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

FORM 10-K

(Mark One)

☑ **ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the fiscal year ended SEPTEMBER 30, 2018

or

☐ **TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the transition period from ____________ to ____________

Commission file number N/A

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, DC 20260
(202) 268-2000
(Address and telephone number, including area code, of registrant's principal executive offices)

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

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

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

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes ☐ No ☐ 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 if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K (§229.405 of this chapter) is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. 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 ☑

The aggregate market value of shares of common stock held by non-affiliates as of March 31, 2018: N/A

The number of shares of common stock outstanding as of November 14, 2018: N/A

Documents incorporated by reference: None

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PART I

ITEM 1. BUSINESS

In accordance with the provisions of the *Postal Reorganization Act* ("PRA"), the United States Postal Service ("Postal Service," "USPS," "we," "our" and "us") began operations on July 1, 1971, succeeding the cabinet-level Post Office Department established in 1792. The PRA established us as an "independent establishment of the executive branch of the Government of the United States" with the mandate to offer a "fundamental service" to the nation "at fair and reasonable rates." We do not receive tax dollars for operating expenses and rely solely on the sale of postage, products and services to fund our operations.

We serve retail and commercial customers in the communications, distribution and delivery, advertising and retail markets throughout the nation and internationally. As a result, we maintain a very diverse customer base and are not dependent upon a single customer or small group of customers. No single customer represented more than 6% of operating revenue for the years ended September 30, 2018, 2017 and 2016.

As an independent establishment of the executive branch, we align specific objectives with those of the U.S. government. We are subject to numerous federal, state and local regulatory and reporting laws, as well as environmental laws and regulations. Our governing statute is codified in Title 39 of the U.S. Code. The *Postal Accountability and Enhancement Act of 2006, Public Law 109-435* ("PAEA") made revisions to the PRA and established the Postal Regulatory Commission ("PRC"), endowing it with regulatory and oversight responsibilities.

We operate and manage a very extensive and integrated retail, distribution, transportation and delivery network. Although PAEA divides our services into Market-Dominant and Competitive products, we monitor and report revenue by mail classes, and we operate as a single segment throughout the U.S., including its possessions and territories.

As used herein, 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 fiscal quarters.

GOVERNANCE

The law stipulates an eleven-member Board of Governors ("Board") which generally consists of our Postmaster General, Deputy Postmaster General and nine independent governors ("Governors"). The Governors are appointed by the President of the United States ("President") with the advice and consent of the United States Senate ("Senate"). The Postmaster General is appointed by the Governors, and the Deputy Postmaster General is appointed by the Governors and the Postmaster General.

The Board is required by law to have a quorum of six members in order to take certain actions. In November 2014, while the Board still had a quorum, it issued a resolution that established a Temporary Emergency Committee of the Board ("TEC") to exercise certain powers reserved to the Board that are necessary for continuity of operations during a period in which it is unable to assemble a quorum.

Also in November 2014, the Governors issued a resolution regarding the exercise of those powers conferred by law solely to the Governors as distinguished from the full Board, which include the appointment and removal of the Postmaster General and the establishment of prices and classifications for our services. The Governors determined that their ability to exercise those powers reserved to the Governors was not impacted by the loss of a Board quorum.

In December 2014, due to the term expiration of one Governor and Senate inaction on pending nominations, the number of sitting Board members dropped to five, thereby rendering the Board unable to assemble a quorum. The TEC has exercised its powers since that time.

We publicly announced the resolutions that established the TEC and regarding the Governors' exercise of power reserved to them in a December 16, 2014, Federal Register notice.

Our two current Governors were appointed on August 30, 2018, following their confirmation by the Senate. The President has made four additional Governor nominations, including the nomination of one of our current Governors for an additional seven-year term, and those nominations await Senate action.

The TEC currently consists of the members of the Board and exercises those Board powers necessary for operational continuity. The TEC will continue in existence until the Board is again able to assemble a quorum.

Additionally, the Audit and Finance Committee of the Board provides oversight of our financial statement preparation, system of internal controls, financial reporting process, compliance with applicable laws and regulations and audit process.

Furthermore, the Board has delegated to its Compensation and Management Resources Committee ("Compensation Committee") authority for initial review of management proposals related to compensation benefits for the officers. The Compensation Committee makes recommendations to the full Board for its review and approval.

SERVICES

We fulfill our legal mandate to provide universal services at fair and reasonable prices by offering a variety of postal services to our many customers. Our Governors approve our prices and fees, subject to a review process by the PRC. Services are sold by approximately 31,000 Postal Service-managed Post Offices, stations and branches, plus approximately 4,000 additional Contract Postal Units, Community Post Offices, Village Post Offices, and a large network of commercial outlets which sell stamps and services on our behalf and through our website *www.usps.com*. Mail deliveries are made to nearly 159 million city, rural, *PO Box* and highway delivery points. Operations are conducted primarily in the domestic market, with international revenue representing approximately 4% of operating revenue for the year ended September 30, 2018.

CLASSIFICATION AND PRICING

Within *First-Class Mail*, *Marketing Mail*, *Periodicals*, *International* and *Other* services, prices do not vary materially by customer for the level of service provided. Although the PAEA classifies our services as Market-Dominant and Competitive "products," the term "services" is often used in this report for consistency with other descriptions of services we offer.

Periodic reclassification of services from Market-Dominant to Competitive, which requires PRC approval, is necessary to rationalize service offerings. The additional flexibility provided in Competitive services allows us to better offer services to meet customer needs, increase our business and price our services competitively within the markets in which we operate. Information regarding PRC decisions and pending dockets can be obtained on the PRC website: *www.prc.gov*.

Market-Dominant Services

Market-Dominant services account for approximately 67% of our annual operating revenues. Such services include, but are not limited to, *First-Class Mail*, *Marketing Mail*, *Periodicals* and certain parcel services. Price increases for these services are currently generally subject to a price cap based on the Consumer Price Index for All Urban Consumers ("CPI-U"). Our Governors approve the prices for Market-Dominant services, subject to a review process by the PRC for legal compliance.

We implemented price increases on certain Market-Dominant services that averaged 1.9% in January 2018, and 0.9% in January 2017. Also during 2017, we changed the name of our former *Standard Mail* service category and class of mail to *USPS Marketing Mail* (more commonly, *Marketing Mail*). On October 10, 2018, we filed with the PRC a notice of our intent to increase prices for certain Market-Dominant services by an average of 2.5%. On November 13, 2018, the PRC approved this plan and the increase is scheduled to go into effect on January 27, 2019.

In December 2013, the PRC ruled that we could collect a 4.3% exigent surcharge on Market-Dominant services beginning in January 2014, and until such time as the surcharge produced $3.2 billion in incremental revenue, an amount the PRC determined was lost due to the Great Recession's suppression of mail volume. On July 29, 2015, after a successful appeal, the PRC authorized us to collect over $1.4 billion in additional incremental revenue from the surcharge, bringing the total amount allowed to just over $4.6 billion in additional incremental revenue. This limit was reached on April 10, 2016, and we therefore reduced the prices of applicable Market-Dominant services on that date.

Competitive Services

Competitive services, such as *Priority Mail*, *Priority Mail Express*, *First-Class Package Service*, *Parcel Select* and *Parcel Return Service* and some types of *International* mail, have greater pricing flexibility and are not limited by a price cap. Prices for Competitive services are set by our Governor(s) and reviewed by the PRC for legal compliance. By law, prices for each Competitive service must cover its "attributable costs" (meaning the Postal Service's costs attributable to such product through reliably identified causal relationships) and Competitive services collectively must contribute an appropriate share to the institutional costs of the Postal Service, currently 5.5%, as determined by the PRC. The "appropriate share" contribution requirement is currently the subject of a rulemaking proceeding before the PRC. In general, we attempt to set our prices for Competitive Services at rates that maximize revenue.

We implemented price increases on certain Competitive services that averaged 4.1% in January 2018, 3.9% in January 2017, and 9.5% in January 2016. In September 2017, we transferred a Market-Dominant product (*First-Class Package Service - Retail*, formerly *First-Class Mail Parcels*) to the Competitive product list and implemented an average price increase of 9.9% on that service. On October 10, 2018, we filed with the PRC a notice of our intent to increase prices for certain Competitive services by an average of 7.4%. On November 13, 2018, the PRC approved this plan and the increase is scheduled to go into effect on January 27, 2019.

The PAEA prohibits the subsidization of Competitive services costs by Market-Dominant services revenue. The PRC reviews our price increase notices, and we are diligent to ensure that each Competitive service covers its attributable costs and that Competitive services collectively contribute an appropriate share of institutional costs.

SERVICE CATEGORIES

Although we operate as a single segment, we monitor and report revenue by mail classes, products and shapes. Our management uses the following broad service categories to describe and report on our performance:

- **First-Class Mail** - This category encompasses letters, cards or any flat advertisement or merchandise destined for either domestic (up to 13 ounces) or international (up to 4 pounds) delivery. *First-Class Mail* letters include postcards, correspondence, bills or statements of account, and payments. Prices for *First-Class Mail* are the same regardless of the distance the mail travels.

- **Marketing Mail** - This category includes advertisements and marketing packages, weighing less than 16 ounces that are not required to be sent using *First-Class Mail*. *Marketing Mail* is typically used for direct advertising to multiple delivery addresses. *Every Door Direct Mail* enables customers to prepare direct mailings without names and addresses for distribution to all business and residential customers on individual carrier routes. In January 2017, upon approval by the PRC, we changed the name of *Standard Mail* to *USPS Marketing Mail* to aid our customers in understanding what *Marketing Mail* is and how it can be used as part of the respective customers' marketing strategies.

- **Shipping and Packages** - This category includes: *First-Class Package Service - Commercial*, a shipping option for high-volume shippers of packages that weigh less than one pound and *First-Class Package Service - Retail*, for shipment of boxes, thick envelopes or tubes of 13 ounces or less; *Package Services* for merchandise or printed matter, such as library and media mail weighing up to 70 pounds; Parcel Services - *Parcel Select and Parcel Return* services, including "last-mile" products, and *USPS Marketing Mail Parcels* (more commonly, *Marketing Mail Parcels*) which provide commercial customers with a means of package shipment ; *Priority Mail*, which is offered as a service both within the U.S. and abroad with the domestic service offering a 1-3 day specified (non-guaranteed) delivery; and *Priority Mail Express*, which provides an overnight, money-back guaranteed service which includes tracking, proof of delivery and basic insurance up to $100. *Priority Mail Express* delivery is offered to most U.S. destinations for delivery 365 days a year.

- **International** - This category offers international mail and shipping services with individual customer contracts and agreements with other postal administrations. *Priority Mail Express International* and *Priority*

Mail International services compete in the e-commerce cross-border business. They provide an option for our retail and business customers for much of their shipping needs to over 180 countries. *Global Express Guaranteed* is the premier international shipping option that offers reliable, date-certain delivery in 1 to 3 business days to major markets, with a money-back guarantee.

- **Periodicals** - This category encompasses the *Periodicals* class of mail offered for newspaper, magazine and newsletter distribution. Customers must receive prior authorization from us to use this service.

- **Other** - This broad category includes: *PO Box* services, which provide customers an additional method for mail delivery that is private and convenient. *Money Orders* offer customers a safe, convenient and economical method for the remittance of payments. *Money Orders* are available for amounts up to $1,000, can be purchased and cashed at most Post Offices, or can be deposited or negotiated at financial institutions. USPS Extra Services offer a variety of service enhancements that provide security, proof of delivery or loss recovery. These services include: *Certified Mail*, *Registered Mail*, *Signature Confirmation*, *Adult Signature* and insurance up to $5,000 and are available online, at Post Offices or at automated postal centers.

For a discussion of economic and other factors affecting the volume of these services and our actions taken to address these factors, see *Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations*, *Results of Operations*, *Operating Revenue and Volume*.

RESEARCH AND DEVELOPMENT

We operate a research and development facility in Virginia for design, development and testing of postal equipment and operating systems. We also contract with independent suppliers to conduct research activities. While research and development activities are important to our business, these expenditures are not material to our results of operations or financial position.

INTELLECTUAL PROPERTY

We own intellectual property that includes trademarks, service marks, patents, copyrights, trade secrets and other proprietary information and routinely generate intellectual property in the course of developing and improving systems, services and operations. While legal protection for intellectual property and proprietary information is significant to our success, the knowledge, ability and experience of our employees and the timeliness and quality of service we provide are equally important.

MARKETING

Our marketing program seeks to capitalize on innovation, technology and data management, including our existing relationships with the mailing industry and our reputation based on our service delivery performance every day. We continue to adjust to changes in customer behaviors and demands to make accessing and using our services more convenient. We have developed innovative mobile applications which enable customers to locate a Post Office, find a ZIP Code, track packages and shop online.

Online service offerings available through *www.usps.com* have also enhanced the customer experience by providing customer-focused applications and services. Included in online services is *Informed Delivery*, which enables customers to preview mail and manage package delivery. We are currently enhancing *Informed Delivery* so that businesses may incorporate marketing campaigns and reinforce the value of the printed mailpiece.

Our marketing approach highlights our value, our enhanced digital technologies and the linkages between digital and physical communications. Additionally, we seek to leverage our brand through the use of media advertising, trade shows, technical seminars and direct mailings.

COMPETITION

We compete for our business in many different market segments. A wide variety of communications media compete for the same types of transactions and communications that are conducted using our services. These channels include, but are not limited to, newspapers, telecommunications, television, email, social networking and electronic funds transfers. The package and express delivery businesses are highly competitive, with both national and local competitors.

The most significant competitive factor for *First-Class Mail* is digital communication, including electronic mail, as well as other digital technologies such as online bill payment and presentment. For *Marketing Mail*, digital forms of advertising including digital mobile advertising and social media, are the most significant form of competition.

The primary competitors of our Shipping and Packages services are FedEx Corporation and United Parcel Service, Inc., as well as other national, regional and local delivery companies and crowdsourced carriers. We see additional competition coming from existing customers who are testing and in some cases implementing "last-mile" services. These companies include Amazon.com, Inc.; WalMart, Inc. and Target Corporation. Our Shipping and Packages business competes on the basis of the breadth of our service network, convenience, reliability and economy of the service provided. The growth in our Competitive service revenues over the past five years is largely attributable to three major customers.

For the years ended September 30, 2018, 2017 and 2016, combined revenue from our three largest customers (excluding mail service providers) represented approximately 8.3%, 7.6% and 5.8% of operating revenue, respectively. The growth in our Competitive service revenues over the past five years is largely attributable to these three customers. Each of these customers is building delivery capability that would enable them to divert volume away from us over time.

SEASONALITY

Mail volume and revenue are historically greatest in the first quarter of our fiscal year, which includes the holiday mailing and shipping season, and lowest in the third and fourth quarters of our fiscal year during the spring and summer. In general election years, political organizations may heavily use *Marketing Mail* to reach their targeted audiences, thereby generating temporary volume and revenue increases during the months preceding an election.

EMPLOYEES

At September 30, 2018, we employed approximately 497,000 career employees and approximately 137,000 non-career employees, substantially all of whom reside in the U.S. Career employees are considered permanent and are entitled to a full range of benefits (e.g., health and retirement) and privileges, while non-career employees are considered temporary and do not receive full employee benefits and privileges. For a more detailed discussion of items that impact our employees, see *Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations*, *Results of Operations*, *Operating Expenses*.

BARGAINING AGREEMENTS

Approximately 92% of employees are covered by collective bargaining agreements. These agreements include provisions governing work rules and provide for general wage increases, step increases and cost of living adjustments ("COLA"), which are linked to the Consumer Price Index – Urban Wage Earners and Clerical Workers ("CPI-W"), as well as provisions that limit our ability to reduce the size of the labor force and restrict the number of non-career employees. Our labor force is primarily represented by the American Postal Workers Union, AFL-CIO ("APWU"); the National Association of Letter Carriers, AFL-CIO ("NALC"); the National Postal Mail Handlers Union, AFL-CIO ("NPMHU") and the National Rural Letter Carriers Association ("NRLCA").

By law, we must consult with management organizations representing most of our employees not covered by collective bargaining agreements. These consultations provide non-bargaining unit employees in the field with an opportunity to participate in the planning, development and implementation of certain programs and policies that affect them.

In April 2016, we reached a three-year collective bargaining agreement with the NRLCA which the NRLCA membership subsequently ratified. The contract includes general wage increases totaling 3.8% over the life of the contract (1.2% of which was retroactive to November 2015) with a COLA base month of July 2014 (no retroactive COLA payments), a reduction in the employer share of health insurance premiums beginning in the 2017 plan year, and the creation of a new non-career employee category to provide weekend and holiday parcel deliveries. Our contract with the NRLCA expired on May 20, 2018, and the respective parties mutually agreed to extend negotiations on a new collective bargaining agreement beyond the deadline. No new agreement has been reached as of the date of this report.

In July 2016, an interest arbitration decision was issued that resulted in an award which established a collective bargaining agreement with the APWU. The award was the result of a legally-mandated binding arbitration process required when the parties reached impasse in negotiating a new collective bargaining agreement after the prior agreement expired in May 2015. The awarded contract includes general wage increases totaling 3.8% over the life of the contract (1.2% of which was retroactive to November 2015) with a COLA base month of July 2014 (no retroactive COLA payments), a reduction in the employer share of health insurance premiums beginning in the 2017 plan year, and annual increases in uniform and work clothing allowances. The award also converted approximately 5,000 non-career positions to career positions. Our contract with the APWU expired on September 20, 2018, and the respective parties mutually agreed to extend the deadline for negotiations on a new collective bargaining agreement to November 20, 2018.

In December 2016, we reached an agreement with the NPMHU on a 40-month labor contract (retroactive to May 2016) which the union membership ratified in February 2017. The contract includes general wage increases totaling 3.8% over the life of the contract (1.2% of which was retroactive to November 2016) with a COLA base month of July 2014 (the first COLA payment was retroactive to September 2016), a reduction in the employer share of health insurance premiums beginning in the 2018 plan year, and annual increases in uniform and work clothing allowances. The contract will expire on September 20, 2019.

In May 2017, we reached an agreement with the NALC on a 40-month labor contract (retroactive to May 2016) which the union membership ratified in August 2017. The contract includes general wage increases totaling 2.5% over the life of the contract (1.2% of which was retroactive to November 2016) with a COLA base month of July 2014 (the first COLA payment was retroactive to September 2016), a November 2018 consolidation of the current two pay grades into a single pay grade, a reduction in the employer share of health insurance premiums beginning in the 2018 plan year, and annual increases in uniform and work clothing allowances. The contract will expire on September 20, 2019.

FEDERAL EMPLOYEE AND RETIREMENT BENEFIT PROGRAMS

We are required, either by law or by union contract, to participate in U.S. government pension and health and benefits programs for employees and retirees, including the Federal Employees Health Benefit ("FEHB") program, the Civil Service Retirement System ("CSRS") and the Federal Employees Retirement System ("FERS"), which the Office of Personnel Management ("OPM") administers. We have no control or influence over the benefits offered by these plans and we contribute to these plans as specified by law or contractual agreements with our employee unions (in the case of health benefits for most active employees).

The PAEA established the Postal Service Retiree Health Benefits Fund ("PSRHBF") in 2006. In accordance with applicable law, we are required to fully prefund retiree health benefits. Such a requirement to fully prefund retiree health benefits is not imposed on most other federal entities or private sector businesses that offer such benefits.

Since its enactment, the PSRHBF prefunding requirement has contributed significantly to our losses. As of September 30, 2018, we have contributed $20.9 billion to the PSRHBF and defaulted on additional statutory prefunding amounts totaling $33.9 billion for the years 2012 through 2016, because we did not have sufficient funds to make the funding payments without adversely impacting our ability to continue operations.

In 2017, the PSRHBF began funding the Postal Service's share of retiree health benefit premiums, and we were required to begin paying the "normal costs" of retiree health benefits (i.e., the present value of the estimated retiree health benefits attributable to active employees' current year of service) into the PSRHBF, as well as an amortization payment of our unfunded liability. For the years ended September 30, 2018 and 2017, the amounts OPM billed us for normal costs were $3.7 billion and $3.3 billion, respectively, and the amounts billed for amortization payments were $815 million and $955 million, respectively. We did not make any of these 2018 or 2017 payments in order to preserve liquidity and to ensure that our ability to fulfill our primary universal service mission was not placed at undue risk.

As of the date of this report, we have not incurred any penalties or negative financial consequences as a result of not making the PSRHBF statutorily set prefunding, normal cost, or amortization payments.

Our retirement plan obligations for FERS consist of FERS normal costs, the employer portion of Thrift Savings Plan ("TSP") contributions, Social Security and amortization of the unfunded retirement benefits for FERS. We incurred a FERS unfunded liability amortization expense of $958 million and $917 million for the years ended September 30, 2018 and 2017, respectively. Although we made all required payments for FERS normal cost, the TSP and Social Security, we did not make the 2018 or 2017 required amortization payments for FERS unfunded retirement benefits, in order to preserve liquidity and to ensure that our ability to fulfill our primary universal service mission was not placed at undue risk. As of the date of this report, we have not incurred any penalties or negative financial consequences as a result of not making these payments.

In addition, in accordance with PAEA, in 2017 we were required to begin making annual payments to amortize the unfunded CSRS liability, and we incurred a CSRS unfunded liability expense of $1.4 billion and $1.7 billion for the years ended September 30, 2018 and 2017, respectively. We did not make the required lump sum payments for the CSRS unfunded retirement benefits amortization, in order to preserve liquidity and to ensure that our ability to fulfill our primary universal service mission was not placed at undue risk. As of the date of this report, we have not incurred any penalties or negative financial consequences as a result of not making these payments.

We are also legally-mandated to participate in the federal workers' compensation program that is managed by the Department of Labor's ("DOL") Office of Workers' Compensation Programs ("OWCP") and governed by the *Federal Employees' Compensation Act* ("FECA"). Our total liability for workers' compensation was $16.4 billion and $17.9 billion as of September 30, 2018 and 2017, respectively. Additionally, we reimburse the DOL for all workers' compensation benefits paid to or on behalf of our employees. For the years ended September 30, 2018, September 30, 2017 and September 30, 2016, these cash payments were $1.4 billion, $1.4 billion and $1.5 billion, respectively.

OVERSIGHT AND REGULATION

As discussed throughout this report, we are subject to oversight by the United States Congress ("Congress") and regulation by the PRC and other government agencies. In addition to Senate confirmation of our Governors, Congress significantly influences how we conduct our business and operations through passage of laws. For example, unless and until new laws become effective, we are legally bound by annual *Financial Services and General Government* appropriations legislation, which is part of the larger U.S. government's budget and spending process each fiscal year for specific U.S. government departments, agencies and programs. Among other restrictions, such legislation requires us to maintain a six-day delivery schedule. We are also bound by Postal Service-specific legislation, such as the PAEA, which impacts our financial performance and restricts our competitiveness by limiting our ability to grow our business, price our services and constrain our expenses. For a more detailed explanation, see *Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations*, *Legislative Update*.

ENVIRONMENTAL MATTERS

Although we are required to comply with various federal, state or local environmental laws and regulations, none of these has had a material impact on our financial results or competitive position, or resulted in material capital expenditures. However, the effect of possible future environmental legislation or regulations on operations cannot be predicted. New laws or regulations that regulate greenhouse gas emissions into the environment may increase our operating costs, including the cost of fuel, and the potential costs of compliance with any such new laws or regulations.

REGULATORY REPORTING

We are not a reporting company under the *Securities Exchange Act of 1934*, as amended ("Exchange Act"), and are not subject to regulation by the Securities and Exchange Commission ("SEC"). However, the PAEA requires us to file with the PRC certain financial reports containing information prescribed by the SEC under Sections 13 and 15(d) of the Exchange Act. These reports include annual reports on Form 10-K ("Annual Report"), quarterly reports on Form 10-Q and current reports on Form 8-K.

We are also required by law and regulations to disclose operational and financial information beyond what the law requires of most U.S. government entities and private-sector companies. Pursuant to Title 39 of the U.S. Code and PRC regulations, we must also file additional information with the PRC, including Cost and Revenue Analysis reports; Revenue, Pieces and Weight reports; financial and strategic plans and the *Comprehensive Statement on Postal Operations*.

All of these reports may be found online at *www.about.usps.com/who-we-are/financials/welcome.htm*, free of charge, as soon as reasonably practicable after we file them with the PRC. Information on our website is not incorporated by reference into this report. Requests for copies of our reports may also be sent to the following address: Corporate Communications, United States Postal Service, 475 L'Enfant Plaza, SW, Washington, DC 20260-3100.

ITEM 1A. RISK FACTORS

We are subject to various risks and uncertainties that could adversely affect our business, financial condition, results of operations and cash flows. In addition to the risks and uncertainties that are described below, others that we do not yet know of or that we currently believe are immaterial could arise or become material and may also impair our business.

Adverse U.S. and global economic conditions may directly impact our business, negatively affecting results of operations. The demand for our services is heavily influenced by the economy. Adverse economic conditions could negatively affect our business and results of operations, primarily through disrupting our customers' businesses. To the extent that the U.S. and other countries experience slow or negative economic growth, our business, financial position and results of operations will be adversely impacted.

Current and future management actions to generate cash flows by increasing efficiency, reducing costs and generating additional revenue may not be sufficient to meet all of our financial obligations or to carry out our strategy.

Our strategies to increase efficiency and reduce costs by adjusting our network, infrastructure and workforce and to retain and grow revenue are currently constrained by contractual, statutory, regulatory and political restrictions. Accordingly, our ability to react quickly to the changing economic climate and industry conditions is inhibited. We have also proposed legislative changes that are needed to provide us with the legal authority to implement additional measures to increase efficiency and cost savings and to grow revenue, but nothing we have proposed has become law.

We are subject to congressional oversight and regulation by the PRC and other government agencies. We have a wide variety of stakeholders whose interests and needs are sometimes in conflict.

We operate as an independent establishment of the executive branch of the U.S. government and, as a result, we are subject to a variety of regulations and other limitations applicable to federal agencies. If the U.S. government curtails its spending due to debt ceiling or other constraints, we may be adversely impacted. Additionally, as an outgrowth of our unique status as a fundamental service provider to the nation, we attempt to balance the interests of many parties. Limitations on our ability to take action could adversely affect operating and financial results.

Existing laws and regulations limit our ability to introduce new products or services, enter new markets, generate new revenue streams or manage our cost structure. These laws and regulations may also prevent us from increasing prices sufficiently or generating sufficient efficiency improvements to offset increased costs. This would adversely affect our results of operations.

In order to offset declining volume and revenue caused by the changing economy and diversion to electronic media, our ability to sell new products and services in new or existing markets will be a key factor in improving our financial condition. However, various laws and regulations significantly limit our ability to enter new markets and/or to provide new services and products, as we are often constrained by traditional industry definitions.

Without legal or regulatory changes that allow us to introduce new products or services to take advantage of our assets, including our strong network and "last-mile" capabilities, we may be unable to respond adequately to consumers' changing needs and expectations. These limitations have the potential to adversely impact our results of operations and long-term financial viability. PAEA currently generally limits price increases on our Market-Dominant services to the rate of inflation as measured by the CPI-U. However, our costs are not similarly limited. A large portion of our cost structure cannot be altered expeditiously, and the number of our delivery points continues to grow. Accordingly, we may not be able to increase prices sufficiently to offset increased costs.

Because our services are provided primarily through our employees, our costs are heavily concentrated in wages and employee and retiree benefits. These costs are significantly impacted by wage inflation, health benefit premium increases, retirement and workers' compensation programs, and COLA. Some of these costs have historically tended to increase at a higher rate than inflation as measured by the CPI-U. We believe that continuing productivity improvements alone will not be sufficient to address the challenges presented by declining volume and revenue and by the current regulatory price cap, nor will our efforts to grow operating revenue keep pace with our increased costs.

We have a substantial amount of indebtedness.

As of September 30, 2018, we reported outstanding debt obligations to the Federal Financing Bank ("FFB") of $13.2 billion.

As of September 30, 2018, we have a total underfunded PSRHBF liability of $66.5 billion as reported by OPM, which we will be required to fund in future periods. Of this amount, we reported $42.6 billion in the accompanying *Balance Sheets* as a current liability due and payable to the PSRHBF for invoiced but unpaid contributions.

As of September 30, 2018, we have estimated underfunded retirement benefits amortization to the CSRS and FERS funds of $25.1 billion and $18.4 billion, respectively, as reported by OPM, which we will be required to fund in future periods. Of these amounts, we have unpaid obligations due to OPM that total nearly $3.2 billion for CSRS amortization payments and $2.4 billion for FERS amortization payments, which we have reported as current liabilities in the accompanying *Balance Sheets*.

Our significant indebtedness and unpaid retirement and retiree health obligations have important consequences. They limit our flexibility in planning for, or reacting to, changes in the business environment or competition. They place us at a competitive disadvantage compared to commercial competitors that may have less debt and which have access to public capital markets. They also could require us to dedicate a substantial portion of our future cash flow from operations to payments on debt and retirement and retiree healthcare obligations, thus reducing the availability of cash flow to fund working capital, capital expenditures and other general organizational activities.

If we are unable to extend our Note Purchase Agreement with the FFB, we may not be able to refinance debt with the FFB in the future at comparable terms to those currently available.

On April 1, 1999, we entered into a Note Purchase Agreement (as amended, the "NPA") with the FFB for the purpose of obtaining debt financing. Under the NPA, FFB is required to purchase notes from us meeting specified conditions, up to the established maximum amounts, within five business days of delivery. The amount that we borrow under the NPA varies from year to year depending upon the needs of the organization. All of our outstanding debt as of September 30, 2018, was obtained through the NPA.

Since April 1, 1999, the NPA has been amended on September 30th of each year, extending our ability to issue debt under the agreement until September 30th of the following year. During this time, the material terms of each such amendment have remained largely unchanged. The Twentieth Amendment to the NPA, dated September 30, 2017, expired on September 30, 2018. Under the Twenty-First Amendment, FFB extended our ability to issue debt under the NPA until December 31, 2018 (one fiscal quarter) as opposed to the previous precedent of extending the NPA for a full fiscal year.

The NPA provides a convenient and flexible mechanism for us to fund our operations according to agreed-upon parameters. Reducing the duration of the NPA from one year to one quarter introduces significant uncertainty as to how we might fund operations in an expeditious and established manner in the face of unanticipated revenue short-falls or inflationary cost increases. We are attempting to negotiate a longer extension before December 31, 2018. If unsuccessful, we may have to pursue additional short-term extensions. If we cannot reach acceptable terms with FFB on an extension of the NPA, we would need to seek debt financing through other means, either through individual agreements with FFB (on terms that may differ from those set forth in the Agreement) or from other sources. We have no assurance that we could obtain alternative debt financing on comparable terms.

Health and pension benefit costs represent a significant expense to us.
With approximately 497,000 career employees and over 600,000 retirees and survivors who receive benefits, our expenses relating to employee and retiree health and pension benefits are significant. We participate in U.S. government pension and health and benefits programs for employees and retirees, including FEHB, CSRS and the FERS, as required by law or contractual agreement with our unions. We have no control or influence over the benefits offered by these plans and are required to make contributions to these plans as specified by law or, in the case of health benefits for the majority of our current employees, by contractual agreements with our unions. Several factors including participant mortality rates, returns on investment and inflation could require us to make significantly higher future contributions to these plans, and all of these factors are beyond our control.

