mail* revenue decreased \$98 million, or 1.6%, and volume declined 361 million pieces, or 2.7%, compared to the same period last year. For the nine months ended June 30, 2019, *First-Class Mail* revenue decreased \$395 million, or 2.1%, and volume declined approximately 1.4 billion pieces, or 3.1%, compared to the same period last year. The most significant factor contributing to the declining trend in *First-Class Mail* volume was the continuing migration from mail to electronic communication and transaction alternatives. Revenue declined at a slower rate than volume for both the three and nine months ended June 30, 2019, due to the January 2019 price increase applicable to Market-Dominant services.

Marketing Mail

USPS Marketing Mail (more commonly, *Marketing Mail*), presented as a mail class and a Market-Dominant service category, generally consists of advertising, newsletters, catalogs, small marketing parcels and other printed matter not required to be processed and delivered as *First-Class Mail* or *Periodicals*.

Marketing Mail has generally proven to be a relatively resilient marketing channel, and its value to U.S. businesses remains strong due to healthy customer returns on investment, and better data and technology integration. Between 2009 and 2016, *Marketing Mail* experienced relatively flat volume. However, *Marketing Mail* volume began to decline at a greater rate beginning in 2017 and continued to decline through the first half of 2018. Aside from a volume rebound between the second half of 2018 through the first quarter of 2019 that was driven by increases in political and election mail associated with the 2018 mid-term elections, *Marketing Mail* resumed its volume decline in the second and third quarters of 2019.

For the three months ended June 30, 2019, *Marketing Mail* revenue decreased \$121 million, or 3.0%, and volume declined 878 million pieces, or 4.7%, compared to the same period last year. For the nine months ended June 30, 2019, *Marketing Mail* revenue decreased \$59 million, or 0.5%, and volume declined by 837 million pieces, or 1.4%, compared to the same period last year. *Marketing Mail* revenue is impacted by the volume of political and election mail with the mailings associated with periodic primary and general election seasons.

For the three months ended June 30, 2019, our revenue and volume from political and election mail decreased by approximately \$70 million and over 350 million pieces, respectively, compared to the same period last year. For the nine months ended June 30, 2019, our revenue and volume from political and election mail increased by approximately \$160 million and nearly 1.0 billion pieces, respectively, compared to the same period last year. If not for the positive impact of political and election mail associated with the 2018 mid-term election season during the first quarter of 2019, *Marketing Mail* revenue and volume would have decreased to an even greater extent for the nine months ended June 30, 2019.

Marketing Mail is subject to intense competition, and price increases are generally capped at the rate of inflation. *Marketing Mail* volume is somewhat reflective of the cyclical nature of the U.S. economy, although targeted advertising campaigns can stimulate demand for this service, and our customers have used *Marketing Mail* to mail to more targeted prospects.

Shipping and Packages

The following table summarizes our operating revenue and volume for Shipping and Packages for the three and nine months ended June 30, 2019, and 2018, by each service subcategory:

(in millions)	Three Months Ended June 30,		Nine Months Ended June 30,	
	2019	2018	2019	2018
Shipping and Packages Revenue:				
Priority Mail Services ¹	\$ 2,510	\$ 2,409	\$ 8,023	\$ 7,752
Parcel Services ²	1,612	1,594	5,337	5,052
First-Class Package Services ³	1,109	975	3,345	2,878
Package Services	185	188	614	617
Total Shipping and Packages revenue	\$ 5,416	\$ 5,166	\$ 17,319	\$ 16,299
Shipping and Packages Volume:				
Priority Mail Services ¹	270	268	866	852
Parcel Services ²	679	737	2,324	2,377
First-Class Package Services ³	339	320	1,056	949
Package Services	135	145	465	481
Total Shipping and Packages volume	1,423	1,470	4,711	4,659
¹ Includes <i>Priority Mail</i> , a 1-3 business day delivery service; <i>Priority Mail Express</i> , an overnight delivery service available 365 days per year; and <i>USPS Retail Ground</i> , a retail-only Competitive service priced identically and functionally equivalent to <i>Priority Mail</i> for Zones 1-4.				
² Includes <i>Parcel Select</i> , <i>Parcel Return</i> , and <i>Marketing Mail Parcels</i> .				
³ Includes <i>First-Class Package Services - Retail</i> and <i>First-Class Package Services - Commercial</i> .				

Our Shipping and Packages category has historically shown revenue and volume growth as a result of our successful efforts to compete in shipping services, including last-mile e-commerce fulfillment markets and Sunday delivery as well as end-to-end markets. However, this service category is subject to intense competition which significantly impacts both our revenue and volume. Shipping and Packages revenue and volume are historically greatest in the first quarter of the year, driven by consumers' continued use of online shopping, which provided a surge in package volume with a record number of packages delivered during both the calendar year 2017 and 2018 holiday seasons.

Shipping and Packages revenue increased 4.8%, despite a volume decline of 3.2%, for the three months ended June 30, 2019, compared to the same period last year. Shipping and Packages revenue increased 6.3%, on volume growth of 1.1%, for the nine months ended June 30, 2019, compared to the same period last year. The revenue increases for both the three-month and nine-month periods were largely due to the January 2019 price increases associated with certain Competitive services and the continued expansion of e-commerce. The volume decline during the three-month period largely resulted from intense competition and certain major commercial customers diverting additional volume from our Parcel Services and Package Services subcategories by in-sourcing the last-mile delivery.

Priority Mail Services

Priority Mail Services is our Shipping and Packages subcategory that includes *Priority Mail*, *Priority Mail Express* and *USPS Retail Ground*. *Priority Mail* and *Priority Mail Express* services allow customers the ability to send documents and packages requiring expedited transportation and handling. While Priority Mail Services revenue has historically grown year-over-year, its service offerings are somewhat price sensitive, particularly with retail customers, and its growth rate has been lower than other Shipping and Packages subcategories used by commercial customers.

Priority Mail Services accounted for our largest portion of Shipping and Packages revenue, representing approximately 46% of the total for both the three and nine months ended June 30, 2019, compared to approximately 47% and 48% for the same periods last year. However, Priority Mail Services accounted for approximately 19% and 18% of the total Shipping and Packages volume for the three and nine months ended June 30, 2019, respectively, compared to 18% for each of the same periods last year.

For the three months ended June 30, 2019, Priority Mail Services revenue increased 4.2% on volume growth of 0.7%, compared to the same period last year. For the nine months ended June 30, 2019, Priority Mail Services revenue increased 3.5% on volume growth of 1.6%, compared to the same period last year. Revenue grew more than volume for the periods due to the January 2018 and January 2019 price increases applicable to Competitive services.

Parcel Services

Our Parcel Services subcategory includes Competitive services *Parcel Select* and *Parcel Return*, as well as Market-Dominant *USPS Marketing Mail Parcels* (more commonly, *Marketing Mail Parcels*). *Parcel Select* and *Parcel Return* services largely consist of last-mile deliveries, offered to large bulk shippers that perform more of the sorting before dropping parcels deeper into our network.

