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

# FORM 10-Q

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

For the Quarterly Period Ended December 31, 2017

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

| | |
|---|---|
| Washington, D.C. | 41-0760000 |
| (State or other jurisdiction of incorporation or organization) | (I.R.S. Employer Identification No.) |
| 475 L'Enfant Plaza, S.W. | |
| Washington, D.C. | 20260 |
| (Address of principal executive offices) | (ZIP Code) |

(202) 268-2000
(Registrant's telephone number, including area code)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the *Securities Exchange Act of 1934* during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes ☐ No ☐ Not Applicable ☑

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes ☐ No ☐ Not Applicable ☑

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

| | | |
|---|---|---|
| Large accelerated filer ☐ | Accelerated filer ☐ | Non-accelerated filer ☐ |
| Smaller reporting company ☐ | Emerging growth company ☐ | Not Applicable ☑ |

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

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

The number of shares of common stock outstanding as of February 8, 2018: N/A

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## PART I. FINANCIAL INFORMATION

### ITEM 1. FINANCIAL STATEMENTS

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

| *(in millions)* | Three Months Ended December 31, 2017 | Three Months Ended December 31, 2016 |
|---|---|---|
| **Revenue:** | | |
| Operating revenue | $ 19,152 | $ 19,192 |
| Other revenue | 12 | 9 |
| **Total revenue** | **19,164** | **19,201** |
| **Operating expenses:** | | |
| Compensation and benefits | 12,928 | 13,019 |
| Unfunded retirement benefits amortization | 663 | 370 |
| Retiree health benefits | 1,179 | 969 |
| Workers' compensation | 266 | (1,123) |
| Transportation | 2,135 | 2,026 |
| Other operating expenses | 2,495 | 2,455 |
| **Total operating expenses** | **19,666** | **17,716** |
| **(Loss) income from operations** | **(502)** | **1,485** |
| Interest and investment income | 22 | 9 |
| Interest expense | (60) | (56) |
| **Net (loss) income** | **$ (540)** | **$ 1,438** |

## UNITED STATES POSTAL SERVICE
## BALANCE SHEETS

| *(in millions)* | December 31, 2017 | September 30, 2017 |
|---|---|---|
| | (Unaudited) | |
| **Current Assets:** | | |
| Cash and cash equivalents | $ 10,389 | $ 10,513 |
| Restricted cash | 278 | 291 |
| Receivables, net | 1,338 | 1,127 |
| Supplies, advances and prepayments | 185 | 134 |
| **Total current assets** | **12,190** | **12,065** |
| Property and equipment, net | 14,783 | 14,891 |
| Other assets | 442 | 438 |
| **Total assets** | **$ 27,415** | **$ 27,394** |
| **Current Liabilities:** | | |
| Compensation and benefits | $ 2,050 | $ 2,397 |
| Unfunded retirement benefits | 3,816 | 3,153 |
| Retiree health benefits | 39,339 | 38,160 |
| Workers' compensation costs | 1,494 | 1,513 |
| Payables and accrued expenses | 2,025 | 1,930 |
| Deferred revenue-prepaid postage | 2,159 | 2,168 |
| Customer deposit accounts | 1,212 | 1,196 |
| Other current liabilities | 1,176 | 1,210 |
| Current portion of debt | 10,600 | 10,100 |
| **Total current liabilities** | **63,871** | **61,827** |
| Workers' compensation costs, noncurrent | 15,327 | 16,397 |
| Employees' accumulated leave, noncurrent | 2,023 | 1,918 |
| Other noncurrent liabilities | 1,058 | 1,076 |
| Noncurrent portion of debt | 4,400 | 4,900 |
| **Total liabilities** | **86,679** | **86,118** |
| **Net Deficiency:** | | |
| Capital contributions of the U.S. Government | 3,132 | 3,132 |
| Deficit since 1971 reorganization | (62,396) | (61,856) |
| **Total net deficiency** | **(59,264)** | **(58,724)** |
| **Total liabilities and net deficiency** | **$ 27,415** | **$ 27,394** |

*See accompanying notes to the unaudited financial statements.*

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

| *(in millions)* | Three Months Ended December 31, 2017 | 2016 |
|---|---|---|
| **Cash flows from operating activities:** | | |
| Net (loss) income | $ (540) | $ 1,438 |
| Adjustments to reconcile net (loss) income to cash provided by operations: | | |
| Depreciation and amortization | 417 | 408 |
| (Gain) on disposals of property and equipment, net | (8) | (2) |
| (Increase) in other assets | (4) | (10) |
| (Decrease) in noncurrent workers' compensation | (1,070) | (2,502) |
| (Decrease) in noncurrent deferred appropriations and other revenue | (2) | (90) |
| Increase in other noncurrent liabilities | 103 | 157 |
| Changes in current assets and liabilities: | | |
| Receivables, net | (216) | (104) |
| Other current assets | (51) | (55) |
| Unfunded retirement benefits | 663 | 370 |
| Retiree health benefits | 1,179 | 969 |
| Payables, accrued expenses and other | (241) | 126 |
| Deferred revenue-prepaid postage, prepaid box rents and other | (37) | (38) |
| **Net cash provided by operating activities** | **193** | **667** |
| **Cash flows from investing activities:** | | |
| Purchases of property and equipment | (323) | (442) |
| Proceeds from sales of property and equipment | 8 | (3) |
| **Net cash used in investing activities** | **(315)** | **(445)** |
| **Cash flows from financing activities:** | | |
| Issuance of notes payable | 15,900 | 2,700 |
| Payments on notes payable | (15,900) | (2,700) |
| Payments on capital lease obligations and other | (15) | (20) |
| **Net cash used in financing activities** | **(15)** | **(20)** |
| Net (decrease) increase in cash, cash equivalents and restricted cash | (137) | 202 |
| Cash, cash equivalents and restricted cash at beginning of period | 10,804 | 8,330 |
| **Cash, cash equivalents and restricted cash at end of period** | **$ 10,667** | **$ 8,532** |
| **Supplemental cash flow disclosures:** | | |
| Cash paid for interest | $ 67 | $ 56 |

*See accompanying notes to the unaudited financial statements.*

## NOTES TO UNAUDITED FINANCIAL STATEMENTS

### *NOTE 1 - BASIS OF PRESENTATION*

**Interim Financial Statements**

The accompanying unaudited interim financial statements of the United States Postal Service (the "Postal Service") have been prepared in accordance with accounting principles generally accepted in the United States ("GAAP") for interim financial information and with the instructions to Form 10-Q and Rule 10-01 of the U.S. Securities and Exchange Commission ("SEC") Regulation S-X. These financial statements should be read in conjunction with the Postal Service's financial statements for the year ended September 30, 2017, included in its Annual Report on Form 10-K ("Annual Report") filed with the Postal Regulatory Commission ("PRC") on November 14, 2017, and do not include all information and footnotes which are normally included in the Annual Report. Except as otherwise specified, all references to years are to the fiscal year beginning October 1 and ending September 30, and quarters are quarters within fiscal years 2018 and 2017.

In the opinion of management, the accompanying unaudited interim financial statements reflect all material adjustments, including recurring adjustments, necessary to fairly present the financial position as of December 31, 2017, the results of operations for the three months ended December 31, 2017, and 2016, and cash flows for the three months ended December 31, 2017, and 2016. Operating results for the three months ended December 31, 2017, are not necessarily indicative of the results that may be expected for all of 2018. Mail volume and revenue are historically greatest in the first quarter of the fiscal year, which includes the holiday mailing season.