Over the last decade, we have experienced significant increases in retiree health benefits costs, primarily as a result of PAEA, which obligates us to fully prefund the health benefits of current Postal Service employees and retirees. Additionally, we are required to continue contributing to the FERS pension program at rates specified by OPM and to make amortization payments for the unfunded liability. We were required, beginning in 2017, to begin to make amortization payments to pay down the unfunded liability of the CSRS when OPM determines that such payments are necessary.

Although the PRA established our Board with eleven members, including nine seats for independent Governors, eleven Presidential nominations for Governor have expired due to Senate inaction since 2014, and our Board is currently unable to assemble a quorum given that we have only two Governors in place.
On December 8, 2014, due to the term expiration of one Governor and Senate inaction on pending nominations, the number of sitting Board members dropped to five, thereby rendering the Board unable to assemble a quorum. The TEC has exercised its powers since that time.

On December 8, 2016, the hold-over term expired of our last independent Governor at the time, and as a result the Board had no presidentially appointed Governors for the first time since we began operations as the United States Postal Service in 1971. During this period when we had no Governors in place, the Board consisted only of our Postmaster General and Deputy Postmaster General.

On August 28, 2018, the Senate confirmed the nominations of two Governors, and the President formally appointed them to these positions on August 30, 2018. However, the hold-over terms of these Governors will expire on December 8, 2019, and December 8, 2020, and the Board remains without a quorum.

The President has made four additional Governor nominations, including the nomination of one of our current Governors for an additional seven-year term. However, if the Senate does not take action on any of these nominations, they will expire upon the adjournment of the 115th Congress. If the Senate does not confirm any new Governor nominations prior to December 8, 2019, our Board will be left with only one Governor, and if no Governors are confirmed prior to December 8, 2020, our Board will have lost all of its independent Governors and will again consist of only our Postmaster General and Deputy Postmaster General.

As described elsewhere in this report, certain powers are vested in the Governors alone. These critical responsibilities include setting our prices, approving new services and appointing (and, if necessary, removing) our Postmaster General and Deputy Postmaster General. In the event that no Governors are in place, these critical duties may not be able to be executed, potentially leaving us without the ability to adjust our prices as needed, introduce new services or appoint or replace our two most critical senior executive officers.

Our business and results of operations are significantly affected by competition from both competitors in the delivery marketplace as well as substitute products and digital communication. If we do not compete effectively and operate efficiently, grow marketing mail and package delivery services, and increase revenue and contribution from other sources, this adverse impact will become more substantial over time.
Our marketplace competitors include both local and national providers of package delivery services. Our competitors have different cost structures and fewer regulatory restrictions than we do and are able to offer differing services and pricing, which may hinder our ability to remain competitive in these service areas. In addition, some of our competitors have access to public capital markets, which allows them greater freedom in their financing and expansion of their business.

Customer usage of postal services continues to shift to substitute products and digital communication. *First-Class Mail*, such as the presentment and payment of bills, has been eroded by competition from electronic media, driven by some of our major commercial mailers which actively promote the use of online services. *Marketing Mail* has recently experienced declines due to mailers' growing use of digital advertising including digital mobile advertising. The volume of our *Periodicals* service continues to decline as consumers increasingly use electronic media for news and information. Periodical advertising has also experienced a decline as a result of the move to electronic media.

Although the Postal Service's Competitive service volumes have increased, this increase is largely due to significant volume growth from three major customers, all of which are building the delivery capability that would enable them to divert volume away from the Postal Service.
The growth in our Competitive service volumes over the past five years is largely attributable to our three largest customers. Each of these customers is building delivery capability that would enable them to divert volume away from the Postal Service over time. If these customers divert significant volume away from the Postal Service, the growth in our Competitive service volumes may not continue.

Adverse events may call into question our reputation for quality and reliability or our ability to deliver the mail and could diminish the value of our brand. This could adversely affect our business operations and operating revenue.
Our brand represents quality and reliable service, and therefore is a valuable asset. We use our brand extensively in sales and marketing initiatives and exercise care to defend and protect it. Any event, whether real or perceived, that calls into question our long-term existence, our ability to deliver mail, our quality or our reliability could diminish the value of our brand and reputation and could adversely affect our business operations and operating revenue.

Our need to streamline our operations in response to declining mail volume may result in significant costs. It is possible that the measures being considered would be insufficient to reduce our workforce and physical infrastructure to a level commensurate with declining mail volume.
Our ongoing reviews of cost-savings opportunities may identify opportunities that impact mail processing operations or affect lobby hours of retail units, Post Offices or other facilities. Presently, our regular review of the carrying value of our assets has not resulted in significant write-downs of our physical assets. However, future changes in business strategy, operations, legislation, government regulations or economic or market conditions may result in material impairment write-downs of our assets.

A union contract arrived at either through negotiation or arbitration could have a significant adverse impact on our future results of operations by impacting our control over wages and benefits and/or by limiting our ability to manage our workforce effectively.
Our collective bargaining agreements currently in force include provisions for mandatory COLAs, which are linked to the CPI-W. Although CPI-W has been relatively low since 2008 when our employees received COLA-based pay increases of nearly $1.1 billion, a resurgence of consumer inflation could have a significant adverse impact on our labor costs. The agreements also contain provisions that limit our ability to reduce the size of the labor force and employ non-career personnel. Reductions in the size and cost of our labor force may be necessary to offset the effects of declining volume and revenue.

Our ability to negotiate contracts that control labor costs is essential to achieving financial stability. We have no assurance that we will be able to negotiate contracts in the future with our unions that will result in a cost structure that is sustainable within current and projected future revenue levels. In addition, if our future negotiations should fail and involved parties proceed to arbitration, the risk of an adverse outcome exists, as there is no current statutory mandate requiring an interest arbitrator to consider our financial health in issuing an award. An unfavorable award in arbitration could have significant adverse consequences on our ability to meet future financial obligations.

Furthermore, an increase in the CPI-W may not correspond to an equivalent increase in the CPI-U, which affects the prices of our Market-Dominant services under current law, as the two indexes are calculated differently. Therefore, we may not be able to increase the prices of our services to keep up with increases in our wages.

We rely on the terms and conditions of our contracts with vendors and customers to deliver our services. These contracts are renegotiated on a routine and periodic basis. Significant changes in the costs, pricing or terms associated with these contracts could adversely affect our business.

Some of our suppliers and customers enter into long-term contracts with us to supply goods and services and to procure our services. These contracts are renegotiated from time to time and to the extent that contracts are not renewed, or are renewed with terms that may not sufficiently cover our costs or increase our costs, may have an adverse effect on our business. Certain vendors and customers are significant to the delivery of certain product lines, including a large courier service for air transportation. Our ability to maintain current or improved contract terms with customers and suppliers is critical to our initiatives to return to financial sustainability.

We rely on third-parties for air transportation to deliver our mail throughout the nation and abroad. A significant disruption in air transportation service could adversely affect our business and results of operations.

We do not own or operate aircraft and we rely on third-parties for the air transportation service required to deliver our mail and packages to various destinations within the U.S. and abroad. We are therefore subject to the risk of these providers' business operations and also to the adoption of regulatory requirements and other events that affect specific airlines or the airline industry as a whole, which could affect air service or temporarily ground the fleets of one or more of our providers. We may also be unable to negotiate terms as favorable with replacement carriers should one or more of our existing providers experience a disruption.

Fuel expenses are a material part of our operating costs. A significant increase in fuel prices could adversely affect costs and results of operations.

We are exposed to changes in commodity prices, primarily for diesel fuel, unleaded gasoline and aircraft fuel for transportation of mail, and natural gas and heating oil for facilities. For the year ended September 30, 2018, our expenses for fuel represented 3.4% of operating expenses. The price and availability of fuel can be unpredictable and is beyond our control. Additionally, as we use contracted carriers to transport the mail, we anticipate that increased operating costs for these independent carriers, including increased costs resulting from rising fuel prices, will ultimately be passed through to us, which would result in increased costs.

A failure to protect the privacy of customer information could damage our reputation and result in a loss of business.

We have invested in technology and employ a variety of technology security initiatives aimed at protecting organizational information, as well as customer information. As one of the U.S. government entities most trusted by the nation, protecting the confidentiality of data that we obtain is paramount to us. However, should our information technology security initiatives not fully insulate us from a security breach or data loss, our reputation could be damaged, resulting in an adverse effect on our operations and financial results. Moreover, unlike other non-governmental entities in our industry, we must abide by the *Privacy Act of 1974*, which restricts how we can collect, use, maintain and disseminate personally-identifiable information and prescribes civil remedies for non-compliance.

We rely extensively on computer systems and technology to manage the delivery of mail, process transactions, summarize results and manage our business.

Our operational and administrative information systems are among the largest and most complex systems maintained by any organization in the world. Any disruption to our infrastructure, including those impacting computer systems that facilitate mail handling and delivery and customer-utilized websites, could adversely impact customer service, mail volume and revenue, and result in significant increased costs. Any significant systems failure could cause delays in the processing and delivery of mail or result in the inability to process operational and financial data. Such disruptions could impair our reputation for reliable service, which would also adversely affect results of operations.

Reports of cyber incidents affecting national security, intellectual property and individuals have been widespread, with reported incidents involving data loss or theft, economic loss, computer intrusions and privacy breaches. The source of such threats is wide-ranging. The ability to maintain confidentiality, integrity and availability of information is critical to fulfilling our mission, and system failures resulting from these threats could damage our reputation, resulting in loss of business and increased costs.

Due to our recent and projected cash constraints, our operational performance in the future could be at risk as a result of inadequate capital investment in facilities, transportation equipment, mail processing equipment or information technology infrastructure, all of which are essential for our operations.

If our operations do not generate the liquidity we require, we may be forced to reduce, delay or cancel investments in technology, facilities and/or transportation equipment, as we have done in the recent past, while our competitors and other businesses are pursuing advanced, competing technologies and equipment.

Additionally, our aging facilities, equipment and transportation fleet could inhibit our ability to be competitive in the marketplace, deliver a high-quality service and meet the needs of the American public. The changes in the economic landscape in recent years have increased the importance for us to invest in our operations in order to remain competitive. Failure to anticipate or react to our competition, market demands and/or new technology due to inadequate cash reserves is a significant operational risk. An aging or potentially obsolete infrastructure could result in a loss of business and increased costs.

Workers' compensation insurance and claims expenses could have a material adverse effect on our business, financial condition and results of operations.

Workers' compensation liabilities are established for estimates of cash outlays that we are expected to ultimately incur on reported claims, as well as estimates of the costs of claims that have been incurred but not yet reported. Trends in actual experience and management judgments about the present and expected levels of cost per claim are significant factors in the determination of such accruals. Several other factors which are beyond our control, such as discount and inflation rates, could cause us to incur higher workers' compensation expenses.

We believe our estimated liability for such claims is adequate, but if actual experience results in an increase in the number of claims, and/or severity of claims for which we retain risk, this could cause a material difference from our estimates and adversely affect our financial condition and results of operations. In addition, our workers' compensation program is administered for us by the DOL, and as such, we do not have the same level of control over the execution of the program, including the costs we incur for certain medical and pharmacy costs, that a private company has with its workers' compensation insurance provider.

The potential liability associated with existing and future litigation against us could have a material adverse effect on our business, results of operations, financial condition and cash flows.

In the normal course of operations, we are subject to threatened and actual legal proceedings from time to time. Any litigation, regardless of its merits, could result in substantial legal fees and costs incurred by us. Further, actions that have been or will be brought against us may not be resolved in our favor and, if significant monetary judgments are rendered, we may not have the ability to pay them. Such disruptions, legal fees and any losses resulting from these claims could have a material adverse effect on our business, results of operations, financial condition and cash flows.

Natural disasters and adverse weather conditions that can damage property and disrupt business operations could have an adverse impact on our business operations and our financial results.

Natural disasters, such as hurricanes, earthquakes, tornadoes, floods, wildfires and severe winter storms place our employees in harm's way and make it challenging to deliver mail under these unpredictable and dangerous conditions. Damage to our facilities could also have a negative impact on business operations. We may incur significant additional operating costs in order to maintain continuity in fulfilling our mission.

ITEM 1B. UNRESOLVED STAFF COMMENTS

None.

ITEM 2. PROPERTIES

We own nearly 8,400 and lease over 23,000 Postal Service facilities ranging in size from 60 square feet to 32 acres. Our facilities support retail, delivery, mail processing, maintenance, administrative and support activities and are located in numerous communities throughout the U.S. and its territories. We believe our properties are generally in good physical condition and require only routine repairs and maintenance and periodic capital improvements. In addition, we monitor the productive capacity of our properties and our operational needs, which may, from time to time, result in the consolidation of some of our facilities.

ITEM 3. LEGAL PROCEEDINGS

As previously reported, on January 14, 2010, the Equal Employment Opportunity Commission's Office of Federal Operations certified the case *McConnell v. Brennan* (first instituted in 2006 as *McConnell v. Potter*) as a class action against us, with the class consisting of permanent-rehabilitation and limited-duty Postal Service employees who we assessed under the National Reassessment Process ("NRP") between the dates of May 5, 2006, and July 1, 2011. We 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 us.

In 2015, the Administrative Judge assigned to handle *McConnell* granted in-part both the Class Agent's and our motions for summary judgment. In her decision, the Administrative Judge found that the NRP violated the Rehabilitation Act. We appealed this decision to the Equal Employment Opportunity Commission's Office of Federal Operations, which was denied in 2018. We have begun implementing this 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 our National Equal Employment Opportunity Investigative Services Office. The claims submission deadline has now passed. Class Agent's counsel is challenging our implementation of the decision and many issues remain unresolved. As a result, the ultimate outcome could be greater or less than the amount accrued as of September 30, 2018.

We are subject to other legal proceedings and claims that arise in the ordinary course of our business. For further discussion of the legal proceedings affecting us, see *Item 8. Financial Statements and Supplementary Data*, *Notes to Financial Statements*, *Note 10 - Commitments and Contingencies*.

ITEM 4. MINE SAFETY DISCLOSURES

Not applicable.

PART II

ITEM 5. MARKET FOR REGISTRANT'S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES

As an "independent establishment of the Executive Branch of the Government of the United States," we do not issue equity or other securities.

ITEM 6. SELECTED FINANCIAL DATA

The selected financial data presented below for each year ended September 30 is derived from our audited financial statements. The selected financial data should be read in conjunction with *Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations* and the related notes to the financial statements in *Item 8. Financial Statements and Supplementary Data*, *Notes to Financial Statements*:

(in millions)	2018	2017	2016	2015	2014
Operating results					
Revenue:					
Total revenue before temporary exigent surcharge and change in accounting estimate	$ 70,660	$ 69,636	$ 69,301	$ 66,810	$ 66,427
Temporary exigent surcharge[1]	—	—	1,136	2,118	1,403
Total revenue before change in accounting estimate	$ 70,660	$ 69,636	$ 70,437	$ 68,928	$ 67,830
Change in accounting estimate[2]	—	—	1,061	—	
Total revenue	**$ 70,660**	**$ 69,636**	**$ 71,498**	**$ 68,928**	**$ 67,830**
Operating expenses:					
Compensation and benefits	$ 50,004	$ 49,108	$ 48,441	$ 47,278	$ 45,993
Unfunded retirement benefits amortization	2,398	2,658	248	241	7
Retiree health benefits	4,481	4,260	9,105	8,811	8,685
Workers' compensation	4	(797)	2,682	1,760	2,554
Transportation	7,861	7,238	6,992	6,579	6,586
All other operating expenses	9,697	9,743	9,431	9,157	9,353
Total operating expenses	**$ 74,445**	**$ 72,210**	**$ 76,899**	**$ 73,826**	**$ 73,178**
Loss from operations	**$ (3,785)**	**$ (2,574)**	**$ (5,401)**	**$ (4,898)**	**$ (5,348)**
Net loss	**$ (3,913)**	**$ (2,742)**	**$ (5,591)**	**$ (5,060)**	**$ (5,508)**
Financial position					
Assets:					
Cash and cash equivalents	$ 10,061	$ 10,513	$ 8,077	$ 6,634	$ 4,906
Property and equipment, net	14,616	14,891	15,296	15,686	16,338
All other assets	2,011	1,990	1,846	1,694	1,718
Total assets	**$ 26,688**	**$ 27,394**	**$ 25,219**	**$ 24,014**	**$ 22,962**
Liabilities:					
Retiree health benefits	$ 42,641	$ 38,160	$ 33,900	$ 28,100	$ 22,417
Workers' compensation costs	16,409	17,910	20,039	18,811	18,422
Debt	13,200	15,000	15,000	15,000	15,000
All other liabilities	17,075	15,048	12,262	12,494	12,454
Total liabilities	**$ 89,325**	**$ 86,118**	**$ 81,201**	**$ 74,405**	**$ 68,293**
Total net deficiency	**$(62,637)**	**$(58,724)**	**$(55,982)**	**$(50,391)**	**$(45,331)**

[1] The PRC authorized that we could collect a 4.3% exigent surcharge on Market-Dominant service beginning in January 2014 until such time that the surcharge produced just over $4.6 billion in incremental revenue. The limit was reached and the temporary exigent surcharge expired on April 10, 2016.

[2] The 2016 change in accounting estimate relates to changes in estimates of stamp usage and breakage for *Forever Stamps* sold from 2011 through June 30, 2016, reflected as a decrease in the *Deferred revenue-prepaid postage* liability as of June 30, 2016.

ITEM 7. 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 our financial results, liquidity, capital resources and critical accounting estimates. Our results of operations may be impacted by risks and uncertainties, many of which we cannot control or influence, and may cause actual results to differ materially from those currently contemplated.

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 are included in this report and 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. Important factors that could cause actual results to differ materially from those anticipated in our forward-looking statements include, but are not limited to, those described under *Item 1A. Risk Factors*.

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 as a single segment throughout the U.S., its possessions and territories.

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.

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 targeted legislative and regulatory reform as we continue to identify and create innovative and affordable services, and deliver high levels of performance and service, and that such financial stability would provide Congress and the Executive Branch with additional time to address the broader issues regarding our overall cost structure and revenue-generating opportunities.

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, growth in more labor-intensive Shipping and Packages volume and an increasing number of delivery points. We operate as a single segment and report our performance as such.

2018 Compared with 2017

Our reported operating revenue was $70.6 billion in 2018, an increase of $1.0 billion, or 1.5%, from the prior year.

As more fully described below in *Operating Revenue and Volume*, combined revenue from *First-Class Mail* and *Marketing Mail* declined by $827 million for the year ended September 30, 2018, compared to the prior year. This decline was attributable to a decline in combined volume of nearly 3.2 billion pieces. These declines in *First-Class Mail* and *Marketing Mail* revenue were more than offset by the increase in Shipping and Packages revenue of nearly $2.0 billion, or 10.1%, as we continued to experience growth in this lower-contribution service category throughout 2018.

As more fully described below in *Operating Expenses*, our 2018 operating expenses increased $2.2 billion, or 3.1%, compared to the prior year. The increase in operating expenses was primarily due to the following:

- Compensation and benefits expense increase of $896 million, or 1.8%, due to contractual wage adjustments, an increase in total work hours, particularly straight-time hours for non-career employees, and additional overtime hours for both career and non-career employees;
- Workers' compensation expense increase of $801 million, primarily resulting from the impact of changes in rules for pharmaceutical compounding which generated a $549 million one-time benefit in 2017 and were not repeated in 2018;
- Transportation expense increase of $623 million, or 8.6%, primarily due to higher air volumes, increasing fuel costs (both jet fuel and diesel), and higher unit costs per mile for third-party highway contractors; and
- Retiree health benefits expense increase of $221 million, or 5.2%, primarily due to the impact of discount rate changes on actuarial assumptions and calculations as per OPM.

This resulted in a net loss of $3.9 billion for the year ended September 30, 2018, compared to a net loss of $2.7 billion for 2017.

2017 Compared with 2016

Our reported operating revenue was $69.6 billion in 2017, a decrease of $1.8 billion, or 2.6%, from the prior year. This decrease was due to the combined effects of the $1.1 billion one-time, non-cash adjustment for deferred revenue in the prior year, discussed below in *2016 Change in Accounting Estimate*, and the April 2016 expiration of the exigent surcharge, which generated approximately $1.1 billion in incremental revenue during 2016. Excluding the effects of both the 2016 change in accounting estimate and the expiration of the exigent surcharge, operating revenue for the year ended September 30, 2017, would have increased by $361 million, or 0.5%, from the prior year on a 3.1% decrease in volume.

As more fully described below in *Operating Revenue and Volume*, combined revenue from *First-Class Mail* and *Marketing Mail* declined by $2.8 billion for the year ended September 30, 2017, compared to the prior year. This decline was attributable to a decline in combined volume of nearly 5.0 billion pieces, as well as the April 2016 exigent surcharge expiration. These declines in *First-Class Mail* and *Marketing Mail* revenue were partially offset by the increase in Shipping and Packages revenue of $2.1 billion, or 12.1%, as we continued to experience growth in this business throughout 2017.

As more fully described below in *Operating Expenses*, our 2017 operating expenses decreased $4.7 billion, or 6.1%, compared to the prior year. The decrease in operating expenses was primarily due to the following:

- Retiree health benefits expense decrease of $4.8 billion, or 53.2%, resulting from the expiration of the PAEA lump sum statutory funding schedule; and
- Workers' compensation expense decrease of $3.5 billion, or 129.7%, driven largely by the $2.4 billion impact of discount rates increasing in 2017.

These decreases in operating expenses were partially offset by the following:

- Unfunded retirement benefits amortization expense increase of $2.4 billion, resulting from provisions of the PAEA that became effective in 2017 and changes in actuarial estimations;
- Compensation and health benefits expense increase of $667 million, or 1.4%; and
- Transportation expense increase of $246 million, or 3.5%, the result of increased highway transportation expenses.

This resulted in a net loss of $2.7 billion for the year ended September 30, 2017, compared to a net loss of $5.6 billion for 2016.

2016 Change in Accounting Estimate

We recognize revenue for postage at the time a piece of mail is processed and delivered, not when we receive cash for the sale of postage. We estimate the amount of postage that we have sold, but customers have not yet used, and include this amount as a liability in our *Balance Sheets* as *Deferred revenue-prepaid postage*. The majority of this liability consists of our estimate of sold, but unused, *Forever Stamps*, the non-denominated postage stamps we introduced in 2007.

We have developed and validated the usage portion of our deferred revenue estimate through complex mathematical and statistical methods, including regression analysis, of postage stamp usage trends. Small differences in inputs can lead to significant differences in our estimate of the liability. "Breakage" represents the portion of sold *Forever Stamps* that we estimate will never be used by customers due to loss, damage or stamp collection. Assumptions regarding estimated usage and breakage of a particular postage stamp issue cannot be refined until each "series" of postage stamps nears the end of its life cycle.

During 2016, we revised the estimation technique utilized to estimate our *Deferred revenue-prepaid postage* liability for *Forever Stamps*. The change resulted from new information regarding customer's retention and usage habits of applicable postage, and enabled the Postal Service to update its estimate of stamps that will never be used for mailing. As a result of this change, *Deferred revenue-prepaid postage* was decreased by nearly $1.1 billion. In accordance with accounting principles generally accepted in the U.S. ("GAAP"), the change was accounted for as a change in accounting estimate, and was reflected in operating results as an increase to revenue and a decrease in net loss by the same amount in the year ended September 30, 2016. This adjustment had no impact on our liquidity nor did it lessen the severity of our liquidity outlook.

Non-GAAP Controllable (Loss) Income

In the day-to-day operation of our business, we focus on costs within our control, such as salaries and transportation. We calculate controllable (loss) income, a non-GAAP measure, by excluding items we cannot control, such as PSRHBF actuarial revaluation and amortization expenses, workers' compensation expenses caused by actuarial revaluation and discount rate changes, retirement expenses caused by actuarial revaluation, and adjustments for non-recurring items, such as the 2016 change in accounting estimate for *Deferred revenue-prepaid postage*. Controllable (loss) income should not be considered a substitute for net (loss) income and other GAAP reporting measures.

The following table reconciles our GAAP net loss to controllable (loss) income for the years ended September 30, 2018, 2017 and 2016:

(in millions)	**2018**	**2017**	**2016**
Net loss	**$ (3,913)**	**$ (2,742)**	**$ (5,591)**
PSRHBF unfunded liability amortization expense[1]	815	955	—
PSRHBF prefunding fixed amount[2]	—	—	5,800
Change in workers' compensation liability resulting from fluctuations in discount rates	(1,066)	(1,362)	1,026
Other change in workers' compensation liability[3]	(323)	(850)	188
Change in accounting estimate[4]	—	—	(1,061)
CSRS unfunded liability amortization expense[5]	1,440	1,741	—
FERS unfunded liability amortization expense[6]	958	917	248
Change in normal cost of retiree health benefits due to revised actuarial assumptions[7]	138	527	—
Controllable (loss) income	**$ (1,951)**	**$ (814)**	**$ 610**

[1] Expense for the annual payment due by September 30, 2018, and 2017, on the unfunded liability as calculated by OPM.

[2] Expense for the annual prefunding payment to the PSRHBF due on September 30, 2016, upon which the Postal Service defaulted.

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

[4] This change in accounting estimate relates to changes in estimates of stamp usage and breakage for *Forever Stamps* sold from 2011 through June 30, 2016, reflected as a decrease in the *Deferred revenue-prepaid postage* liability as of June 30, 2016.

[5] Expense for the annual payments due September 30, 2018, and 2017, calculated by OPM, to amortize the unfunded CSRS retirement obligation. Payments are to be made in equal installments through 2043.

[6] Expense for the annual payment due September 30, 2018, and 2017, calculated by OPM, to amortize the unfunded FERS retirement obligation. Payments are to be made in equal installments through 2047.

[7] Represents the annual portion of the normal cost payment due September 30, 2018, and 2017, attributable to revised actuarial assumptions and discount rate changes. The total normal cost payment amount, calculated by OPM, is $3.7 billion and $3.3 billion, respectively.

For the year ended September 30, 2018, we recognized a nearly $2.0 billion controllable loss compared to an $814 million controllable loss in 2017, an increase in controllable loss of $1.1 billion. This increase was driven by the increases in compensation and benefits of $896 million, the controllable portion (before adjustments for actuarial changes) of the normal cost of retiree health benefits expenses of $750 million, and transportation expenses of $623 million, partially offset by the $1.0 billion increase in operating revenue. These items are discussed in greater detail in *Operating Revenue and Volume* and *Operating Expenses*.

For the year ended September 30, 2017, we recognized an $814 million controllable loss compared to $610 million of controllable income in 2016, an increase in controllable loss of $1.4 billion. This decrease was driven by the $775 million decline in operating revenue before the 2016 change in accounting estimate, along with increases in compensation and benefits of $667 million and transportation expenses of $246 million, respectively. These items are discussed in greater detail in *Operating Revenue and Volume* and *Operating Expenses*.

OPERATING REVENUE AND VOLUME

Combined *First-Class Mail* and *Marketing Mail* have continued to provide the majority of our operating revenue. As a percentage of operating revenue, *First-Class Mail* and *Marketing Mail* combined represented 58.7%, 60.8% and 64.1% (before the 2016 change in accounting estimate) of our revenue for the years ended September 30, 2018, 2017 and 2016, respectively. *First-Class Mail* and *Marketing Mail* combined volume represented 91.5%, 91.7% and 92.1% of our volume in 2018, 2017 and 2016, respectively.

While we continue to experience strong results in our Shipping and Packages business, it represented only 30% of our revenues for the year ended September 30, 2018, compared to *First-Class Mail*, which represented 35%. Furthermore, Shipping and Packages generated only 4% of our volume for the year ended September 30, 2018, and the costs to process and deliver Shipping and Packages services are higher than the costs associated with *First-Class Mail* on a per-piece basis.

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 serve to stabilize *Marketing Mail* volume.

With our Shipping and Packages business, we have focused on growing e-commerce and implementing marketing campaigns that have helped us grow this business. By offering day-specific delivery, 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.

As described below, we implemented price increases on various Market-Dominant and Competitive services in January 2016, January 2017, September 2017, and January 2018. We have filed with the PRC notices of our intent to increase prices for certain Market-Dominant and Competitive services by an average of 2.5% and 7.4%, respectively. On November 13, 2018, the PRC approved both the Market-Dominant service price increase plan and the Competitive service price increase plan. These price increases are scheduled to go into effect on January 27, 2019.

As referenced throughout this report, the PRC authorized us to collect an exigent surcharge on most Market-Dominant services beginning in January 2014 until it produced incremental revenue of just over $4.6 billion, a figure the PRC ultimately determined was lost due to the Great Recession's suppression of mail volume. The limit on the amount of the exigent surcharge collected was reached on April 10, 2016, and we therefore reduced the prices of applicable Market-Dominant services on that date.

The following table details our operating revenue and volume for the years ended September 30, 2018, 2017 and 2016 by service category:

(in millions)	2018	2017	2016
Operating revenue:			
First-Class Mail[1]	$ 24,976	$ 25,689	$ 27,508
Marketing Mail[2]	16,512	16,626	17,622
Shipping and Packages[3]	21,507	19,529	17,427
International	2,630	2,614	2,674
Periodicals	1,277	1,375	1,507
Other[4]	3,720	3,760	3,630
Operating revenue before change in accounting estimate	**$ 70,622**	**$ 69,593**)	**$ 70,368**
Change in accounting estimate	—	—	1,061
Total operating revenue	**$ 70,622**	**$ 69,593**	**$ 71,429**
Volume:			
First-Class Mail[1]	56,714	58,834	61,240
Marketing Mail[2]	77,269	78,329	80,885
Shipping and Packages[3]	6,152	5,758	5,159
International	941	1,001	1,005
Periodicals	4,993	5,301	5,586
Other[5]	333	367	467
Total volume	**146,402**	**149,590**	**154,342**

Note: The totals for certain mail categories for prior years have been reclassified to conform to classifications used in the current year. Non-operating revenue is no longer included in this schedule.

[1] Excludes *First-Class Package Service - Retail* and *First-Class Package Service - Commercial*.

[2] Excludes *Marketing Mail Parcels*.

[3] Includes *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*.

[4] Revenue includes *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.

[5] Volume includes Postal Service internal mail and free mail provided to certain Congressionally-mandated groups.

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 for *First-Class Mail*, our most profitable service category, are the same regardless of the distance 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").

First-Class Mail volume continues to decline, with decreases of 3.6% in 2018, 3.9% in 2017 and 2.2% in 2016, due to the continuing migration toward electronic communication and transaction alternatives. *First-Class Mail* generated approximately 39%, 39% and 40% of the total volume for the years ended September 30, 2018, 2017 and 2016, respectively, but represented approximately 35%, 37% and 39% of operating revenue for the three years ended September 30, 2018, 2017 and 2016, respectively.

For the year ended September 30, 2018, *First-Class Mail* revenue fell by $713 million, or 2.8%, on a volume decline of 3.6%, compared to the prior year. The most significant factor contributing to the declining trend in *First-Class Mail* revenue and volume was the continuing migration from mail to electronic communication and transaction alternatives.