For the three months ended June 30, 2019, revenue from Parcel Services increased 1.1%, despite a volume decline of 7.9%, compared to the same period last year. For the nine months ended June 30, 2019, revenue from Parcel Services increased 5.6%, despite a volume decline of 2.2%, compared to the same period last year. This subcategory is primarily a last-mile service that bypasses much of our infrastructure and therefore is one of our lowest-priced package services, and as a result, produces a lower-contribution per piece when compared to many of our other services. Volume declined at a greater rate in the three months ended June 30, 2019, due to certain major commercial customers diverting additional volume from our *Parcel Select* and *Parcel Return* services by in-sourcing the last-mile delivery. Revenue grew despite the volume declines for both periods largely due to the January 2018 and January 2019 price increases applicable to Competitive services.

First-Class Package Services

Our First-Class Package Services subcategory includes the competitively priced *First-Class Package Service - Retail*, a Competitive service for under-13-ounce packages targeted to retail customers, and *First-Class Package Service - Commercial*, an under-one-pound Competitive service targeted to commercial customers. This subcategory offers commercial customers that ship primarily lightweight fulfillment parcels the lowest-priced expedited end-to-end tracked package option in the marketplace. First-Class Package Services revenue and volume performance has experienced strong increases for the past several years, particularly from our commercial customers. These increases are primarily attributable to growth in e-commerce.

For the three months ended June 30, 2019, First-Class Package Services revenue increased 13.7% on strong volume growth of 5.9%, compared to the same period last year. For the nine months ended June 30, 2019, First-Class Package Services revenue increased 16.2% on strong volume growth of 11.3%, compared to the same period last year. Revenue grew more than volume for the periods due to the January 2018 and January 2019 price increases applicable to Competitive services.

Package Services

Our Package Services subcategory is a Market-Dominant service that includes both Bound Printed Matter for materials up-to-15 pounds and Library and Media Mail for materials up-to-70 pounds. For the three months ended June 30, 2019, Package Services revenue decreased 1.6% on a volume decline of 6.9%, compared to the same period last year. For the nine months ended June 30, 2019, Package Services revenue decreased 0.5% on a volume decline of 3.3%, compared to the same period last year. Revenue declines were less than the volume declines for the periods due to the January 2018 and January 2019 price increases applicable to Competitive services.

International Mail

Our *International Mail* category includes several services that enable customers, both domestic and abroad, to send international mail, including postcards, envelopes, flats and packages with either standard or express delivery options. "Outbound" services, which allow customers in the U.S. to send mail and packages to other countries, generate approximately two thirds of *International Mail* revenue, but "inbound" services are the opposite, generating two thirds of volume but only a third of the revenue. This is primarily due to the smaller size and lower rates for inbound international e-commerce packages.

For the three months ended June 30, 2019, *International Mail* revenue decreased 0.3% and volume declined 8.1%, compared to the same period last year. For the nine months ended June 30, 2019, *International Mail* revenue decreased 6.2% and volume declined 11.0%, compared to the same period last year. These revenue decreases are directly correlated to the declines in both inbound and outbound volume due to various pricing, political and economic factors.

The U.S. is a member of the Universal Postal Union ("UPU"), a specialized agency of the United Nations that facilitates the exchange of international mail. The Postal Service is the designated postal operator for the U.S. Under the UPU, payments to the designated postal operator for the delivery of foreign origin letter post mail are known as "terminal dues." In August 2018, the President issued a Presidential Memorandum identifying reforms that are needed to the terminal dues system in order for the U.S. to continue to participate in the UPU. In October 2018, the Administration determined that meaningful progress towards achieving those reforms was not being made within the UPU, and the Secretary of State gave notice to the UPU that the U.S. is withdrawing from the UPU effective October 18, 2019. During this one-year period, the U.S. Department of State will seek to negotiate agreements that resolve the problems discussed in the Memorandum.

If such negotiations are successful, the U.S. will rescind the notice of withdrawal before it takes effect. The UPU will hold an extraordinary Congress from September 24 to 26, 2019, at which time efforts to accommodate the concerns of the U.S. and other countries with the terminal dues system will be considered and may or may not be adopted. We are accordingly planning for the contingency that the U.S. may no longer be a member of the UPU by the middle of October 2019, in the event that a solution that accommodates U.S. concerns is not achieved.

Periodicals

Periodicals, also presented as a mail class and a Market-Dominant service category, is designed for newspapers, magazines and other periodical publications whose primary purpose is transmitting information to an established group of subscribers. For the three months ended June 30, 2019, *Periodicals* revenue decreased 11.2% and volume declined 12.8%, compared to the same period last year. For the nine months ended June 30, 2019, *Periodicals* revenue decreased 7.1% and volume declined 8.1%, compared to the same period last year.

Periodicals revenue and volume have been in decline for more than a decade as trends in hard-copy reading behavior and shifts of advertising away from print have depressed this business. The *Periodicals* category is not expected to rebound as electronic content continues to grow in popularity with the public.

Other

Other services include ancillary services such as *Certified Mail*, *PO Box* services, and *Return Receipt* services. Also included in this category are money orders and passport services. Other services revenue increased 2.1% and 7.1% for the three and nine months ended June 30, 2019, respectively, compared to the same periods last year. The January 2019 price increases applicable to various Market-Dominant and Competitive services contributed to these increases, with *PO Box* services among the larger revenue increases in this category. Passport services also experienced a large revenue increase resulting from an April 2018 price increase.

OPERATING EXPENSES

In an effort to align our resources with anticipated future mail and package volume, we continue to aggressively manage operating expenditures under management's control.

Our mail processing and distribution network was designed to provide overnight delivery service of *First-Class Mail* within specified delivery areas for a much higher volume of mail than we are required to process and deliver today, and the network's legacy capabilities are not completely aligned to today's mail mix and volumes. Consequently, certain of our processing and distribution facilities continue to operate at less than full capacity. Our challenge to contain costs is also compounded by the increasing number of delivery points, which, when combined with lower mail volume, has resulted in a drop in the average number of pieces delivered per delivery point per day from approximately 5.5 pieces in 2007 to 3.5 pieces in 2018, a reduction of approximately 37%.

Compensation and Benefits

Compensation and benefits is our largest operating expense category. These expenses consist of costs, other than retirement, related to our active career and non-career employees. Overall, our compensation and benefits expenses increased 0.4% and 2.3% for the three and nine months ended June 30, 2019, respectively, compared to the same periods last year.

The following table presents compensation and benefits expenses for the three and nine months ended June 30, 2019, and 2018:

<i>(in millions)</i>	Three Months Ended June 30,		Nine Months Ended June 30,	
	2019	2018	2019	2018
Compensation	\$ 9,374	\$ 9,300	\$ 29,335	\$ 28,551
Employee health benefits	1,271	1,297	3,843	3,887
Other	77	80	237	238
Total compensation and benefits	\$ 10,722	\$ 10,677	\$ 33,415	\$ 32,676

Compensation

Compensation expense increased 0.8% and 2.7% for the three and nine months ended June 30, 2019, respectively, compared to the same periods last year. These increases were primarily due to contractual wage adjustments and additional overtime hours during the 2018 holiday season, compared to the same periods last year.