**Reclassifications**

Certain reclassifications have been made to the financial statements as of and for the three months ended December 31, 2016, to conform to the current period presentation. Specifically, certain retirement benefit expenses have been reclassified from *Compensation and benefits* and separately identified as *Unfunded retirement benefits amortization* within *Operating expenses* in the accompanying unaudited *Statements of Operations.* In addition, the liabilities associated with these retirement benefits have been reclassified from *Compensation and benefits* and separately identified as *Unfunded retirement benefits* within *Current liabilities* in the accompanying *Balance Sheets*. Corresponding reclassification occurred within *Changes in current assets and liabilities* in the accompanying unaudited *Statements of Cash Flows*. These reclassifications had no effect on previously reported operating expenses, income from operations or net income.

**Recently Issued 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 new standard outlines a single comprehensive model for entities to use in accounting for revenue arising from contracts with customers and supersedes most current revenue recognition guidance, including industry-specific guidance. The new standard may be adopted either retrospectively or on a modified retrospective basis whereby the 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.

The new standard becomes effective for the Postal Service's 2019 fiscal year (beginning October 1, 2018) and the quarters therein. The Postal Service is in the process of evaluating the impact of the standard. As of the date of this filing, the Postal Service has completed its identification of revenue streams in order to determine which streams require further analysis. The Postal Service has completed its initial scoping analysis based on the revenue streams identified and continues its contract analysis based on the five-step model as outlined in the authoritative literature.

The Postal Service is utilizing a comprehensive approach to assess the impact of the guidance on its contract portfolio by reviewing its current 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, breakage and variable consideration. The Postal Service anticipates using the modified retrospective approach, and does not currently expect the adoption of the standard to have a material impact on its financial statements.

***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 capital 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. The Postal Service has completed its initial scoping exercise and is in the process of evaluating whether embedded leases exist in its service contracts. In addition, the Postal Service has developed a plan to abstract all of the necessary information to properly account for over 23,000 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 December 31, 2017, the Postal Service had $7.6 billion of future minimum operating lease commitments that are not currently recognized on its balance sheets. Therefore, the Postal Service expects that the adoption will have a material effect on its financial statements and disclosures. These changes will be effective for the Postal Service's fiscal year 2020 (beginning October 1, 2019), with a modified retrospective adoption method to the beginning of fiscal year 2018.

***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 new 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 gift card breakage will be recognized under ASU 2014-09, referenced earlier.

ASU 2016-04 will become effective for the Postal Service's 2019 fiscal year (beginning October 1, 2018) and the quarters therein, with early adoption permitted. The Postal Service anticipates using the modified retrospective approach with a cumulative catch-up adjustment recorded to beginning retained earnings or net deficiency as of the beginning of the fiscal year the standard is effective. The standard is applicable to the Postal Service's determination of outstanding money orders and related escheatment. The Postal Service does not expect the adoption of this standard to have a material impact on its financial statements and disclosures.

## ***NOTE 2 - LIQUIDITY***

The Postal Service generates its cash almost entirely through the sale of postal products and services. The Postal Service holds its cash with the Federal Reserve Bank of New York and invests its excess cash, when available, in highly-liquid, short-term investments issued by the U.S. Department of the Treasury. As of December 31, 2017, and September 30, 2017, the Postal Service held unrestricted cash and cash equivalents of $10.4 billion and $10.5 billion, respectively.

### **Debt**

The Federal Financing Bank ("FFB"), a government-owned corporation under the general supervision of the Secretary of the Treasury, holds all of the Postal Service's debt, which consists of two revolving credit facilities totaling up to $4.0 billion and fixed-rate notes with various maturities of $11.0 billion. As of both December 31, 2017, and September 30, 2017, the aggregate principal balance of debt outstanding was $15.0 billion, the maximum borrowing amount allowed under the Postal Service's statutory debt ceiling. The Postal Service has reported $15.0 billion in outstanding debt each quarter since September 30, 2012.

The two revolving credit facilities referenced above have interest rates determined by the U.S. Department of the Treasury each business day and enable the Postal Service to draw up to $4.0 billion in total. As of December 31, 2017, and September 30, 2017, these facilities were fully drawn and were included in the current portion of debt. These annually-renewable facilities were renewed on April 20, 2017, and are scheduled to expire and be renewed in April 2018.

## Liquidity Concerns

The Postal Service is constrained by laws and regulations, including the *Postal Accountability and Enhancement Act*, Public Law 109-435 ("PAEA"), which restricts revenue sources and mandates certain expenses. Additionally, as noted above, the Postal Service has reached the maximum borrowing capacity under its statutory debt ceiling.

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 7 - Retirement Plans*. Additionally, the PAEA established the Postal Service Retiree Health Benefits Fund ("PSRHBF") and mandated certain obligations for paying the normal costs and full prefunding of retiree health benefits, obligations that are unlike those imposed on most other federal entities or private sector businesses, described in greater detail below and in *Note 8 - Health Benefits Plans*.

The Postal Service reported operating expenses of approximately $72 billion in 2017 and has incurred cumulative net losses of $65.6 billion from 2007 through December 31, 2017. The Postal Service defaulted on $33.9 billion in PSRHBF prefunding payments for the years 2012 through 2016. The Postal Service also did not make payments owed to the Office of Personnel Management ("OPM") by September 30, 2017, totaling $6.9 billion in amortization payments for CSRS, FERS and PSRHBF unfunded liabilities as well as the normal cost of retiree health benefits. The Postal Service did not make these payments in order to preserve liquidity and to ensure that its ability to fulfill its primary universal service mission was not placed at undue risk.

As a result of these losses and its liquidity concerns, the Postal Service is unlikely to have sufficient liquidity, absent legislative and regulatory change, 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, while fulfilling its statutory universal service obligation. Additionally, the Postal Service believes that continuing productivity improvements and cost reduction measures alone will not be sufficient to address the challenges presented by declining Market-Dominant volume and revenue, and that it is unlikely that revenue growth will keep pace with increased costs driven by network growth, inflationary pressures, contractual agreements, and legal mandates.

### *Business Model Challenges/Constraints*

Market-Dominant services, which account for approximately 70% 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, which currently includes a legal requirement to deliver mail six days per week, as the number of delivery points continues to grow by approximately one million per year, which further drives up delivery costs. As described above, certain employee and retiree benefit costs are mandated by law and cannot be altered without legislative change. Under current law, the Postal Service is generally unable to increase prices sufficiently to offset increased costs, and is likewise constrained by law from reducing many of its costs, or from pursuing many alternate sources of revenue.

Aside from its universal service obligation, a significant factor contributing to Postal Service losses is the ongoing decline in the volume of Market-Dominant services. 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, which has taken place over the last decade and is expected to continue. *Marketing Mail* volume has also been challenged by commercial mailers' increasing use of digital advertising. Further exacerbating losses is the increasing number of delivery points, which, when combined with the reduction in 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 3.6 pieces in 2017, a decline of approximately 35%.

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

### *Retirement Benefits Amortization and Retiree Health Benefits*

OPM periodically notifies the Postal Service regarding its revaluation of unfunded CSRS and FERS liabilities. OPM calculates these obligations using government-wide economic growth and demographic data, rather than Postal Service-specific demographics and economic assumptions. The Postal Service records these expenses as *Unfunded retirement benefits amortization* in the accompanying unaudited *Statement 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 revalue the unfunded liabilities.

In October 2017, OPM provided the Postal Service with an actuarial report which estimates that projected amortization payment amounts due September 30, 2018, will be $1.7 billion for the CSRS obligation and $917 million for the FERS obligation. The Postal Service has therefore accrued expenses of $434 million and $229 million, respectively, for the three months ended December 31, 2017, for these obligations. In October 2017, OPM issued a new rule announcing its intent to calculate future unfunded FERS retirement obligations using Postal Service-specific demographic assumptions. The new rule did not address the Postal Service's concerns regarding the use of government-wide versus Postal Service-specific economic assumptions. The Postal Service expects to receive the invoices from OPM for actual amounts due after June 2018 and these may differ from the projected amounts due to changes in discount rates, actuarial assumptions and experience as of the calculation date, in addition to the impact of the new OPM rule.