For the year ended September 30, 2017, *First-Class Mail* revenue decreased by $1.8 billion, or 6.6%, on a volume decline of 3.9%, compared to the prior year. The percentage of decline in revenue was greater than the percentage of decline in volume for 2017 due to the April 10, 2016, expiration of the exigent surcharge, which we estimate generated approximately $648 million in incremental *First-Class Mail* revenue in the first six months of 2016. The prices of certain *First-Class Mail* services also increased in January 2017, but the CPI increase was not sufficient to offset the loss of the exigent prices and lower volume.

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* volume is reflective of the cyclical nature of the U.S. economy and competition from other forms of advertising. Price increases for *Marketing Mail* are currently generally capped at the rate of inflation because they are classified by law as Market-Dominant.

Marketing Mail generated approximately 52.8%, 52.4% and 52.4% of the total volume, but represented approximately 23%, 24% and 25% of operating revenue for the three years ended September 30, 2018, 2017 and 2016, respectively.

Marketing Mail had experienced relatively flat volume between 2009 and 2016, although its share of the total advertising market declined somewhat due to the continued migration toward electronic communication. *Marketing Mail* volume declined significantly during 2017 and the first half of 2018, although this decline slowed in the second half of 2018. Relative to other forms of print advertising, *Marketing Mail* has generally proven to be a 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.

For the year ended September 30, 2018, *Marketing Mail* revenue decreased $114 million, or 0.7%, on a volume decline of 1.4%, compared to the prior year. *Marketing Mail* revenue and volume were negatively affected by a decline in political and election mail of approximately $30 million in revenue and approximately 300 million in volume, compared to the prior year. The current year included mailings associated with the 2018 mid-term primary elections, whereas the prior year included mailings associated with the 2016 general election.

For the year ended September 30, 2017, *Marketing Mail* revenue decreased by nearly $1.0 billion, or 5.7%, on a volume decline of 3.2%, compared to the prior year. The percentage of decline in revenue was greater than the percentage of decline in volume for 2017 due to the April 10, 2016, expiration of the exigent surcharge, which we estimate generated approximately $396 million in incremental *Marketing Mail* revenue in the first six months of 2016. Revenue and volume were also adversely affected by a reduction in mail advertising campaigns by certain large mailers.

Shipping and Packages

Our Shipping and Packages business consists largely of Competitive services that can be priced to reflect current market conditions. These include *Priority Mail, Priority Mail Express*, *Parcel Select, Parcel Return, First-Class Package Services - Retail*, and *First-Class Package Services - Commercial. Bound Printed Matter* and *Media and Library Mail*, and certain other package delivery classes that are also part of Shipping and Packages, but are considered Market-Dominant services and are therefore currently subject to price caps.

As a percentage of operating revenue, Shipping and Packages generated approximately 30%, 28% and 24% for the years ended September 30, 2018, 2017 and 2016, respectively. As a percentage of total volume, Shipping and Packages represented 4.2%, 3.8% and 3.3% for the years ended 2018, 2017 and 2016, respectively. Prices for these Competitive services increased an average of 4.1%, 3.9% and 9.5% in January 2018, January 2017 and January 2016, respectively.

For the year ended September 30, 2018, Shipping and Packages revenue grew by 10.1% on volume growth of 6.8%, compared to the prior year. For the year ended September 30, 2017, Shipping and Packages revenue grew by 12.1% on volume growth of 11.6%, compared to the prior year.

Our Shipping and Packages business has continued to show solid 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, although the rate of growth is slowing. The reasons for the slowing growth rate are: 1) strong competition, 2) growing package density leading some large shippers to shift volume away from the Postal Service, and 3) a narrowing of the shipping cost differential between the Postal Service and its competitors due to several years of above-average price increases.

Volume growth has been 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 2016 holiday seasons. To accommodate the surge in volume and to avoid service disruptions during the peak holiday seasons, we increased Sunday delivery service for some of our customers in limited U.S. markets and added non-career employees for the peak seasons in accordance with our labor agreements.

The following table details our operating revenue and volume for Shipping and Packages for the years ended September 30, 2018, 2017 and 2016 by each service:

(in millions)	2018	2017	2016
Shipping and Packages revenue:			
Priority Mail Services[1]	$ 10,138	$ 9,483	$ 9,015
Parcel Services[2]	6,670	5,890	4,830
First-Class Package Services[3]	3,871	3,353	2,782
Package Services	828	803	800
Total Shipping and Packages revenue	**$ 21,507**	**$ 19,529**	**$ 17,427**
Shipping and Packages volume:			
Priority Mail Services[1]	1,117	1,075	1,062
Parcel Services[2]	3,120	2,906	2,478
First-Class Package Services[3]	1,275	1,157	1,028
Package Services	640	620	591
Total Shipping and Packages volume	**6,152**	**5,758**	**5,159**

Note: The totals for certain mail categories for the prior year have been reclassified to conform to classifications used in the current year. Such reclassifications may impact total Shipping and Packages revenue for the prior years.

[1] Includes *Priority Mail*, a 1-3 business day delivery service; *Priority Mail Express*, an overnight delivery service available 365 days per year; and *USPS Retail Ground,* a retail-only Competitive service priced identically and functionally equivalent to *Priority Mail* for Zones 1-4.

[2] Includes *Parcel Select*, *Parcel Return* and *Marketing Mail Parcels*.

[3] Includes *First-Class Package Services - Retail* and *First-Class Package Services - Commercial*.

Priority Mail Services

Priority Mail Services, our Shipping and Packages subcategory that includes *Priority Mail*, *Priority Mail Express* and *Retail Ground*, allows customers the ability to send documents and packages requiring expedited transportation and handling. As our flagship Shipping and Packages subcategory for retail and commercial customers, Priority Mail Services accounted for 47.1%, 48.6% and 51.7% of Shipping and Packages revenue for the years ended 2018, 2017 and 2016, respectively. While Priority Mail Services continues to grow year-over-year, its service offerings are somewhat price sensitive, particularly with retail customers, and its growth rate is lower than other Shipping and Packages subcategories used by commercial customers.

For the year ended September 30, 2018, Priority Mail Services revenue grew by 6.9% on volume growth of 3.9%, compared to the prior year. The January 2018 price increase applicable to Competitive services contributed to higher growth in revenue versus volume for the year ended September 30, 2018.

For the year ended September 30, 2017, Priority Mail Service revenue grew by 5.2% on volume growth of 1.2%, compared to the prior year. The January 2017 price increase applicable to Competitive services contributed to higher growth in revenue versus volume for the year ended September 30, 2017.

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 Services largely consist of "last-mile" deliveries, offered to large bulk shippers that drop parcels deeper into our network. Parcel Services represented 31.0%, 30.2% and 27.7% of Shipping and Packages revenue for the years ended September 30, 2018, 2017 and 2016, respectively. Parcel Services showed strong revenue growth of 13.2% and 21.9% and volume growth of 7.4% and 17.3% for the years ended September 30, 2018, and 2017, respectively.

The increase in year-over-year growth for Parcel Services revenue and volume were driven largely by our competitive pricing on these services and the continuing growth of e-commerce, as such businesses are heavy users of our *Parcel Select* services. This high-growth subcategory has rapidly become a significant contributor to our overall Shipping and Packages growth. However, because *Parcel Select* services are pre-sorted by customers and bypass most of our processing network, these are some of our lowest-priced services with a relatively lower contribution margin, and as a result, do not provide as much revenue per piece when compared to many of our other package services.

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

For the year ended September 30, 2018, First-Class Package Services revenue increased 15.4% on volume growth of 10.2%, compared to the prior year. For the year ended September 30, 2017, First-Class Package Services revenue grew by 20.5% on volume growth of 12.5%, compared to the prior year. The higher growth in revenue compared to volume for both 2018 and 2017 was due in large part to the impacts of the January 2018 and January 2017 price increases applicable to Competitive services.

Package Services
Customers use our Package Services subcategory for shipping merchandise or bound printed matter, including library and media mail, weighing up to 70 pounds. For the year ended September 30, 2018, Package Services revenue increased by 3.1%, on volume growth of 3.2%, compared to the prior year. For the year ended September 30, 2017, Package Services revenue increased by 0.4% on volume growth of 4.9%, compared to the prior year. Revenue growth in this subcategory has not kept up with volume growth due to price caps and bulk rates offered to certain high-volume shippers of bound printed matter parcels.

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. International Mail revenue represented 3.7%, 3.8% and 3.7% of total operating revenue for 2018, 2017 and 2016, respectively.

"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 only one-third of its volume, whereas "inbound" services are the opposite, generating two-thirds of International Mail volume but only one-third of its revenue. For the past several years, we have experienced an increase in inbound mail volume, much of that from letter post packets and parcels related to international e-commerce.

For the year ended September 30, 2018, International Mail revenue increased by 0.6% despite a volume decline of 6.0%, compared to the prior year. The increase in revenue is largely the result of higher rates resulting from the January 2018 price increases, higher packet rates under the terminal dues system and new negotiated service agreements between the U.S. and several countries.

For the year ended September 30, 2017, International Mail revenue decreased by 2.2% and volume declined 0.4%, compared to the prior year. The January 2017 price increases positively affected revenue from *First-Class International Package Service* and other international Competitive services, which offset the revenue lost from declines in higher-priced outbound volume. We continued to experience an increase in inbound mail volume, much of that from letter post packets and parcels related to international e-commerce. This increase in inbound volume was not enough to offset declines in *First-Class Mail International* and other outbound volume.

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. Under the UPU, payments for the delivery costs for 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 Secretary of State gave notice to the UPU that the U.S. is withdrawing from the UPU effective mid-October 2019. During this one-year period, the Department of State will seek to negotiate bilateral and multilateral 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.

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 list of subscribers or requesters. For the year ended September 30, 2018, *Periodicals* revenue decreased by 7.1% and volume decreased by 5.8%, compared to the prior year. For the year ended September 30, 2017, *Periodicals* revenue decreased by 8.8% and volume decreased by 5.1%, compared to the prior year.

Periodicals revenues and volumes 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 revenue includes ancillary services such as *Certified Mail*, *PO Box* services, and *Return Receipt* services. Also included in this category are money orders, passport services, "signature on delivery" services, insurance, and our own internal mail, which generates no revenue and has volume that can vary significantly from year to year.

For the year ended September 30, 2018, Other services revenue declined by 1.1%, compared to the prior year. For the year ended September 30, 2017, Other services revenue increased by 3.6%, compared to the prior year.

OPERATING EXPENSES

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

As described above in *Operating Revenue and Volume*, we anticipate that the continued migration of communications and commerce to electronic media will adversely affect *First-Class Mail* volume and revenue for the foreseeable future. Although increased Shipping and Packages volume has offset some of these declines, the costs of transporting and delivering packages on a per-piece basis are higher than the costs for *First-Class Mail*.

Our challenge to contain costs is compounded by the continuing increase in the number of delivery points, which, when combined with the impact of lower hard copy 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%.

Furthermore, our mail processing and distribution network was originally designed to provide overnight delivery service of *First-Class Mail* within specified delivery areas for a much higher volume of mail than what we process and deliver today, and therefore the network's legacy capabilities are excessive relative to today's mail volume. Consequently, many of our processing and distribution facilities continue to operate at much less than full capacity.

Compensation and Benefits

Compensation and benefits, our largest operating expense category, represented approximately 67%, 68% and 63% of our total operating expenses for the years ended September 30, 2018, 2017 and 2016, and consist of costs related to our active career and non-career employees.

The majority of our employees participate in either CSRS or FERS based on the starting date of employment with us or another U.S. government employer. Employees may also participate in the TSP, a defined contribution savings and investment plan administered by the Federal Retirement Thrift Investment Board. By law, we do not incur normal costs for CSRS retirement benefits. 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.

For the year ended September 30, 2018, compensation and benefits increased by 1.8%, compared to a 1.4% increase the prior year. The following table provides the components of compensation and benefits for active employees as of September 30, 2018, 2017 and 2016:

(in millions)	2018	2017	2016
Compensation	$ 37,795	$ 37,026	$ 36,634
FERS employees' current year service	6,720	6,604	6,509
Employee health benefits	5,169	5,163	4,972
Other	320	315	326
Total compensation and benefits	**$ 50,004**	**$ 49,108**	**$ 48,441**

Compensation

During the year ended September 30, 2018, compensation expense increased $769 million, or 2.1%, compared to 2017. The 2018 increase was attributable primarily to contractual wage adjustments including COLAs, an increase in total work hours, particularly hours for non-career employees, and additional overtime hours for both career and non-career employees.

During the year ended September 30, 2017, compensation expense increased $392 million, or 1.1%, compared to 2016. The 2017 increase was attributable primarily to contractually-obligated salary escalations, and additional work hours, driven by the more labor-intensive Shipping and Package business, partially offset by the impact of attrition of higher paid employees, who were largely replaced by newly converted career employees and non-career employees earning lower wages.

Workforce Composition

The composition of our workforce is a significant factor of our compensation expense. As of September 30, 2018, our career workforce consisted of approximately 497,000 career employees, a reduction of approximately 6,000 career employees from the previous year. As of September 30, 2018, the number of non-career employees decreased by approximately 4,000 from the previous year. Our overall workforce consisted of approximately 634,000 career and non-career employees, a decrease of 10,000, or 1.6%, compared to the prior year. These decreases reflect normal attrition as we continue to align our workforce with declining mail volume.

The number of total employees increased 4,000, or 0.6%, between 2017 and 2016. This increase was the result of an increase in non-career employees. Beginning in 2013, our labor contracts permitted us to use more non-career employees, allowing us to replace career work hours with non-career work hours at reduced rates and to support the continuing growth in our Shipping and Packages business and the continuing growth in the delivery network.

During 2018 and 2017, we converted approximately 35,000 and 28,000 employees, respectively, from non-career to career status, as dictated by our operational needs and contractual provisions. These conversions were necessary to offset attrition of career employees, primarily through retirement. Although career employees are more costly than non-career, these converted employees represent a significant savings relative to the career employees they replace who were compensated on a higher wage scale.

The following table provides the totals of career and non-career employees as of September 30, 2018, 2017 and 2016:

	2018	2017	2016
Career employees	497,000	503,000	509,000
Non-career employees	137,000	141,000	131,000
Total employees	**634,000**	**644,000**	**640,000**

Work Hours

Work hours are an important component of compensation expense. During the year ended September 30, 2018, total work hours increased by approximately 6 million, or 0.5%, compared to 2017. During the year ended September 30, 2017, total work hours increased by approximately 6 million, or 0.5%, compared to 2016. These increases were influenced by the growth in the number of delivery points and the growing Shipping and Packages volume. The number of delivery points increased by approximately 1.2 million in both 2018, and 2017.

Collective Bargaining Agreements

As of September 30, 2018, approximately 92% of our employees are covered by collective bargaining agreements. The contracts with the four labor unions representing the majority of our employees include provisions granting annual increases and COLAs, which are linked to the CPI-W. For further discussion of collective bargaining agreements, see *Item 8. Financial Statements and Supplementary Data*, *Notes to Financial Statements*, *Note 10 - Commitments and Contingencies*.

Non-bargaining Salaries

Annual salary increases for non-bargaining unit employees only occur through a Pay-For-Performance ("PFP") system. With only minor exceptions, no COLA or locality pay programs apply to non-bargaining unit employees. PFP salary increases averaged 2.0% for 2017 (implemented in January 2018), 2.9% for 2016 (implemented in January 2017), and 1.6% for 2015 (implemented in January 2016).

FERS Employees' Current Year Service

Our expense for FERS employees' current year service consists of FERS normal cost, Social Security and TSP contributions, and is reported within *Compensation and benefits* under *Operating expenses* in the accompanying *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 cost of unfunded FERS retirement benefits is reported separately within *Unfunded retirement benefits* in the accompanying *Balance Sheets*, as discussed below. For additional information, see *Item 8. Financial Statements and Supplementary Data*, *Notes to Financial Statements*, *Note 11 - Retirement Plans*.

The following table presents the components of FERS employees' current year service as included within *Compensation and benefits* for the years ended September 30, 2018, 2017 and 2016:

(in millions)	2018	2017	2016
FERS normal costs	$ 3,479	$ 3,474	$ 3,436
Social security	2,128	2,039	2,009
TSP	1,113	1,091	1,064
Total FERS employees' current year service	**$ 6,720**	**$ 6,604**	**$ 6,509**

For the years ended September 30, 2018, and 2017, total FERS employees' current year service costs increased 1.8% and 1.5%, respectively, compared to the previous years.

For the years ended September 30, 2018, and 2017, FERS normal costs increased 0.1% and 1.1%, respectively, compared to the previous years. As most of our employees participate in FERS and FERS-FRAE, these increases were consistent with the general increases in compensation and employer normal cost contribution percentages for the respective years and the slight changes in career employee headcount compared to the preceding years, as described above in *Compensation*. Our employer normal cost contribution rate was unchanged at 13.7% of basic pay for most employees who participated in FERS during both 2018 and 2017, although over 100,000 of our employees participate in FERS–FRAE, and we have a lower contribution rate for them.

For the years ended September 30, 2018, and 2017, employer Social Security costs increased 4.4% and 1.5%, respectively, compared to the previous years. The increase in 2018 was driven primarily by general increases in compensation, and to a lesser extent, the 7.3% increase in the annual salary cap for calendar year 2017, which increased the amounts that we contributed to Social Security during the first quarter of fiscal year 2018, the period in which certain employees became subject to the cap.

For the years ended September 30, 2018, and 2017, employer TSP matching contributions increased 2.0% and 2.5%, respectively, compared to the previous years. These increases were also consistent with the general increases in compensation for the respective years and the slight changes in career employee headcount compared to the preceding years, as described above in *Compensation*.

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 FEHB, which is administered by OPM. We account for employee benefit costs as an expense in the period in which our contributions to the plans under the program are due. Average premium increases were 4.0% in 2018, 4.4% in 2017 and 3.8% in 2016.

Employee health benefits expense was $5.2 billion for the year ended September 30, 2018, a 0.1% increase over 2017. For the year ended September 30, 2017, the expense was $5.2 billion, a 3.8% increase compared to the 2016 expense of $5.0 billion.

Our employer contribution rates for the majority of our employees are subject to collective bargaining agreements. Our share of healthcare premiums for employees represented 72.8%, 73.8% and 74.4% of premiums for 2018, 2017 and 2016, respectively. Employee health benefits expense was 10.3%, 10.5% and 10.3% of total compensation and benefits expense for the years ended September 30, 2018, 2017 and 2016, respectively.

CSRS and FERS Unfunded Retirement Benefits

OPM periodically notifies us regarding its revaluation of unfunded CSRS and FERS retirement benefits. OPM began calculating these obligations using Postal Service-specific demographic assumptions for its valuation as of September 30, 2017, but not Postal Service-specific salary growth assumptions. Prior to that, OPM used government-wide salary growth and demographic data. OPM's rule announcing this change did not fully address our concerns regarding the use of government-wide versus Postal Service-specific economic assumptions.

We record the expenses for our unfunded CSRS and FERS liabilities as *Unfunded retirement benefits amortization* in the accompanying *Statement of Operations*. These amounts may be significantly impacted by changes in actuarial assumptions used to revalue the unfunded liabilities.

The following table presents the cost of CSRS and FERS unfunded retirement benefits amortization expense for the years ended September 30, 2018, 2017 and 2016:

(in millions)	2018	2017	2016
CSRS unfunded retirement benefits amortization	$ 1,440	$ 1,741	$ —
FERS unfunded retirement benefits amortization	958	917	248
Total cost of CSRS and FERS unfunded retirement benefits amortization	**$ 2,398**	**$ 2,658**	**$ 248**

The Board of Actuaries of the Civil Service Retirement System ("Board of Actuaries") makes recommendations regarding the interest, salary inflation, COLA and investment return rate assumptions used to determine the funded status of both CSRS and FERS. In June 2017 and in April 2018, the Board of Actuaries updated these actuarial assumptions.

During 2018, OPM invoiced us $1.4 billion and $958 million for our CSRS and FERS unfunded benefits payments, respectively, due September 30, 2018, and we recorded the invoiced amounts as expenses. We received invoices from OPM for $1.7 billion and $917 million for our CSRS and FERS unfunded benefits payments, respectively, due September 30, 2017. For both 2018 and 2017, we determined that we would not be able to make these payments, in order to preserve adequate liquidity and ensure that we would be able to continue to fulfill our primary universal service mission.

As of the date of this report, we have not incurred any penalties or negative financial consequences as a result of not making our CSRS and FERS unfunded benefit payments to OPM.

We believe that the OPM methodology increases our present and future costs because it fails to fully consider the Postal Service's lower rate of salary growth, relative to the remainder of the federal government. Experience over the past decade demonstrates that the average salary increases of our employees are lower than the government-wide estimates that OPM currently uses. As described elsewhere in this report, OPM calculated that our portion of the FERS plan was underfunded by $17.1 billion as of September 30, 2017. We continue to assert that OPM should reconsider its use of such government-wide economic factors and apply both Postal Service-specific economic and demographic assumptions, which we believe would result in a reduction in the unfunded liability. However, it is unlikely the overstatement of the unfunded obligation resulting from OPM's use of government-wide economic assumptions would be sufficiently large to allow for an appeal of the liability calculation under OPM's present rules.

In addition to OPM's use of government-wide economic factors to calculate our liability and contribution rates to the plans, we are subject to the following constraints and risks that would otherwise not apply with a Postal Service-specific structure:

- Assets contributed to the plans by a single participating U.S. government employer may be used to provide benefits to employees of other participating employers.
- If a participating U.S. government employer ceases contributing to a plan, any unfunded obligations of the plan may be borne by the remaining participating employers.
- Federal law mandates our participation in the plans. If a change in the law permitted us to discontinue this participation, we may be required to contribute to the discontinued plan(s) an amount based on any underfunded status, referred to as a withdrawal liability, if such a liability exists at that time.

Funded Status

OPM administers the CSRS and FERS plans via the Civil Service Retirement and Disability Fund ("CSRDF"). Although CSRDF is a single fund that does not maintain a separate account for each participating U.S. government employer, PAEA requires certain disclosures regarding obligations and changes in net assets as if the funds were separate. Such disclosures, which are presented below, are based solely on information provided to us by OPM.

Because CSRS and FERS are not subject to the rules and regulations of the *Pension Protection Act of 2006*, typical plan measurements such as zone status and financial improvement plan status, or rehabilitation plan status are not available for these plans.

Each October, OPM provides us with an actuarial report prepared for the purpose of providing financial reporting information with respect to our CSRS and FERS pension obligations, in accordance with PAEA requirements. The actuarial report contains information regarding: 1) the funded status of our CSRS and FERS pension obligations; 2) components and analysis of net change in actuarial liabilities and fund balances for CSRS and FERS; 3) cost methods and assumption underlying actuarial valuations; and 4) actual and estimated contributions to and outlays from our accounts for CSRS and FERS.

In its October 2018 report to the Postal Service, OPM provided estimated 2018 information for CSRS and FERS in which estimates are rolled-forward from the actual actuarial liability and fund balances as of September 30, 2017. The actual actuarial liability and fund balances as of September 30, 2018, may differ from these rolled-forward estimates, as data will be updated and actuarial assumptions may be revised during the course of the year.

The following table provides OPM's calculations of the funded status of CSRS and FERS for our employees as of September 30, 2018 (estimated), 2017 and 2016, and represents the most recent data available. The actuarial liability presented below represents our share of the CSRS and FERS actuarial liabilities, as estimated by OPM. The fund balance presented below represents contributions made by us to CSRS and FERS, plus a rate of return on such contributions as estimated by OPM.

(in billions)	Estimated[1] 2018	Actual 2017	Actual 2016
CSRS			
Actuarial liability as of September 30	$ 185.3	$ 189.5	$ 199.3
Fund balance per OPM[2]	161.6	165.3	172.4
(Less) amount past due[3]	(1.4)	—	—
Unfunded	$ (25.1)	$ (24.2)	$ (26.9)
FERS			
Actuarial liability as of September 30	$ 137.4	$ 130.7	$ 124.7
Fund balance per OPM[4]	120.0	113.6	109.4
(Less) amount past due[5]	(1.0)	—	—
Unfunded	$ (18.4)	$ (17.1)	$ 15.3
Total CSRS and FERS			
Actuarial liability as of September 30	$ 322.7	$ 320.2	$ 324.0
Fund balance per OPM	281.6	278.9	281.8
(Less) amount past due	(2.4)	—	—
Unfunded	$ (43.5)	$ (41.3)	$ (42.2)

[1] The most current actual data from OPM is as of September 30, 2017. The estimated information for 2018 was provided by OPM, but is subject to change when final 2018 information is provided in 2019.

[2] The CSRS estimated fund balance for 2018 provided by OPM assumes we made the amortization payments due on September 30, 2018. However, no such payment was made.

[3] Amount past due represents the CSRS amortization payment due on September 30, 2018. However, no such payment was made.

[4] The FERS estimated fund balance for 2018 provided by OPM assumes we made the amortization payment due on September 30, 2018. However, no such payment was made.

[5] Amount past due represents the FERS amortization payment due on September 30, 2018. However, no such payment was made.

We have reported this information based on the same valuation techniques and economic assumptions that are used by the Board of Actuaries to establish the normal cost and funding requirements for the plans. OPM actuarial valuations utilize the long-term economic assumptions established by the Board of Actuaries. These economic assumptions are prepared for U.S. government employers as a whole, rather than those specific to the Postal Service.

As disclosed in OPM's *Civil Service Retirement and Disability Fund Annual Report* dated February 2018, which reported data for government-wide employers for 2016, the most current period available, we provided significantly more than 5% of the total plan contributions for FERS.

As a result of the unfunded liabilities for CSRS and FERS, OPM calculated an amortization schedule to pay down the FERS deficit over 30 years, and, accordingly, billed us $958 million, $917 million and $248 million for 2018, 2017 and 2016, respectively. Likewise, in accordance with the provisions of the PAEA, OPM calculated an amortization schedule to pay down the CSRS deficit by September 30, 2043, and, accordingly, billed us $1.4 billion and $1.7 billion for 2018 and 2017, respectively. There was no amount billed by OPM for CSRS deficit in 2016. As noted above, none of these amounts were paid and all are included within *Unfunded retirement benefits* in the accompanying *Balance Sheets*.

The following table provides U.S. government-wide information for plan assets, accumulated benefit obligations, the unfunded actuarial liability amounts and percentage funded for both the CSRS and FERS retirement plans, as published in OPM's *Civil Service Retirement and Disability Fund Annual Report* (dated February 2018), for the year ended September 30, 2016, the date of the most recent available information, as well as comparative Postal Service amounts for the same period:

($ in billions)	U.S. Government	Postal Service	Postal Service as a % of the U.S. Government
CSRS:			
Plan assets	$ 293.2	$ 172.4	58.8%
Accumulated benefit obligations	1,084.2	199.3	18.4%
Unfunded actuarial liability	$ (791.0)	$ (26.9)	
% Funded	27.0%	86.5%	
FERS:			
Plan assets	$ 595.2	$ 109.4	18.4%
Accumulated benefit obligations	715.7	124.7	17.4%
Unfunded actuarial liability	$ (120.5)	$ (15.3)	
% Funded	83.2%	87.7%	

When CSRS and FERS data for the Postal Service were excluded from the 2016 U.S. government-wide data, the CSRS plan was less than 14% funded, while the FERS plan was approximately 82% funded. This is because the Postal Service funding of CSRS and FERS was greater than 86% and 87%, respectively.

Cost Methods and Assumptions

The Board of Actuaries recommended revisions to certain government-wide demographic assumptions including additional future mortality improvement, effective for the September 30, 2017, valuation. The following table details the long-term economic assumptions recommended by the Board of Actuaries and included in OPM's valuation reports for the years ended September 30, 2018, 2017 and 2016:

	2018		2017		2016	
	CSRS	FERS	CSRS	FERS	CSRS	FERS
Rate of inflation	2.50%	2.50%	2.50%	2.50%	2.50%	2.50%
Long-term COLA	2.50%	2.00%	2.50%	2.00%	2.50%	2.00%
Actual COLA applied	2.00%	2.00%	0.30%	0.30%	0.00%	0.00%
Long-term salary increase	2.75%	2.75%	2.75%	2.75%	2.75%	2.75%
Actual salary increase	3.10%	3.10%	2.10%	2.10%	1.30%	1.30%
Long-term interest rate	4.25%	4.25%	4.25%	4.25%	4.50%	4.50%

Net Periodic Costs

The following, provided by OPM, details the changes in our estimated actuarial liability for CSRS and FERS as of September 30, 2018, (estimated) and 2017, and represents the most recent data available:

(in billions)	Estimated[1] 2018	Actual 2017
CSRS		
Actuarial liability as of October 1	$ 189.5	$ 199.3
+ Contributions[2]	0.1	0.1
- Benefit disbursements	(12.1)	(12.1)
+ Interest expense	7.8	8.7
- Actuarial gain	—	(6.5)
Actuarial liability as of September 30	**$ 185.3**	**$ 189.5**
FERS		
Actuarial liability as of October 1	$ 130.7	$ 124.7
+ Normal costs	4.4	4.4
- Benefit disbursements	(3.3)	(2.9)
+ Interest expense	5.6	5.6
- Actuarial gain	—	(1.1)
Actuarial liability as of September 30	**$ 137.4**	**$ 130.7**
Total actuarial liability as of September 30	**$ 322.7**	**$ 320.2**

[1] The most current actual data from OPM is as of September 30, 2017. The estimated information for 2018 was provided by OPM, but is subject to change when final 2018 information is provided in 2019.

[2] Contributions for CSRS consist of employee contributions only.

Components of Net Change in Plan Assets

As described above, CSRDF is a single fund and does not maintain separate accounts for CSRS and FERS or for individual U.S. government employers. The investment holdings of the CSRDF consist entirely of long-term special-issue U.S. Treasury securities with maturities of up to 15 years. The long-term securities bear interest rates ranging from 1.38% to 5.13%, while the short-term securities bear an interest rate of 2.88%.

The assumed rate of return on the CSRS fund balance was 4.25% for 2017 and 4.50% for 2016, and the actual rates of return were 2.94% and 4.10%, respectively. For the FERS fund, the assumed rate of return was 4.25%

for 2017 and 4.50% for 2016, while the actual rates of return were 2.97% and 2.95%, respectively. The projected long-term rate of return for both the CSRS and FERS fund balances for 2018 was 4.25%.

The following table details OPM's 5-year estimates for our CSRS and FERS contributions (both employee and employer), unfunded liability amortization payments and benefit payments:

(in billions)	CSRS			
Year	Employee contributions	USPS contributions	Amortization payments	Total benefit payments
2019	$ 0.1	$ —	$ 1.4	$ 1.5
2020	0.1	—	1.4	1.5
2021	0.1	—	1.4	1.5
2022*	—	—	1.4	1.4
2023*	—	—	1.4	1.4
(in billions)	**FERS**			
Year	**Employee contributions**	**USPS contributions**	**Amortization payments**	**Total benefit payments**
2019	$ 0.4	$ 3.3	$ 1.0	$ 4.7
2020	0.4	3.4	1.0	4.8
2021	0.4	3.5	1.0	4.9
2022	0.4	3.3	1.0	4.7
2023	0.4	3.2	1.0	4.6

* Employee contributions in 2022 and 2023 are projected to continue, but at less than $0.1 billion per year.