For the three months ended June 30, 2019, total work hours were approximately 288 million, which was a decrease of 0.6% compared to the nearly 290 million total work hours for the three months ended June 30, 2018. This decrease was the result of management's efforts to reduce hours in line with volume workloads.

For the nine months ended June 30, 2019, total work hours were approximately 886 million, which was an increase of 0.5%, compared to approximately 882 million total work hours for the nine months ended June 30, 2018. This increase occurred in the first half of the fiscal year as a result of additional overtime hours for peak period, as well as political and election mail.

The number of career employees at June 30, 2019, was approximately 482,000, an increase of approximately 5,500 employees, or 1.1%, compared to the same date a year ago. This increase primarily reflects the conversion of non-career employees to career status, in accordance with our contractual agreements.

The number of non-career employees at June 30, 2019, was approximately 127,000, a decrease of approximately 3,200 employees, or 2.5%, compared to the same date a year ago. This decrease primarily reflects the conversion of non-career employees to career status, in accordance with our contractual agreements.

In May 2019, we reached a new collective bargaining agreement with the National Rural Letter Carriers' Association ("NRLCA"), which was subsequently ratified by NRLCA membership in August 2019. The previous contract with the NRLCA expired on May 20, 2018. The new contract includes general wage increases totaling 3.4% over the three-year term of the contract (1.3% of which is retroactive to November 2018) with a Cost of Living Allowance ("COLA") base of April 2018 (the first COLA payment is retroactive to September 1, 2018), the introduction of proportional COLA for new career hires, a reduction in our share of health insurance premiums, no increase in the Equipment Maintenance Allowance base rate, additional operational flexibility to use Rural Carrier Associates, administrative cost savings from elimination of mail counts over the contract term, enhanced health benefits for non-career rural employees, and a comprehensive Memorandum of Understanding on implementation of the rural standards study. The new contract will expire on May 20, 2021.

In September 2018, we agreed to extend contract negotiations relating to a new collective bargaining agreement with the American Postal Workers Union, AFL-CIO ("APWU"). The contract with the APWU expired on September 20, 2018, and the respective parties mutually agreed to extend negotiations beyond the deadline. On December 21, 2018, our negotiations with the APWU came to an impasse. On April 3, 2019, the APWU invoked mediation. On June 7, 2019, the mediation process concluded and the parties have moved forward with interest arbitration, during which a three-member arbitration panel will decide the terms of the successor collective bargaining agreement. The respective parties will continue to follow the current agreement until a new contract is reached through the interest arbitration process. No new agreement has been reached as of the date of this report.

Employee Health Benefits

Our expense for employee health benefits (which includes the employer portion of Medicare taxes) is most significantly impacted by the number of employees electing coverage and the premium costs of the selected plans. Our active employees may participate in the Federal Employees Health Benefits ("FEHB") Program, which OPM administers. We account for employee health benefit costs as an expense in the period in which our contributions to the plans under the program are due. Separate from FEHB, we offer our own self-insured healthcare plan to certain non-career employees who are ineligible for FEHB.

Employee health benefits expense decreased 2.0% and 1.1% for the three and nine months ended June 30, 2019, respectively, compared to the same periods last year, driven by the lower contribution rate of the employer portion of healthcare premiums that we paid and by management efforts to provide employees with information and tools for selecting optimal health benefit plans. These decreases were partially offset by a 1.2% increase in average premium contributions affecting the three and nine months ended June 30, 2019, and the small increase in number of career employees, as previously discussed.

Our share of healthcare premiums for our employees represented 71.8% and 72.5% of the total healthcare premium costs for the three months ended June 30, 2019, and 2018, respectively. Our share of healthcare premiums for our employees represented 72.1% and 72.9% of the total healthcare premium costs for the nine months ended June 30, 2019, and 2018, respectively. These decreases in our share of healthcare premium costs for employees were consistent with the terms of our contractual agreements.

Retirement Plan Expenses

The majority of our career employees participate in one of two U.S. government defined benefit pension programs, CSRS and FERS, based on the starting date of their employment with us or another U.S. government employer. We incur normal costs (the amount estimated to be equal to the employer portion of retirement benefits for participating employees and their qualifying survivors, upon retirement, for each employee's current year service) for FERS employees; however, by law we do not pay normal costs for CSRS retirement benefits. Career employees may also participate in the Thrift Savings Plan ("TSP"), a defined contribution retirement savings and investment plan administered by the Federal Retirement Thrift Investment Board. Our TSP expenses are related only to our contributions for FERS employees who participate in the TSP.

FERS Employees' Current Year Service

Our expense for FERS employees' current year service consists of our contributions for FERS normal costs, Social Security and TSP, and is reported within *Retirement benefits* under *Operating expenses* in the accompanying unaudited *Statements of Operations*. We record our contributions to FERS, Social Security and TSP as an expense in the period during which the contribution is due. We recognize the expense for each period's legally required contribution, and record a liability for any contribution due and unpaid at the end of each reporting period. The amounts owed related to unfunded FERS retirement benefits is reported within *Retirement benefits* in the accompanying *Balance Sheets*, as discussed below. For additional information, see below and see *Item 1. Financial Statements, Notes to Unaudited Financial Statements, Note 9 - Retirement Plans*.

The following table presents the details of FERS employees' current year service expenses for the three and nine months ended June 30, 2019, and 2018:

<i>(in millions)</i>	Three Months Ended June 30,		Nine Months Ended June 30,	
	2019	2018	2019	2018
FERS normal costs	\$ 878	\$ 871	\$ 2,635	\$ 2,609
Social Security	522	519	1,640	1,599
TSP	282	276	854	829
Total FERS employees' current year service	\$ 1,682	\$ 1,666	\$ 5,129	\$ 5,037

FERS employees' current year service expenses increased 1.0% and 1.8% for the three and nine months ended June 30, 2019, respectively, compared to the same periods last year.

Our FERS normal cost contribution rates remained steady at 13.7% of basic pay for most participants during both 2019 and 2018. Expenses for the FERS normal costs, Social Security and employer TSP contributions were essentially flat for both the three and nine months ended June 30, 2019, compared to the same periods last year. As most of our employees participate in FERS, this was also consistent with the trends in compensation for the period, previously described in *Compensation*.

CSRS and FERS Unfunded Retirement Benefits Amortization

OPM periodically notifies us regarding its revaluation of unfunded CSRS and FERS retirement benefits. The amounts we record as expenses for our unfunded CSRS and FERS liabilities may be significantly impacted by changes in actuarial assumptions used by OPM to revalue the unfunded liabilities. Prior to 2018, OPM calculated these obligations using government-wide economic and demographic data, rather than Postal Service-specific demographics and economic assumptions. In October 2017, OPM issued a new rule announcing its intent to calculate future unfunded CSRS and FERS obligations using Postal Service-specific demographic assumptions, effective with the October 2018 actuarial report.