The Postal Service remains obligated to fund the amortization payments for CSRS and FERS of $1.7 billion and $917 million, respectively, which it did not pay in 2017. Given that OPM considers these amounts to be due and payable, the Postal Service has recorded them as current liabilities within *Unfunded retirement benefits* in the accompanying *Balance Sheets*.

As required by PAEA, OPM periodically 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. The Postal Service has estimated that the amortization payment amount due September 30, 2018, is $1.2 billion, and has therefore accrued an expense of $297 million for the three months ended December 31, 2017. This amount is included within *Retiree health benefits* in the accompanying unaudited *Statements of Operations,* and as a current liability within *Retiree health benefits* in the accompanying *Balance Sheets*.

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. OPM's October 2017, actuarial statement estimated that the normal cost payment amount, also payable by September 30, 2018, will be $3.5 billion. The Postal Service has therefore accrued an expense of $882 million for the three months ended December 31, 2017. This amount is included within *Retiree health benefits* in the accompanying unaudited *Statements of Operations,* and as a current liability within *Retiree health benefits* in the accompanying *Balance Sheets*.

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, as well as the amortization and normal cost payments of $955 million and $3.3 billion, respectively, that it did not pay in 2017. Given that OPM considers these payments to be due and payable, the Postal Service has recorded them as current liabilities within *Retiree health benefits* in the accompanying *Balance Sheets*.

The following table shows the composition of certain expenses related to retiree health benefits, CSRS and FERS for the three months ended December 31, 2017, and 2016, respectively:

| | Three Months Ended December 31, | |
|---|---|---|
| *(in millions)* | **2017** | **2016** |
| PSRHBF unfunded liability amortization expense[1] | $ 297 | $ 227 |
| Normal cost of retiree health benefits[2] | 882 | 742 |
| CSRS unfunded liability amortization expense[3] | 434 | 308 |
| FERS unfunded liability amortization expense[4] | 229 | 62 |
| FERS normal costs[5] | 868 | 871 |

[1] Expense for the accrual for the annual payment due to the PSRHBF by September 30 of the respective fiscal year, based on Postal Service estimates to OPM's preliminary calculations with updated discount rate assumptions.

[2] Expense for the accrual for the annual payment due to the PSRHBF by September 30 of the respective fiscal year, based on OPM projections, for actuarially-determined normal cost of retiree health benefits for current employees.

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

[4] Expense for the accrual for the annual payment due to OPM by September 30 of the respective fiscal year, based on information provided by OPM, to amortize the unfunded FERS retirement obligation. Payments are to be made in equal installments through 2046.

[5] Represents the Postal Service's employer cash contributions, which excludes employee Social Security contributions and period-end unpaid employer amounts due, for FERS employees.

**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. 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 largely eliminate the current retiree health benefits unfunded liability and substantially reduce annual amortization and normal cost payment requirements.

The Postal Service's status as an independent establishment of the executive branch that does not receive tax dollars for its operations presents unique requirements and restrictions, but also potentially mitigates some of the financial risk that would otherwise be associated with a cash shortfall. With annual total revenue in 2017 of approximately $70 billion, a financially-sound Postal Service continues to be vital to U.S. commerce.

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

***NOTE 3 - RELATED PARTIES***

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

The following table presents related-party assets and liabilities as of December 31, 2017, and September 30, 2017:

| *(in millions)* | December 31, 2017 | September 30, 2017 |
|---|---|---|
| **Related-party assets:** | | |
| Receivables and advances[1] | $ 67 | $ 47 |
| Carrying amount of revenue forgone installment receivable[2] | 431 | 426 |
| **Related-party liabilities:** | | |
| Current portion of debt | $ 10,600 | $ 10,100 |
| Other current liabilities[3] | 44,867 | 43,504 |
| Noncurrent portion of debt | 4,400 | 4,900 |
| Other noncurrent liabilities[4] | 15,349 | 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*.
[3] Amounts include CSRS, FERS and PSRHBF obligations and current workers' compensation obligations.
[4] Amounts include noncurrent workers' compensation obligations.

The following table presents related-party revenue and expenses for the three months ended December 31, 2017, and 2016:

| | Three Months Ended December 31, | |
|---|---|---|
| *(in millions)* | 2017 | 2016 |
| Related-party operating revenue[1] | $ 233 | $ 229 |
| Related-party operating expenses[2] | $ 4,217 | $ 3,693 |
| Related-party interest income[3] | $ 21 | $ 9 |
| Related-party interest expenses[4] | $ 55 | $ 50 |

[1] Included within *Operating revenue* in the accompanying unaudited *Statements of Operations*.
[2] Included within *Operating expenses* in the accompanying unaudited *Statements of Operations*.
[3] 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 unaudited *Statements of Operations*.
[4] Incurred on debt issued to the FFB, and included within *Interest expense* in the accompanying unaudited *Statements of Operations*.

## *NOTE 4 - 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 December 31, 2017, and 2016, respectively, and as of September 30, 2017, and 2016, respectively (to disclose the opening balances), that sum to the totals of the same such amounts shown in the accompanying unaudited *Statements of Cash Flows* for the three months ended December 31, 2017, and 2016:

| | December 31, | | September 30, | |
|---|---|---|---|---|
| *(in millions)* | 2017 | 2016* | 2017 | 2016 |
| Cash and cash equivalents | $ 10,389 | $ 8,196 | $ 10,513 | $ 8,077 |
| Restricted cash | 278 | 336 | 291 | 253 |
| **Total *Cash, cash equivalents and restricted cash* as shown in the accompanying unaudited *Statements of Cash Flows*** | **$ 10,667** | **$ 8,532** | **$ 10,804** | **$ 8,330** |

* The December 31, 2016, amounts were impacted by the Postal Service's decision to early adopt ASU 2016-18 *Statement of Cash Flows, Restricted Cash* during the second quarter of 2017. Adoption of the standard was considered a change in accounting principle using a retrospective application approach resulting in some reclassification for presentation purposes of *Cash, cash equivalents and restricted cash* in the accompanying unaudited *Statements of Cash Flows*.

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

### *NOTE 5 - PROPERTY AND EQUIPMENT, NET*

Assets within *Property and equipment, net* in the accompanying *Balance Sheets* are recorded at cost, which includes the interest on borrowings used to finance construction of major capital additions, less allowances for depreciation and amortization. Interest capitalized during both the three months ended December 31, 2017, and 2016, was not significant. Fixed assets are depreciated over estimated useful lives ranging from 3 to 40 years using the straight-line method.

The book values of assets classified as held for sale were approximately $15 million and $18 million as of December 31, 2017, and September 30, 2017, respectively, and are included within *Property and equipment, net* in the accompanying *Balance Sheets*.

For the three months ended December 31, 2017, and 2016, depreciation and amortization expense was $417 million and $408 million, respectively, and impairment charges were de minimis. These items are included within *Other operating expenses* in the accompanying unaudited *Statements of Operations*.

### *NOTE 6 - COMMITMENTS AND CONTINGENCIES*

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.

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 December 31, 2017, and September 30, 2017:

| *(in millions)* | **December 31, 2017** | **September 30, 2017** |
|---|---|---|
| **Current/noncurrent portions of contingent liabilities:** | | |
| Current portion[1] | $ 202 | $ 161 |
| Noncurrent portion[2] | 498 | 500 |
| **Total contingent liabilities** | **$ 700** | **$ 661** |
| **Contingent liabilities by category:** | | |
| Labor and employment matters | $ 585 | $ 549 |
| Asset retirement obligations | 54 | 54 |
| Tort matters | 57 | 54 |
| Contractual matters | 4 | 4 |
| **Total contingent liabilities** | **$ 700** | **$ 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 accruals for probable losses in the financial statements, the Postal Service also has claims which it deems reasonably possible of an unfavorable outcome, which are not accrued for in the financial statements. These ranged in amount from $200 million to $675 million at December 31, 2017, and from $200 million to $675 million at September 30, 2017. The Postal Service is from time to time involved in other litigation incidental to the conduct of its business, none of which is expected to be material to its financial condition or operations.