The following information, provided by OPM, details the components of the net change in our estimated portion of plan assets for CSRS and FERS for the years ended September 30, 2017, and 2016, and represents the most recent data available:

(in billions)	Actual 2017	Actual 2016
CSRS		
Net assets as of October 1	$ 172.4	$ 177.4
+ Contributions	0.1	0.2
- Benefit disbursements	(12.1)	(12.2)
+ Investment income	4.9	7.0
CSRS net assets as of September 30	**$ 165.3**	**$ 172.4**
FERS		
Net assets as of October 1	$ 109.4	$ 105.2
+ Contributions	3.8	3.7
- Benefit disbursements	(2.9)	(2.6)
+ Investment income	3.3	3.1
FERS net assets as of September 30	**$ 113.6**	**$ 109.4**

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. Under PAEA, we are obligated to fully fund the PSRHBF for the estimated employer's portion of the established health benefits of retirees and our current employees.

Our total cost for retiree health benefits in both 2018 and 2017 consists of two components: 1) the normal cost of the estimated retirement health benefits of active career employees, and 2) the amortization of the unfunded liability of the PSRHBF. We recognize an expense when the payment is due. In 2016, our total cost for retiree health benefits consisted of two different components: 1) our portion of the current premium expense for beneficiaries, and 2) the statutorily set PSRHBF prefunding payment, which we recognized as an expense when due.

In addition to changes in premium amounts each year, several other factors could significantly affect our future retiree health benefits expenses, including investment performance of the PSRHBF, changes in demographics, changes in actuarial assumptions and increased or decreased benefits to participants. See *Item 8. Financial Statements and Supplementary Data*, *Notes to Financial Statements*, *Note 12 - Health Benefits Plans*, *Retiree Health Benefits* for additional information.

Normal Costs and Retiree Health Benefits Premiums

In accordance with PAEA, beginning in 2017, the PSRHBF began funding our share of retiree health benefit premiums, and we were obligated to begin paying into the PSRHBF the normal costs of retiree health benefits attributable to the current year's service of our employees. We received invoices from OPM in the amounts of $3.7 billion and $3.3 billion for normal costs that we were obligated to pay by September 30, 2018, and September 30, 2017, respectively. We did not make these payments in order to preserve liquidity and to ensure that our ability to fulfill our primary universal service mission was not placed at undue risk.

According to OPM, the number of Postal Service annuitants receiving retiree health benefits was approximately 495,000, 496,000, and 497,000 for the years ended September 30, 2018, 2017 and 2016, respectively.

PSRHBF Funded Status

OPM valuations of post-retirement health liabilities and normal costs were prepared in accordance with Federal Accounting Standards Advisory Board Statement of Federal Financial Accounting Standards ("SFFAS") No. 5 and SFFAS No. 33, which require the use of the aggregate entry age normal actuarial cost method. Demographic assumptions are consistent with the pension valuation assumptions, but decrements are based upon counts or numbers rather than dollars.

The following information, provided by OPM, details the PSRHBF funded status. The amounts invoiced but not paid to the PSRHBF are reported in *Retiree health benefits* in the accompanying *Balance Sheets*.

(in billions)	2018	2017
Beginning actuarial liability at October 1	$ 112.1	$ 104.0
+ Actuarial (gain) loss	(2.2)	4.0
+ Normal costs	3.8	3.5
+ Interest at 4.5% and 4.8%, respectively	4.0	4.0
Subtotal net periodic costs	$ 5.6	$ 11.5
- Premium payments	(3.7)	(3.4)
Actuarial liability at September 30	$ 114.0	$ 112.1
- Fund balance at September 30	(90.1)	(88.0)
+ Amounts past due	42.6	38.2
Unfunded obligations at September 30	**$ 66.5**	**$ 62.3**

The determination of the liability assumes a single equivalent discount rate of 3.6% based on the most recent ten-year historical average yield curve. The normal cost, which is on a per-participant basis, is computed to increase annually by a variable medical inflation rate which is assumed to be 4.6% per annum as of the valuation date, grading down to an ultimate value of 3.2% in 2075. This results in a single equivalent trend rate of 4.5%. Normal costs are derived from the current FEHB on-rolls population with an accrual period from entry into FEHB to assumed retirement. The amounts and variables used to determine the liability are the same as the assumptions used under

OPM's methodology, except that the average government share of premium payments for annuitants is substituted for annuitant medical costs less annuitant premium payments.

Because the calculation of the PSRHBF liability involves several areas of judgment, estimates of the liability could vary significantly depending on the assumptions used. Utilizing the same underlying data that was used in preparing the estimate in the table above, the September 30, 2018, unfunded obligation could range from $51 billion to $85 billion, solely by varying the inflation rate by plus or minus 1%, and the September 30, 2017 unfunded obligation would range from $47 billion to $81 billion. If the actuarial liability had been calculated using the Board of Actuaries long-term rate assumption of 4.25%, the liability would have been approximately $104 billion, or 9% lower, as of September 30, 2018, and approximately $100 billion, or 11% lower, as of September 30, 2017.

For our current annuitants, the government share of premium payments is adjusted to reflect the pro rata share of civilian service to total service for which we are responsible. The pro rata adjustment is made by applying calculated factors based upon actual payments that vary by the age and Medicare status of enrollees. For our active employees, the pro-rata share in retirement is assumed to be 95% of the total.

PSRHBF assets are comprised entirely of long-term, special-issue U.S. Treasury securities with maturities of up to 15 years bearing interest rates from 1.38% to 5.00%. The following table details the fund balance, including both contribution and interest receivables, of the PSRHBF, as reported by OPM:

(in billions)		2018		2017
Beginning balance (including both contribution and interest receivables) at October 1	$	88.0	$	85.8
Amounts past due[1]		4.5		4.3
Contributions and transfers		—		—
Earnings at 2.8% and 2.8%, respectively		1.3		1.4
Payments for annuitant premiums[2]		(3.7)		(3.5)
Net increase	$	2.1	$	2.2
Fund balance (including both contribution and interest receivables) at September 30	**$**	**90.1**	**$**	**88.0**

[1] Amounts past due represent the combined amount of normal costs of retiree health benefits and unfunded liability amortization due on September 30 of the respective years. However, no such payments were made.

[2] Includes premium payments for certain annuitant/employees under workers' compensation coverage.

Although PAEA dictates the PSRHBF prefunding requirements, the amounts and the timing of required funding could change at any time with enactment of a new law or an amendment of existing law. The total amount of payments due to the PSRHBF through September 30, 2018, and 2017, was $42.6 billion and $38.2 billion, respectively. In order to preserve liquidity to ensure that we would be able to continue to fulfill our primary universal service mission, we did not make the annual payments due on September 30, 2018, and 2017 for the PSRHBF unfunded liability amortization of $815 million and $955 million, respectively, or the normal costs of retiree health benefits of $3.7 billion and $3.3 billion, respectively.

The following information, provided under the PAEA mandate, details OPM's preliminary 5-year estimates for payments into the PSRHBF for normal costs and unfunded liability expenses, and payments out of the PSRHBF for annuitant premiums:

(in billions)	Estimated payments into the PSRHBF				Estimated payments out of the PSRHBF
Year	**Normal costs**	**Amortization of unfunded liability**	**Payable to PSRHBF**	**Total**	**Annuitant premiums**
2019	$ 3.9	$ 1.0	$ 42.6	$ 47.5	$ 4.0
2020	4.0	1.0	—	5.0	4.2
2021	4.2	1.0	—	5.2	4.5
2022	4.4	1.0	—	5.4	4.8
2023	4.6	1.0	—	5.6	5.0

Workers' Compensation

Our employees who are injured on the job are covered by FECA, administered by the DOL's OWCP, which makes all decisions regarding injured workers' eligibility for benefits. We are legally mandated to participate in the federal workers' compensation program. Additionally, we reimburse the DOL for all workers' compensation benefits paid to or on behalf of our employees.

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.

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. The expense also includes an administrative fee paid to DOL.

In the day-to-day operation of our business, we focus on costs within our control and exclude items that we cannot control, including workers' compensation expenses caused by actuarial revaluation and discount rate changes. We subtract the cash payments made by DOL on behalf of workers' compensation obligations from total workers' compensation expense (benefit) in order to determine the non-cash component of workers' compensation expense (benefit), a non-GAAP financial measure.

The table below details the components of workers' compensation expense for the years ended September 30, 2018, 2017 and 2016, including a reconciliation to non-GAAP measures:

(in millions)	2018	2017	2016
Impact of discount rate changes	$ (1,066)	$ (1,362)	$ 1,026
Actuarial revaluation of existing cases	(205)	(1,138)	(113)
Costs of new cases	1,194	1,552	1,697
Administrative fee	81	151	72
Total workers' compensation expense (benefit)	**$ 4**	**$ (797)**	**$ 2,682**
(Less) cash payments made by DOL on behalf of workers' compensation obligations	(1,393)	(1,415)	(1,468)
Total non-cash component of workers' compensation (benefit) expense (non-GAAP)	**$ (1,389)**	**$ (2,212)**	**$ 1,214**

For the year ended September 30, 2018, workers' compensation expense was $4 million, compared to a benefit of $797 million for the prior year, a net increase in expenses of $801 million. Payments made by DOL on behalf of workers' compensation obligations and the associated administrative fee were approximately $1.4 billion for each of the years ended September 30, 2018, and 2017. For additional information, see *Item 8. Financial Statements and Supplementary Data, Notes to Financial Statements*, *Note 13 - Workers' Compensation*

Impact of Discount Rate Changes

For the year ended September 30, 2018, the portion of workers' compensation expense attributable to the impact of discount rate changes resulted in a lower benefit of $296 million, compared to 2017. This lower benefit was driven by a less significant increase in discount rates in 2018 compared to 2017, an event outside of management's control.

For the year ended September 30, 2017, the portion of workers' compensation expense attributable to the impact of discount rate changes decreased $2.4 billion compared to 2016. These changes were the result of increasing discount rates, also outside of management's control.

Actuarial Revaluation of Existing Cases and Costs of New Cases

Changes in actuarial valuation are primarily attributable to the combined impacts of routine changes in actuarial estimation, the progression of existing cases and updated COLA assumptions, which are largely outside of management's control.

For the year ended September 30, 2018, the cost of new workers' compensation cases decreased $358 million, compared to 2017, due largely to management's continued efforts to emphasize workplace safety. For the year ended September 30, 2018, the actuarial revaluation of existing cases increased by $933 million, compared to 2017. This is primarily due to the 2017 decrease in medical costs associated with pharmaceutical compounding, which was not repeated on the same scale during 2018.

For the year ended September 30, 2017, the combined costs of new workers' compensation cases and actuarial revaluation of existing cases decreased approximately $1.2 billion, compared to 2016. These cost savings were largely the result of DOL's change in rules for pharmaceutical compounding.

In July 2016, DOL implemented a new pharmaceutical compounding policy and in October 2016, DOL implemented a "Letter of Medical Necessity" requirement for compound pharmaceuticals. Largely due to these changes in rules for pharmaceutical compounding, we recorded a $549 million benefit for the year ended September 30, 2017, and have reduced the cash outlays for compound pharmaceuticals by 97% since the new rules took effect in October 2016. No such benefit was recorded for the year ended September 30, 2018.

Transportation

Transportation expense includes 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 expense does not include the compensation of employees responsible for transporting mail and other products between our facilities.

Variations in the volume and weight of transported mail and packages and the mode of transportation utilized has had a significant impact on our transportation expenses. The table below details the components of transportation expense for the years ended September 30, 2018, 2017 and 2016:

(in millions)	2018	2017	2016
Highway	$ 4,319	$ 4,070	$ 3,827
Air	2,892	2,481	2,469
International	611	631	642
Other	39	56	54
Total transportation expense	**$ 7,861**	**$ 7,238**	**$ 6,992**

Overall, transportation expense increased $623 million, or 8.6%, during the year ended September 30, 2018, compared to the prior year.

Highway transportation expenses increased $249 million, or 6.1%, during the year ended September 30, 2018, compared to the prior year, primarily due to higher unit costs per mile due to supplier cost pressures resulting in part from a national shortage of long-haul truck drivers, and higher diesel fuel prices.

Air transportation expenses increased $411 million, or 16.6%, during the year ended September 30, 2018, compared to the prior year, primarily due to increased package volume, higher jet fuel prices and increased expenditures on charters.

International transportation expenses, which represent expenses related only to outbound services that allow customers in the U.S. to send mail and packages to other countries, decreased slightly, primarily due to a decline in *Priority Mail International* and other international service volumes.

During the year ended September 30, 2017, overall transportation expense increased $246 million, or 3.5%, compared to the prior year. Highway transportation expenses increased $243 million, or 6.3%, during the year ended September 30, 2017, compared to the prior year, due largely to the higher price per mile we paid on contract routes, and to a lesser extent, higher diesel fuel prices for the year. Air transportation expenses increased $12 million, or 0.5%, during the year ended September 30, 2017, compared to the prior year, due to a modest increase in average jet fuel prices for the year, offset slightly by lower air network volume and increased use of lower cost carriers. International transportation expenses, which represent expenses related only to outbound services, decreased slightly, primarily due to a decline in *Priority Mail International* and other international service volumes.

Other Operating Expenses

The following table details other operating expenses for the periods ended September 30, 2018, 2017 and 2016:

(in millions)		2018		2017		2016
Supplies and services	$	2,991	$	2,980	$	2,755
Depreciation and amortization		1,669		1,677		1,740
Rent and utilities		1,694		1,590		1,560
Vehicle maintenance service		629		640		624
Delivery vehicle fuel		502		409		359
Information technology and communications		913		914		852
Rural carrier equipment maintenance		552		503		484
Miscellaneous other		747		1,030		1,057
Total other operating expenses	**$**	**9,697**	**$**	**9,743**	**$**	**9,431**

Other operating expenses decreased 0.5% in 2018 compared to 2017. The decrease was largely the result of a decrease in miscellaneous other expenses. This decrease was partially offset by increases in delivery vehicle fuel, rural carrier equipment maintenance, and rent and utilities.

The miscellaneous other component decreased approximately 27% due to a reduction in expenses associated with contingent liabilities pertaining to labor and employment matters.

The delivery vehicle fuel component increased approximately 23% primarily due to increases in average diesel fuel prices and the number of delivery points. The rural carrier equipment maintenance component increased approximately 10% primarily due to an increase in rates allocated to rural carriers for vehicles and higher usage due to the increasing number of delivery points and increasing fuel prices. The rent and utilities component increased approximately 7% primarily due to increased fuel-related utility costs associated with our buildings and facilities.

Other operating expenses increased 3.3% in 2017 compared to 2016, driven by increases in supplies and services, delivery vehicle fuel and information technology and communications components. The supplies and services component increased approximately 8% primarily due to an increase in information security services. The delivery vehicle fuel component increased approximately 14% primarily due to increases in average diesel fuel prices. The information technology and communications component increased approximately 7% primarily due to increased commercial software license and maintenance fees.

NON-OPERATING REVENUES AND EXPENSES

Interest and Investment Income

We generate income from investments in securities issued by the U.S. Treasury. Investment income was $102 million, $37 million and $10 million for the years ended September 30, 2018, 2017 and 2016, respectively. Interest income increased during 2018 due to higher short-term interest rates.

In addition to the income we generate from investments, we record imputed interest on the future installment payments that are owed to us under the *Revenue Forgone Reform Act of 1993* (the "RFA"). Under the RFA, Congress agreed to reimburse us $1.2 billion in 42 annual installments of $29 million each through 2035 for services we performed in prior years. Imputed interest for the future revenue forgone installments was $20 million, $21 million and $22 million for the years ended September 30, 2018, 2017 and 2016, respectively. See *Item 8. Financial Statements and Supplementary Data*, *Notes to Financial Statements*, *Note 14 - Revenue Forgone* for additional information.

Interest Expense

Interest expense was $251 million, $226 million and $222 million, for the years ended September 30, 2018, 2017 and 2016, respectively. Interest expense increased during 2018 due to higher short-term interest rates. Although long-term debt generally carries higher interest rates than short-term debt, financing a portion of our debt at longer-term fixed rates decreases our interest rate risk and interest expense volatility in subsequent years.

LIQUIDITY AND CAPITAL RESOURCES

We held unrestricted cash and cash equivalents of $10.1 billion and $10.5 billion as of September 30, 2018, and September 30, 2017, respectively. Our average daily liquidity balance during the year ended September 30, 2018, was $11.3 billion, which represents approximately 54 days of liquidity available, which we define as unrestricted cash plus available borrowing capacity, divided by estimated average cash disbursements (including capital expenditures) per calendar day (365 days per year). This measurement represents a change in methodology from previous periods when we calculated our average daily liquidity balance by dividing estimated average cash disbursements (including capital expenditures) per business day (usually 251 cash disbursement days per year). See *Item 8. Financial Statements and Supplementary Data*, *Notes to Financial Statements*, *Note 3 - Liquidity* for additional information.

CASH FLOW ANALYSIS

Our year-end cash balances have increased by approximately $8 billion from the reported low in 2012. This improvement would not have occurred had the Postal Service not defaulted on the annual statutorily set PSRHBF prefunding payments from 2012 through 2016, and not paid the RHB normal cost, and RHB, CSRS and FERS amortization payments in 2017 and 2018. Aside from the defaults and non-payments, the improvement is largely attributable to the temporary exigent surcharge (discussed below) which generated approximately $4.6 billion in incremental revenue from January 2014 through April 10, 2016.

We must maintain adequate liquidity to support our annual operating expenses of approximately $74 billion, to make capital investments necessary for continuity of operations and to prepare for unexpected contingencies. In addition to not making $33.9 billion of PSRHBF statutorily set prefunding payments, we did not make the $6.9 billion and $6.9 billion in payments due September 30, 2018, and 2017, respectively, 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.

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 retirement 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 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 $15 billion debt ceiling, we do not have sufficient cash balances to meet all of our existing legal obligations, pay down our debt 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 nearly $1.1 billion, or 27.6%, for the year ended September 30, 2018, compared to the previous year. This decrease was largely the result of increases in cash expenses, primarily compensation, transportation and other expenses, exceeding increased revenue for the year.

Cash provided by operating activities increased by nearly $1.1 billion, or 39.7%, for the year ended September 30, 2017, compared to the previous year. This increase occurred primarily because we did not pay certain obligations which totaled over $6.9 billion due to OPM as of September 30, 2017, as discussed below.

In 2018, our cash balances were not sufficient to pay the normal cost of retirement health benefits of $3.7 billion, and the PSRHBF, CSRS and FERS unfunded liability amortization expenses of $815 million, $1.4 billion and $958 million, respectively, while also preserving adequate liquidity to ensure that our ability to fulfill our primary universal service mission was not placed at undue risk. In 2017, our cash balances were not sufficient to pay the normal cost of retirement health benefits of $3.3 billion, and the PSRHBF, CSRS and FERS unfunded liability amortization expenses of $955 million, $1.7 billion and $917 million, respectively, while also preserving adequate liquidity to ensure that our ability to fulfill our primary universal service mission was not placed at undue risk.

In prior years, our cash balances were not sufficient to pay the legally-mandated PSRHBF prefunding payments, including $5.8 billion that was due by September 30, 2016. Although our cash balances were higher than the respective amounts due each year, making these payments would have made it impossible to maintain a prudent level of liquidity and to adequately fund our normal operations and necessary capital investments necessary to fulfill our fundamental service mandate.

As of September 30, 2018, past due amounts payable to the PSRHBF totaled $42.6 billion, past due amounts payable to OPM for CSRS totaled nearly $3.2 billion and past due amounts payable to OPM for FERS totaled $2.4 billion. We have incurred no penalties or negative financial consequences resulting from our inability to make these payments.

Exigent Surcharge
As described in *Operating Revenue and Volume*, we collected an exigent surcharge on most Market-Dominant services beginning in January 2014 until it produced incremental revenue of just over $4.6 billion, a figure the PRC determined was lost due to the Great Recession's suppression of mail volume. This limit was reached on April 10, 2016, and we therefore reduced the prices of applicable Market-Dominant services on that date.

Price Increases
The following table reflects our recent price increases along with the service category, date the notice was filed with the PRC, effective date of the increase, increase percentage, and the estimated annual revenue expected to be generated by the respective increase.

Service Category	Date Notice Filed with PRC	Effective Date of Increase	Average Increase %	Estimated Annual Revenue *($ in millions)*
Competitive	October 16, 2015	January 17, 2016	9.5%	$ 1,000
Market-Dominant	October 12, 2016	January 22, 2017	0.9%	360
Competitive	October 19, 2016	January 22, 2017	3.9%	507
Competitive*	July 26, 2017	September 3, 2017	9.9%	—
Market-Dominant	October 6, 2017	January 21, 2018	1.9%	655
Competitive	October 6, 2017	January 21, 2018	4.1%	356

* Represents a transfer of *First-Class Package Service - Retail* (formerly *First-Class Mail Parcels*) from a Market-Dominant service to a Competitive service, along with an average price increase of 9.9% on that service. The estimated impact to annual revenue is immaterial as the annual volume for this service is low.

On October 10, 2018, we filed a notice with the PRC of our intent to increase prices for Market-Dominant services by an average of 2.5%. On November 13, 2018, the PRC approved this plan and the increase is scheduled to go into effect on January 27, 2019. We estimate it will generate approximately $891 million in annualized revenue.

On October 10, 2018, we filed a notice with the PRC of our intent to increase prices for certain Competitive services by an average of 7.4%. On November 13, 2018, the PRC approved this plan and the increase is scheduled to go into effect on January 27, 2019. We estimate this price increase will generate approximately $870 million in annualized revenue.

Investing Activities
In 2018, we invested $1.4 billion in the purchase of property and equipment, which represents an increase of $65 million over 2017. In 2017, we invested $1.3 billion in the purchase of property and equipment, which represented a decrease of $84 million from 2016.

Our capital expenditures have declined from an annual average of approximately $1.5 billion in years 2009 through 2011 to an annual average of approximately $1.4 billion in years 2015 through 2018, a reduction of approximately 8%. However, we will need to increase our capital expenditures in order to address our aging facilities and delivery fleet and to upgrade our equipment to remain competitive in the marketplace and to ensure that we will be able to continue to meet our statutory obligation to provide prompt, efficient and reliable postal services to the nation. The source of funds needed to fulfill these commitments has been generated from our operating activities and defaults or non-payment on certain retirement and retiree healthcare obligations.

We assign priority to proposed capital investments based on the following factors:

1. Needed for safety and/or health or legal requirements;
2. Required to provide service to our customers; and
3. Initiatives with a high return on investment and a short payback period.

Our delivery fleet includes approximately 145,000 vehicles that are at least 20 years old and need significant maintenance to continue in service. As a result, repair and maintenance costs, including applicable labor costs, have risen significantly in recent years. We purchased approximately 8,000 new vehicles to add to our fleet during the year ended September 30, 2018. Additionally, we continue to invest in upgrades of letter sorting equipment that is at or near the end of its useful life, while also investing in equipment to fully capitalize on business opportunities in the growing package delivery market. To conserve cash, we have deferred facilities maintenance in instances where this could be done without adversely impacting employee and customer health or safety.

Financing Activities

As an "independent establishment of the Executive Branch of the Government of the United States," we receive no tax dollars for ongoing operations and have not received an appropriation for operational costs since 1982. We fund our operations chiefly through cash generated from operations and by borrowing from the FFB. See *Item 8. Financial Statements and Supplementary Data*, *Notes to Financial Statements*, *Note 9 - Debt* for additional information.

In 1999, we entered into the NPA with the FFB 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.

The maximum borrowing amount allowed under our statutory debt ceiling is $15.0 billion, which we first reached in September 2012, and have generally maintained 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. Our current plan is to reduce our debt level by an additional $2.2 billion as existing notes come due in February and May 2019.

As of September 30, 2018, the aggregate principal balance of our outstanding debt was $13.2 billion. Of this amount, the current portion of our debt was $11.0 billion, and the noncurrent portion was $2.2 billion.

Within our current portion of debt, the two revolving credit facilities have interest rates determined by the U.S. Department of Treasury each business day and enable us to draw up to $4.0 billion in total. As of September 30, 2018, and September 30, 2017, these facilities were fully drawn and are included in the current portion of debt in the accompanying *Balance Sheets*. The facilities currently have maturity dates in April 2019.

Net cash used in financing activities, for the periods ended September 30, 2018, 2017 and 2016 were approximately $1.9 billion, $63 million and $51 million, respectively, consisting primarily of cash payments on capital lease obligations, along with the $1.8 billion reduction in our debt in September 2018.

On September 28, 2018, under the most recent amendment to the NPA, the FFB extended the NPA until December 31, 2018, (one quarter) as opposed to its prior practice of annually extending the NPA for a full fiscal year. This change did not affect the terms of any of our outstanding debt as of September 30, 2018.

If we are unable to extend the NPA beyond December 31, 2018, 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 includes the following terms:
    a. Allowing us to adopt Postal Service-specific economic and demographic assumptions for calculating pension liabilities,
    b. Establishing a set of healthcare plans within the FEHB that would fully integrate with Medicare for current and future retirees, which we believe would improve the affordability of our retiree health benefits system and eliminate most of the unfunded PSRHBF obligations, and
    c. Restoring half of the exigent surcharge (the 4.3% surcharge on Market-Dominant services that was effective from January 2014 to April 2016), as a permanent part of our rate base; 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

On December 1, 2017, the PRC announced its initial decision in connection with its ten-year review of the system for regulating rates and classes for Market-Dominant products as required by the PAEA. The purpose of the ten-year review was to determine if the system for regulating such rates and classes has achieved the objectives established by Congress 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 necessary 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. The Postal Service continues 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 set by the Postal Service to ensure that those prices are just and reasonable.

The PRC has been 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. 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

The following table provides details of estimated future cash obligations as of September 30, 2018:

(in millions)	Total	Past due and payable	Less than 1 year	1-3 years	3-5 years	After 5 years
Debt[1]	$ 13,200	$ —	$ 11,000	$ 1,000	$ —	$ 1,200
Interest on debt[1]	1,073	—	148	133	91	701
CSRS unfunded liability (off balance sheet)[2]	25,100	—	1,440	2,880	2,880	17,900
CSRS unfunded liability - past due[3]	3,181	3,181	—	—	—	—
FERS unfunded liability (off balance sheet)[4]	18,400	—	958	1,916	1,916	13,610
FERS unfunded liability - past due[5]	2,370	2,370	—	—	—	—
PSRHBF unfunded liability (off balance sheet)[6]	25,629	—	815	1,630	1,630	21,554
PSRHBF unfunded liability - past due[7]	1,770	1,770	—	—	—	—
PSRHBF fixed payment and normal cost defaults - past due[8]	40,871	40,871	—	—	—	—
Workers' compensation[9]	24,641	—	1,383	4,194	2,928	16,136
Capital lease obligations	207	—	59	74	27	47
Operating leases	3,524	—	815	1,326	750	633
Capital commitments[10]	1,360	—	1,044	316	—	—
Purchase obligations[10]	5,204	—	939	1,744	1,685	836
Employees' leave[11]	2,033	—	127	236	208	1,462
Total commitments	**$ 168,563**	**$ 48,192**	**$ 18,728**	**$ 15,449**	**$ 12,115**	**$ 74,079**

[1] For overnight and short-term debt, the table assumes the balance as of period end remains outstanding for all periods presented.

[2] Represents OPM's preliminary calculation of annual payments for amortization of the CSRS unfunded liability that we are obligated to pay through 2043.

[3] Represents cumulative amortization payments of the CSRS unfunded liability invoiced by OPM in 2017 and 2018, which the Postal Service defaulted on. OPM considers the defaulted amounts to be past due and payable, and the Postal Service continues to reflect these amounts as a current liability within *Unfunded retirement benefits* in the accompanying *Balance Sheets*.

[4] Represents OPM's preliminary calculation of annual payments for amortization of the FERS unfunded liability that we are obligated to pay through 2047.

[5] Represents cumulative amortization payments of the FERS unfunded liability invoiced by OPM in 2017 and 2018, which the Postal Service defaulted on. OPM considers the defaulted amounts to be past due and payable, and the Postal Service continues to reflect these amounts as a current liability within *Unfunded retirement benefits* in the accompanying *Balance Sheets*.

[6] Represents OPM's preliminary calculation of annual payments for amortization of the PSRHBF unfunded liability that we are obligated to pay through 2056.

[7] Represents cumulative amortization payments of the PSRHBF unfunded liability invoiced by OPM in 2017 and 2018, which the Postal Service defaulted on. OPM considers the defaulted amounts to be past due and payable, and the Postal Service continues to reflect these amounts as a current liability within *Retiree health benefits* in the accompanying *Balance Sheets*.

[8] Represents the cumulative annual prefunding payments to the PSRHBF between 2012 and 2016, and the normal cost payments invoiced in 2017 and 2018, all of which the Postal Service defaulted on. OPM considers the defaulted amounts to be due and payable, and the Postal Service continues to reflect these amounts as a current liability within *Retiree health benefits* in the accompanying *Balance Sheets*.

[9] Represents the undiscounted expected future workers' compensation payments plus $101 million in administrative fees, of which $81 million was due and paid October 15, 2018, and assumes no new cases in future years. The obligation to pay administrative fees in future years as determined by DOL is currently not estimated.

[10] Capital commitments pertain to purchases of equipment, building improvements and vehicles for legally binding obligations. Purchase obligations pertain to items (including highway and air transportation obligations) that are expensed when received or amortized over a short period of time. These are not reflected on the accompanying *Balance Sheets*.

[11] Employees' leave includes both annual and holiday leave.

As discussed above, our obligations pertaining to CSRS changed in 2017 and OPM now determines the amount of annual payments we will need to make to amortize the CSRS unfunded liabilities. We estimate this payment obligation, which was $1.4 billion in 2018, will continue at approximately that amount annually going forward to 2043. Additionally, our FERS obligation was $958 million in 2018, and we estimate approximately that amount will continue annually going forward to 2047.

Also in 2017, our retiree health benefit obligations changed according to law. The PSRHBF began funding our share of retiree health benefit premiums, and we were to begin paying into the PSRHBF the normal costs of retiree health benefits, which was $3.7 billion and payable on September 30, 2018. OPM estimates that the RHB normal cost will increase by approximately $200 million per year for the next five years. Additionally, OPM will determine the amount of annual payments we will need to make to amortize the PSRHBF unfunded liabilities, which was $815 million in 2018. Based on OPM's 5-year estimate for payments into the PSRHBF for amortization of unfunded liability expenses, we expect the annual obligation will continue at approximately that amount going forward.

We also estimate that our cash outlays for capital assets will amount to approximately $1.7 billion in 2019 and an additional $10.6 billion for the periods of 2020 through 2023. Although our future projections include these capital cash outlays, future cash flow from operations alone may not generate the cash needed for such necessary capital expenditures.

Contingency Plans

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 revenue of nearly $71 billion, generated almost entirely through the sale of postal services, 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 we support, and disruption of the mail would cause undue hardship to businesses and consumers.

In the event that circumstances leave us with insufficient cash, we would likely be required to implement additional contingency plans to ensure that mail deliveries continue. These measures may require us to prioritize payments to our employees and suppliers ahead of some payments to U.S. government entities, as has been done in the past. Without structural change to our business model and legislative change, the factors discussed above will continue to negatively impact us resulting in continuing losses and liquidity challenges for the foreseeable future.