In its actuarial report, OPM projects the annual amortization payments due September 30, 2019, to be \$1.4 billion for CSRS and \$958 million for FERS. Accordingly, we have accrued \$360 million and \$1.1 billion for the three and nine months ended June 30, 2019, respectively, for the CSRS amortization expense. Likewise, we have accrued \$239 million and \$718 million for the three and nine months ended June 30, 2019, respectively, for the FERS amortization expense.

Our expense for CSRS and FERS unfunded retirement benefits amortization is reported within *Retirement benefits* under *Operating expenses* in the accompanying unaudited *Statements of Operations*. The following table presents the expense recorded for CSRS and FERS unfunded retirement benefits amortization for the three and nine months ended June 30, 2019, and 2018:

(in millions)	Three Months Ended June 30,		Nine Months Ended June 30,	
	2019	2018	2019	2018
CSRS unfunded retirement benefits amortization ¹	\$ 360	\$ 456	\$ 1,080	\$ 1,369
FERS unfunded retirement benefits amortization ²	239	322	718	966
Total CSRS and FERS unfunded retirement benefits amortization	\$ 599	\$ 778	\$ 1,798	\$ 2,335

¹ Expense for the accrual for the annual payment due to OPM by September 30 of the respective year, based on information provided by OPM, to amortize the unfunded CSRS retirement obligation. Payments are to be made through 2043 based on OPM invoices.

² Expense for the accrual for the annual payment due to OPM by September 30 of the respective year, based on information provided by OPM, to amortize the unfunded FERS retirement obligation. Payments are to be made over a 30-year rolling period based on OPM invoices.

Our CSRS and FERS unfunded retirement benefits amortization expenses decreased 23.0% for both the three and nine months ended June 30, 2019, compared to the same periods last year. These decreases were largely due to lower OPM projected annual amortization payments resulting from revised actuarial assumptions and discount rate changes compared to the previous periods.

We expect to receive invoices from OPM for the actual amounts due September 30, 2019, for CSRS and FERS during the fourth quarter of 2019, and the amounts invoiced could differ from the original projected amounts, due to changes in experience, discount rates and/or actuarial assumptions as of the calculation date.

The following table presents the combined retirement benefits expenses for the three and nine months ended June 30, 2019, and 2018:

(in millions)	Three Months Ended June 30,		Nine Months Ended June 30,	
	2019	2018	2019	2018
FERS employees' current year service	\$ 1,682	\$ 1,666	\$ 5,129	\$ 5,037
CSRS and FERS unfunded retirement benefits amortization	599	778	1,798	2,335
Total retirement benefits expenses	\$ 2,281	\$ 2,444	\$ 6,927	\$ 7,372

Our retirement benefits expenses decreased 6.7% and 6.0% for the three and nine months ended June 30, 2019, respectively, compared to the same periods last year. These decreases were largely due to the decreases in the CSRS and FERS unfunded retirement benefits amortization, as previously discussed above.

For additional information, see *Item 1. Financial Statements, Notes to Unaudited Financial Statements, Note 9 - Retirement Plans*.

Retiree Health Benefits

We participate in federal employee benefit programs for retiree health benefits. Retirees who participated in FEHB for the five years immediately preceding their retirement may continue to participate in the plan during retirement. Qualifying survivors of retirees are also eligible to receive benefits.

In accordance with PAEA, since the beginning of 2017, the PSRHBF has been used to fund our share of retiree health benefit premiums. Also since 2017, we have been obligated to pay into the PSRHBF the actuarially determined normal costs of retiree health benefits attributable to the service of our employees, as well as the amortization payment for the PSRHBF unfunded liability. Our total retiree health benefits expenses therefore

consists of both the normal and the amortization costs. We record the required contributions to the plan as an expense in the period in which each contribution is due.

Based on preliminary calculations provided by OPM in October 2018 and our updates to discount rate assumptions, we originally projected the PSRHBF amortization payment amount due September 30, 2019, to be \$1.1 billion, and therefore accrued an expense of \$550 million for the first six months of 2019. On July 2, 2019, we received OPM's invoice for 2019, which indicated the year-end amortization payment amount due is \$789 million. This amount was lower than our original estimate largely due to OPM's use of revised discount rates. Due to the lower-than-estimated invoiced amount, we have adjusted our accrual for the amortization payment, resulting in expenses of \$42 million and \$592 million for the three and nine months ended June 30, 2019, respectively.

Also, based on preliminary calculations provided by OPM in October 2018 using updated discount rate assumptions, we originally estimated the amount of our PSRHBF normal cost payment due September 30, 2019, to be \$4.0 billion, and therefore accrued an expense of \$2.0 billion for the first six months of 2019. OPM's July 2, 2019 invoice indicated the year-end normal cost payment amount due is approximately \$3.8 billion. This amount was lower than our original estimate largely due to OPM's use of revised discount rates. Due to the lower-than-estimated invoiced amount, we have adjusted our accrual for the normal costs, resulting in expenses of \$831 million and \$2.8 billion for the three and nine months ended June 30, 2019, respectively.

For the three months ended June 30, 2019, our total retiree health benefits expenses decreased by \$27 million, or 3.0%, compared to the same period last year. Of this decrease, \$26 million is attributable to an increase in the amortization of the PSRHBF unfunded liability, while normal cost decreased by \$53 million.

For the nine months ended June 30, 2019, our total retiree health benefits expenses increased by \$62 million, or 1.8%, compared to the same period last year. Of this increase, \$81 million is attributable to normal cost, while amortization of the PSRHBF unfunded liability decreased by \$19 million.

For additional information, see *Item 1. Financial Statements, Notes to Unaudited Financial Statements, Note 10 - Health Benefits Plans, Retirees.*

Workers' Compensation Expenses

Our employees injured on the job are covered by the Federal Employees' Compensation Act ("FECA"), administered by the U.S. Department of Labor's ("DOL") Office of Workers' Compensation Programs, which makes all decisions regarding injured workers' eligibility for benefits. We are legally mandated to participate in the federal workers' compensation program. Our workers' compensation expense reflects the impacts of changes in discount rates, as well as the actuarial valuation of new workers' compensation cases and revaluation of existing ones. We reimburse the DOL for all workers' compensation benefits paid to or on behalf of our employees, plus an administrative fee.

On a daily basis we focus on costs that can be managed in the course of normal business operations, such as salaries and transportation. Certain aspects of workers' compensation can be managed through human resource initiatives, safety measures and training. Other workers' compensation costs cannot be managed in the course of normal business operations and are less predictable, including expenses caused by actuarial revaluation and discount rate changes. We subtract the cash payments made by DOL on behalf of workers' compensation obligations, which are relatively predictable, from total workers' compensation expense in order to determine the non-cash component of workers' compensation expense, a non-GAAP financial measure.