### *NOTE 7 - RETIREMENT PLANS*

The majority of career employees participate in one of two U.S. government defined benefit 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. The Postal Service's TSP expenses are related only to its contributions for FERS employees who participate in the TSP.

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

From 2007 to 2017, 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.

Effective January 1, 1987, FERS covers employees hired since December 31, 1983, and FERS employees are covered by an annuity, Social Security and TSP benefits. For most FERS employees, OPM has set the Postal Service's normal cost contribution rates at 13.7% of base salary for both 2018 and 2017. For FERS employees who participate in TSP, the Postal Service contributes 1% of basic pay and matches voluntary employee contributions up to an additional 4% of basic pay.

**FERS Employees' Current Year Service Expense**

The Postal Service records expenses for FERS employees' current year service consisting of FERS normal cost, Social Security and TSP contributions, each of which is included within *Compensation and benefits* in the accompanying unaudited *Statement of Operations*. The following table presents these expenses for the three months ended December 31, 2017, and 2016:

| | Three Months Ended December 31, | |
|---|---|---|
| *(in millions)* | **2017** | **2016** |
| FERS normal costs[1] | $ 868 | $ 871 |
| Social Security[2] | $ 544 | $ 536 |
| TSP | $ 271 | $ 266 |

[1] Represents the Postal Service's employer cash contributions, which excludes employee Social Security contributions and period-end unpaid employer amounts due, for FERS employees.

[2] Represents the Postal Service's Social Security contributions for FERS employees.

**CSRS and FERS Unfunded Retirement Benefits Amortization**

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

In October 2017, OPM provided the Postal Service with an actuarial report indicating the projected amortization payments due September 30, 2018, would be $1.7 billion for the CSRS obligation and $917 million for the FERS obligation. In October 2017, OPM issued a new rule announcing its intent to calculate future unfunded retirement FERS obligations using Postal Service-specific demographic assumptions. The new rule did not address the Postal Service's concerns regarding the use of government-wide versus Postal Service-specific demographic and economic assumptions. The Postal Service expects to receive the invoices from OPM for the actual amounts due after June 2018 and these may differ from the projected amounts due to changes in discount rates, actuarial assumptions and experience as of the calculation date, in addition to the impact of the new OPM rule.

The following table presents the expenses recorded for CSRS and FERS unfunded retirement benefits amortization for the three months ended December 31, 2017, and 2016:

| | Three Months Ended December 31, | |
|---|---|---|
| *(in millions)* | **2017** | **2016** |
| CSRS unfunded liability amortization expense | $ 434 | $ 308 |
| FERS unfunded liability amortization expense | 229 | 62 |
| **Total CSRS and FERS unfunded retirement benefits amortization** | **$ 663** | **$ 370** |

The amounts the Postal Service has accrued for CSRS and FERS unfunded retirement benefits but has not yet paid are recorded as a current liability within *Unfunded retirement benefits* in the accompanying *Balance Sheets*.

For the three months ended December 31, 2017, and 2016, total expenses related to multiemployer retirement plans (which includes FERS normal cost expense, CSRS unfunded retirement benefits amortization and FERS unfunded retirement benefits amortization) totaled $1.5 billion and $1.2 billion, respectively.

***NOTE 8 - HEALTH BENEFITS PLANS***

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

**Active Employees**

The Postal Service paid 73.7% and 74.2% of FEHB premium costs during the three months ended December 31, 2017, and 2016, respectively. Postal Service employee healthcare expense was approximately $1.3 billion for each of the three months ended December 31, 2017, and 2016. These expenses are included within *Compensation and benefits* in the accompanying unaudited *Statements of Operations*.

**Retirees**

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

The PAEA required the Postal Service to prefund retiree health benefits during years 2007 through 2016 by paying annual amounts 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. 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, as well as the amortization and normal cost payments of $955 million and $3.3 billion, respectively, that it did not pay in 2017. As of the date of this report, the Postal Service has not been assessed any penalties associated with these non-payments.

As required by PAEA, OPM periodically 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. The Postal Service has estimated that the amortization payment due September 30, 2018, is $1.2 billion based on preliminary calculations provided by OPM, and has therefore accrued an expense of $297 million for the three months ended December 31, 2017. This amount is included within *Retiree health benefits* in the accompanying unaudited *Statements of Operations*.

Furthermore, 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 October 2017 actuarial statement estimated the projected normal cost payment, also payable by September 30, 2018, to be $3.5 billion. The Postal Service has therefore accrued an expense of $882 million for the three months ended December 31, 2017. This amount is included within *Retiree health benefits* in the accompanying unaudited *Statements of Operations*. The Postal Service expects to receive the invoice from OPM for the actual amount due after June 2018 and this may differ from the projected amount due to changes in discount rates, actuarial assumptions and experience as of the calculation date.

The cumulative amount of PSRHBF statutorily-specified, normal cost and amortization payments the Postal Service has not made is $38.2 billion as of December 31, 2017. Given that OPM considers this cumulative amount to be due and payable, the Postal Service reflects the amount as a current liability within *Retiree health benefits* in the accompanying *Balance Sheets*.

The following table details retiree health benefits expenses for the three months ended December 31, 2017, and 2016:

| | Three Months Ended December 31, | |
|---|---|---|
| *(in millions)* | **2017** | **2016** |
| PSRHBF unfunded liability amortization expense[1] | $ 297 | $ 227 |
| Normal cost of retiree health benefits[2] | 882 | 742 |
| **Total retiree health benefits expense** | **$ 1,179** | **$ 969** |

[1] Expense for the accrual for the annual payment due to the PSRHBF by September 30 of the respective fiscal year, based on Postal Service estimates to OPM's preliminary calculations with updated discount rate assumptions.

[2] Expense for the accrual for the annual payment due to the PSRHBF by September 30 of the respective fiscal year, based on OPM projections, for actuarially-determined normal cost of retiree health benefits for current employees.

## *NOTE 9 - WORKERS' COMPENSATION*

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

### Workers' Compensation Liability

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

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 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 actuarial valuation 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 inflation rates, including long-term cost-of-living-adjustment ("COLA") rates for compensation claims, and medical rates for medical claims. These rates are updated as of the balance sheet date and factored into the model in accordance with GAAP.

The Postal Service then calculates the amount that would need to be invested at current discount (interest) rates to fully fund the future total cost of claims, and this calculated present value is the recorded value of workers' compensation liability. This liability calculation is highly sensitive to changes in discount rates. For example, a 1% increase in the discount rate would decrease the December 31, 2017, liability and related expense by approximately $1.9 billion. Likewise, a 1% decrease in the discount rate would increase the December 31, 2017, liability and related expense by approximately $2.3 billion.

The following table details the applicable discount rates for compensation and medical claims as of December 31, 2017, and September 30, 2017:

| | December 31, 2017 | September 30, 2017 |
|---|---|---|
| **Discount rates:** | | |
| Compensation claims | 2.5% | 2.5% |
| Medical claims | 2.5% | 2.5% |

As of December 31, 2017, and September 30, 2017, the Postal Service's total liability for workers' compensation was $16.8 billion and $17.9 billion, respectively. As of December 31, 2017, and September 30, 2017, the current portion of the liability was $1.5 billion and $1.5 billion, respectively, and the noncurrent portion of the liability was $15.3 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 unaudited *Statements of Operations*. In addition, the Postal Service pays an administrative fee to DOL, which is considered a component of workers' compensation expense.