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 Governors are appointed by the President with the advice and consent of the Senate.

Appropriations

On June 13, 2018, the House Appropriations Committee approved the *Financial Services and General Government Act, 2019* (H.R. 6258), which includes $58,118,000 in funding for free mail for the blind and overseas voting. Representative David Joyce (R-OH) introduced an amendment to restore our 2012 service standards for *First-Class Mail* and *Periodicals*, which was passed by a voice vote and included in the bill. The bill also 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 July 19, 2018, the House passed the appropriations bill, which had been combined with the *Department of the Interior, Environment, and Related Agencies Appropriations Act, 2019* (H.R. 6147).

On June 21, 2018, the Senate Appropriations Committee approved the *Financial Services and General Government Appropriations Act, 2019* (S. 3107), which includes $55,235,000 in funding for free mail for the blind and overseas voting. The six-day delivery frequency provision remains in the bill. No amendments regarding a service standard rollback for *First-Class Mail* and *Periodicals* were offered. On August 1, 2018, the Senate passed the four-bill spending package (H.R. 6147) that included the Financial Services bill, and later, in conference with the House, removed the service standard amendment that was included in that chamber's bill.

On September 28, 2018, the President signed into law H.R. 6157 (P.L. 115-245), the *Continuing Appropriations Act, 2019*, providing 2019 funding for the departments of Defense, Labor, Health and Human Services (HHS), and

Education. The bill contained language that would fund any part of the government not covered by already-passed appropriations bills through December 7, 2018, including agencies covered by the *Financial Services and General Government Appropriations Act, 2019*. The House and Senate will continue negotiations on H.R. 6157 after the midterm elections.

Postal Service Reform

As previously reported, on March 16, 2017, the House Oversight and Government Reform Committee passed the *Postal Service Reform Act of 2017* (H.R. 756 - 115th Congress) with a single dissenting vote. The core provisions of the bipartisan measure would institute separate, Postal Service-only plans within FEHB that are fully integrated with Medicare, require Postal Service-specific demographic and economic assumptions in calculating pension liabilities, reinstate half of the exigent surcharge and authorize the provision of non-postal services to state, local and tribal governments. The measure would also reduce the number of Governors from nine to five, clarify their duties and allow them to set their own quorum requirements.

On June 12, 2018, the Postal Service reform bill was reintroduced as the *Postal Reform Act of 2018* (H.R. 6076), with Subcommittee on Government Operations Chairman Mark Meadows (R-NC) as the lead sponsor. The reintroduced bill is identical to the previous bill and was referred to the House Oversight and Government Reform, Energy and Commerce, and Ways and Means Committees.

On March 22, 2018, Senator Thomas Carper (D-Del) introduced the *Postal Service Reform Act of 2018* (S. 2629 - 115th Congress). The bipartisan measure would institute separate, Postal Service-only plans within FEHB that are integrated with Medicare. It would also establish a lump-sum payment from the PSRHBF to Medicare funds, in an amount equal to the ten-year increase in Medicare expenditures due to the bill's Medicare integration provisions. The lump-sum requirement would begin the first fiscal year beginning with 2021 in which the PSRHBF has assets above the 80% funding level provided for by the bill. Additionally, the measure would reinstate half of the temporary exigent surcharge as a rate increase, establish a moratorium of at least two years on service standard changes, and modify or defer rate-regulation reforms concerning products that do not fully cover costs like *Periodicals* and *Marketing Mail Flats*. The bill includes governance reforms that would reduce the number of Governors from nine to five, clarify their duties and allow them to set their own quorum requirements. The measure would also authorize us to ship beer, wine and distilled spirits and to work with state and local governments in offering government services. S. 2629 has been placed on the Senate Legislative Calendar and awaits Senate floor action.

STOP Act

On October 24, 2018, the President signed into law H.R. 6 (P.L. 115-271), the *SUPPORT for Patients and Communities Act*, a package of bills designed to address the opioid epidemic. The bill includes the *STOP Act,* which requires us to arrange to transmit advance electronic data ("AED") to the U.S. Customs and Border Protection on at least 70% of aggregate inbound International Mail shipments, including 100% of shipments from the People’s Republic of China, by December 31, 2018, and 100% of aggregate inbound mail shipments by December 31, 2020. We could be subject to civil penalties if we accept inbound International Mail shipments without AED starting January 1, 2021. Additionally, under the *STOP Act*, a new $1 customs fee will be required on each international U.S.-bound Express Mail Service item, effective January 1, 2020. The amount of that $1 fee may be adjusted once a year starting on October 1, 2020.

Board of Governors Nominations

On August 28, 2018, the Senate confirmed the nominations of Robert M. Duncan and David C. Williams as Governors for terms expiring December 8, 2018, and December 8, 2019, respectively. The President originally nominated Mr. Duncan for an additional term expiring December 8, 2025, and this nomination awaits action by the full Senate.

Also on August 30, 2018, the President nominated the following two individuals to serve as Governors:

- Ron A. Bloom, for the remainder of a seven-year term expiring December 8, 2020; and
- Roman Martinez IV, for the remainder of a seven-year term expiring December 8, 2024.

These nominees join Calvin R. Tucker, whom the President previously nominated to serve as Governor for the remainder of a term expiring December 8, 2023, for consideration by the Senate Homeland Security and Governmental Affairs Committee.

TASK FORCE ON THE UNITED STATES POSTAL SERVICE

On April 12, 2018, the President issued Executive Order 13829 to establish a *Task Force on the United States Postal Service* ("Task Force"), to be chaired by the Secretary of the Treasury, as Secretary and as Chairman of the FFB, or his designee. In addition to the Task Force Chair, the Task Force is composed of the Director of the Office of Management and Budget and the Director of OPM, or their designees. The Task Force shall conduct a thorough evaluation of our operations and finances of the Postal Service, including:

- The expansion and pricing of the package delivery market and the Postal Service's role in competitive markets;
- The decline in mail volume and its implications for Postal Service self-financing and the Postal Service monopoly over letter delivery and mailboxes;
- The definition of the "universal service obligation" in light of changes in technology, e-commerce, marketing practices, and customer needs;
- The Postal Service's role in the U.S. economy and in rural areas, communities, and small towns; and
- The state of the Postal Service business model, workforce, operations, costs, and pricing.

In accordance with the Executive Order, the Task Force submitted its report to the President in August 2018. The release of the report is within the discretion of the Administration, and we do not know when it is going to be released. Furthermore, we have not been briefed on the report's findings and recommendations.

FAIR VALUE MEASUREMENTS

We did not have any recognized gains as a result of fair valuation measurements in the years ended September 30, 2018, 2017 and 2016. All recognized losses have been incorporated into our financial statements and the unrecognized gains and losses are not considered to have a significant impact upon our operations. See *Item 8. Financial Statements and Supplementary Data*, *Notes to Financial Statements*, *Note 15 - Fair Value Measurement* for additional information.

RELATED PARTY TRANSACTIONS

We have significant transactions with other U.S. government entities, which are considered related parties for reporting purposes. See *Item 8. Financial Statements and Supplementary Data*, *Notes to Financial Statements*, *Note 4 - 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. Management discusses the development and selection of these accounting policies and estimates with the Audit and Finance Committee of the Board. However, even under optimal circumstances, estimates routinely require adjustment based on changing circumstances and new or better information.

The three accounting policies that are considered either the most judgmental, or involve the selection or application of alternative accounting policies, and are material to the financial statements, are those related to the recording of workers' compensation costs, deferred revenue-prepaid postage and contingent liabilities. For further information, see *Item 8. Financial Statements and Supplementary Data*, *Notes to Financial Statements*, *Note 1 - Organization and Summary of Significant Accounting Policies*, *Note 13 - Workers' Compensation* and *Note 10 - Commitments and Contingencies*.

WORKERS' COMPENSATION

Workers' compensation costs reflected in our accompanying *Statements of Operations* are subject to actuarial estimates of future claim payments based upon past claim payment experience. Workers' compensation costs are highly sensitive to discount and inflation rates, which we update on a quarterly basis, and the length of time recipients are expected to stay on the compensation rolls. However, the annual cash payment for claims is relatively stable and predictable.

The discount rate reflects the current rate at which the workers' compensation liabilities could be effectively settled at the measurement date (e.g., the end of the accounting period). In setting the discount rates, we use the current yield, as of the measurement date, on U.S. Treasury securities that are matched to the expected duration of both the medical and compensation payments. Expected inflation in compensation claim obligations are estimated using the consensus inflation forecast from the Federal Reserve Bank of Philadelphia Survey of Professional Forecasters. For medical claims, we use the average rate of medical cost increases experienced by our workers' compensation claimants over the past five years as an estimate for future medical inflation. Workers' compensation liabilities are recorded in the accompanying *Balance Sheets* as *Workers' compensation costs* with both current and noncurrent components.

DEFERRED REVENUE-PREPAID POSTAGE

Deferred revenue-prepaid postage is an estimate of postage that has been sold, but not yet used by customers. Revenue is recognized only when mail is delivered, not when postage is purchased, and revenue is deferred and reflected in the accompanying *Balance Sheets* as *Deferred revenue-prepaid postage.* The deferred revenue estimate is developed and validated through complex mathematical and statistical methods of stamp usage trends. Small differences in inputs can lead to significant differences in the estimate of the liability. Three categories of postage sales account for the majority of *Deferred revenue-prepaid postage*: *Forever stamp* sales, metered postage and mail-in-transit, which is mail that has not reached its final destination.

During 2016, we revised the estimation technique utilized to estimate our *Deferred revenue-prepaid postage* liability for *Forever Stamps*. The change resulted from new information regarding customer's retention and usage habits of applicable postage, and enabled the Postal Service to update its estimate of stamps that will never be used for mailing. As a result of this change, *Deferred revenue-prepaid postage* was decreased by nearly $1.1 billion. In accordance with GAAP, the change was accounted for as a change in accounting estimate, and was reflected in operating results as an increase to revenue and a decrease to net loss by the same amount in the year ended September 30, 2016.

CONTINGENT LIABILITIES

The recording of contingent liabilities requires significant judgment in estimating potential losses for legal and other claims. Each quarter, we evaluate significant new claims and litigation for the probability of an adverse outcome. We record liabilities deemed both probable and estimable in the accompanying *Balance Sheets* within *Trade payables and accrued expenses* and *Other noncurrent liabilities*.

In addition, we review any prior claims and litigation and, when necessary, we adjust the liability balances for resolutions or revisions to prior estimates. Estimates of loss can therefore change as individual claims develop and additional information becomes available. We disclose the range of amounts for pending claims and litigations that are deemed to be reasonably possible of an unfavorable outcome, but do not accrue for or include such provisions in our financial statements.

RECENT ACCOUNTING STANDARDS

New accounting guidance that we have recently adopted, as well as accounting guidance that has been recently issued but that we have not yet adopted, are included in *Item 8. Financial Statements and Supplementary Data*, *Notes to Financial Statements*, *Note 2 - Recent Accounting Pronouncements*.

ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

The market rate risks we encounter are primarily related to foreign currency exchange rate fluctuations, interest rates and commodity prices. Historically, we have not entered into derivatives contracts or commodity instruments for trading or speculative purposes or to manage market risks.

FOREIGN EXCHANGE RISK

While we operate outside of the U.S., and foreign currency fluctuations may favorably or unfavorably impact our reported earnings, we believe that foreign exchange risk is immaterial since the vast majority of our business transactions are denominated in U.S. dollars. Because of this, we estimate that a 1% increase or decrease in foreign exchange rates would not have a material impact on our financial statements.

INTEREST RATE RISK

We are impacted by changes in interest rates in the normal course of our business operations as a result of our ongoing investing and financing activities, which include our revolving credit line facilities and floating note purchase agreements as well as our cash and cash equivalents. We assess our interest rate risks on a regular basis and currently estimate that a 1% increase in interest rates would have resulted in approximately a $42 million increase in 2018 interest expense.

We currently have no significant exposure to changing interest rates on our noncurrent debt as interest rates are fixed on such debt. As disclosed in *Item 8. Financial Statements and Supplementary Data*, *Notes to Financial Statements*, *Note 15 - Fair Value Measurement*, the fair value of our noncurrent debt, exclusive of capital leases, was $2.3 billion and $5.2 billion for the years ended September 30, 2018, and 2017, respectively. We estimated the underlying fair value of our noncurrent debt using prices and discount rates provided by the FFB.

We also have interest rate risk associated with our workers' compensation liability, which is highly sensitive to changes in discount rates. An increase of 1% in the interest rates would decrease the liability at September 30, 2018, and related 2018 expense by approximately $1.6 billion. A decrease of 1% would increase the liability at September 30, 2018, and related 2018 expense by approximately $2.0 billion. See *Item 8. Financial Statements and Supplementary Data*, *Notes to Financial Statements*, *Note 13 - Workers' Compensation* for further explanation.

COMMODITY PRICES RISK

We currently have market risk for changes in fuel and natural gas costs. As of September 30, 2018, we estimated that a 1% increase in fuel and natural gas would have resulted in a $25 million increase in 2018 expense.

ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Temporary Emergency Committee of the Board of Governors of the United States Postal Service

Opinion on the Financial Statements

We have audited the accompanying balance sheets of the United States Postal Service as of September 30, 2018 and 2017, the related statements of operations, changes in net deficiency, and cash flows for each of the three years in the period ended September 30, 2018, and the related notes (collectively referred to as the "financial statements"). In our opinion, the financial statements present fairly, in all material respects, the financial position of the United States Postal Service at September 30, 2018 and 2017, and the results of its operations and its cash flows for each of the three years in the period ended September 30, 2018, in conformity with U.S. generally accepted accounting principles.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States) (PCAOB) and in accordance with auditing standards generally accepted in the United States of America, the United States Postal Service's internal control over financial reporting as of September 30, 2018, based on criteria established in Internal Control-Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (2013 framework) and our report dated November 14, 2018 expressed an unqualified opinion thereon.

Basis for Opinion

These financial statements are the responsibility of the United States Postal Service's management. Our responsibility is to express an opinion on these financial statements based on our audits. We are a public accounting firm registered with the PCAOB and are required to be independent with respect to the United States Postal Service in accordance with U.S. federal securities laws and the applicable rules and regulations of the Securities and Exchange Commission and the PCAOB.

We conducted our audits in accordance with the standards of the PCAOB, the auditing standards generally accepted in the United States of America, and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement, whether due to error or fraud. Our audits included performing procedures to assess the risks of material misstatement of the financial statements, whether due to error or fraud, and performing procedures that respond to those risks. Such procedures included examining, on a test basis, evidence regarding the amounts and disclosures in the financial statements. Our audits also included evaluating the accounting principles used and significant estimates made by management, as well as evaluating the overall presentation of the financial statements. We believe that our audits provide a reasonable basis for our opinion.

Emphasis of a Matter

As discussed more fully in Note 3 to the financial statements, the United States Postal Service, an independent establishment of the executive branch of the Government of the United States, is dependent upon future actions of the Government to continue its operations in the ordinary course as a result of continuing operating losses and statutory funding requirements for employee benefit obligations. The Postal Service has incurred recurring losses from its operations primarily due to sustained declines in mail volume, and statutory and regulatory restrictions have constrained the ability of the Postal Service to implement strategies to improve efficiency, reduce costs and increase revenues. Due to these conditions, the Postal Service remains in default of the $33.9 billion of required prefunding payments, which were due in previous years, that was to be paid to the Postal Service Retiree Health Benefits Fund (PSRHBF) by Public Law (P.L.) 109-435, per the Postal Accountability and Enhancement Act. The Postal Service also did not make payments due by September 30, 2018 and 2017, totaling $6.9 billion and $6.9 billion, respectively, for the normal cost of retiree health benefits and amortization payments for PSRHBF, the Civil Service Retirement System and the Federal Employee Retirement System unfunded liabilities. The Postal Service does not expect to have sufficient cash to satisfy these obligations. The Postal Service does not, at this time, anticipate any legal consequences, under current law, from its inability to make the required payments. In addition, the Note Purchase Agreement (NPA) with the Federal Financing Bank is due to expire on December 31, 2018, which creates additional uncertainty regarding the Postal Service's ability to obtain financing and maintain adequate liquidity throughout the fiscal year ending September 30, 2019. At this time, 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. Management expects, but no assurances can be given, that additional legislation will be enacted to address the liquidity constraints of the United States Postal Service and to address regulatory restrictions that have not allowed the Postal Service to adjust its operations to levels commensurate with its current revenue base.

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated November 14, 2018 on our consideration of the United States Postal Service's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, and contracts and other matters. The purpose of that report is solely to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the United States Postal Service's internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the United States Postal Service's internal control over financial reporting and compliance.

/s/ Ernst & Young LLP

We have served as the United States Postal Service's auditor since 1972.

Tysons, Virginia
November 14, 2018

UNITED STATES POSTAL SERVICE
STATEMENTS OF OPERATIONS

(in millions)	Year Ended September 30, 2018	2017	2016
Revenue			
Operating revenue	$ 70,622	$ 69,593	$ 71,429
Other revenue	38	43	69
Total revenue	**70,660**	**69,636**	**71,498**
Operating expenses			
Compensation and benefits	50,004	49,108	48,441
Unfunded retirement benefits amortization	2,398	2,658	248
Retiree health benefits	4,481	4,260	9,105
Workers' compensation	4	(797)	2,682
Transportation	7,861	7,238	6,992
Other operating expenses	9,697	9,743	9,431
Total operating expenses	**74,445**	**72,210**	**76,899**
Loss from operations	**(3,785)**	**(2,574)**	**(5,401)**
Interest and investment income	123	58	32
Interest expense	(251)	(226)	(222)
Net loss	**$ (3,913)**	**$ (2,742)**	**$ (5,591)**

See accompanying notes to the financial statements.

UNITED STATES POSTAL SERVICE
BALANCE SHEETS

(in millions)	September 30, 2018	September 30, 2017
Current Assets:		
Cash and cash equivalents	$ 10,061	$ 10,513
Restricted cash	275	291
Receivables, net	1,094	1,127
Supplies, advances and prepayments	153	134
Total current assets	**11,583**	**12,065**
Property and equipment, net	14,616	14,891
Other assets	489	438
Total assets	**$ 26,688**	**$ 27,394**
Current Liabilities:		
Compensation and benefits	$ 2,234	$ 2,397
Unfunded retirement benefits	5,551	3,153
Retiree health benefits	42,641	38,160
Workers' compensation costs	1,383	1,513
Payables and accrued expenses	2,217	1,930
Deferred revenue-prepaid postage	2,066	2,168
Customer deposit accounts	1,198	1,196
Other current liabilities	1,180	1,210
Current portion of debt	11,000	10,100
Total current liabilities	**69,470**	**61,827**
Workers' compensation costs, noncurrent	15,026	16,397
Employees' accumulated leave, noncurrent	1,906	1,918
Other noncurrent liabilities	723	1,076
Noncurrent portion of debt	2,200	4,900
Total liabilities	**89,325**	**86,118**
Net Deficiency:		
Capital contributions of the U.S. government	3,132	3,132
Deficit since 1971 reorganization	(65,769)	(61,856)
Total net deficiency	**(62,637)**	**(58,724)**
Total liabilities and net deficiency	**$ 26,688**	**$ 27,394**

See accompanying notes to the financial statements.

UNITED STATES POSTAL SERVICE
STATEMENTS OF CHANGES IN NET DEFICIENCY

(in millions)	Capital Contributions of U.S. Government	Accumulated Deficit Since Reorganization	Total Net Deficiency
Balance, September 30, 2015	**$ 3,132**	**$ (53,523)**	**$ (50,391)**
Net loss	—	(5,591)	(5,591)
Balance, September 30, 2016	**$ 3,132**	**$ (59,114)**	**$ (55,982)**
Net loss	—	(2,742)	(2,742)
Balance, September 30, 2017	**$ 3,132**	**$ (61,856)**	**$ (58,724)**
Net loss	—	(3,913)	(3,913)
Balance, September 30, 2018	**$ 3,132**	**$ (65,769)**	**$ (62,637)**

See accompanying notes to the financial statements.

UNITED STATES POSTAL SERVICE
STATEMENTS OF CASH FLOWS

(in millions)	Years Ended September 30, 2018	2017	2016
Cash flows from operating activities:			
Net loss	$ (3,913)	$ (2,742)	$ (5,591)
Adjustments to reconcile net loss to cash provided by operations:			
Depreciation and amortization	1,669	1,677	1,740
Gain on disposals of property and equipment, net	(31)	(7)	(11)
(Increase) decrease in other assets	(51)	(27)	2
(Decrease) increase in noncurrent workers' compensation	(1,371)	(2,215)	1,202
Decrease in noncurrent deferred appropriations and other revenue	(4)	(94)	(40)
(Decrease) increase in other noncurrent liabilities	(322)	61	(122)
Changes in current assets and liabilities:			
Receivables, net	28	(85)	(112)
Other assets	(19)	6	(22)
Retiree health benefits	4,481	4,260	248
Unfunded retirement benefits	2,398	2,658	5,800
Payables, accrued expenses and other	1	383	687
Deferred revenue-prepaid postage, prepaid box rents and other	(99)	(52)	(1,045)
Net cash provided by operating activities	**2,767**	**3,823**	**2,736**
Cash flows from investing activities:			
Purchases of property and equipment	(1,409)	(1,344)	(1,428)
Proceeds from sales of property and equipment	32	58	206
Net cash used in investing activities	**(1,377)**	**(1,286)**	**(1,222)**
Cash flows from financing activities:			
Issuance of notes payable	69,000	29,800	7,600
Payments on notes payable	(70,800)	(29,800)	(7,600)
Changes in capital lease obligations and other	(58)	(63)	(51)
Net cash used in financing activities	**(1,858)**	**(63)**	**(51)**
Net (decrease) increase in cash, cash equivalents and restricted cash	(468)	2,474	1,463
Cash, cash equivalents and restricted cash at beginning of year	10,804	8,330	6,867
Cash, cash equivalents and restricted cash at end of year	**$ 10,336**	**$ 10,804**	**$ 8,330**
Supplemental cash flow disclosures:			
Cash paid for interest	$ 248	$ 214	$ 188

See accompanying notes to the financial statements.

NOTES TO FINANCIAL STATEMENTS

NOTE 1 - ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Organization

The United States Postal Service (the "Postal Service") provides postage, mail delivery and shipping services to retail and commercial customers in the communications, distribution and delivery, advertising and retail markets throughout the nation and internationally. As a result, the Postal Service maintains a very diverse customer base and is not dependent upon a single customer or small group of customers. No single customer represented more than 6% of operating revenue for the years ended September 30, 2018, 2017 and 2016. The Postal Service is subject to congressional oversight and regulation by the Postal Regulatory Commission ("PRC"), but does not receive tax dollars for operating expenses, relying solely on the sale of postage, products and services to fund its operations.

The *Postal Accountability and Enhancement Act of 2006*, Public Law 109-435 ("PAEA") classifies the services offered by the Postal Service as either Market-Dominant or Competitive products; however, the term "services" is used in this report for consistency with other descriptions of services the Postal Service offers. The Postal Service provides services through approximately 31,000 Postal Service-managed Post Offices, stations and branches, plus approximately 4,000 additional Contract Postal Units, Community Post Offices, Village Post Offices, and a large network of commercial outlets which sell postage stamps and services on the Postal Service's behalf and through its website *www.usps.com*. The Postal Service delivers to nearly 159 million city, rural, *PO Box* and highway delivery points. Operations are conducted primarily in the domestic market, with international revenue representing approximately 4% of operating revenue.

Approximately 92% of employees are covered by collective bargaining agreements and are primarily represented by the American Postal Workers Union, AFL-CIO ("APWU"); the National Association of Letter Carriers, AFL-CIO ("NALC"); the National Postal Mail Handlers Union, AFL-CIO ("NPMHU") and the National Rural Letter Carriers Association ("NRLCA"). The contracts with these four labor unions represent the majority of Postal Service employees and include provisions granting annual wage increases and cost-of-living adjustments ("COLAs"), which are linked to the Consumer Price Index – Urban Wage Earners and Clerical Workers ("CPI-W"). For further information on collective bargaining agreements, see *Note 10 - Commitments and Contingencies.*

By law, the Postal Service must consult with management organizations representing most of its employees not covered by collective bargaining agreements. These consultations provide non-bargaining unit employees in the field with an opportunity to participate in the planning, development and implementation of certain programs and policies that affect them.

Summary of Significant Accounting Policies

The preparation of financial statements in accordance with accounting principles generally accepted in the U.S. ("GAAP") requires management to make estimates and judgments that affect the reported amounts of assets, liabilities, revenue and expenses and related disclosure of contingent assets and liabilities. On an ongoing basis, management evaluates its estimates which are based on historical experience and various other assumptions that management believes are reasonable under the circumstances. The results of these evaluations form the basis for making judgments about the carrying value of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates; however, management believes that its estimates are reasonable and that the actual results will not vary significantly from the estimated amounts.

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 fiscal quarters.

Cash and Cash Equivalents

Cash and Cash Equivalents consists of unrestricted cash and short-term, highly-liquid investments with maturities of 90 days or less. See *Note 5 - Cash, Cash Equivalents and Restricted Cash* for additional information.

Restricted Cash
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 other restriction. See *Note 5 - Cash, Cash Equivalents and Restricted Cash* for additional information.

Receivables, net
Receivables, net represents Postal Service receivables recorded at the amount invoiced, net of allowances. Allowances for potential losses are recognized at each balance sheet date. These estimates are determined based on historical collection experience, trends in customer payment frequency and judgments about the probable effects of observable data, including present economic conditions and the financial health of specific customers and market sectors. See *Note 6 - Receivables and Customers* for additional information.

Property and Equipment, net
Property and Equipment, net represents property and equipment recorded at cost, including the interest on borrowings used to pay for the construction of major capital additions, less accumulated depreciation. Depreciation expense is recorded using the straight-line method over estimated useful life, which ranges from 3 to 40 years. Depreciation expense is included within *Other operating expenses* in the accompanying *Statements of Operations*. The costs and accumulated depreciation of assets sold or retired are removed from balance sheet accounts in the period in which the transaction occurred. General maintenance and repair costs are charged to expense as incurred. See *Note 7 - Property and Equipment, net* for additional information.

Software Capitalization
Software costs, including internal development costs, are capitalized when they meet certain criteria. Costs to be capitalized include both contracted resources and employee labor costs involved in the development of internal-use software. Interest costs incurred while developing internal-use software are also capitalized. Costs are accumulated until the software is put into production, at which time amortization of the internal-use software begins for a period not to exceed 3 years. See *Note 7 - Property and Equipment, net* for additional information.

Leases
The Postal Service leases over 23,000 real properties. As the lessee, the Postal Service classifies a lease which has substantially all the risks and rewards of ownership as a capital lease. These leases are capitalized on the lease commencement date at the lower of the fair value of the leased assets or the present value of the minimum lease payments. The discount rate used to determine the present value is based on average U.S. Treasury rates. Property acquired under a capital lease is amortized over the lease term. Capital leases are included within *Property and equipment, net* in the accompanying *Balance Sheets*.

Other lease arrangements in which substantially all risks and rewards of ownership are retained by the lessor are classified as operating leases. Rent expense for operating leases is included in *Other operating expenses* in the accompanying *Statements of Operations* on a straight-line basis over the term of the lease.

Impaired Assets
Impairment losses on long-lived assets are recorded when events or circumstances indicate that an asset's fair value is less than its carrying value. When such a determination is made, the carrying values of the assets are written down to fair value. Fair value is typically determined by independent appraisals for real property. Due to the absence of a market for most types of mailing equipment, impaired equipment assets are typically assigned a fair value of zero. See *Note 7 - Property and Equipment, net* for additional information.

Employees' Accumulated Leave
Employees' accumulated leave represents leave earned but unused as of the balance sheet date and is recorded as a liability net of advances. Career employees earn annual leave based on the number of creditable years of service with the federal government. The Postal Service notifies employees at the beginning of each calendar year of the amount of leave they will earn for that year. Leave taken by employees before it is earned is considered an advance. Advances were $158 million and $159 million at September 30, 2018, and 2017, respectively, and are

netted against the liability for *Employees' accumulated leave, noncurrent* as presented in the accompanying *Balance Sheets*. The current portion of employees' accumulated leave, which consists of holiday leave, was $127 million and $131 million at September 30, 2018, and 2017, respectively, and is included under *Current liabilities* within *Compensation and benefits* in the accompanying *Balance Sheets*.

Retiree Benefits
Career employees are eligible to participate in U.S. government pension and retiree health benefits programs. The Postal Service is required to provide funding for these plans as determined by the Office of Personnel Management ("OPM"), the administrator of the plans. The Postal Service cannot direct the costs, benefits or funding requirements of the plans. Accordingly, the plans are accounted for using multiemployer plan accounting rules, and expenses are recorded in the period in which the contributions are due and payable. See *Note 11 - Retirement Plans* and *Note 12 - Health Benefits Plans* for additional information.

Workers' Compensation
Postal Service employees are covered by the *Federal Employees' Compensation Act* ("FECA"), administered by the Department of Labor ("DOL") Office of Workers' Compensation Programs ("OWCP"). The Postal Service uses an estimation model to forecast and record the workers' compensation liability for the present value of estimated future payments. See *Note 13 - Workers' Compensation* for additional information.

Deferred Revenue–Prepaid Postage
Deferred revenue–prepaid postage is an estimate of postage that the Postal Service has sold but customers have not yet used. Revenue is recognized at the time mail and packages are delivered. Because payments for postage are collected in advance of the satisfaction of related performance obligations, the Postal Service defers and reflects this revenue as *Deferred revenue–prepaid postage* in the accompanying *Balance Sheets*. Stamp sales and metered postage account for the majority of *Deferred revenue–prepaid postage*. Included in the estimate of the liability is an estimate for mail that is in-transit within the Postal Service network. See *Note 8 - Payables, Accrued Expenses and Deferred Revenue* for additional information.

Contingent Liabilities
The Postal Service is a party to various legal proceedings and claims in the normal conduct of its operations. Contingent liabilities require significant judgment in estimating potential losses. Each quarter, the Postal Service evaluates significant new claims and litigation for the probability of an adverse outcome. The Postal Service also reviews prior claims and litigation, and when necessary, adjusts the liability balance for resolutions or revisions to prior estimates. Estimates of loss can therefore change as additional information becomes available. See *Note 10 - Commitments and Contingencies* for additional information.

Revenue Forgone
Under the *Revenue Forgone Reform Act of 1993*, Congress agreed to reimburse the Postal Service $1.2 billion in 42 annual "installments" of $29 million through the year 2035 for certain services the Postal Service performed during years 1991 through 1998. Additionally, each year the Postal Service estimates the costs it incurs to provide "free and reduced mail" services to groups of mailers that Congress has determined should be subsidized, and the Postal Service submits these estimates annually to Congress. After consideration, Congress may deny, modify and/or approve the submission under an appropriation for one or both revenue forgone components. See *Note 14 - Revenue Forgone* for additional information.

Advertising
Advertising costs, which the Postal Service expenses as they are incurred, were $164 million, $164 million and $163 million for the years ended September 30, 2018, 2017 and 2016, respectively, and are included within *Other operating expenses* in the accompanying *Statements of Operations*.