The following table presents the components of workers' compensation expense, including the cash payments made by DOL on behalf of workers' compensation obligations, for the three and nine months ended June 30, 2019, and 2018:

<i>(in millions)</i>	Three Months Ended June 30,		Nine Months Ended June 30,	
	2019	2018	2019	2018
Impact of discount rate changes	\$ 697	\$ (137)	\$ 1,656	\$ (694)
Actuarial revaluation of existing cases	28	49	80	(112)
Cost of new cases	291	275	893	920
Administrative fee	22	19	67	58
Total workers' compensation expense	\$ 1,038	\$ 206	\$ 2,696	\$ 172
Less cash payments made by DOL on behalf of workers' compensation obligations	(332)	(402)	(1,029)	(1,050)
Total workers' compensation non-cash expense (benefit)	\$ 706	\$ (196)	\$ 1,667	\$ (878)

For the three months ended June 30, 2019, the portion of workers' compensation expense due to the impact of discount rate changes increased \$834 million, compared to the same period last year. For the nine months ended June 30, 2019, the portion of workers' compensation expense due to the impact of discount rate changes increased nearly \$2.4 billion, compared to the same period last year. These changes are the result of changes in interest rates, outside of management's control.

The combined costs of new workers' compensation cases and revaluation of existing workers' compensation cases decreased by \$5 million for the three months ended June 30, 2019, and increased by \$165 million for the nine months ended June 30, 2019, compared to the same periods last year. Changes in actuarial valuation are primarily attributable to the combined impacts of routine changes in actuarial estimation, the progression of existing cases and updated cost-of-living-adjustment ("COLA") assumptions, which are largely outside of management's control.

Under FECA, workers' compensation claims for many types of injuries cannot be settled through lump-sum payments, and in some instances with regard to those claims, compensation may be paid over many years. Federal law grants COLA rates to those claims, and these factors result in substantially higher costs to us than would likely result if we managed our own claims. Additionally, since we do not manage the FECA program, we have no ability to control the significant administrative costs associated with managing the claims and payments process.

For additional information, see *Item 1. Financial Statements, Notes to Unaudited Financial Statements, Note 11 - Workers' Compensation*.

Transportation

Transportation expenses include the costs we incur to transport mail and other products between our facilities, comprising highway, air and international transportation contracts, plus contract delivery services.

With the exception of contract delivery services, our costs to deliver mail and other products to delivery points are not included within *Transportation* but in *Compensation and benefits* for employee costs and in *Other operating expenses* for fuel, vehicle maintenance and repair, and other costs. Furthermore, transportation expenses do not include the compensation of employees responsible for transporting mail and other products between our facilities.

Variations in the volume and weight of mail transported, the mode of transportation used, and fuel prices have significant impact on transportation expenses.

The components of transportation expenses for the three and nine months ended June 30, 2019, and 2018, are presented in the following table:

<i>(in millions)</i>	Three Months Ended June 30,		Nine Months Ended June 30,	
	2019	2018	2019	2018
Highway	\$ 1,040	\$ 1,037	\$ 3,462	\$ 3,258
Air	790	693	2,375	2,178
International	130	142	441	475
Other	8	10	32	29
Total transportation expenses	\$ 1,968	\$ 1,882	\$ 6,310	\$ 5,940

Overall, transportation expenses increased 4.6% and 6.2% for the three and nine months ended June 30, 2019, respectively, compared to the same periods last year.

Highway transportation expenses increased 0.3% and 6.3% during the three and nine months ended June 30, 2019, respectively, compared to the same periods in last year. These increases were due primarily to higher average diesel fuel prices, an increase in the number of miles driven and higher unit costs per mile due to supplier cost pressures resulting in part from a national shortage of truck drivers, though the diesel fuel prices began to recede during the three months ended June 30, 2019.

Air transportation expenses increased 14.0% and 9.0% during the three and nine months ended June 30, 2019, respectively, compared to the same periods last year. These increases were due primarily to higher air rates and volumes for certain carriers and higher average jet fuel prices.

International transportation expenses are related only to outbound services that allow customers in the U.S. to send mail and packages to other countries. For the three and nine months ended June 30, 2019, international transportation expenses decreased 8.5% and 7.2%, respectively, compared to the same periods last year, primarily due to decreases in our international service volumes.

Other Operating Expenses

Other operating expenses for the three and nine months ended June 30, 2019, and 2018, are detailed in the following table:

<i>(in millions)</i>	Three Months Ended June 30,		Nine Months Ended June 30,	
	2019	2018	2019	2018
Supplies and services	\$ 695	\$ 716	\$ 2,107	\$ 2,243
Depreciation and amortization	430	421	1,271	1,247
Rent and utilities	410	384	1,274	1,271
Information technology and communications	223	238	631	659
Vehicle maintenance service	151	164	471	477
Rural carrier equipment maintenance	143	138	441	406
Fuel - delivery vehicles	124	125	372	375
Miscellaneous other	275	241	778	809
Total other operating expenses	\$ 2,451	\$ 2,427	\$ 7,345	\$ 7,487

Other operating expenses increased by 1.0% for the three months ended June 30, 2019, and decreased 1.9% for the nine months ended June 30, 2019, compared to the same periods in the prior year. While these aggregate changes were relatively immaterial, the period-over-period changes in the various components of other operating expenses for the three and nine months ended June 30, 2019, were also relatively immaterial.

LIQUIDITY AND CAPITAL RESOURCES

Our liquidity consists of unrestricted cash and cash equivalents plus available borrowing capacity. We held unrestricted cash and cash equivalents of \$8.0 billion and \$10.1 billion as of June 30, 2019, and September 30, 2018, respectively. Our available borrowing capacity as of June 30, 2019, and September 30, 2018, was \$4.0 billion and \$1.8 billion, respectively. Our average daily liquidity balance during the nine months ended June 30, 2019, was \$12.0 billion, representing approximately 57 days of liquidity available, which we define as liquidity divided by estimated average cash disbursements (including capital expenditures) per calendar day (365 days per year).

CASH FLOW ANALYSIS

Although our combined unrestricted cash and available borrowing capacity levels have generally increased since 2012, they remain insufficient to support an organization with approximately \$74 billion in annual operating expenses, to make capital investments necessary for continuity of operations and to prepare for unexpected contingencies. Almost half of this unrestricted cash and available borrowing capacity improvement would not have occurred but for the temporary exigent surcharge, which allowed us to collect a total of \$4.6 billion in incremental revenue between January 2014 and April 2016.

Aside from the temporary exigent surcharge, we defaulted on \$33.9 billion of PSRHBF statutorily specified prefunding payments from 2012 through 2016, and did not make the approximately \$6.9 billion in payments due both September 30, 2018, and 2017, for PSRHBF normal cost and amortization on PSRHBF, CSRS and FERS unfunded liabilities, in order to preserve liquidity, and to ensure that our ability to fulfill our primary universal service mission was not placed at undue risk. The combination of these defaults and non-payments, plus the incremental revenue associated with the temporary exigent surcharge referred to above, and the increased revenue from growth in our Shipping and Packages business, are the primary reasons why our cash and available liquidity has improved.