The following table presents the components of workers' compensation expense (benefit) for the three months ended December 31, 2017, and 2016:

| | Three Months Ended December 31, | |
|---|---|---|
| *(in millions)* | 2017 | 2016 |
| Impact of discount rate changes | $ — | $ (1,670) |
| Actuarial revaluation of existing cases | (79) | 52 |
| Cost of new cases | 326 | 402 |
| Administrative fee | 19 | 93 |
| **Total workers' compensation expense (benefit)** | **$ 266** | **$ (1,123)** |

***NOTE 10 - FAIR VALUE MEASUREMENT***

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

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

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

For the periods ended December 31, 2017, and September 30, 2017, no significant transfers between *Level 1* and *Level 2* assets or liabilities transpired. The carrying amount and fair value of the revenue forgone installment receivable and the noncurrent portion of debt are presented for disclosure purposes only in the following table:

| | December 31, 2017 | | September 30, 2017 | |
|---|---|---|---|---|
| *(in millions)* | Carrying Amount | Fair Value | Carrying Amount | Fair Value |
| Revenue forgone installment receivable* | $ 431 | $ 501 | $ 426 | $ 496 |
| Noncurrent portion of debt | $ 4,400 | $ 4,681 | $ 4,900 | $ 5,210 |

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

The revenue forgone installment receivable qualifies as a financial instrument in accordance with authoritative literature. To calculate its fair value, the Postal Service recognizes the imputed interest it is owed as interest income and estimates the value of this receivable using the interest method, which converts future cash flows to a single discounted amount using interest rates for similar assets, which are considered *Level 2* inputs. The Postal Service then calculates the net present value of anticipated annual installment payments to be received, discounted by the 20-year U.S. Treasury Constant Maturity Rate, which was 2.58% and 2.63% as of December 31, 2017, and September 30, 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.

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

### CAUTIONARY STATEMENTS

The following *Management's Discussion and Analysis of Financial Condition and Results of Operations* and other parts of this report describe the principal factors affecting the financial results, liquidity, capital resources and critical accounting estimates of the United States Postal Service ("Postal Service," "USPS," "we," "our" and "us"). Our results of operations may be impacted by risks and uncertainties discussed here and in our Annual Report on Form 10-K for the year ended September 30, 2017 ("Annual Report") filed with the Postal Regulatory Commission ("PRC") on November 14, 2017. Such factors, many of which we cannot control or influence, may cause actual results to differ materially from those currently contemplated.

Our operating results for the three months ended December 31, 2017, are presented in accordance with accounting principles generally accepted in the United States ("GAAP"). These results are not necessarily indicative of the results to be expected for the year ended September 30, 2018, and should be read in conjunction with our Annual Report. All references to years in this report, unless otherwise stated, refer to fiscal years beginning October 1 and ending September 30. All references to quarters, unless otherwise stated, refer to quarters within fiscal years 2018 and 2017.

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

### OVERVIEW

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

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

We have successfully implemented initiatives that have reduced our costs by billions of dollars while offering broader services. However, legal restrictions on pricing, service diversification and operations restrict our ability to fully implement our strategic objectives and 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 revenue 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.

## 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.

### Three Months Ended December 31, 2017

Operating revenue for the three months ended December 31, 2017, decreased $40 million, or 0.2%, compared to the same period last year. Combined revenue from *First-Class Mail* and *Marketing Mail* declined by $557 million, or 4.8% for the three-month period on a volume decline of nearly 2.0 billion pieces. This decline in revenue was mostly offset by an increase in Shipping and Packages revenue of $505 million, or 9.3%, as we continued to see growth in this lower-margin business throughout the quarter.

Operating expenses for the three months ended December 31, 2017, increased $2.0 billion, or 11.0%, compared to the same period last year, despite a reduction in compensation and benefits expenses of $91 million. The compensation and benefits expense reduction was more than offset by an increase in workers' compensation expense of nearly $1.4 billion, compared to the same period last year, resulting from having no change in discount rates this quarter compared to an increase in discount rates during the same period last year, which generated a benefit of $1.7 billion during last year's comparable quarter. Also contributing to the increase in operating expenses was a $293 million increase in unfunded retirement benefit costs, due to revised actuarial assumptions, a $210 million increase in retiree health benefits expense driven by an increase in normal costs, and higher transportation expenses of $109 million.

These changes in revenue and expenses resulted in a net loss of $540 million for the three months ended December 31, 2017, compared to net income of $1.4 billion for the same period last year.

### Non-GAAP Controllable 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 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, and retirement expenses caused by actuarial revaluation. Controllable income should not be considered a substitute for net (loss) income and other GAAP reporting measures.

The following table reconciles our GAAP net loss (income) to controllable income for the three months ended December 31, 2017, and 2016:

| | Three Months Ended December 31, | |
|---|---|---|
| *(in millions)* | **2017** | **2016** |
| **Net (loss) income** | **$ (540)** | **$ 1,438** |
| PSRHBF unfunded liability amortization expense[1] | 297 | 227 |
| Change in workers' compensation liability resulting from fluctuations in discount rates | — | (1,670) |
| Other change in workers' compensation liability[2] | (67) | 157 |
| CSRS unfunded liability amortization expense[3] | 434 | 308 |
| FERS unfunded liability amortization expense[4] | 229 | 62 |
| **Controllable income** | **$ 353** | **$ 522** |

[1] Expense for the accrual for the annual payment due to the PSRHBF by September 30 of the respective fiscal year, based on Postal Service estimates to OPM's preliminary calculations with updated discount rate assumptions.

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

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

[4] Expense for the accrual for the annual payment due to OPM by September 30 of the respective fiscal year, based on information provided by OPM, to amortize the unfunded FERS retirement obligation. Payments are to be made in equal installments through 2046.

For the three months ended December 31, 2017, controllable income decreased $169 million from the same period last year. This decrease was largely driven by higher normal cost of retiree health benefits expenses of $140 million and higher transportation expenses of $109 million, partially offset by a reduction in compensation and benefits expenses of $91 million. These items are discussed in greater detail in *Operating Revenue and Volume* and *Operating Expenses*.

***OPERATING REVENUE AND VOLUME***

The combined categories of *First-Class Mail* and *Marketing Mail* continued to provide the majority of our revenue, despite long-term trends away from hard-copy communication to electronic media. Although this migration to electronic media has resulted in significant volume declines in *First-Class Mail* over the last decade, *Marketing Mail* volume had remained relatively steady over that same period, although *Marketing Mail* volume declined at a greater rate beginning in 2017 and continuing through the present.

The following table summarizes our operating revenue and volume for the three months ended December 31, 2017, and 2016, by each service line:

| | Three Months Ended December 31, | |
|---|---|---|
| *(in millions)* | **2017** | **2016** |
| **Operating Revenue:** | | |
| First-Class Mail[1] | $ 6,683 | $ 6,992 |
| Marketing Mail[2] | 4,448 | 4,696 |
| Shipping and Packages[3] | 5,917 | 5,412 |
| International | 838 | 770 |
| Periodicals | 338 | 361 |
| Other[4] | 928 | 961 |
| **Total operating revenue** | **$ 19,152** | **$ 19,192** |
| **Volume:** | | |
| First-Class Mail[1] | 15,248 | 15,894 |
| Marketing Mail[2] | 21,048 | 22,361 |
| Shipping and Packages[3] | 1,718 | 1,607 |
| International | 279 | 285 |
| Periodicals | 1,316 | 1,369 |
| Other[5] | 93 | 104 |
| **Total volume** | **39,702** | **41,620** |

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

[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.

For the three months ended December 31, 2017, *First-Class Mail* generated approximately 35% of operating revenue, a 1% decrease in percentage from the same quarter last year, and 38% of our volume, which was essentially unchanged compared to the same period last year. *Marketing Mail* generated approximately 23% of operating revenue, a 1% decrease in percentage from the same quarter last year, and 53% of our volume, a 1% decrease in percentage from the same quarter last year.