Foreign Currency Risk
Foreign currency risk can arise from international mail transactions related to settlements of receivables and payables with foreign postal administrations. The majority of international accounts are denominated in special drawing rights, based on a group of currencies comprised of the Euro, Japanese yen, British pound sterling and the U.S. dollar, which fluctuate daily. Changes in the relative value of these currencies increase or decrease the value of the settlement accounts and result in a gain or loss that is included in operating results. The impact of

foreign currency translation on operating results was not material for the years ended September 30, 2018, 2017 and 2016.

Segment Information
The Postal Service operates as one segment throughout the U.S., its possessions and territories.

Related Parties
As disclosed throughout this report, the Postal Service conducts significant transactions with other U.S. government entities. See *Note 4 - Related Parties* for additional information.

2016 Change in Accounting Estimate
During 2016, the Postal Service revised the estimation technique utilized to estimate its *Deferred revenue-prepaid postage* liability for a certain series of postage stamps. The change resulted from new information regarding customers' retention and usage habits of *Forever Stamps*, and enabled the Postal Service to update its estimate of usage and "breakage" (representing stamps that will never be used for mailing due to loss, damage or stamp collection).

As a result of this change in estimate, the *Deferred revenue-prepaid postage* liability was decreased by nearly $1.1 billion. In accordance with GAAP, the change was accounted for as a change in accounting estimate, and was reflected in operating results as an increase to revenue and a decrease to net loss by the same amount in the year ended September 30, 2016.

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* ("ASU 2014-09"). The 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 new 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. ASU 2014-09 has become effective for the Postal Service's 2019 fiscal year (beginning in the first quarter). The Postal Service will adopt the new standard in the first quarter of 2019, using the modified retrospective approach.

The Postal Service has 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 and variable consideration. The Postal Service has completed its contract analysis based on the five-step model as outlined in the authoritative literature, and has quantified the impact of adopting the new standard on its financial statements.

Through its comprehensive approach of assessing the impact of adopting the new guidance, the Postal Service has determined that the October 1, 2018, opening balance of accumulated deficit will increase to account for changes in the method the Postal Service recognizes the "breakage" and "Mail-in-Transit" components of deferred revenue associated with prepaid postage. The amount of this increase is estimated to represent less than 1% of the Postal Service's 2018 operating revenue and is therefore immaterial.

The Postal Service has assessed the impact that adopting the standard will have on its footnote disclosures for periods subsequent to October 1, 2018, and has determined that additional qualitative and quantitative disclosures will be required to include information about its disaggregation of revenue, performance obligations, the timing of revenue recognition and significant judgments made that impact the amount and timing of revenue from its contracts with customers.

Accounting Standards Update 2016-04 Liabilities - Extinguishments of Liabilities

In March 2016, the FASB issued Accounting Standards Update 2016-04 *Liabilities - Extinguishments of Liabilities* ("ASU 2016-04"). The standard requires entities that sell prepaid stored-value products redeemable for goods, services or cash at third-party merchants to recognize "breakage" (i.e., the value that is ultimately not redeemed by the consumer) as revenue on a pro-rata basis using an estimate based on past redemption patterns, consistent with how breakage will be recognized under ASU 2014-09, discussed earlier. ASU 2016-04 became effective for the Postal Service's 2019 fiscal year (beginning in the first quarter). The Postal Service will adopt the standard in the first quarter of 2019, using the modified retrospective approach.

The Postal Service is finalizing its quantification of the impact of adopting ASU 2016–04. Through its assessment of the impact of adopting the new guidance, the Postal Service has determined that the October 1, 2018, opening balance of accumulated deficit will likely decrease to account for the method the Postal Service recognizes breakage revenue related to money orders. The amount of this decrease is estimated to represent less than 1% of the Postal Service's 2018 operating revenue and is therefore immaterial. The opening balance of other current liabilities will decrease by the same amount.

Accounting Pronouncements Issued but not Adopted

Accounting Standards Update 2016-02 Leases

In February 2016, the FASB issued Accounting Standards Update 2016-02 *Leases* ("ASU 2016-02"). 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 are presented separately in the statements of operations.

ASU 2016-02 will become effective for the Postal Service's 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 intends to utilize this transition method.

The Postal Service has completed its initial scoping exercise and continues to evaluate whether embedded leases exist in its service contracts. In addition, the Postal Service has begun abstracting all of the necessary information to properly account for over 23,000 facilities property leases under the new standard. The Postal Service continues to evaluate the full impact of adopting this standard on its financial statements and disclosures, as well as its impact of adoption on Postal Service policies, practices and systems. As of September 30, 2018, the Postal Service had $3.5 billion of future minimum operating lease commitments that are not currently recognized on its balance sheet. Therefore, the Postal Service expects that the adoption will have a material effect on its balance sheet and disclosures, and immaterial impact on its statements of operations and statements 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* ("ASU 2016-13"). 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.

ASU 2016-13 will become effective for the Postal Service's 2020 fiscal year (beginning October 1, 2019) and the quarters therein, with early adoption permitted. The standard is applicable to the Postal Service's valuation of trade accounts receivable and its revenue forgone receivables. While the Postal Service continues to evaluate the impact of adopting this standard, it does not expect the adoption of this standard to have a material impact on its financial statements and 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 Fees Paid in a Cloud Computing Arrangement* ("ASU 2018-15"). This is an update to a standard 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 to internal-use software, then the software license is accounted for by the customer in accordance with Subtopic 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.

ASU 2018-15 will become effective for the Postal Service's 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 disclosures.

NOTE 3 - LIQUIDITY

The Postal Service generates its cash almost entirely through the sale of postage and other services. It 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 September 30, 2018, and 2017, the Postal Service held unrestricted cash and cash equivalents of $10.1 billion and $10.5 billion, respectively. As of September 30, 2018, the Postal Service had $1.8 billion of remaining borrowing capacity under its statutory debt ceiling, whereas at September 30, 2017, the Postal Service had no remaining borrowing capacity under its statutory debt ceiling. See *Note 9 - Debt* for additional information.

Liquidity Concerns

The Postal Service is constrained by laws and regulations, including the PAEA, which restricts revenue sources and mandates certain expenses. These expenses include prefunding requirements for retiree health benefits, and amortization schedules to provide full funding of retirement and health benefits that are unlike those imposed on most other federal entities or private sector businesses.

PAEA-mandated expenses include amortization payments to provide full funding of retirement benefits under the Civil Service Retirement System (“CSRS”) and the Federal Employee Retirement System (“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 prefunding of retiree health benefits, described below and in *Note 12 - Health Benefits Plans*.

For the year ended September 30, 2018, the Postal Service reported operating expenses of $74.4 billion and a net loss of $3.9 billion. The Postal Service has incurred cumulative net losses of $69.0 billion from 2007 through 2018.

Business Model Challenges/Constraints

Market-Dominant services, which account for approximately 67% of the Postal Service's annual operating revenues, 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 its cost structure cannot be altered expeditiously due to the Postal Service's universal service obligation. Further, the number of delivery points continues to grow by approximately one million per year, which drives up delivery costs. Many 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.

Aside from its universal service obligation, a significant factor contributing to Postal Service losses is the ongoing decline in Market-Dominant mail volume. Specifically, secular 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, while *Marketing Mail* volume declined in 2017 and 2018 largely due to mailers' increasing use of digital advertising. Also contributing to losses as noted above is the increase in the number of delivery points, which, when combined with the impact of the reduction in hard-copy 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 decline of approximately 37%.

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 and inflation, health benefit premium increases, and retirement and workers' compensation programs. Some of these costs have historically tended to increase at a higher rate than inflation.

Retiree Health and Unfunded Retirement Benefits

Postal Service liquidity is significantly impacted by its obligations to pay for retirement and retiree health benefits, including obligations for FERS normal costs, PSRHBF normal costs, and the amortization of unfunded CSRS, FERS and PSRHBF liabilities.

OPM periodically notifies the Postal Service regarding its revaluation of unfunded CSRS and FERS liabilities. 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 but not Postal Service-specific salary growth assumptions, and OPM implemented this for its valuation as of September 30, 2017. OPM's rule announcing this change did not fully address the Postal Service's concerns regarding the use of government-wide versus Postal Service-specific economic assumptions.

The Postal Service records CSRS and FERS amortization expenses as *Unfunded retirement benefits amortization* in the accompanying *Statements of Operations*, and as current liabilities within *Unfunded retirement benefits* in the accompanying *Balance Sheets*. These amounts may be significantly impacted by changes in actuarial assumptions used to value the unfunded liabilities. Additionally, the Postal Service is obligated to pay FERS normal costs, representing its employer contributions to the FERS plan for participating employees.

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. In addition, the Postal Service is obligated to pay the estimated normal costs of retiree health benefits attributable to the service of its employees during the most recently ended fiscal year.

The Postal Service also did not make payments to OPM totaling $13.8 billion 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 accrued but unpaid related to retiree health benefits, CSRS and FERS by the Postal Service and the fiscal years in which the accruals were recorded:

(in millions)	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 accrued but unpaid	**$ 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.

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 not have sufficient liquidity to meet all of its existing legal obligations when due, to pay down its debt and to make the critical infrastructure investments that have been deferred in recent years.

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

For additional information regarding retirement benefits and retiree health benefits, see *Note 11 - Retirement Plans* and *Note 12 - Health Benefits Plans*, respectively.

Status of Note Purchase Agreement

Under the *Postal Reorganization Act*, as amended by Public Laws 101-227 and 109-435 (the "PRA"), the Postal Service can issue debt obligations. 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 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 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.

On September 28, 2018, under the most recent amendment to the NPA, the FFB extended the NPA until December 31, 2018, (one quarter) as opposed to its prior practice of annually extending the NPA for a full fiscal year. This change did not affect the terms of any of the Postal Service's outstanding debt as of September 30, 2018.

If the Postal Service is unable to extend the NPA beyond December 31, 2018, 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.

For additional information regarding the Postal Service's debt, see *Note 9 - Debt*.

Mitigating Circumstances

The Postal Service continues to pursue strategies within its control to increase operational efficiency and improve liquidity. The Postal Service has conserved capital in recent years by spending only what it believed essential to maintain its existing facilities and service levels and to increase efficiencies. However, an increase in capital investment is necessary to upgrade its facilities, fleet of vehicles and processing equipment in order to remain operationally viable.

The Postal Service continues to support legislation that will enable it to increase revenue and reduce costs. Specifically, reforms to establish a set of health care plans within the Federal Employees Health Benefits ("FEHB") Program, fully integrated with Medicare, for current and future Postal Service retirees, would eliminate most of the current retiree health benefits unfunded liability and substantially reduce annual amortization and normal cost payment requirements.

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 changes that are required to restore its financial stability.

NOTE 4 - RELATED PARTIES

The Postal Service conducts significant transactions with other U.S. government entities, which are considered related parties.

The following table presents related-party assets and liabilities as of September 30, 2018, and 2017:

(in millions)	September 30, 2018	September 30, 2017
Related-party assets:		
Receivables and advances[1]	$ 61	$ 47
Carrying amount of revenue forgone installment receivable[2]	446	426
Related-party liabilities:		
Current portion of debt	$ 11,000	$ 10,100
Other current liabilities[3]	50,312	43,504
Noncurrent portion of debt	2,200	4,900
Other noncurrent liabilities[4]	15,047	16,420

[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 15 - Fair Value Measurement*.
[3] Amounts include CSRS, FERS and PSRHBF obligations 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 years ended September 30, 2018, 2017 and 2016:

(in millions)	2018	2017	2016
Related-party operating revenue[1]	$ 999	$ 975	$ 1,054
Related-party operating expenses[2]	16,394	16,544	18,830
Related-party interest income[3]	123	58	31
Related-party interest expenses[4]	235	205	195

[1] Included within *Operating revenue* in the accompanying *Statements of Operations*.

[2] Included within *Operating expenses* in the accompanying *Statements of Operations*.

[3] Imputed on the revenue forgone installment receivable or generated on cash equivalents held with the Federal Reserve Bank of New York or short-term investments in U.S. Treasury instruments. Included within *Interest and investment income* in the accompanying *Statements of Operations*.

[4] Incurred on debt issued to the Federal Financing Bank, and included within *Interest expense* in the accompanying *Statements of Operations*.

NOTE 5 - CASH, CASH EQUIVALENTS AND RESTRICTED CASH

The following table provides a reconciliation of cash, cash equivalents and restricted cash reported in the accompanying *Balance Sheets* as of September 30, 2018, and 2017, respectively, along with the reported cash, cash equivalents and restricted cash balances as of September 30, 2016, that sum to the totals of the same such amounts reported in the accompanying *Statements of Cash Flows* for the years ended September 30, 2018, 2017 and 2016:

	September 30,		
(in millions)	2018	2017	2016*
Cash and cash equivalents	$ 10,061	$ 10,513	$ 8,077
Restricted cash	275	291	253
Total cash, cash equivalents and restricted cash as reported in the accompanying *Statements of Cash Flows*	**$ 10,336**	**$ 10,804**	**$ 8,330**

* As reported in the accompanying *Statements of Cash Flows*, the 2016 opening balances for *Cash and cash equivalents*; *Restricted cash*; and *Total cash, cash equivalents and restricted cash* were $6.6 billion, $233 million and $6.9 billion, respectively.

NOTE 6 - RECEIVABLES AND CUSTOMERS

The Postal Service's revenue is generated primarily from deliveries within the domestic market, with international revenue representing 3.7%, 3.8% and 3.7% of operating revenue for the years ended September 30, 2018, 2017 and 2016, respectively. For the years ended September 30, 2018, 2017 and 2016, combined revenue from the Postal Service's three largest customers (excluding mail service providers) represented approximately 8.3%, 7.6% and 5.8% of operating revenue, respectively.

The following table details *Receivables, net* from the accompanying *Balance Sheets* as of September 30, 2018, and 2017:

(in millions)		2018		2017
Foreign countries	$	807	$	800
U.S. government*		29		39
Other		323		342
Receivables before allowances		1,159		1,181
Less: Allowances		65		54
Receivables, net	**$**	**1,094**	**$**	**1,127**

* U.S. government receivables amounts exclude noncurrent receivables.

Receivables from foreign countries were 69.6% and 67.7% of the total receivables before allowances as of September 30, 2018 and 2017, respectively. The largest of these receivables was from China, which represented 53.3% and 39.6% of the total foreign balance outstanding in 2018 and 2017, respectively. U.S. government receivables consist primarily of military and official mail receivables of $25 million and $17 million as of September 30, 2018, and 2017, respectively, and appropriations receivables of $19 million as of September 30, 2017, only. The Postal Service had no current appropriations receivables as of September 30, 2018.

Total provisions for allowances charged to expense for the years ended September 30, 2018, 2017 and 2016 were $17 million, $10 million and $22 million, respectively, and are included within *Other operating expenses* in the accompanying *Statements of Operations.*

NOTE 7 - PROPERTY AND EQUIPMENT, NET

Assets within *Property and equipment, net* are recorded at cost, which includes the interest on borrowings used to finance the construction of major capital additions, less allowances for depreciation and amortization. Interest capitalized during the years ended September 30, 2018, 2017 and 2016, was not significant. Assets within *Property and equipment, net* are depreciated over estimated useful lives that range from 3 to 40 years using the straight-line method.

The following table provides details for *Property and equipment, net* from the accompanying *Balance Sheets* as of September 30, 2018, and 2017:

(in millions, except years)	Estimated life in years		2018		2017
Buildings	3 - 40	$	25,403	$	25,027
Equipment	3 - 20		15,717		15,761
Vehicles	5 - 24		4,389		4,268
Land	-		2,830		2,820
Leasehold improvements	3 - 20		1,624		1,542
Property and equipment, at cost		**$**	**49,963**	**$**	**49,418**
Less: Accumulated depreciation and amortization			35,956		35,157
Construction in progress			609		630
Property and equipment, net		**$**	**14,616**	**$**	**14,891**

Gains recognized on assets sold are reported in *Other revenue* within the accompanying *Statements of Operations*. For the years ended September 30, 2018, 2017 and 2016, total net gains, including the amortization of deferred gains noted below, were approximately $16 million, $25 million and $58 million, respectively.

The Postal Service defers gains when it enters into any lease-back arrangements or contractual obligations requiring continued Postal Service involvement with the property. Total deferred gains on the sale of property were $301 million and $318 million as of September 30, 2018, and 2017, respectively. The current portions of deferred gains were $3 million and $16 million as of September 30, 2018, and 2017, respectively, and are included within *Other current liabilities* in the accompanying *Balance Sheets*. The noncurrent portions of deferred gains were $298 million and $302 million as of September 30, 2018, and 2017, respectively, and are included within *Other noncurrent liabilities* in the accompanying *Balance Sheets*.

Deferred gains are amortized over the periods during which the Postal Service has continuing involvement with the applicable properties. The amounts amortized, included within *Other revenue* in the accompanying *Statements of Operations*, were $16 million, $9 million and $9 million for the years ended September 30, 2018, 2017 and 2016, respectively.

Impairment charges were approximately $3 million, $6 million and $17 million for the years ended September 30, 2018, 2017 and 2016, respectively, and are included in *Other operating expenses* in the accompanying *Statements of Operations*.

Depreciation and amortization expenses were approximately $1.7 billion for each of the years ended September 30, 2018, 2017 and 2016, and are included within *Other operating expenses* in the accompanying *Statements of Operations*.

The book values of assets classified as held for sale were approximately $13 million and $18 million as of September 30, 2018, and 2017, respectively, and are included within both *Land* and *Buildings* in the table above.

NOTE 8 - PAYABLES, ACCRUED EXPENSES AND DEFERRED REVENUE

Payables and Accrued Expenses

The following table provides details for *Payables and accrued expenses* from the accompanying *Balance Sheets* as of September 30, 2018, and 2017:

(in millions)	2018	2017
Trade payables	$ 820	$ 694
Foreign countries	445	471
U.S. government	74	87
Other accrued expenses	878	678
Total payables and accrued expenses	**$ 2,217**	**$ 1,930**

Deferred Revenue–Prepaid Postage

Deferred revenue for postage sales is developed and validated through complex mathematical and statistical sampling methods for estimating postage stamp usage. The estimated postage stamp usage is deducted from stamp sales with the difference representing the Postal Service's obligation to perform future services. That obligation is reduced by recognizing a provision for postage sold that may never be used, either through loss, damage, or stamp-collecting activity. The Postal Service recognizes revenue from "breakage" (representing stamps that will never be used for mailing due to loss, damage or stamp collection) upon initial sale of postage.

Metered postage is primarily used by businesses. Deferred revenue related to meters is estimated by monitoring the actual usage of all postage meters that had postage added during the month preceding the financial measurement date. The information from the two most recent meter readings is used to derive a deferral percentage, which is applied to all postage meter receipts for the month.

Included in the estimate of *Deferred revenue–prepaid postage* is an estimate for mail that is in-transit within the Postal Service processing and delivery network. The following table provides details for *Deferred revenue–prepaid postage* from the accompanying *Balance Sheets* as of September 30, 2018, and 2017:

(in millions)	**2018**	**2017**
Forever stamps	$ 1,156	$ 1,220
Mail in-transit	478	499
Meters	302	325
Other	130	124
Total deferred revenue-prepaid postage	**$ 2,066**	**$ 2,168**

NOTE 9 - DEBT

Under the PRA, the Postal Service can issue debt obligations. In 1974, the Postal Service began issuing debt through individual debt agreements to the FFB, a government-owned corporation under the general supervision of the Secretary of the Treasury. 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 1999, the Postal Service entered into the 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.

These note arrangements and credit line facilities provide the flexibility to borrow short or long term, using floating or fixed-rate instruments. At its option, the Postal Service can issue its fixed-rate notes as either callable or non-callable. All of the Postal Service's debt is unsecured, not subject to sinking fund requirements and can be repaid at any time at a price determined by the Secretary of the Treasury based on prevailing interest rates in the U.S. Treasury securities market at the time of repayment. As of September 30, 2018, the premium associated with a prepayment of all debt was $109 million based on prevailing interest rates. The weighted average interest rate for all outstanding debt was 2.612% as of September 30, 2018.

The two revolving credit facilities are renewable annually and have been extended to April 2019. As of September 30, 2018, these facilities were fully drawn. The first revolving credit facility, a short-term credit line, enables the Postal Service to draw up to $3.4 billion with two days prior notice. Borrowings under this credit line are typically on an overnight basis, but can have a maximum term of up to one year. The second revolving credit facility allows for borrowings on an overnight basis and up to $600 million on the same business day that funds are requested. The interest rates for borrowings under these credit facilities are determined by the U.S. Treasury each business day.

As the Postal Service reported in a Current Report on Form 8-K filed with the PRC on September 28, 2018, under the most recent amendment to the NPA, the FFB extended the NPA until December 31, 2018, (one quarter) as opposed to its prior practice of annually extending the NPA for a full fiscal year. This change did not affect the terms of any of the Postal Service's outstanding debt as of September 30, 2018.

If the Postal Service is unable to extend the NPA beyond December 31, 2018, it has no assurance that it could obtain alternative debt financing beyond 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.

The following table provides details for *Current portion of debt* and *Noncurrent portion of debt* from the accompanying *Balance Sheets* as of September 30, 2018, and 2017:

(in millions, except percentages)	2018		2017	
Maturity	**Balance**	**Rate %**	**Balance**	**Rate %**
Current portion of debt:				
Fixed rate notes:				
October 26, 2017	$ —		$ 4,400	1.104
November 9, 2017	—		1,000	0.895
December 7, 2017	—		700	0.994
October 25, 2018	4,300	2.237	—	
November 15, 2018*	500	3.048	—	
February 15, 2019*	700	3.296	—	
May 15, 2019*	1,000	3.704	—	
May 15, 2019*	500	3.513	—	
Current revolving credit line:				
October 1, 2018	3,400	2.237	3,400	0.267
Overnight revolving credit line:				
October 1, 2018	600	2.247	600	0.318
Total current portion of debt	**11,000**		**10,100**	
Noncurrent portion of debt - fixed rate notes:				
November 15, 2018*	—		500	3.048
February 15, 2019*	—		700	3.296
May 15, 2019*	—		1,000	3.704
May 15, 2019*	—		500	3.513
August 16, 2021	1,000	2.066	1,000	2.066
May 17, 2038	200	3.770	200	3.770
February 15, 2039	1,000	3.790	1,000	3.790
Total noncurrent portion of debt	**2,200**		**4,900**	
Total debt	**$ 13,200**		**$ 15,000**	

*Note reported as noncurrent as of September 30, 2017, and current as of September 30, 2018.

At September 30, 2018, scheduled repayments of debt principal are listed below:

(in millions)	**Principal Amount**
2019	$ 11,000
2020	—
2021	1,000
2022	—
2023	—
Thereafter	1,200
Total debt maturities	**$ 13,200**

NOTE 10 - COMMITMENTS AND CONTINGENCIES

Leases

The Postal Service leases premises and equipment under operating and capital leases generally having terms from one to 20 years with options to renew. Certain non-cancellable real estate leases have purchase options at prices specified in the leases.

The following table provides details for total rental expense for the years ended September 30, 2018, 2017 and 2016:

(in millions)	2018	2017	2016
Non-cancellable real estate leases[1]	$ 984	$ 940	$ 908
GSA facilities leases[2]	29	32	31
Equipment and other short-term rentals	159	157	155
Total rental expense	**$ 1,172**	**$ 1,129**	**$ 1,094**

[1] Sublease income was not material to the financial statements for the years ended September 30, 2018, 2017 and 2016.
[2] General Services Administration leases subject to 120-day cancellation notice.

The amounts below represent future minimum payments for all non-cancellable leases with original lease terms greater than one year, including leases where renewal options have been exercised:

(in millions)	Operating*	Capital
2019	$ 815	$ 59
2020	728	44
2021	598	30
2022	447	16
2023	303	11
Thereafter	633	47
Total lease obligations	**$ 3,524**	**$ 207**
Less: Interest		44
Total capital lease obligations		**$ 163**
Less: Current portion of capital lease obligations		83
Noncurrent portion of capital lease obligations		**$ 80**

*The information provided in the prior year footnote included future lease payments for all renewal options, whether exercised or not.

Capital leases, recorded at historical cost within *Property and equipment, net* in the accompanying *Balance Sheets*, were $590 million and $689 million as of September 30, 2018, and 2017, respectively. Total accumulated amortization related to capital leases was $470 million and $536 million at September 30, 2018, and 2017, respectively. Amortization expense for capital leases was approximately $37 million, $39 million and $42 million for the years ended September 30, 2018, 2017 and 2016, respectively and are included within *Other operating expense* in the accompanying *Statements of Operations*.

Capital Commitments

Capital commitments consist primarily of commitments to invest in equipment and building construction and improvements. The following table provides details for approved capital projects in progress at September 30, 2018, and 2017:

(in millions)	2018	2017
Mail processing equipment	$ 320	$ 370
Building improvements, construction and building purchase	512	393
Postal support equipment	98	95
Vehicles and other	430	314
Total capital commitments	**$ 1,360**	**$ 1,172**

Contingent Liabilities

The Postal Service's contingent liabilities consist primarily of claims resulting from labor, employment, 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 new claim to determine if it is probable of an unfavorable outcome and if the amount of the potential resolution is reasonably estimable. If so, a liability for the amount is recorded. Preexisting claims are also reviewed and adjusted quarterly for resolutions or revisions to prior estimates.

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 September 30, 2018, and 2017:

(in millions)	2018	2017
Current/noncurrent portions of contingent liabilities:		
Current portion[1]	$ 244	$ 161
Noncurrent portion[2]	193	500
Total contingent liabilities	**$ 437**	**$ 661**
Contingent liabilities by category:		
Labor and employment matters	$ 297	$ 549
Asset retirement obligations	67	54
Tort matters	67	54
Contractual matters	6	4
Total contingent liabilities	**$ 437**	**$ 661**

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

In addition to the amounts accrued in the financial statements, the Postal Service is subject to other claims and lawsuits which it deems reasonably possible of an unfavorable outcome, which ranged from $225 million to $1.1 billion and from $200 million to $675 million at September 30, 2018, and 2017, respectively. The Postal Service has not recorded accruals for these reasonably possible losses in its financial statements. 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 business, financial condition or operations.

Class Action Litigation

As previously reported, on January 14, 2010, the Equal Employment Opportunity Commission's Office of Federal Operations 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 *McConnell* 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 Equal Employment Opportunity Commission's Office of Federal Operations, which was denied in 2018. The Postal Service is now implementing this 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. Class Agent's counsel is challenging the Postal Service's implementation of the decision and many issues remain unresolved. As a result, the ultimate outcome could be greater or less than the amount accrued as of September 30, 2018.

Collective Bargaining Agreements

In April 2016, the Postal Service reached a three-year collective bargaining agreement with the NRLCA which was ratified by NRLCA membership. The new contract includes general wage increases totaling 3.8% over three years (1.2% of which was retroactive to November 2015) with a COLA base month of July 2014 (no retroactive COLA payments), a reduction in the employer share of health insurance premiums, beginning in the 2017 plan year, and the creation of a new non-career employee category to provide weekend and holiday parcel deliveries. The Postal Service's contract with the NRLCA expired on May 20, 2018, and the respective parties mutually agreed to extend negotiations on a new collective bargaining agreement beyond the deadline. No new agreement has been reached as of the date of this report.

In July 2016, an interest arbitration decision was issued and an arbitrated contract was awarded that established a collective bargaining agreement between the Postal Service and the APWU. The contract was the result of a legally-mandated binding arbitration process that was required when the parties reached impasse in negotiating a new collective bargaining agreement after the prior agreement expired in May 2015. The awarded contract includes general wage increases totaling 3.8% over three years (1.2% of which was retroactive to November 2015) with a COLA base month of July 2014 (no retroactive COLA payments), a reduction in the employer share of health insurance premiums, beginning in the 2017 plan year, and annual increases in uniform and work clothing allowances. The award also converted approximately 5,000 non-career positions to career positions. The Postal Service's contract with the APWU expired on September 20, 2018, and the respective parties mutually agreed to extend the deadline for negotiations on a new collective bargaining agreement to November 20, 2018.

In December 2016, the Postal Service reached a tentative agreement with the NPMHU on a 40-month labor contract (retroactive to May 2016) which was subsequently ratified by the union membership in February 2017. The contract includes general wage increases totaling 3.8% over the life of the contract (1.2% of which was retroactive to November 2016) with a COLA base month of July 2014 (the first COLA payment was retroactive to September 2016), a reduction in the employer share of health insurance premiums beginning in the 2018 plan year, and annual increases in uniform and work clothing allowances. The contract will expire on September 20, 2019.

In May 2017, the Postal Service reached a tentative agreement with the NALC on a 40-month labor contract (retroactive to May 2016) which was subsequently ratified by the union membership in August 2017. The contract includes general wage increases totaling 2.5% over the life of the contract (1.2% of which was retroactive to November 2016) with a COLA base month of July 2014 (the first COLA payment was retroactive to September 2016), a November 2018 consolidation of the current two pay grades into a single pay grade, a reduction in the employer share of health insurance premiums beginning in the 2018 plan year, and annual increases in uniform and work clothing allowances. The contract will expire on September 20, 2019.

NOTE 11 - RETIREMENT PLANS

The majority of career employees participate in one of two U.S. government pension programs, CSRS and FERS, which are administered by OPM. 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. 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.

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

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. The Postal Service's TSP expenses are related only to its contributions for FERS employees who participate in the TSP.

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 incur normal costs 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 the past three years, as a percentage of employee basic pay, were 7.0% for CSRS.

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. Employee contributions for FERS, FERS - RAE and FERS - FRAE employees, as a percentage of employee basic pay, were 0.8%, 3.1% or 4.4%, respectively. Aside from these different employee contribution rates, the Postal Service uses the term "FERS employees" to apply to all of the FERS employee categories as a whole.

For most current FERS employees, the Postal Service's contribution rates of participating employees' base salaries were 13.7% for each of the years ended September 30, 2018, 2017 and 2016. 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.

The following table provides details for the number of active employees enrolled in CSRS and FERS for the years ended September 30, 2018, 2017 and 2016:

	2018	2017	2016
CSRS and Dual CSRS	22,581	27,830	33,224
FERS	323,505	350,658	371,321
FERS - RAE	7,427	7,378	7,549
FERS - FRAE	142,902	116,546	95,456
Total enrollment	**496,415**	**502,412**	**507,550**

FERS Employees' Current Year Service

The Postal Service records expenses for FERS employees' current year service consisting of FERS normal cost, Social Security and TSP contributions.

The Postal Service's employer cash contributions to the FERS plan for normal costs were $3.5 billion, $3.5 billion and $3.4 billion in 2018, 2017 and 2016, respectively. These cash contributions are included within *Compensation and benefits* in the accompanying *Statements of Operations*.

The Postal Service's Social Security contributions related to FERS and non-career employees were $2.1 billion, $2.0 billion and $2.0 billion in 2018, 2017 and 2016, respectively. These amounts are included in *Compensation and benefits* in the accompanying *Statements of Operations.*

The Postal Service's employer cash contributions to the TSP were $1.1 billion in each of 2018, 2017 and 2016. These amounts are included within *Compensation and benefits* in the accompanying *Statements of Operations.*

CSRS and FERS Unfunded Retirement Benefits

OPM periodically notifies the Postal Service regarding its revaluation of unfunded CSRS and FERS liabilities. OPM calculates these obligations using Postal Service-specific demographics data and government-wide economic assumptions, including salary growth assumptions. The Postal Service records these expenses as *Unfunded retirement benefits amortization* in the accompanying *Statement of Operations*. These amounts may be significantly impacted by changes in actuarial assumptions used to revalue the unfunded liabilities.