We continue to face challenges from the ongoing migration of mail to electronic alternatives, and we are legally limited under current law in how we can price our products and streamline our legacy business model. We are further challenged by onerous payment requirements for legacy pension and PSRHBF obligations that, barring legislative reform, will continue indefinitely.

Our operations will require significant capital investment over the next few years to modernize and improve our processing and delivery infrastructure and update our delivery fleet in order to continue to meet our primary statutory obligation to provide prompt, reliable and efficient postal services to the nation. Furthermore, given our inability to raise cash through the issuance of additional debt beyond the statutory \$15.0 billion debt ceiling, we will not be likely to have sufficient cash balances to meet all of our existing legal obligations and make all of the critical investments in our infrastructure that are necessary for operational continuity and that have been deferred in recent years.

Operating Activities

Cash provided by operating activities decreased by \$375 million for the nine months ended June 30, 2019, compared to the same period last year. This decrease is primarily the result of higher cash expenditures for compensation and benefits and transportation, along with an increase in receivables, partially offset by the increase in revenue.

Investing Activities

We invested \$953 million in the purchase of property and equipment for the nine months ended June 30, 2019, which is an increase of \$48 million, or 5.3%, compared to the same period last year. As of the date of this report, the amount of our full year projected capital expenditures is approximately \$1.4 billion for 2019.

Financing Activities

Except as described otherwise in this quarterly report, the nature and amounts of our payment obligations under our debt, capital and operating lease agreements, purchase commitments and other liabilities as of June 30, 2019, have not materially changed from those described in our Annual Report.

In 1999, we entered into a Note Purchase Agreement ("NPA") with the Federal Financing Bank ("FFB"), a government-owned corporation under the general supervision of the Secretary of the Treasury, to establish standardized procedures for us to issue our debt. Under the NPA, we can issue a series of notes with established terms and conditions by providing two days prior notice. Also under the NPA, we can make borrowings against two annually renewable revolving credit line facilities with interest rates determined by the U.S. Department of the Treasury each business day which enable us to draw up to \$4.0 billion in total. These annually renewable revolving facilities were renewed on April 22, 2019, and are scheduled to expire in April 2020.

Under the *Postal Reorganization Act* (the "PRA"), the maximum borrowing amount allowed under our statutory debt ceiling is \$15.0 billion, and we are limited to net annual debt increases of \$3.0 billion. We first reached our statutory debt ceiling in September 2012, and had generally maintained it at that level until mid-September 2018. In late September 2018, we reduced our debt level by \$1.8 billion, lowering it from \$15.0 billion to \$13.2 billion. In late February 2019, we reduced our debt level by another \$2.2 billion, lowering it from \$13.2 billion to \$11.0 billion.

As of June 30, 2019, the aggregate principal balance of our outstanding debt was \$11.0 billion, consisting of a combination of fixed-rate notes, floating-rate notes, and two fully drawn revolving credit facilities. Of this amount, the current portion of our debt was \$4.0 billion, and the noncurrent portion was \$7.0 billion.

As of September 30, 2018, the aggregate principal balance of our outstanding debt was \$13.2 billion, consisting of fixed-rate notes and two fully drawn revolving credit facilities. Of this amount, the current portion of our debt was \$11.0 billion, and the noncurrent portion was \$2.2 billion.

The NPA must be periodically extended through an amendment jointly with the FFB to extend the agreement so that we may continue to issue debt to the FFB pursuant to the standardized procedures and terms and conditions established by the NPA. Prior to September 28, 2018, the FFB's standard practice was to provide us with extensions for a full year. Since September 28, 2018, the FFB has provided amendments extending our agreements for shorter two-to-three month intervals. These amendments did not affect the terms of any of our outstanding debt as of June 30, 2019, and September 30, 2018, respectively.

On June 30, 2019, the FFB amended the NPA agreement by extending it until August 31, 2019. If we are unable to extend the NPA beyond August 31, 2019, we have no assurance that we could obtain alternative debt financing after that date on comparable terms. However, we believe that should the NPA not be renewed, we would be able to maintain adequate liquidity through existing and new financing arrangements, as necessary and allowed by statute, to fund our operations for the foreseeable future.

LIQUIDITY OUTLOOK

With the anticipated continued migration to electronic communication and transactional alternatives, we continue to pursue long-term financial sustainability by focusing on the following items:

1. Continued efforts to control costs and drive efficiencies, innovate to keep mail relevant and generate increased revenue;
2. Postal Service reform legislation that addresses our overall cost structure and enhances our revenue-generating opportunities; and
3. Favorable outcome of the PRC's ten-year review (discussed below), which would allow additional pricing flexibility.

Although we continue to inform the Executive Branch, Congress, the PRC and other stakeholders of the immediate and long-term financial challenges we face, we have no assurances that our requests will result in meaningful reform in the foreseeable future.

PRC Ten-year Review

In December 2016, the PRC initiated its ten-year review of the system for regulating rates and classes for Market-Dominant products as required by the PAEA. On December 1, 2017, the PRC announced its initial decision in connection with its ten-year review. The purpose of the ten-year review was to determine if the system for regulating such rates and classes has achieved the objectives Congress established in the PAEA. As part of this review, the PRC evaluated the CPI-U price cap for our Market-Dominant services.

The PRC concluded that the rates system has not achieved its objectives and needs to be changed, primarily because it does not enable us to achieve our mission of providing prompt, reliable, and efficient universal postal services to the American people in a financially sustainable manner. The PRC's proposed changes to the system do not include the elimination of the CPI-U price cap; however, its proposal does provide for some additional pricing authority within a price cap system. We continue to assert that the price cap should be eliminated and that the PRC should engage in after-the-fact, light-touch review of the Market-Dominant prices we set to ensure that those prices are just and reasonable.

The PRC was expected to issue a final rule after considering the comments and reply comments of any interested stakeholders, which were due no later than March 1, 2018, and March 30, 2018, respectively. As of the date of this report, the PRC has not issued a final rule. Additional information regarding the ten-year review may be found at the PRC website: <https://www.prc.gov/press-releases/prc-concludes-rate-system-has-not-achieved-necessary-objectives-and-issues-proposed>.

2019 and Beyond

We anticipate that given our ongoing liquidity concerns, and without legislative action and regulatory reform, we may not be able to pay all legally required obligations and also invest in much-needed capital expenditures in 2019 and future years that are necessary to ensure our ability to fulfill our primary mission. Furthermore, we believe that continuing productivity improvements alone will not be sufficient to address the challenges presented by declining Market-Dominant volume and revenue, and that growth in operating revenue will unlikely be able to keep pace with increased costs.

Legally Required Obligations

In addition to our previously discussed obligations for unfunded retirement and retiree health benefits of approximately \$7.0 billion due on September 30, 2019, we expect to pay the DOL approximately \$1.4 billion in October 2019, representing the workers' compensation claims paid by DOL for the chargeback year July 1, 2018, to June 30, 2019, plus the estimated administrative fee.