We continued to experience strong results in our Shipping and Packages business, as it represented approximately 31% of our revenues for the three months ended December 31, 2017, a 3% increase in percentage from the same quarter last year. Shipping and Packages generated 4% of our volume for the three months ended December 31, 2017, which was unchanged, compared to the same period last year.

We implemented price increases on certain Market-Dominant services in January 2017. We also implemented price increases on certain Competitive services in January 2016 and January 2017.

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 been active in addressing growth opportunities. We continue to concentrate on our customers' needs, increased our marketing investment, and have focused on mail and package innovation. However, our revenue growth is constrained by laws and regulations restricting the types of products, services and prices we can offer to our customers and the speed with which we can bring new products to market.

To address the long-term trend that technological changes have had on our *First-Class Mail* revenue and volume, we have focused on providing new services, innovating with *Marketing Mail*, growing our e-commerce shipping business and implementing marketing campaigns that help us grow our Shipping and Packages 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' needs.

**First-Class Mail**

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

For the three months ended December 31, 2017, *First-Class Mail* revenue decreased $309 million, or 4.4%, and volume declined 646 million pieces, or 4.1%, compared to the same period last year. The most significant factor contributing to the declining trend in *First-Class Mail* volume was the continuing migration from mail toward electronic communication and transaction alternatives.

**Marketing Mail**

*USPS Marketing Mail* (more commonly, *Marketing Mail*), presented as a mail class and a 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.* For the three months ended December 31, 2017, *Marketing Mail* revenue decreased $248 million, or 5.3%, and volume declined by 1.3 billion pieces, or 5.9%, compared to the same period last year.

*Marketing Mail* had experienced relatively stagnant volume between 2009 and 2016, although its share of the total advertising market declined somewhat due to the continued migration toward mobile and digital advertising. Although *Marketing Mail* volume declined significantly in 2017, *Marketing Mail* has generally proven to be a relatively resilient marketing channel, and its value to U.S. businesses remains strong due to healthy customer returns on investment, better data and technology integration.

Compared to the prior year, *Marketing Mail* was negatively impacted by a decline in political and election mail, which produced approximately $46 million in revenue on volume of 240 million pieces during the three months ended December 31, 2017, compared to $241 million in revenue on volume of 1.3 billion pieces for the same period last year, a period that included the 2016 general election.

In addition, *Marketing Mail* revenue was negatively impacted by the mail mix within various *Marketing Mail* services. *Marketing Mail* revenue and volume were also adversely affected by a reduction in mail advertising campaigns by certain large mailers.

*Marketing Mail* volume is somewhat reflective of the cyclical nature of the U.S. economy, although targeted advertising campaigns can stimulate demand for these services. *Marketing Mail* is also subject to intense competition. Price increases for *Marketing Mail* are generally capped at the rate of inflation because they are classified by law as Market-Dominant.

## Shipping and Packages

The following table summarizes our operating revenue and volume for Shipping and Packages for the three months ended December 31, 2017, and 2016, by each service:

| | Three Months Ended December 31, | |
|---|---|---|
| *(in millions)* | 2017 | 2016 |
| **Shipping and Packages Revenue:** | | |
| Priority Mail Services[1] | $ 2,832 | $ 2,691 |
| Parcel Services[2] | 1,893 | 1,657 |
| First-Class Package Services[3] | 969 | 848 |
| Package Services | 223 | 216 |
| **Total Shipping and Packages revenue** | **$ 5,917** | **$ 5,412** |
| **Shipping and Packages Volume:** | | |
| Priority Mail Services[1] | 306 | 302 |
| Parcel Services[2] | 906 | 827 |
| First-Class Package Services[3] | 326 | 300 |
| Package Services | 180 | 178 |
| **Total Shipping and Packages volume** | **1,718** | **1,607** |

[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 Market-Dominant 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*.

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, although the rate of growth is slowing. Volume also experienced end-to-end growth as consumers continued to utilize online shopping, which provided a surge in package volume with a record number of packages delivered during both the calendar year 2016 and 2017 holiday seasons. To accommodate this surge in volume and to avoid service disruptions during the holiday season, we increased Sunday delivery service for some of our customers in limited U.S. markets and added non-career employees for the season in accordance with our labor agreements.

### *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. While Priority Mail Services revenue continues to grow year over year, its service offerings are somewhat price sensitive, particularly with retail customers, and its growth rate is lower than some other Shipping and Packages subcategories used by commercial customers.

Priority Mail Services accounts for our largest portion of Shipping and Packages revenue, representing approximately 47.9% of the total for the three months ended December 31, 2017, compared to 49.7% for the same period last year.

For the three months ended December 31, 2017, Priority Mail Services revenue grew by 5.2% on essentially flat volume, compared to the same period last year. Revenue grew more than volume for the period due to the January 2017 price increases in certain Competitive services.

### *Parcel Services*

Our Parcel Services subcategory includes Competitive services *Parcel Select* and *Parcel Return* as well as Market-Dominant *USPS Marketing Mail Parcels* (more commonly, *Marketing Mail Parcels*). Parcel Services largely consist of "last-mile" deliveries, offered to bulk shippers or price-sensitive customers. For the three months ended December 31, 2017, revenue from Parcel Services increased by 14.2% compared to the same period last year. This subcategory showed strong volume growth of 9.6% over the same period last year, driven largely by the continuing growth of e-commerce. However, this subcategory is primarily a "last-mile" service and is one of our lowest-priced package services, and as a result, produces a lower yield piece when compared to many of our other services.

***First-Class Package Services***

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

For the three months ended December 31, 2017, First-Class Package Services revenue increased 14.3% on volume growth of 8.7%, compared to the same period last year. Revenue grew more than volume for the period due to the January 2017 price increases in certain 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 three months ended December 31, 2017, Package Services revenue increased 3.2% on volume growth of 1.1%, compared to the same period last year. Revenue grew more than volume for the period due to the January 2017 price increases in certain Competitive services.

**International Mail**

Our International Mail category includes several services that enable customers, both domestic and abroad, to send international mail, including postcards, envelopes, flats and packages with either standard or express delivery options. "Outbound" services, which allow customers in the U.S. to send mail and packages to other countries, generate approximately two thirds of International Mail revenue. However, as compared to "inbound" services, which allow foreign customers to send mail and packages to U.S. destinations, outbound volume only represents about one third of total International Mail volume.

For the three months ended December 31, 2017, International Mail revenue increased 8.8%, while volume decreased 2.1%, compared to the same period last year. The increase in revenue was largely the result of higher rates resulting from the January 2017 price increases and new Negotiated Service Agreements. We continue to experience an increase in inbound mail volume, much of that from tracked letter packets and parcels related to international e-commerce.

**Periodicals**

*Periodicals*, also presented as a mail class and a 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 three months ended December 31, 2017, *Periodicals* revenue decreased 6.4% and volume decreased by 3.9%, compared to the same period last 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 include ancillary services such as *Certified Mail*, *PO Box* services, and *Return Receipt* services. Also included in this category are money orders and passport services. For the three months ended December 31, 2017, Other services revenue decreased by 3.4%, compared to the same period last year.

This category includes our internal mail, which generated no revenue and has volume that can vary significantly from period to period. We experience our highest volume in this category during the first quarter of each year.

***OPERATING EXPENSES***

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

Our mail processing and distribution network was originally designed to provide overnight delivery service of *First-Class Mail* within specified delivery areas to a much higher volume of mail than we are required to process and deliver today, and the network's legacy capabilities are not aligned to today's mail mix and volumes. Consequently, certain of our processing and distribution facilities continue to operate at less than full capacity. Our challenge to contain costs is also compounded by the increasing number of delivery points, which, when combined with lower 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 3.6 pieces in 2017, a reduction of approximately 35%.