The Postal Service received invoices from OPM in the amounts of $1.4 billion and $1.7 billion for the annual CSRS amortization payments due September 30, 2018, and 2017, respectively. The Postal Service also received invoices from OPM in the amounts of $958 million, $917 million, and $248 million for its 2018, 2017 and 2016 FERS amortization obligations, respectively. As indicated in *Note 3 - Liquidity*, the Postal Service did not make any of these payments in order to preserve liquidity to ensure that the ability to fulfill the primary universal service mission was not placed at undue risk. These expenses are recorded as *Unfunded retirement benefits amortization* in the accompanying *Statements of Operations*.

The following table presents the cost of CSRS and FERS unfunded retirement benefits amortization expense for the years ended September 30, 2018, 2017 and 2016:

(in millions)	2018	2017	2016
CSRS unfunded retirement benefits amortization	$ 1,440	$ 1,741	$ —
FERS unfunded retirement benefits amortization	958	917	248
Total cost of CSRS and FERS unfunded retirement benefits amortization expense	**$ 2,398**	**$ 2,658**	**$ 248**

The amounts the Postal Service has accrued for CSRS and FERS unfunded retirement benefits but has not yet paid, including approximately $241 million and $7 million from the years ended September 30, 2015 and 2014, respectively, are recorded as a liability within *Unfunded retirement benefits* in the accompanying *Balance Sheets*.

For the year ended September 30, 2016, the most current period available, the Postal Service provided significantly more than 5% of the total plan contributions for FERS from all U.S. government employers (as disclosed in OPM's *Civil Service Retirement and Disability Fund Annual Report* dated February 2018).

As noted above, the latest available actual data for the government-wide CSRS and FERS plans is September 30, 2016. As of that date, the CSRS plan for the U.S. government, taken as a whole, was approximately 27% funded. Total plan assets and accumulated benefit obligations for the CSRS plan were approximately $293 billion and approximately $1.1 trillion, respectively. The FERS plan for the U.S. government, taken as a whole, was approximately 83% funded. Total plan assets and accumulated benefit obligations for the FERS plan were approximately $595 billion and approximately $716 billion, respectively.

Total expense related to multiemployer retirement plans (which includes FERS normal cost expense, CSRS unfunded retirement benefits amortization, and FERS unfunded retirement benefits amortization) totaled $5.9 billion, $6.1 billion and $3.7 billion for the years ended September 30, 2018, 2017 and 2016, respectively.

NOTE 12 - HEALTH BENEFITS PLANS

The 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 active employees is determined through agreements with Postal Service labor unions.

In 2014, the Postal Service began to offer its own separate healthcare plan to certain non-career employees who are ineligible for FEHB. For the years ended September 30, 2018, 2017 and 2016, the Postal Service incurred expenses of $131 million, $88 million and $33 million, respectively, for this plan. These amounts are included within *Compensation and benefits* under *Operating Expenses* in the accompanying *Statements of Operations*.

Active Employees

The Postal Service paid 72.8%, 73.8% and 74.4% of FEHB premium costs for active employees during the years ended September 30, 2018, 2017 and 2016, respectively. The Postal Service's employer share of employee healthcare expenses (including Medicare taxes) was $5.2 billion, $5.2 billion, and $5.0 billion for the years ended September 30, 2018, 2017 and 2016, respectively, and these amounts are included within *Compensation and benefits* under *Operating Expenses* in the accompanying *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 annually contribute to the PSRHBF an amount estimated to be equal to the employer portion of FEHB insurance premiums for participating employees and their qualifying survivors, upon retirement, attributable to each eligible 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 PSRHBF 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 in retirement 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 annual amounts that were statutorily set ranging from $1.4 billion to $5.8 billion, totaling $54.8 billion, into the PSRHBF, which began paying the Postal Service's share of retiree health benefit premiums in 2017. Most federal entities and private sector businesses are not subject to this type of prefunding requirement. Because the amounts required to be paid into the PSRHBF were set by PAEA, retiree health benefits expenses during the years 2007 through 2016 may have represented more or less than the full cost of the benefits earned by Postal Service employees during those specific years.

The Postal Service remains obligated to fund the $33.9 billion in PSRHBF prefunding payments that it defaulted on for the years 2012 through 2016. Additionally, the Postal Service is obligated to fund the amortization and normal cost payments of $955 million and $3.3 billion, respectively, that it did not pay in 2017, and the amortization and normal cost payments of $815 million and $3.7 billion, respectively, that it did not pay in 2018. The Postal Service notified key stakeholders including the Executive Branch and Congress prior to each of these non-payments. PAEA contains no provisions addressing non-payments, and as of the date of this report, the Postal Service has not been assessed any resulting penalties.

The cumulative amounts of defaulted PSRHBF prefunding and normal cost payments were $42.6 billion and $38.2 billion as of September 30, 2018, and 2017, respectively, and are recorded as *Retiree health benefits* under *Current Liabilities* in the accompanying *Balance Sheets*. Given that OPM considers these amounts to be due and payable, the Postal Service continues to reflect these amounts as a current liability within *Retiree health benefits* in the accompanying *Balance Sheets*.

As required by PAEA, OPM performed an actuarial valuation for the purpose of developing a payment schedule to fund the remaining unfunded PSRHBF obligation by 2056. The Postal Service received invoices from OPM for 2018 and 2017 amortization payments of $815 million and $955 million, which were due by September 30, 2018, and 2017, respectively. As indicated above, the Postal Service recorded an expense for these amounts but did not make these payments in order to preserve liquidity to ensure that the ability to fulfill the primary universal service mission was not placed at undue risk.

Furthermore, beginning in 2017, the Postal Service is obligated to pay the estimated normal costs of retiree health benefits attributable to the service of its employees during the most recently ended fiscal year. OPM's invoices for the normal cost payments, also due by September 30, 2018, and 2017, were $3.7 billion and $3.3 billion, respectively. As indicated above, the Postal Service also recorded an expense for these amounts but did not make these payments in order to preserve liquidity to ensure that the ability to fulfill the primary universal service mission was not placed at undue risk.

The following table details retiree health benefits expense for the years ended September 30, 2018, 2017 and 2016:

(in millions)	2018	2017	2016
PSRHBF unfunded liability expense[1]	$ 815	$ 955	$ —
PSRHBF prefunding fixed amount[2]	—	—	5,800
Normal cost of retiree health benefits[3]	3,666	3,305	—
Retiree health benefits premiums[4]	—	—	3,305
Total retiree health benefits expense	**$ 4,481**	**$ 4,260**	**$ 9,105**

[1] Expense for the annual payment due by September 30, 2018, and 2017, on the unfunded liability as calculated by OPM.

[2] Expense for the annual prefunding payment to the PSRHBF due on September 30, 2016, upon which the Postal Service defaulted.

[3] Expense for the annual payment due to the PSRHBF by September 30, 2018, and 2017, as calculated by OPM, for the actuarially-determined normal cost of retiree health benefits for current employees.

[4] Expense for the amount the Postal Service incurred for its share of retiree health benefit premiums. Beginning in 2017, the PSRHBF pays the Postal Service's share of retiree health benefit premiums.

NOTE 13 - WORKERS' COMPENSATION

Postal Service employees injured on the job are covered by FECA, and the Postal Service reimburses DOL for 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. To determine the actuarial valuation of new and existing cases, 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 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 fair value of workers' compensation liability.

An independent actuary assists in determining the liability for claims arising more than 15 years ago for years 1972 through 2003. The percentage increase in payments between 15-year old claims and closure of all claims is applied to the latest 15 years' estimates directly calculated within the estimation model for both compensation and medical losses.

The liability calculation is highly sensitive to changes in discount rates. For example, a 1% increase in the discount rate would decrease the September 30, 2018, liability and related expense by approximately $1.6 billion. Similarly, a 1% decrease in the discount rate would increase the September 30, 2018, liability and related expense by approximately $2.0 billion.

The following table details the applicable discount rates for compensation and medical claims used to estimate the workers' compensation liability as of September 30, 2018, 2017 and 2016:

	2018	2017	2016
Compensation claims liability:			
Discount rate	3.10%	2.53%	1.91%
Long-term wage inflation	2.60%	2.60%	2.60%
Medical claims liability:			
Discount rate	3.10%	2.54%	1.93%
Historical medical inflation rate	3.00%	1.40%	5.50%

The Postal Service's total liability for workers' compensation was $16.4 billion and $17.9 billion as of September 30, 2018 and 2017, respectively. As of September 30, 2018 and 2017, the current portion of the liability was $1.4 billion and $1.5 billion, respectively, and the noncurrent portion of the liability was $15.0 billion and $16.4 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 *Statements of Operations*. As described above, the Postal Service pays an administrative fee to DOL, which is also considered a component of workers' compensation expense.

Included in the workers' compensation expenses are prescription drug charges of $6 million, $41 million and $173 million which are for pharmaceutical compounding costs for the years ended September 30, 2018, 2017 and 2016, respectively. During 2018, the Postal Service paid $151 million to DOL related to previously disputed charges associated with pharmaceutical compounding costs that were originally withheld from the Postal Service's October 2016 payment to DOL, and which had been included within *Workers' compensation costs* in the accompanying *Balance Sheet* at September 30, 2017. The Postal Service did not withhold any amount from its October 2017 or October 2018 payments to DOL.

DOL implemented a new pharmaceutical compounding policy in July 2016, and in October 2016, it implemented a "Letter of Medical Necessity" requirement for compound pharmaceuticals. The Postal Service recorded a $549 million benefit for the year ended September 30, 2017, largely due to these changes in rules for pharmaceutical compounding. No such benefit was recorded for the year ended September 30, 2018.

The table below details the components of workers' compensation expense for the years ended September 30, 2018, 2017 and 2016:

(in millions)	2018	2017	2016
Impact of discount rate changes	$ (1,066)	$ (1,362)	$ 1,026
Actuarial revaluation of existing cases	(205)	(1,138)	(113)
Costs of new cases	1,194	1,552	1,697
Administrative fee	81	151	72
Total workers' compensation expenses (benefit)	**$ 4**	**$ (797)**	**$ 2,682**

NOTE 14 - REVENUE FORGONE

The Postal Service is required by law to offer below-cost postage prices to certain categories of mailers, including, but not limited to, non-profit organizations, blind individuals, local newspapers, publishers of educational material, and oversees mailers of absentee voting ballots. Between 1971, when the Postal Service became independent, and 1991, Congress reimbursed the Postal Service for the revenue it had "forgone" by offering below-cost postage prices to these mailers.

The *Revenue Forgone Reform Act of 1993* (the "RFA") phased in higher postage prices for certain of these mailers, retaining "free and reduced mail" only for the blind and for overseas absentee ballots. The RFA also authorized $1.2 billion to be paid to the Postal Service in 42 annual "installment" payments of $29 million each from 1994 through 2035 as reimbursement for revenue forgone during the RFA's 1991-to-1998 phase-in period.

Installment Payments

The Postal Service has recognized the present value of the installment payments as revenue and recorded a corresponding receivable, which is reduced each year that the installment payment is received. Although the RFA authorized the reimbursement, the Postal Service must submit an appropriation request to Congress each year in order to receive the annual revenue forgone payment.

During the years 2015 and 2016, Congress appropriated and paid $29 million for each of the respective annual installments. However, for the years 2011 through 2014, and for the years 2017 and 2018, some or all of these installment amounts were not appropriated and therefore not received by the Postal Service. The total unfunded amount was $163 million as of September 30, 2018, and is included within *Receivables, net* in the accompanying *Balance Sheets*. The Postal Service includes the total past-due installments in each annual appropriations request.

Outstanding receivables associated with the installment payments were $446 million and $426 million as of September 30, 2018, and 2017, respectively. These are not expected to be paid within one year due to the prolonged appropriation process, and are therefore classified as noncurrent within *Other assets* in the accompanying *Balance Sheets*.

The Postal Service recognized interest income of $20 million, $21 million, and $22 million for the years ended September 30, 2018, 2017 and 2016, respectively, for interest imputed on the outstanding receivable for the installment payments, and this imputed interest is included within *Interest and investment income* in the accompanying *Statements of Operations*.

Free and Reduced Mail

Congress has historically appropriated funds each year to subsidize the Postal Service's costs to provide free and reduced mail, however the annual appropriation may be higher or lower than the amount the Postal Service requests. At the end of each fiscal year, any difference between the actual amount Congress appropriated and actual amounts the Postal Service incurred to provide the subsidy during prior periods is reflected through an adjustment of the following year's funding request. Likewise, the Postal Service recognizes revenue based upon the actual amounts the Postal Service incurred to provide the subsidy during the year.

For free and reduced mail, the Postal Service recognized revenue of $61 million, $48 million and $59 million for the years ended September 30, 2018, 2017 and 2016, respectively, and this is included within *Operating Revenue* in the accompanying *Statements of Operations*. As of September 30, 2018, outstanding receivables associated with free and reduced mail were $32 million, all of which were considered noncurrent. As of September 30, 2017, outstanding receivables associated with free and reduced mail were $27 million, of which $19 million was considered current and $8 million was considered noncurrent. The current portion of these receivables are reflected within *Receivables, net* in the accompanying *Balance Sheets,* and the noncurrent portion of these receivables are reflected within *Other assets* in the accompanying *Balance Sheets*.

NOTE 15 - FAIR VALUE MEASUREMENT

The Postal Service defines fair value based on 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 inputs of the fair value hierarchy. This model prioritizes observable and unobservable inputs used to measure fair value, and consists of three broad levels, as defined in the authoritative literature:

- *Level 1* inputs include unadjusted quoted prices in active markets for identical assets or liabilities as of the balance sheet date.
- *Level 2* inputs include observable data, such as quoted prices for similar assets and liabilities in active markets, quoted prices for identical or similar assets or liabilities in inactive markets, observable data, other than quoted market prices for the asset or liability (i.e., interest rates, yield curves, etc.) and inputs that are derived from, or corroborated by, observable market data.
- *Level 3* inputs include unobservable data that reflect current assumptions about the judgments and estimates that market participants would use when pricing the asset or liability. These inputs are based on the best information available, including internal data.

Considerable judgment is involved in using this model to determine estimates of fair value and, accordingly, they may not necessarily be indicative of amounts that would be realized upon disposition of a specific asset or liability.

For the years ended September 30, 2018, and 2017, no significant transfers between *Level 1* and *Level 2* assets or liabilities occurred. The carrying amounts and fair value of these items are presented for disclosure purposes only in the following table:

	2018		**2017**	
(in millions)	**Carrying Amount**	**Fair Value**	**Carrying Amount**	**Fair Value**
Revenue forgone installment receivable*	$ 446	$ 475	$ 426	$ 496
Noncurrent portion of debt	$ 2,200	$ 2,295	$ 4,900	$ 5,210

* The carrying amount is included within *Other assets* (which includes items in addition to 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 3.13% and 2.63% as of September 30, 2018, and 2017, respectively.

The noncurrent portion of debt also qualifies as a financial instrument. Because no active market exists for the Postal Service's debt with the FFB, the fair value of the noncurrent portion of this liability has been estimated using expected future payments at risk-adjusted discount rates provided by the FFB, considered *Level 3* inputs.

NOTE 16 - QUARTERLY FINANCIAL DATA (UNAUDITED)

The following table sets forth the Postal Service's unaudited *Statements of Operations* for the quarterly periods ending September 30, 2018, and 2017:

	2018			
(in millions)	**Quarter 1**	**Quarter 2**	**Quarter 3**	**Quarter 4**
Total revenue	$ 19,164	$ 17,503	$ 17,077	$ 16,916
Total operating expenses	19,666	18,806	18,536	17,437
Loss from operations	(502)	(1,303)	(1,459)	(521)
Interest income (expense), net	(38)	(32)	(30)	(28)
Net loss	**$ (540)**	**$ (1,335)**	**$ (1,489)**	**$ (549)**
	2017			
(in millions)	**Quarter 1**	**Quarter 2**	**Quarter 3***	**Quarter 4**
Total revenue	$ 19,201	$ 17,268	$ 16,675	$ 16,492
Total operating expenses	17,716	17,787	18,776	17,931
Income (loss) from operations	1,485	(519)	(2,101)	(1,439)
Interest income (expense), net	(47)	(43)	(39)	(39)
Net income (loss)	**$ 1,438**	**$ (562)**	**$ (2,140)**	**$ (1,478)**

ITEM 9. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE

None.

ITEM 9A. CONTROLS AND PROCEDURES

DISCLOSURE CONTROLS AND PROCEDURES

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 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 Chief Financial Officer, of the effectiveness of the design and operation of disclosure controls and procedures as of September 30, 2018. Based upon and as of the date of the evaluation, the Postmaster General and Chief Financial Officer concluded that our disclosure controls and procedures were effective.

CHANGES IN INTERNAL CONTROL OVER FINANCIAL REPORTING

There were no changes in our internal controls over financial reporting during the quarter ended September 30, 2018, that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

MANAGEMENT'S REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING

Our management is responsible for establishing and maintaining adequate controls over financial reporting. Internal control over financial reporting is a process to provide reasonable assurance regarding the reliability of our financial reporting for external purposes in accordance with GAAP. Internal control over financial reporting includes maintaining records that, in reasonable detail, accurately and fairly reflect our transactions, providing reasonable assurance that transactions are recorded as necessary for the preparation of our financial statements, providing reasonable assurance that receipts and expenditures of assets are made in accordance with management authorization and providing reasonable assurance that unauthorized acquisition, use, or disposition of assets that could have a material effect on our financial statements would be prevented or detected on a timely basis. Because of its inherent limitations, internal control over financial reporting is not intended to provide absolute assurance that a misstatement of our financial statements would be prevented or detected.

Management conducted an evaluation of the effectiveness of our internal control over financial reporting based on the framework in *Internal Control – Integrated Framework (2013)* issued by the Committee of Sponsoring Organizations of the Treadway Commission. Based on this evaluation, management concluded that our internal control over financial reporting was effective as of September 30, 2018.

Ernst & Young LLP, an independent registered public accounting firm, has audited our financial statements and issued an attestation report on our internal control over financial reporting as of September 30, 2018, a copy of which appears on the following page.

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Temporary Emergency Committee of the Board of Governors of the United States Postal Service

Opinion on Internal Control over Financial Reporting

We have audited the United States Postal Service's internal control over financial reporting as of September 30, 2018, based on criteria established in Internal Control - Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (2013 framework) (the COSO criteria). In our opinion, the United States Postal Service maintained, in all material respects, effective internal control over financial reporting as of September 30, 2018, based on the COSO criteria.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States) (PCAOB), the auditing standards generally accepted in the United States of America, and the standards applicable to financial audits contained in *Government Auditing Standards*, the balance sheets of the United States Postal Service as of September 30, 2018 and 2017, the related statements of operations, changes in net deficiency, and cash flows for each of the three years in the period ended September 30, 2018 and the related notes and our report dated November 14, 2018 expressed an unqualified opinion thereon that included an explanatory paragraph regarding the United States Postal Service's ability to generate sufficient cash flow to meet all of its financial obligations throughout their fiscal year ending September 30, 2019.

Basis for Opinion

The United States Postal Service's management is responsible for maintaining effective internal control over financial reporting, and for its assessment of the effectiveness of internal control over financial reporting included in the accompanying Management's Report on Internal Control over Financial Reporting. Our responsibility is to express an opinion on the United States Postal Service's internal control over financial reporting based on our audit. We are a public accounting firm registered with the PCAOB and are required to be independent with respect to the United States Postal Service in accordance with the U.S. federal securities laws and the applicable rules and regulations of the Securities and Exchange Commission and the PCAOB.

We conducted our audit in accordance with the standards of the PCAOB and in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects.

Our audit included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, testing and evaluating the design and operating effectiveness of internal control based on the assessed risk, and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

Definition and Limitations of Internal Control Over Financial Reporting

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

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

/s/ Ernst & Young LLP

Tysons, Virginia
November 14, 2018

ITEM 9B. OTHER INFORMATION

None.

PART III

ITEM 10. DIRECTORS, EXECUTIVE OFFICERS AND CORPORATE GOVERNANCE

BOARD OF GOVERNORS

We are governed by an eleven-member Board which generally consists of our Postmaster General, Deputy Postmaster General and nine independent Governors. The Governors are appointed by the President with the advice and consent of the Senate. Two Governors currently sit on our Board:

Name, Age and Term of Office	Positions and Experience
Robert M. Duncan, Chairman of the Board of Governors, Age 67 Governor since August 2018. Term expiring December 2018.	Member of the Board of Governors since August 2018. Chairman of the Board of Governors and Vice Chairman of the Temporary Executive Committee since September 2018. Chairman of the Compensation and Management Resources Committee and Chairman of the Audit and Finance Committee. Chairman of the board of trustees at Alice Lloyd College. Former Chairman of the Board of Directors of the Tennessee Valley Authority. Former Chairman of the Republican National Committee.
David C. Williams, Vice Chairman of the Board of Governors, Age 71 Governor since August 2018. Term expiring December 2019.	Member of the Board of Governors since August 2018. Vice Chairman of the Board of Governors and Chairman of the Temporary Executive Committee since September 2018. Member of the Audit and Finance Committee. Former Inspector General of the Postal Service. Former Vice Chair of the Government Accountability and Transparency Board.

TEMPORARY EMERGENCY COMMITTEE

As referenced throughout this report, the Board is currently without a statutory quorum due to the failure of the Senate to act on past nominations for the Board. Given the loss of a statutory quorum, we filed a Federal Register notice that was published on December 16, 2014, which advised the public of actions taken during the November 2014 Board meeting to ensure that we continue to operate, notwithstanding the loss of a statutory Board quorum. During the November 2014 meeting, the Board adopted a resolution establishing the TEC, composed of the remaining members of the Board, to exercise those powers reserved to the Board that are necessary for continuity of operations.

The Governors also issued a resolution regarding the exercise of the powers vested solely in the Governor(s), as distinguished from the Board. The resolution clarifies that the inability of the Board to constitute a quorum does not inhibit or affect the authority of the Governor(s) then in office to exercise those powers vested solely in the Governor(s), upon the concurrence of an absolute majority of the Governor(s) then in office. For ease of use, references to the "Board" or the "Board of Governors" encompass the TEC as appropriate.

AUDIT AND FINANCE COMMITTEE

The Audit and Finance Committee is composed of Governor Duncan (Chair) and Governor Williams (member). The Board has determined that each of these Governors qualifies as an "audit committee financial expert" as defined by the rules of the SEC. All Audit and Finance Committee members are independent as defined by the rules of the SEC.

COMPENSATION AND MANAGEMENT RESOURCES COMMITTEE

The Compensation and Management Resources Committee ("Compensation Committee") is composed of Governor Duncan (Chair), Governor Williams (Member) and Postmaster General Brennan (member).

EXECUTIVE OFFICERS

We had eight executive officers as of September 30, 2018, as per the schedule below:

Name and Age	Positions and Experience
Megan J. Brennan Age 56	74th Postmaster General, Chief Executive Officer and a member of the Board since February 2015; Vice Chairman of the Board since December 2015. Chief Operating Officer and Executive Vice President from December 2010 to February 2015. Previously, Vice President, Eastern Area Operations from December 2006 to December 2010, and Vice President, Northeast Area Operations from April 2005 to December 2006.
Ronald A. Stroman Age 66	20th Deputy Postmaster General and Government Relations Officer and member of the Board since April 2011. Served as Staff Director, Committee on Oversight and Government Relations at the U.S. House of Representatives, from 2009 to April 2011. Prior to this, served as Managing Director, Office of Opportunity and Inclusiveness, U.S. General Accounting Office, from 2001 to 2009.
David E. Williams Age 54	Chief Operating Officer and Executive Vice President since February 2015. Previously, Vice President, Network Operations from December 2006 to December 2010, and Vice President, Engineering from April 2005 to December 2006.
Kristin A. Seaver Age 50	Chief Information Officer and Executive Vice President since April 2016. Previously, Vice President, Capital Metro Area Operations from October 2013 to April 2016. Prior to that, served as Area Manager, Operations Support in the Northeast Area from October 2011 to 2013 and Area Manager, Operations Support in the Eastern Area from June 2007 to September 2011.
Joseph Corbett Age 59	Chief Financial Officer and Executive Vice President since 2009 (except for a brief period from June 20 through September 30, 2012, when he served as Acting Chief Information Officer and Executive Vice President). Founder and Managing Director of FinSol, LLC, a finance and accounting CFO services firm from 2005 to 2009. Consultant, Chief Financial Officer and Executive Vice President of BearingPoint, Inc., a U.S. government contracting, consulting, and systems integration company, from 2004 to 2005. Executive Vice President and Chief Financial Officer of Intelsat, Ltd., from 1998 to 2004 and Intelsat Controller from 1995 to 1998.
Jacqueline Krage Strako Age 52	Acting Chief Customer and Marketing Officer and Executive Vice President since February 2018. Previously, Great Lakes Area Operations Vice President from February 2012 to February 2018. Prior to that, served as Area Manager, Operations Support for Great Lakes from April 2006 to February 2012 and Area Finance Manager from December 2000 to April 2006.
Thomas J. Marshall Age 56	General Counsel and Executive Vice President since May 2013. Previously, Deputy General Counsel from March 2009 to May 2013. Prior to that, Managing Counsel, Civil Practice, from February 2004 to March 2009.
Jeffrey Williamson Age 43	Chief Human Resources Officer and Executive Vice President since March 2013. Previously, Vice President, Pricing from June 2012 to March 2013. Postal Service MIT Sloan Fellow Representative from May 2011 to June 2012. Manager, Performance and Field Operations from September 2009 to May 2011. Prior to that, Manager, Network Development and Support from October 2006 to September 2009.

CODE OF ETHICS

All of our employees are required to comply with the Standards of Ethical Conduct for Employees of the Executive Branch ("Standards"). The Standards are published in the Code of Federal Regulations ("CFR") at *5 CFR Part 2635* and cover prohibitions and restrictions on the acceptance of gifts, conflicting financial interests, the obligation of all employees to perform their duties impartially, restrictions on the misuse of government positions, restrictions on certain outside activities and other related ethical obligations.

Our employees are also covered by a set of additional restrictions that apply only to Postal Service employees. These "Supplemental Standards" can be found at *5 CFR Part 7001* and focus on limitations on outside employment and outside business activities that could give rise to a conflict with their official duties.

The Standards and the Supplemental Standards contain many examples to help employees identify and resolve ethical issues. New employees receive ethics training at their orientation and ethics officials provide training throughout the year as required by law and as otherwise deemed appropriate. To ensure that all of our employees can receive timely and accurate ethics advice, we have established a dedicated ethics telephone helpline and an email address that is managed by ethics specialists.

Certain high-level employees are also subject to the Senior Financial Managers' Code of Ethics. This Code of Ethics can be found on our website at: *http://about.usps.com/who-we-are/financials/senior-financial-managers-code-of-ethics-07-29-2016.pdf*.

ITEM 11. OFFICER COMPENSATION

COMPENSATION DISCUSSION AND ANALYSIS

The Board establishes officer compensation and benefits, subject to the requirements and limitations of federal law. The Board has delegated to its Compensation Committee authority for initial review of management proposals related to compensation benefits for the officers. The Compensation Committee makes recommendations to the full Board for its review and approval.

Between December 8, 2016, and August 30, 2018, the Postal Service did not have any Governors, therefore the Compensation Committee did not meet. The TEC performed the functions of the Compensation Committee to the extent necessary for the continuity of operations, including functions pertaining to officer compensation for 2018.

Set forth in Title 39 of the U.S. Code, federal law provides that compensation and benefits for all of our officers shall be comparable to the compensation and benefits paid for comparable levels of work in the private sector of the economy. We are the second largest civilian employer in the nation, with approximately 634,000 employees as of the end of 2018. We operate approximately 233,000 motor vehicles and approximately 31,000 retail units. In 2018, we delivered 146.4 billion pieces of mail, 47% of the world's mail, and generated nearly $71 billion in revenue. In 2018, we ranked 123rd in *Fortune* magazine's listing of *Fortune Global 500* companies. By way of comparison, two of our largest competitors ranked 138th and 155th on this list. If we were listed on the *Fortune 500* annual ranking of America's largest corporations, we would be ranked 40th. The same two of our largest competitors are ranked 44th and 50th on that list.

Comparably sized companies typically provide their top executives with annual salaries well in excess of $1 million and total compensation and benefits valued at several million dollars. These compensation packages typically consist of annual and long-term performance incentives, including a combination of cash payments and stock options and a number of benefits and perquisites.

Although our governing law provides that officers and others should be compensated at a level comparable to the private sector, the law does not afford the Board or the Governor(s) the tools to achieve this standard of compensation. Compensation for our officers remains significantly below that of similarly-ranked senior executives in the private sector.

The law imposes three different compensation caps. The first cap provides that no officer or employee may be paid compensation "at a rate in excess of the rate for level I of the Executive Schedule under *Section 5312* of Title 5" of the U.S. Code *39 U.S.C. §1003(a)*. In calendar year 2018, the upper limit on federal salaries rose 1.4% to $210,700.

With the approval of the Board, we may develop a program to award a bonus or other reward in excess of the compensation cap discussed above, as long as the total compensation paid to the officer in a year does not "exceed the total annual compensation payable to the Vice President [of the United States] under [*3 U.S.C. §104*] as of the end of the calendar year in which the bonus or award is paid." *39 U.S.C. §3686(a)-(b)*. In calendar year 2018, this cap rose 1.4% to $243,500. The Board may approve a program allowing for bonuses or other rewards if it determines, for the annual appraisal period involved, that the performance appraisal system for impacted employees makes meaningful distinctions based on relative performance.

In addition, the Board may allow up to 12 of our officers or employees in critical senior executive or equivalent positions to be paid total annual compensation up to "120 percent of the total annual compensation payable to the Vice President [of the United States] under [*3 U.S.C. §104*] as of the end of the calendar year in which such payment is received." *39 U.S.C. §3686(c)*. Based on the Vice President's salary for calendar year 2018, the compensation cap for calendar year 2018 was $292,200.

By law, our employees, including officers, are entitled to participate in either CSRS or FERS, depending on when their federal employment began. As applicable to our officers, these retirement systems are described later in this *Compensation Discussion and Analysis*. In addition, in order to remain competitive with comparable employment in private industry and other parts of the U.S. government, our policy also authorizes certain additional benefits our officers. Other than changes required by law, the Board must authorize increases to benefits for officers.

COMPENSATION PHILOSOPHY AND OBJECTIVES

The Board recognizes that a significant disconnect exists between the comparability requirement and the compensation caps in the law governing us and that the various compensation caps do not enable the Board to provide compensation and benefits for our officers that are fully comparable to those in the private sector. This is especially true given our current financial challenges. The Board also recognizes that many of the compensation and benefit tools available in the private sector, such as equity ownership, are not available to us, given our status as a U.S. government agency. These limitations make it more difficult for us to competitively recruit in the marketplace for officers and to retain current officers. We have taken significant steps, described elsewhere in this report, to reduce costs and generate revenue. However, we have sought and continue to need significant legislative and regulatory change in order to have greater flexibility to reduce costs, generate new revenue and return to financial stability.