Capital Investments

We currently estimate that our required cash outlays for capital investments necessary to ensure that we can continue to perform our universal service obligation will amount to approximately \$400 million for the remainder of 2019, and an additional \$10.6 billion for years 2020 through 2023, as we plan to invest in a new fleet of delivery vehicles and other capital expenditures. Although our future projections include these capital cash outlays, future cash flow from operations alone may not generate the cash needed to enable us to fully fund such necessary capital investments.

Mitigating Circumstances

We continue to pursue strategies within our control to increase operational efficiency and improve liquidity. We have managed capital in recent years by spending only what we believed was essential to maintain our existing facilities and service levels, and to increase efficiencies. However, continued increases in capital investment are necessary to upgrade our facilities, fleet of vehicles and processing equipment in order to remain operationally viable. Aggressive management of the business operations, as well as legislative and regulatory reforms that will enable us to increase revenue and reduce costs, will all be necessary to restore our financial health.

Our status as an independent establishment of the executive branch that does not receive tax dollars for our operations presents unique requirements and restrictions, but also potentially mitigates some of the financial risk that would otherwise be associated with a cash shortfall. With annual total revenue in 2018 of approximately \$71 billion, a financially sound Postal Service continues to be vital to U.S. commerce.

The U.S. economy benefits greatly from us and the many businesses that provide the printing and mailing services that we support. Disruption of the mail would cause undue hardship to businesses and consumers as it would significantly inhibit the remittance of payments through the mail, and in the event of a cash shortfall, the U.S. government would likely prevent us from significantly curtailing or ceasing operations. We continue to inform the Executive Branch, Congress, the PRC and other stakeholders of the immediate and long-term financial challenges we face and the legislative and regulatory changes that are required to restore our financial stability.

LEGISLATIVE, REGULATORY AND RELATED MATTERS

LEGISLATIVE UPDATE

As a self-funded independent establishment of the executive branch, our business model and operations are significantly influenced by congressional oversight and legislation. Additionally, Congress intended for us to be governed by an eleven-member Board of Governors (“Board”) which generally consists of our Postmaster General, Deputy Postmaster General and nine independent governors (“Governors”). The President appoints the Governors with the advice and consent of the Senate. We have two Senate-confirmed Governors currently in office.

Appropriations

On June 11, 2019, the House Appropriations Committee approved the *Financial Services and General Appropriations Act, 2020* (H.R. 3351), which includes \$56.7 million in funding for free mail for the blind and overseas voting. The bill requires continuation of six-day delivery and prohibits any of the appropriated funds from being used to consolidate or close small rural or other small Post Offices. On June 26, 2019, the House passed H.R. 3351. The Senate has yet to introduce its 2020 appropriations bill.

Postal Service Reform

The 116th Congress has not introduced any major Postal Service reform bills to date. Legislative and regulatory reforms remain critical for us to meet the needs of the American public, and we will continue to work with Congress and all of our stakeholders to enact Postal Service reform legislation.

Board of Governors Nominations

On June 12, 2019, the Senate Homeland Security and Governmental Affairs Committee (“Senate Committee”) held a hearing to consider the nomination of John McLeod Barger to be a member of the Board for the remainder of a term expiring December 8, 2021. On June 19, 2019, the Senate Committee voted favorably to report his nomination to the full Senate. On July 24, 2019, the Senate Committee voted favorably to report the nomination of Robert M. Duncan, one of our current Governors, for a second term expiring December 8, 2025, to the full Senate, where he now awaits consideration. On August 1, 2019, the Senate confirmed the nominations of Ron A. Bloom, for a term expiring December 8, 2020; Roman Martinez IV, for a term expiring December 8, 2024; and John McLeod Barger.

TASK FORCE ON THE UNITED STATES POSTAL SYSTEM

There has been no further congressional activity related to the President’s Task Force report on the Postal Service pursuant to the March 12, 2019, Senate Committee hearing titled, “*A Path to Sustainability: Recommendations from the President’s Task Force on the United States Postal Service.*”

FAIR VALUE MEASUREMENTS

As required by authoritative accounting literature, certain fair value disclosures for the periods ended June 30, 2019, and September 30, 2018, are contained in *Item 1. Financial Statements, Notes to Unaudited Financial Statements*. We did not recognize gains as a result of valuation measurements during the three and nine months ended June 30, 2019. All recognized losses have been incorporated into our financial statements as of June 30, 2019. See *Item 1. Financial Statements, Notes to Unaudited Financial Statements, Note 12 - Fair Value Measurement*.

RELATED PARTY TRANSACTIONS

As disclosed throughout this quarterly report, we have significant transactions with other U.S. government entities, which are considered related parties for reporting purposes. For a more detailed description, see *Item 1. Financial Statements, Notes to Unaudited Financial Statements, Note 5 - Related Parties*.

CRITICAL ACCOUNTING POLICIES AND ESTIMATES

The preparation of financial statements in accordance with GAAP requires management to make significant judgments and estimates to develop certain amounts reflected and disclosed in the financial statements. In many cases, alternative policies or estimation techniques may be used.

We maintain a thorough process to review the application of accounting policies and to evaluate the appropriateness of the many estimates that are required to prepare the financial statements of a large organization. However, even under optimal circumstances, estimates routinely require adjustment based on changing circumstances and new or better information.

The accounting policies deemed either the most judgmental or which involve the selection or application of alternative accounting policies, and are material to the interim financial statements, are described in *Critical Accounting Estimates* contained in *Management's Discussion and Analysis of Financial Condition and Results of Operations* of the Annual Report. Management normally discusses the development and selection of accounting policies and estimates with the Audit and Finance Committee of the Board.

RECENT ACCOUNTING STANDARDS

See *Item 1. Financial Statements, Notes to Unaudited Financial Statements, Note 2 - Recent Accounting Pronouncements*, for a description of recently announced accounting standards.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

In the normal course of business we are exposed to market risks from changes in commodity prices, certain foreign currency exchange rates and interest rates. Our commodity price risk consists primarily of exposure to changes in prices for diesel fuel, unleaded gasoline and aircraft fuel for transportation of the mail, and fuel for heating facilities. We have foreign currency risk related to the settlement of terminal dues and transit fees with foreign postal administrations for international mail.

We have not used derivative commodity or financial instruments to manage market risk related to commodities, foreign currency exchange or interest rate fluctuations for debt instruments. Additionally, we do not purchase or hold derivative financial instruments for speculative purposes.

We also have provisions in our debt agreements that allow us to prepay our \$11.0 billion debt at any time at a price determined by the Secretary of the Treasury, based on prevailing interest rates in the U.S. Treasury market at the time of repayment.

See *Item 7A. Quantitative and Qualitative Disclosures about Market Risk* in the Annual Report for additional information.

ITEM 4. CONTROLS AND PROCEDURES

Management is responsible for the preparation, integrity and fair presentation of our financial statements.