**Compensation and Benefits**

Compensation and benefits is our largest operating expense category. These expenses consist of costs related to our active career and non-career employees. Overall, our compensation and benefits expenses decreased 0.7% for the three months ended December 31, 2017, compared to the same period last year.

The following table presents compensation and benefits expenses for the three months ended December 31, 2017, and 2016:

| | **Three Months Ended December 31,** | |
|---|---|---|
| *(in millions)* | **2017** | **2016** |
| Compensation | $ 9,860 | $ 9,986 |
| FERS employees' current year service | 1,683 | 1,673 |
| Employee health benefits | 1,301 | 1,273 |
| Other | 84 | 87 |
| **Total compensation and benefits** | **$ 12,928** | **$ 13,019** |

***Compensation***

Compensation expense decreased 1.3% for the three months ended December 31, 2017, compared to the same period last year. The decrease was primarily due to a decrease in total work hours for the three months ended December 31, 2017, compared to the same period last year, as well as the impact of a decrease in the number of career employees at December 31, 2017, compared to the same date a year ago.

For the three months ended December 31, 2017, total work hours were approximately 304 million, which was a decrease of 1.6%, compared to the 309 million total work hours for the three months ended December 31, 2016. This reflects management's continued emphasis on holding work hours steady and increased operational efficiencies.

The number of career employees decreased by approximately 10,900, or 2.2%, at December 31, 2017, compared to the same date a year ago. The decrease in the number of career employees primarily reflects normal attrition as we continue to align our workforce with declining mail volume.

The number of non-career employees increased by approximately 4,100, or 2.8%, at December 31, 2017, compared to the same date a year ago. The additional use of both non-career employees and employees newly converted from non-career to career mitigates some of the upward wage and benefit pressures for career employees.

Beginning January 8, 2018, we extended voluntary early retirement offers to eligible mail handlers and clerks. The offers contain three retirement-effective dates from which eligible employees may choose: January 31, 2018; February 28, 2018; and March 31, 2018. We are exercising the Voluntary Early Retirement Authority ("VERA") delegated to us by OPM. This VERA action is part of ongoing efforts to right size our workforce and reposition our network to match current workloads. Employees who accept the offers will be able to retire before they reach the standard requirements for age and years of service. We are not offering separation incentives attached to this early-retirement offer. This action did not result in any impact to our financial statements for the three months ended December 31, 2017.

***FERS Employees' Current Year Service***

The majority of our career employees participate in either CSRS or FERS based on the starting date of their employment with us or another U.S. government employer. We incur normal costs for FERS employees; however, by law we do not incur normal costs for CSRS retirement benefits. Career employees may also participate in the Thrift Savings Plan ("TSP"), a defined contribution retirement savings and investment plan administered by the Federal Retirement Thrift Investment Board. Our TSP expenses are related only to our contributions for FERS employees who participate in the TSP.

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 unaudited *Statements of Operations*. We record our contributions to FERS, Social Security and TSP as an expense in the period during which the contribution is due. We recognize the expense for each period's legally required contribution, and record a liability for any contribution due and unpaid at the end of each reporting period. The 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 below and see *Item 1. Financial Statements, Notes to Unaudited Financial Statements, Note 7 - Retirement Plans*.

The following table presents the details of FERS employees' current year service expenses for the three months ended December 31, 2017, and 2016:

| | **Three Months Ended December 31,** | |
|---|---|---|
| *(in millions)* | **2017** | **2016** |
| FERS normal costs | $ 868 | $ 871 |
| Social Security | 544 | 536 |
| TSP | 271 | 266 |
| **Total FERS employees' current year service** | **$ 1,683** | **$ 1,673** |

FERS employees' current year service expenses increased 0.6% for the three months ended December 31, 2017, compared to the same period last year.

Our FERS normal cost contribution rate remained steady at 13.7% of basic pay for most participants during both fiscal 2018 and 2017. Expenses for the FERS normal costs, Social Security and employer TSP contributions were essentially flat for the three months ended December 31, 2017, compared to the same period last year. This is consistent with the general trends in the number of career employees during the comparable periods. As most of our employees participate in FERS, this was also consistent with the trends in compensation for the period, described above in *Compensation*.

***Employee Health Benefits***

Our expense for employee health benefits is most significantly impacted by the number of employees electing coverage and the premium costs of the selected plans. Our active employees may participate in the Federal Employees Health Benefits ("FEHB") Program, which 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.

Employee health benefits expense increased 2.2% for the three months ended December 31, 2017, compared to the same period last year, due to an increase in premiums for the 2017 calendar year. On average, healthcare premiums rose 5.1% for the 2017 calendar plan year, which affected the three months ended December 31, 2017, although this increase was partially offset by the lower contribution rate of healthcare premiums that we paid.

Our share of healthcare premiums for our employees represented 73.7% and 74.2% of the total healthcare premium cost for the three months ended December 31, 2017, and 2016, respectively. These decreases in our share of healthcare premium costs for employees were consistent with the terms of our contractual agreements; however, these decreases were offset by higher premium costs.

**CSRS and FERS Unfunded Retirement Benefits Amortization**

OPM periodically notifies us regarding its revaluation of unfunded CSRS and FERS retirement benefits. OPM calculates these obligations using government-wide economic growth and demographic data, rather than Postal Service-specific demographics and economic growth assumptions. The amounts we record for the expenses for our unfunded CSRS and FERS liabilities may be significantly impacted by changes in actuarial assumptions used to revalue the unfunded liabilities.

In October 2017, OPM provided an actuarial report estimating the projected amortization payment due to OPM by September 30, 2018, for CSRS unfunded retirement benefits will be $1.7 billion. As a result, we have accrued $434 million for the three months ended December 31, 2017, for this expense. We expect to receive the invoice from OPM for the actual amount due after June 2018, and the amount could differ from the projected amount due to changes in discount rates, actuarial assumptions and experience as of the calculation date.

OPM's actuarial report also estimated the projected amortization payment due to OPM by September 30, 2018, for FERS unfunded retirement benefits will be $917 million. As a result, we have accrued $229 million for the three months ended December 31, 2017, for this expense.

In October 2017, OPM issued a new rule announcing its intent to calculate future unfunded FERS obligations using Postal Service-specific demographic assumptions. The new rule did not address our concerns regarding the use of government-wide versus Postal Service-specific economic assumptions. As such, we anticipate formally requesting that OPM reconsider its use of government-wide factors and instead apply Postal Service-specific economic assumptions in calculating our unfunded liability, as we have done in previous years. As with the CSRS, we expect to receive an invoice from OPM for the actual amount due after June 2018 and the amount could differ from the projected amount due to changes in discount rates, actuarial assumptions and experience as of the calculation date.

For additional information, see *Item 1. Financial Statements, Notes to Unaudited Financial Statements, Note 7 - Retirement Plans*.

**Retiree Health Benefits**

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

In accordance with PAEA, since the beginning in 2017, the PSRHBF has been used to fund our share of retiree health benefit premiums. Also since 2017, we have been obligated to pay into the PSRHBF the normal costs of retiree health benefits attributable to the service of our employees, as well as the amortization payment for the PSRHBF unfunded liability. Our total retiree health benefits expense therefore consists of both the normal and the amortization costs. We recognize an expense when the payment is due.

For the three months ended December 31, 2017, our retiree health benefits expense increased by $210 million, or 21.7%, compared to the same period last year. Of this increase, $140 million is attributable to normal cost, and $70 million is attributable to an increase in amortization of the PSRHBF unfunded liability.

In October 2017, OPM provided a statement which estimated the amount of our projected PSRHBF normal cost payment due September 30, 2018, will be $3.5 billion. As of December 31, 2017, we had accrued $882 million for this expense, an increase from the $742 million that we accrued for the same period last year.