In an attempt to achieve some level of comparability within the confines of the law, the Board designed a compensation system intended to balance an officer's annual salary with the ability to earn additional compensation by meeting performance goals and objectives; however, because of the compensation caps discussed above, a portion of this compensation might need to be deferred.

At the start of calendar year 2018, the compensation system operated pursuant to its terms, and eligible officers received an increase in their basic compensation and a performance lump-sum payment. Increases in basic compensation in calendar year 2018 were dependent upon fiscal year 2017 performance, and averaged 1.45%. The amount of the performance lump-sum payments issued in calendar year 2018 was also based upon fiscal year 2017 performance, and averaged 1.61%. However, uncertainty about future payments and the viability of the compensation system continues to negatively impact our ability to retain and recruit talented employees, including officers.

Within the confines of its legislative authority and our financial constraints, the Board's compensation philosophy is that:

- Individual officer compensation should be strongly connected to our performance on a number of dimensions, including service, net income and productivity;
- Compensation and benefits should be designed to attract and retain high-performing officers to ensure that we have the caliber of officers who will enable us to operate at the highest levels of performance and productivity;
- Lump-sum incentives should be set to motivate officers to improve performance continuously on a long-term basis and to perform above the annually-established goals and objectives. If individual performance exceeds the goals and objectives set for the year, the employee should receive additional compensation. Likewise, if overall performance falls below the annual goals and objectives, the individual could be paid less;
- A significant amount of the officer's compensation should be "at risk" and the "at-risk" amount should increase as the officer's level of responsibility increases;

- Innovation, effectiveness as an agent for change, the ability to balance day-to-day priorities and long-term strategies, and organizational value as defined by the achievement of key corporate goals and objectives should be rewarded;
- Officer compensation should be fair and equitable internally, recognizing the width and breadth of the responsibilities of our officers; and
- Officer success is defined by a number of factors, including financial returns, the quality of service we provide, the results achieved by the officer's actions to enhance the organization's efficiency and overcome challenges and whether an officer met established individual goals.

THE COMPENSATION PROGRAM

In 2007, with the assistance of an independent consulting firm specializing in officer compensation, the Compensation Committee recommended and the Board approved a salary band for the Postmaster General to be set at the legislative salary cap. In doing so, the Board's objectives were to design a compensation program that optimized the legislative flexibility granted by the PAEA, improved external marketplace competitiveness and honored legislative constraints and existing pay ranges. For the other officers, the Board set pay bands based on salary relationships of comparable officers in the external market. In general, the Board has maintained these types of pay band relationships since 2007.

The Governor(s) have authorized the Postmaster General to establish salaries for the other officers within the confines of the salary ranges established by the Governor(s). As noted above in *Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations*, after reviewing recommendations from the Postmaster General, the TEC approved the application of the PFP system according to its terms. The salary ranges for the remaining positions of the Executive Leadership Team remained the same for calendar year 2018.

In 2018, we continued to employ a national performance assessment program ("Performance Assessment") to set annual performance goals and metrics that vary among officers and are weighted to reflect appropriately the degree to which an officer is able to influence our overall performance. The annual Performance Assessment metrics and targets generally take into consideration our performance during the prior fiscal year and the particular challenges that we anticipate having to face during the following year. The Performance Assessment places emphasis on measurable financial, customer service, employee performance indicators. The Postmaster General and Deputy Postmaster General performance goals are governed by our corporate goals. These goals have not changed since the last time we had appointed Governor(s).

The officer compensation system is intended to operate as follows: the Board establishes annual PFP incentives to provide opportunities for the Postmaster General and the Deputy Postmaster General to earn enhanced compensation, directly tied to the level of their performance. The Postmaster General establishes annual PFP incentives for other officers, to provide them opportunities to earn increased compensation based upon their performance. Incentive payouts are not to be made for a particular goal if the Postal Service or the individual fails to meet minimum acceptable performance standards. The payment of PFP incentives may sometimes be deferred for future payment where required due to the compensation caps discussed above.

Our economic challenges have continued to persist over the last several years and these challenges have caused uncertainty as to whether officer salary increases or performance bonuses will be awarded on a year-to-year basis. This uncertainty is largely driven by our flawed business model which limits our ability to be financially successful, and which can only be corrected by comprehensive postal legislation and regulatory reform.

The Governor(s) in the past have repeatedly stated that our economic challenges must be remedied in the near future, and are concerned that if this situation continues much longer, it will further erode our ability to retain highly-qualified individuals as officers and to recruit the best qualified individuals from the marketplace, if external hiring is deemed to be the best solution to fill critical officer vacancies. Additionally, our financial constraints, which largely are the products of structural defects that only Congress can remedy, have prevented us from fully complying with the statutory mandate that our officers be paid in a manner comparable with their private-sector counterparts.

We continued to use the Performance Assessment process to measure performance during 2018. Performance Assessment performance goals and rewards fall into several categories that an officer may directly influence, such as service, efficiency, safety and productivity, as well as those that are more susceptible to being impacted by general economic conditions, such as revenue generation.

For each goal, the Postmaster General establishes indicators identifying the type of performance that will enable us to achieve or surpass the goal. These indicators are aligned at the corporate, functional and individual levels and are weighted. The higher an individual's position is in the organization, the more his or her PFP goals will be tied to our overall corporate performance. The officers' goals are aligned with national performance goals and linked to our overall success.

Once the goals and indicators are established, officers are advised as to what is expected of them in terms of performance during the year, how their performance will impact us, and, in years when incentives are authorized, the potential level of performance-based incentives they can expect depending on their individual performance and our performance as a whole. Under this program, an individual officer can receive a numerical rating within a range of 1 to 15 depending on how we perform on the corporate indicators and the individual's performance, as determined by the Postmaster General.

The system is designed to operate as follows: an individual officer's performance rating would make the officer eligible for an increase to base salary, as well as for a performance-based lump-sum payment. Due to statutory cap limitations, increases to the maximum of the salary range for officers would generally follow the percentage increase in the applicable statutory cap for any given year. Any salary increases for officers are limited by these maximums and are solely performance based, as determined by the Postmaster General. Lump-sum incentive payments would be tied to the Postmaster General's rating of the officer's performance, based on the degree to which the individual achieved previously set individual goals and metrics. The Postmaster General's discretion on PFP incentives for officers in a given year is limited by our overall performance on Performance Assessment goals and metrics. Generally, officer performance scores must average to our overall Performance Assessment performance score for the fiscal year. Salary increases, if any, are generally determined after the end of the fiscal year, and any new salaries become effective for the following calendar year.

COMPONENTS OF OFFICER COMPENSATION AND BENEFITS

Base Salary

Base salaries provide a level of financial security that is appropriate for the officer's position within the Postal Service. Within the confines of law and our difficult financial condition, base salaries are to be scaled within pay ranges designed to be competitive with the market median. As discussed above, maximum payouts in a given year are set by federal law. Officer salaries are reviewed at least annually and adjusted, as appropriate and when permitted by financial constraints, to reflect individual performance, range of responsibilities, value and contribution to the organization, and experience.

Annual Incentive

Annual incentives serve as a mechanism for adjusting total compensation levels commensurate with the attainment of planned results, thereby ensuring affordability and appropriate performance that benefits us. As discussed above, we use the Performance Assessment to set annual corporate performance goals and metrics. The Governors set the goals and indicators for the Postmaster General and the Deputy Postmaster General, and the Postmaster General establishes goals and indicators for the other officers. The Postmaster General's and the Deputy Postmaster General's performance is determined based on the degree to which they have achieved previously set goals and metrics. Likewise, officer's individual performance ratings are determined by the Postmaster General based on the degree to which the individual has achieved the previously set goals and metrics.

Other Compensation Incentives

Officers are also eligible for recognition awards for specific activities that reflect a high degree of leadership. The TEC did not authorize the Postmaster General to specify a budget for awards to officers for exceptional accomplishments during 2018. Officers are eligible for recruitment, relocation and retention incentives designed to attract and retain highly talented and marketable individuals in key positions. Payments of some of these incentives may be deferred, in whole or in part, due to the compensation limits imposed on our employees as more fully discussed above.

Retirement Annuities

Officers are covered either by CSRS or FERS. Both systems have a defined benefit component and a defined contribution component. CSRS and FERS service is creditable for Medicare coverage. FERS service is creditable for Social Security.

CSRS Defined Benefit

The CSRS Basic Benefit annuity is based on a percentage of the high-3 salary multiplied by years of service. The percentage is 1.5% for the first five years of service, plus 1.75% from five years to ten years of service and 2% for all years of service thereafter. Optional retirement thresholds are age 55 with 30 years of service, age 60 with 20 years of service, and age 62 with five years of service, with a requirement of completing at least five years of creditable civilian service. The annuity is fully indexed to the Consumer Price Index ("CPI"). Disability, early retirement, deferred and survivor benefits are available.

FERS Defined Benefit

The FERS Basic Benefit annuity is based on 1.0% of high-3 salary per year of service, or 1.1% for retirement at age 62 with at least 20 years of service. Optional retirement thresholds are the Minimum Retirement Age ("MRA") of 55 to 57 (depending birth year) with 30 years of service, age 60 with 20 years of service, age 62 with five years of service, or MRA with ten years of service (at a reduced benefit), with a requirement of completing at least five years of creditable civilian service. Employees who retire at MRA with 30 years of service, or at age 60 with 20 years of service, receive a retirement supplement approximating the value of Social Security benefits attributable to federal service; this benefit is paid until age 62. Beginning at age 62, the annuity is indexed to CPI, fully when the CPI increase is 2% or less, at 2% when the CPI increase is between 2% and 3%, and at CPI minus 1% when the CPI is at least 3%. Disability, early retirement, deferred and survivor benefits are available.

Defined Contribution

The TSP has a component that mirrors traditional 401(k) plans and an option similar to "Roth" plans. CSRS and FERS employees may contribute up to the indexed IRS maximum ($18,500 in calendar year 2018). We do not make TSP contributions for CSRS employees. For FERS employees, we make an automatic contribution of 1% of basic pay and match a percentage of employee contributions for up to an additional 4% of basic pay, for a total employer contribution of up to 5% of basic pay. Employees who will be at least age 50 in the year of contribution may make a separate catch-up contribution up to the indexed IRS maximum ($6,000 in calendar year 2018). TSP investment options are a government securities fund; index funds that track the Barclays Capital Aggregate Bond Index, the S&P 500, the Dow Jones U.S. Completion TSM Index, and the Morgan Stanley Capital International EAFE (Europe, Australasia and Far East) stock index; and lifecycle funds.

Supplemental Nonqualified Deferred Compensation

Where appropriate and on a highly selective basis, we have offered supplemental nonqualified deferred compensation as a recruitment or retention tool.

Life Insurance

Officers are entitled to *Basic* group life insurance coverage under the Federal Employees Group Life Insurance ("FEGLI") program in the amount of their annual basic salary, rounded up to the next $1,000, plus $2,000. If *Basic* coverage is held, an officer will also receive an additional $10,000 coverage (*Option A*) and *Option B* coverage up to three times their salary. We pay all premiums for *Option A*, *Option B* and *Basic* coverage.

At their own expense, officers may elect additional *Option B* coverage in an amount equal to two times their salary, or *Option C*, family optional insurance coverage, of up to five multiples of $5,000 for their spouse and $2,500 for each eligible dependent child under age 22. Officers continuously covered under FEGLI for the five years of service immediately preceding retirement, or since the first opportunity to enroll, may continue coverage during retirement (if entitled to an immediate annuity). We pay retired officers an actuarially determined lump sum to cover the cost of *Option A* premiums during retirement.

Health Benefits

We participate in FEHB, which allows all career employees to enroll in one of a number of *Self-Only*, *Self-Plus-One* or *Self and Family* health benefit plans offered. We pay a portion of the cost of the premium for our officers and executives. In 2018, our share of the premium was 72% of the federal weighted average premium, limited to not more than 75% of the total premium for any given plan, and enrolled officers and executives paid the balance of the premium for the plan they selected. Employees who retire with immediate entitlement to an annuity are eligible to continue FEHB coverage into retirement, as long as they have participated in FEHB for the five years preceding their retirement or since their first opportunity to enroll.

Other Benefits

To remain competitive in the marketplace, we offer the following additional benefits to our executive officers: periodic physical examinations or *Wellness* reimbursement incentive, parking, financial planning, retirement counseling services and membership in up to two airline clubs per year. In November 2015, the Governors, in connection with their annual review of the compensation and benefits for the Postmaster General and Deputy Postmaster General, clarified and updated their policies to provide that the Postmaster General and Deputy Postmaster General are entitled to a separation payment in an amount of one year's salary if either is asked to separate from the Postal Service for any reason other than cause and they are otherwise not eligible for immediate retirement (not including early retirement, discontinued service retirement, or retirement at the minimum retirement age with less than 30 years of service). Severance may be paid in a single lump-sum payment or in bi-weekly payments following the date of separation from the Postal Service.

COMPENSATION AND MANAGEMENT RESOURCES COMMITTEE REPORT

The Compensation Committee has reviewed and discussed the *Compensation Discussion and Analysis* with management, and, based on such review and discussions, the Compensation Committee recommended to the Governors that this *Compensation Discussion and Analysis* be included in this report.

The Compensation Committee
Robert M. Duncan, Chair
David C. Williams
Megan J. Brennan

SUMMARY COMPENSATION TABLE

The following represents the compensation of our five most highly compensated executive officers ("named executive officers"):

Name and principal position	Fiscal year	Salary[2]	Bonus[3]	Non-equity incentive plan compensation[4]	Change in pension value and non-qualified deferred compensation earnings[5]	All other compensation	Total
Megan J. Brennan, *Postmaster General & Chief Executive Officer*	2018	$ 290,565	$ —	$ 11,505	$ 329,008	$ 31,726	662,804
	2017	286,979	—	49,917	213,375	28,146	578,417
	2016	286,137	—	—	590,846	27,801	904,784
Joseph Corbett, *Chief Financial Officer & Executive VP*	2018	259,280	3,105	35,000	98,178	21,584	417,147
	2017	256,413	1,315	45,578	78,514	22,130	403,950
	2016	258,195	—	35,000	45,908	21,269	360,372
Kristin A. Seaver, Chief Information *Officer & Executive VP*	2018	258,725	3,105	10,932	227,275	20,614	520,651
	2017	253,087	1,315	15,359	183,569	17,893	471,223
	2016	229,690	771	7,500	86,978	17,392	342,331
Ronald A. Stroman, Deputy Postmaster General & Chief Government Relations Officer	2018	269,404	3,115		327,169	16,096	615,784
	2017	263,516	1,315	16,184	189,455	14,065	484,535
	2016	264,677	—	—	27,501	14,237	306,415
David E. Williams Jr., *Chief Operating Officer & Executive VP*	2018	258,725	3,115		306,415	20,628	588,883
	2017	253,087	1,315	19,198	542,982	19,754	836,336
	2016	251,173	10,000	—	115,441	19,282	395,896

[1] Ms. Seaver was appointed Chief Information Officer and Executive VP as of April 16, 2016

[2] 2016 salary includes one additional pay period of earnings due to a 27th payday which occurred on December 31, 2015.

[3] Mr. Williams received a Postmaster General's award in 2016.

[4] Amounts reflect the performance-based incentive compensation awarded to executive officers for performance in prior fiscal years. The amount shown for Mr. Corbett also reflects the lump sum performance retention payment required by his employment agreement. Any amounts that could not be paid to an executive officer, due to the compensation cap or their contract, were deferred for future payment and are also reflected in the nonqualified deferred compensation table below.

[5] Mr. Stroman participates in CSRS. Ms. Brennan, Mr. Corbett, Ms. Seaver and Mr. Williams participate in FERS. The calculation of retirement annuities under CSRS and FERS is explained in the Pension Benefits table, the associated note and in the Retirement Annuities section of Compensation Discussion and Analysis. The amounts shown for each of these individuals represent the change in annuity value from the prior year. In June 2017, the OPM Board of Actuaries adopted new economic and demographic assumptions for FERS and CSRS. The increase can also include changes in eligibility conditions that allow members to receive benefits earlier. "Nonqualified deferred compensation earnings" is defined as above-market earnings on deferred income. There were no reportable amounts of nonqualified deferred compensation earnings for the named executive officers in 2018, 2017 or 2016, with the exception of Mr. Corbett, whose above-market earnings on deferred income were $2,353 in 2018, $1,992 in 2017, and $1,647 in 2016.

GRANTS OF PLAN-BASED AWARDS

The following table presents information regarding potential non-equity incentive awards to the named officers for 2018. Whether a named officer receives an award and, if so, the amount of an award for 2018 will depend on both the Postal Service's and the individual's performance.

	Estimated future payouts under non-equity incentive plan awards			
Name	**Grant date**	**Threshold**	**Target**	**Maximum**
Megan J. Brennan	November 2018	$ 11,666	$ 34,998	$ 109,369
Joseph Corbett	November 2018	10,371	31,114	97,230
Kristin A. Seaver	November 2018	10,371	15,557	97,230
Ronald A. Stroman	November 2018	10,816	24,336	101,400
David E. Williams Jr.	November 2018	10,371	31,114	97,230

Note: The PFP program relies on a 15-point scale with clearly defined and transparent corporate goals. The PFP target in any given year is set at a rating of 6. The maximum threshold for payment is set at a rating of 15. Individual ratings vary but the corporate score is used as the regulator. Given our financial condition, any individual award is unlikely to exceed the target amount.

PENSION BENEFITS

The following table shows the present value of accumulated pension benefits payable to the named executive officers as of September 30, 2018:

Name	Plan name	Number of years credited service	Present value of accumulated benefit
Megan J. Brennan	FERS Annuity	32	$ 2,010,845
Joseph Corbett	FERS Annuity	9	411,953
Kristin A. Seaver	FERS Annuity	27	915,295
Ronald A. Stroman	CSRS Annuity	40	3,515,136
David E. Williams Jr.	FERS Annuity	31	1,587,691

Note: All named executive officers are eligible for CSRS or FERS. These plans are described in the *Retirement Annuities* section within *Compensation Discussion and Analysis*. The present value of the accumulated CSRS or FERS benefit represents the value of the pension over the individual's actuarial lifetime, as of September 30, 2018. Mr. Stroman participates in CSRS, and Ms. Brennan, Mr. Corbett, Ms. Seaver and Mr. Williams participate in FERS. Mr. Stroman is eligible for retirement, the calculation of which is described in the *Retirement Annuities* section within *Compensation Discussion and Analysis*. The valuation for Ms. Brennan, Mr. Corbett, Ms. Seaver and Mr. Williams assumes that they have satisfied vesting requirements for retirement; however, because of their current tenure with the Postal Service, their retirement annuities have not fully vested.

NONQUALIFIED DEFERRED COMPENSATION

The following table presents contributions to, and earnings on, the named executive officers' deferred compensation for 2018:

Name	Executive contributions in 2018[1]	Aggregate earnings in 2018[2]	Aggregate withdrawals / distributions in 2018	Aggregate balance at September 30, 2018
Megan J. Brennan	$ 11,505	$ 3,129	$ —	$ 82,495
Joseph Corbett	35,000	16,021	—	376,337

[1] This column represents amounts deferred due to the compensation cap or contract agreements. The amount shown for Mr. Corbett reflects the lump-sum performance retention payment required by his employment agreement which has been deferred.

[2] We calculate interest on deferred compensation semi-annually at 5.0% per year for Mr. Corbett per his contract, others are calculated at the Federal Long-Term Rate; 4.04% in 2018. Interest is prorated from the relevant pay period of the deferral.

POTENTIAL PAYMENTS UPON TERMINATION

The Postmaster General and all of the other named executives are subject to the standard policies governing CSRS or FERS, as described in the *Compensation Discussion and Analysis*. The present value of these CSRS and FERS benefits are found in the Pension Benefits table in the O*fficer Compensation* section of this report. The information below describes and quantifies certain compensation, in addition to that due pursuant to CSRS or FERS, that would become payable under existing plans and arrangements if the named officer's employment had terminated on September 30, 2018. Additionally, pursuant to statutes and regulations generally applicable to federal employees, the named officers would be entitled to receive the federal employer's standard contribution toward retiree health benefits, in the event they have qualifying service and participated in FEHB for the requisite period of time prior to retiring.

DEFERRED COMPENSATION

All federal employees, including our employees, are subject to annual compensation limits established pursuant to federal statutes and regulations. When amounts earned by federal employees cannot be paid because of these compensation limits, these payments are deferred until a year in which their payment would not cause total annual compensation paid to exceed the compensation limit, or the year in which an employee leaves federal service, whichever occurs first. Named officers appearing in the nonqualified deferred compensation table in the *Officer Compensation* above have deferred compensation in the amounts indicated therein. These amounts would have been paid to them in a lump sum or pursuant to their contract with us following their departure, had they ended their employment with us on September 30, 2018.

Mr. Corbett's employment agreement provides for deferred incentives linked in part to his performance. Mr. Corbett began accruing deferred performance-based compensation at the end of 2010. When Mr. Corbett concludes his employment with us, or on October 22, 2019, if that date is later than Mr. Corbett's departure from the Postal Service, his deferred compensation will be paid to him in three approximately equal annual installments.

SUPPLEMENTAL PENSION BENEFIT

The Governor(s) have not authorized a supplemental pension benefit for any officer at this time.

SEVERANCE PAYMENT

Mr. Corbett is entitled to a severance payment of $230,000, in the event that we terminate his employment for any reason other than for cause or breach of contract.

INSURANCE BENEFIT

The Governor(s) have not authorized supplemental insurance benefits for any officer at this time. The insurance benefits to which all of our officers are entitled are described above.

OUTPLACEMENT ASSISTANCE

The Governor(s) have not authorized any outplacement assistance for any officer at this time.

ACCRUED ANNUAL LEAVE
All of our employees are entitled to receive and accrue paid days off, known as annual leave. Upon their separation from the Postal Service, all employees, including the named officers, are entitled to be paid, in a lump sum, the value of all accrued annual leave. The table below shows the accrued value of the annual leave of the named executive officers as of September 30, 2018:

Name		Value of accrued annual leave
Megan J. Brennan	$	147,367
Joseph Corbett		115,679
Kristin A. Seaver		—
Ronald A. Stroman		52,000
David E. Williams Jr.		873

CEO PAY RATIO

In accordance with Section 953(b) of the *Dodd-Frank Wall Street Reform and Consumer Protection Act*, we are providing the ratio of the annual total compensation of Megan J. Brennan, our Postmaster General and CEO, to the annual total compensation of our median employee. This ratio is based on our employee and payroll records and the methodology described below.

2018 PAY RATIO
The following ratio of our Postmaster General's annual total compensation to the median employee's for 2018 is a reasonable estimate calculated in a manner consistent with applicable SEC rules.

- The annual total compensation of our Postmaster General, as reported in the *Summary Compensation Table* above, was $662,804.
- The annual total compensation of our median employee was $86,547.
- Based on this information, we estimate that the ratio of our Postmaster General's annual total compensation to that of our median employee is 8:1.

CALCULATING METHODOLOGY
SEC rules for identifying the median compensated employee and calculating the pay ratio based on that employee's annual total compensation allow companies to adopt a variety of methodologies, to apply certain exclusions and to make reasonable estimates and assumptions that reflect their employee populations and compensation practices. Other comparably sized organizations have different employee populations and compensation practices and may utilize different methodologies, exclusions, estimates and assumptions in calculating their own pay ratios. Given the uniqueness of our compensation practices, most notably the caps on compensation for our employees described in *Compensation Discussion and Analysis*, the pay ratio we reported above may significantly differ from ratios reported by comparably sized organizations.

Identify Median Employee
We identified our median compensated employee based on annual taxable wages (W-2 Box 5 or equivalent) from payroll data for calendar year 2017. For the purposes of this determination, taxable wages includes all cash compensation, including base pay, overtime pay, cash bonuses and any other taxable cash awards, before deducting retirement plan contributions or other benefits that are excluded from federal income tax.

We took the following steps to determine our median employee:

1. We used a database of career and non-career (both full-time and part-time) employees who received wages through our payroll system during calendar year 2017.
2. We excluded employees who were not receiving wages as of September 30, 2017, the end of our 2017 fiscal year, either because their employment ended before or began after that date.

The resulting number of employees for calendar year 2017 was 575,106 (not including our Postmaster General), and we identified our median employee from this population. This amount differs somewhat from the total number of employees we reported in the *Workforce Composition* section our Annual Report on form 10-K for the year ended September 30, 2017, as we have historically used employee complement figures, not payroll records, to report employee composition.

Calculate Median Employee Compensation

Once our median employee was identified, we took the following steps to determine that employee's annual total compensation:

1. To normalize our median employee's annual taxable wages for calendar year 2017 to fiscal year 2018, we adjusted this employee's annual taxable wages by a factor of 2.21% for expected payroll growth, based on OPM analysis of historical trends and current pay tables.
2. We then calculated our median employee's annual total compensation by adding to that employee's normalized annual taxable wages any non-cash components of compensation as applicable, including change in pension value, non-qualified deferred compensation earnings and other non-cash adjustments.

To calculate change in pension value for our median employee, we used Postal-Service specific demographic and salary growth assumptions. Given the differences in the nature of work performed, we calculated the change in pension value for our Postmaster General using government-wide demographic and salary growth assumptions. Other than this difference, we calculated annual total compensation of our median employee using the same methodology that we used to calculate annual total compensation of our most highly compensation executive officers, including our Postmaster General, as disclosed in the *Summary Compensation Table*.

GOVERNORS COMPENSATION

The following table presents information regarding the compensation of the Governors during 2018:

Name	Fees earned or paid in cash[1]	All other compensation	Total
Robert M. Duncan[2]	$ 4,167	$ —	$ 4,167
David C. Williams[2]	$ 3,867	$ —	$ 3,867

[1] Each Governor receives a basic stipend of $30,000 per year plus $300 per day for not more than 42 days of meetings each year.

[2] Governors Duncan and Williams were appointed in August 2018. Governor Duncan's term expires on December 8, 2018, while Governor Williams's term expires on December 8, 2019. Each governor may serve for up to one additional year until a successor is confirmed and appointed.

ITEM 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT AND RELATED STOCKHOLDER MATTERS

Not applicable. As an "independent establishment of the executive branch of the Government of the United States," we do not issue equity securities.

ITEM 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS AND DIRECTOR INDEPENDENCE

CERTAIN TRANSACTIONS

We enter into significant transactions with other government agencies, which are considered related parties for reporting purposes, as disclosed throughout this report and the financial statements. See *Item 8. Financial Statements and Supplementary Data*, *Notes to Financial Statements*, *Note 4 - Related Parties*.

DIRECTOR INDEPENDENCE

Our Governors are appointed by the President with the advice and consent of the Senate, and are independent based on the New York Stock Exchange definition of independence.

ITEM 14. PRINCIPAL ACCOUNTANT FEES AND SERVICES

Annually, the Audit and Finance Committee reviews and pre-approves the audit services to be provided by our independent auditors. The Audit and Finance Committee must approve other specific services before the independent auditors may perform such services. The Audit and Finance Committee also has delegated to the Audit and Finance Committee Chairman pre-approval authority with respect to permitted services, provided that any pre-approval decisions must be reported to the Audit and Finance Committee at its next scheduled meeting.

Audit fees totaled approximately $9.3 million and $10.2 million for the years ended September 30, 2018, and 2017, respectively. Audit fees include fees for professional services associated with the annual financial statement audit, the reviews of our quarterly reports on Form 10-Q and testing of our internal control over financial reporting. We did not incur any other fees from our independent auditors.

PART IV

ITEM 15. EXHIBITS, FINANCIAL STATEMENT SCHEDULES

(a) The following documents are filed as part of this Annual Report:

1. Financial Statements

The following consolidated financial statements of the United States Postal Service for each of the years ended and as of the periods noted are submitted in *Part II. Item 8. Financial Statements and Supplementary Data* of this report.

Description	Page
Statements of Operations for the Years Ended September 30, 2018, 2017 and 2016	53
Balance Sheets as of September 30, 2018 and 2017	54
Statements of Changes in Net Deficiency for the Years Ended September 30, 2018, 2017 and 2016	55
Statements of Cash Flows for the Years Ended September 30, 2018, 2017 and 2016	56
Notes to Financial Statements	57

2. Financial Statement Schedules

None.

All other financial statement schedules have been omitted because they are not applicable or the required information is included in the United States Postal Service's financial statements or the notes thereto.

3. Exhibits

10.1	Employment/Compensation Contract with Joseph Corbett, Chief Financial Officer (filed with the Postal Regulatory Commission on January 29, 2009, as Exhibit No. 10.1 to the Current Report on Form 8-K).
31.1	Certificate of United States Postal Service's Principal Executive Officer Adopted Pursuant to Section 302 of the *Sarbanes-Oxley Act of 2002*.
31.2	Certificate of United States Postal Service's Principal Financial Officer Adopted Pursuant to Section 302 of the *Sarbanes-Oxley Act of 2002*.
32.1	Certificate of United States Postal Service's Principal Executive Officer Adopted Pursuant to Section 906 of the *Sarbanes-Oxley Act of 2002*.
32.2	Certificate of United States Postal Service's Principal Financial Officer Adopted Pursuant to Section 906 of the *Sarbanes-Oxley Act of 2002*.

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: November 14, 2018

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

Date: November 14, 2018

Pursuant to the requirements of the *Postal Accountability and Enhancement Act of 2006*, this Report has been signed below by the following persons on behalf of the United States Postal Service and in the capacities indicated as of November 14, 2018.

Signature	Title
/s/ Robert M. Duncan Robert M. Duncan	Chairman, Board of Governors
/s/ David C. Williams David C. Williams	Governor
/s/ Megan J. Brennan Megan J. Brennan	Board Member, Postmaster General and Chief Executive Officer
/s/ Ronald A. Stroman Ronald A. Stroman	Board Member and Deputy Postmaster General
/s/ Joseph Corbett Joseph Corbett	Chief Financial Officer and Executive Vice President (Principal Financial Officer)
/s/ Cara M. Greene Cara M. Greene	Acting Vice President, Controller (Acting Principal Accounting Officer)

EXHIBIT 31.1

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 Annual Report on Form 10-K 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 a significant role in the Postal Service's internal control over financial reporting.

/s/Megan J. Brennan	Date: November 14, 2018
Megan J. Brennan	
Postmaster General and Chief Executive Officer	

EXHIBIT 31.2

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 Annual Report on Form 10-K 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 a significant role in the Postal Service's internal control over financial reporting.

/s/Joseph Corbett	Date: November 14, 2018
Joseph Corbett Chief Financial Officer and Executive Vice President	

EXHIBIT 32.1

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 Annual Report of the United States Postal Service ("Postal Service") on Form 10-K for the period ended September 30, 2018, (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.

/s/Megan J. Brennan	Date: November 14, 2018
Megan J. Brennan Postmaster General and Chief Executive Officer	

EXHIBIT 32.2

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 Annual Report of the United States Postal Service ("Postal Service") on Form 10-K for the period ended September 30, 2018, (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.

/s/Joseph Corbett	Date: November 14, 2018

Joseph Corbett

Chief Financial Officer and Executive Vice President