DISCLOSURE CONTROLS

We maintain disclosure controls and procedures that are designed to ensure that information required to be disclosed in quarterly and annual reports is recorded, processed, summarized, and reported within the time frames specified by PAEA, and that this information is accumulated and communicated to our management, including the Postmaster General and Chief Financial Officer, as appropriate, to allow timely decisions regarding required disclosure.

We carried out an evaluation under the supervision and with the participation of management, including the Postmaster General and the Chief Financial Officer, of the effectiveness of the design and operation of disclosure controls and procedures as of June 30, 2019. Based upon and as of the date of the evaluation, the Postmaster General and the Chief Financial Officer concluded that our disclosure controls and procedures were effective.

INTERNAL CONTROLS

We have made no changes in our internal control over financial reporting during the three months ended June 30, 2019, that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

PART II. OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

For a discussion of legal proceedings affecting us, please refer to *Item 1. Financial Statements, Notes to Unaudited Financial Statements* and *Note 8 - Commitments and Contingencies*, as well as our Annual Report.

ITEM 1A. RISK FACTORS

No material changes have transpired in our risk factors from those disclosed in *Item 1A. Risk Factors* of our Annual Report.

ITEM 6. EXHIBITS

Exhibit Number	Description
31.1	Certification of Principal Executive Officer Pursuant to Rules 13a-14(a) and 15d-14(a) under the <i>Securities and Exchange Act of 1934</i> , as Adopted Pursuant to Section 302 of the <i>Sarbanes-Oxley Act of 2002</i> .
31.2	Certification of Principal Financial Officer Pursuant to Rules 13a-14(a) and 15d-14(a) under the <i>Securities and Exchange Act of 1934</i> , as Adopted Pursuant to Section 302 of the <i>Sarbanes-Oxley Act of 2002</i> .
32.1	Certification of Principal Executive Officer Pursuant to <i>18 U.S.C. Section 1350</i> , as Adopted Pursuant to Section 906 of the <i>Sarbanes-Oxley Act of 2002</i> .
32.2	Certification of Principal Financial Officer Pursuant to <i>18 U.S.C. Section 1350</i> , as Adopted Pursuant to Section 906 of the <i>Sarbanes-Oxley Act of 2002</i> .

Signatures

Pursuant to the requirements of the *Postal Accountability and Enhancement Act of 2006*, the United States Postal Service has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

United States Postal Service

/s/Megan J. Brennan

Megan J. Brennan
Postmaster General and Chief Executive Officer

Date: August 8, 2019

/s/Joseph Corbett

Joseph Corbett
Chief Financial Officer and Executive Vice
President

Date: August 8, 2019

CERTIFICATION PURSUANT TO
RULES 13a-14(a) AND 15d-14(a) UNDER THE SECURITIES AND EXCHANGE ACT OF
1934, AS ADOPTED PURSUANT TO SECTION 302 OF THE SARBANES-OXLEY ACT OF
2002.

I, Megan J. Brennan, certify that:

1. I have reviewed this quarterly report on Form 10-Q of the United States Postal Service ("Postal Service");
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the Postal Service as of, and for, the periods presented in this report;
4. The Postal Service's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the Postal Service and have:
 - a. Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the Postal Service, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - b. Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - c. Evaluated the effectiveness of the Postal Service's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - d. Disclosed in this report any change in the Postal Service's internal control over financial reporting that occurred during the Postal Service's most recent fiscal quarter (the Postal Service's fourth fiscal quarter in the case of an Annual Report) that has materially affected, or is reasonably likely to materially affect, the Postal Service's internal control over financial reporting; and
5. The Postal Service's other certifying officer and I have disclosed based on our most recent evaluation of internal control over financial reporting, to the Postal Service's independent registered accounting firm and the Audit and Finance Committee of the Postal Service's Board of Governors:
 - a. All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the Postal Service's ability to record, process, summarize and report financial information; and
 - b. Any fraud, whether or not material, that involves management or other employees who have significant role in the Postal Service's internal control over financial reporting.

Date: August 8, 2019

/s/Megan J. Brennan

Megan J. Brennan

Postmaster General and Chief Executive Officer

CERTIFICATION PURSUANT TO
RULES 13a-14(a) AND 15d-14(a) UNDER THE SECURITIES AND EXCHANGE ACT OF
1934, AS ADOPTED PURSUANT TO SECTION 302 OF THE SARBANES-OXLEY ACT OF
2002.

I, Joseph Corbett, certify that:

1. I have reviewed this quarterly report on Form 10-Q of the United States Postal Service ("Postal Service");
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the Postal Service as of, and for, the periods presented in this report;
4. The Postal Service's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the Postal Service and have:
 - a. Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the Postal Service, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - b. Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - c. Evaluated the effectiveness of the Postal Service's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - d. Disclosed in this report any change in the Postal Service's internal control over financial reporting that occurred during the Postal Service's most recent fiscal quarter (the Postal Service's fourth fiscal quarter in the case of an Annual Report) that has materially affected, or is reasonably likely to materially affect, the Postal Service's internal control over financial reporting; and
5. The Postal Service's other certifying officer and I have disclosed based on our most recent evaluation of internal control over financial reporting, to the Postal Service's independent registered accounting firm and the Audit and Finance Committee of the Postal Service's Board of Governors:
 - a. All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the Postal Service's ability to record, process, summarize and report financial information; and
 - b. Any fraud, whether or not material, that involves management or other employees who have significant role in the Postal Service's internal control over financial reporting.

Date: August 8, 2019

/s/Joseph Corbett

Joseph Corbett

Chief Financial Officer and Executive Vice President

CERTIFICATION PURSUANT TO
18 U.S.C. SECTION 1350, AS ADOPTED PURSUANT TO
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002.

In connection with the Quarterly Report of the United States Postal Service ("Postal Service") on Form 10-Q for the period ended June 30, 2019, (the "Report"), I, Megan J. Brennan, certify, pursuant to *18 U.S.C. Section 1350*, as adopted pursuant to Section 906 of the *Sarbanes-Oxley Act of 2002* that:

- (1) The Report fully complies with the requirements of Section 13(a) or 15(d) of the *Securities Exchange Act of 1934*; and
- (2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Postal Service.

Dated: August 8, 2019

/s/Megan J. Brennan

Megan J. Brennan

Postmaster General and Chief Executive Officer

CERTIFICATION PURSUANT TO
18 U.S.C. SECTION 1350, AS ADOPTED PURSUANT TO
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002.

In connection with the Quarterly Report of the United States Postal Service ("Postal Service") on Form 10-Q for the period ended June 30, 2019, (the "Report"), I, Joseph Corbett, certify, pursuant to *18 U.S.C. Section 1350*, as adopted pursuant to Section 906 of the *Sarbanes-Oxley Act of 2002* that:

- (1) The Report fully complies with the requirements of Section 13(a) or 15(d) of the *Securities Exchange Act of 1934*; and
- (2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Postal Service.

Dated: August 8, 2019

/s/Joseph Corbett
Joseph Corbett
Chief Financial Officer and Executive Vice President