Also, based on preliminary calculations provided by OPM, we have projected that the PSRHBF amortization payment amount due September 30, 2018, amounts to $1.2 billion, and we have therefore accrued an expense of $297 million for this expense. We expect to receive the invoices from OPM for the actual amounts due after June 2018 and these may differ from the projected amounts due to changes in discount rates, actuarial assumptions and experience as of the calculation date.

For additional information, see *Item 1. Financial Statements*, *Notes to Unaudited Financial Statements*, *Note 8 - Health Benefits Plans*, *Retirees.*

**Workers' Compensation**

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

The following table presents the components of workers' compensation expense (benefit), including the cash payments made by DOL on behalf of workers' compensation obligations, for the three months ended December 31, 2017, and 2016:

| *(in millions)* | Three Months Ended December 31, 2017 | Three Months Ended December 31, 2016 |
|---|---|---|
| Impact of discount rate changes | $ — | $ (1,670) |
| Actuarial revaluation of existing cases | (79) | 52 |
| Cost of new cases | 326 | 402 |
| Administrative fee | 19 | 93 |
| **Total workers' compensation expense (benefit)** | **$ 266** | **$ (1,123)** |
| Less: cash payments made by DOL on behalf of workers' compensation obligations | 333 | 316 |
| **Total non-cash workers' compensation expense** | **$ (67)** | **$ (1,439)** |

For the three months ended December 31, 2017, workers' compensation expense was $266 million, compared to a benefit provided of $1.1 billion for the three months ended December 31, 2016, a net increase in expense of $1.4 billion.

For the three months ended December 31, 2017, the portion of workers' compensation expense (benefit) due to the impact of discount rate changes was zero, compared to a $1.7 billion benefit for the same period last year. These changes are the result of changes in interest rates, outside of management's control.

The combined costs of new workers' compensation cases and revaluation of existing workers' compensation cases have decreased by $207 million for the three months ended December 31, 2017, compared to the same period last year. This decrease is largely driven by the positive changes that DOL implemented in the rules associated with pharmaceutical compounding during 2017. Changes in actuarial valuation are primarily attributable to the combined impacts of routine changes in actuarial estimation, the progression of existing cases and updated cost-of-living-adjustment ("COLA") assumptions, which are largely outside of management's control.

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

For additional information, see *Item 1. Financial Statements*, *Notes to Unaudited Financial Statements*, *Note 9 - Workers' Compensation*.

**Transportation**

Transportation expense includes the costs we incur to transport mail and other products between our facilities, comprising of highway, air and international transportation contracts, plus contract delivery services. Our costs of transportation to delivery points, excluding contract delivery services, are included within *Other operating expenses.* Transportation expenses do not include the compensation of employees responsible for transporting mail and other products between our facilities.

Variations in the volume and weight of mail transported and the mode of transportation used have significant impact on transportation expenses. The components of transportation expense for the three months ended December 31, 2017, and 2016, are presented in the following table:

| | Three Months Ended December 31, | |
|---|---|---|
| *(in millions)* | **2017** | **2016** |
| Highway | $ 1,203 | $ 1,157 |
| Air | 748 | 660 |
| International | 175 | 183 |
| Other | 9 | 26 |
| **Total transportation expenses** | **$ 2,135** | **$ 2,026** |

For the three months ended December 31, 2017, transportation expense increased 5.4% compared to the same period in the prior year.

For the three months ended December 31, 2017, highway transportation expenses increased 4.0%, compared to the same period in the prior year. These increases were due primarily to higher diesel fuel prices, trailer lease costs due to new contracts and our strategic efforts to continue to improve our delivery service results, as we have increased the volume we transport via highway.

For the three months ended December 31, 2017, air transportation expenses increased 13.3% compared to the same period in the prior year, due to a combination of higher jet fuel prices, charter costs resulting from the effects of hurricanes affecting Puerto Rico and an increase in air network volume to meet package growth during peak season.

International transportation expenses are related only to outbound services that allow customers in the U.S. to send mail and packages to other countries. For the three months ended December 31, 2017, international transportation expenses decreased 4.4% primarily due to a decline in *Priority Mail International* and other international service volumes.

**Other Operating Expenses**

Other operating expenses for the three months ended December 31, 2017, and 2016, are detailed in the following table:

| | Three Months Ended December 31, | |
|---|---|---|
| *(in millions)* | **2017** | **2016** |
| Supplies and services | $ 767 | $ 770 |
| Depreciation and amortization | 417 | 408 |
| Rent and utilities | 419 | 397 |
| Information technology and communications | 205 | 196 |
| Vehicle maintenance service | 160 | 164 |
| Rural carrier equipment maintenance | 137 | 129 |
| Fuel - delivery vehicles | 122 | 96 |
| Miscellaneous other | 268 | 295 |
| **Total other operating expenses** | **$ 2,495** | **$ 2,455** |

Aside from a 27.1% increase for fuel associated with our delivery vehicles that was driven by both higher unleaded gas prices and usage, compared to the same period in the prior year, the period-over-period changes in other operating expenses for the three months ended December 31, 2017, and 2016, were relatively immaterial, increasing 1.6% overall, compared to the same period in the prior year.

## LIQUIDITY AND CAPITAL RESOURCES

We held unrestricted cash and cash equivalents of $10.4 billion and $10.5 billion as of December 31, 2017, and September 30, 2017, respectively. Our average daily liquidity balance during the three months ended December 31, 2017, was $10.4 billion, representing approximately 35 days of liquidity available, which we define as unrestricted cash plus available borrowing capacity divided by estimated average cash disbursements (including capital expenditures) per business day (usually 251 cash disbursement days per year).

### *CASH FLOW ANALYSIS*

Although our cash balances have increased since 2012, they remain insufficient to support an organization with approximately $72 billion in annual operating expenses. More significantly, this increase would not have occurred at all had we not been forced to default on $33.9 billion in legally-obligated PSRHBF prefunding payments. We also did not make payments due to OPM by September 30, 2017, totaling $6.9 billion, which included amortization payments for CSRS, FERS and PSRHBF unfunded liabilities, and the normal cost of retiree health benefits. 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.

Looking forward, our operations will require significant capital investment over the next few years to modernize and improve our processing and delivery infrastructure in order to be able to continue to meet our statutory obligation to provide prompt, efficient and reliable postal services to the nation. Furthermore, given our inability to raise cash through the issuance of additional debt, our current level of available liquidity may be insufficient to support our operations in the event of another significant downturn in the U.S. economy.

#### Operating Activities

Cash provided by operating activities decreased by $474 million, or 71.1%, for the three months ended December 31, 2017, compared to the same period last year. This decrease is primarily attributable to timing differences in payroll and its related accrual, given that a biweekly payroll disbursement took place on December 29, 2017, the last business day of the period, and to the timing of collections on certain international receivables which were not collected until after the end of the period.

#### *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 and cash flow expected to be generated by the respective increase.

| Service Category | Date Notice Filed with PRC | Effective Date of Increase | Increase % | Estimated Annual Revenue and Cash Flow ($ in millions) | |
|---|---|---|---|---|---|
| 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 and cash flow is immaterial.

#### *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 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, 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 PRC will issue a final rule after considering the comments and reply comments of any interested stakeholders. Additional information regarding the 10-year review may be found at the PRC website: www.prc.gov.

**Investing Activities**

We invested $323 million in the purchase of property and equipment for the three months ended December 31, 2017, which is a decrease of $119 million, or 26.9%, compared to the same period last year. This decrease is principally related to the timing of our capital investment purchases; however, the amount of our projected capital expenditures remains $1.8 billion for 2018.

**Financing Activities**

Except as described otherwise in this quarterly report, the nature and amounts of our payment obligations under our debt, capital and operating lease agreements, purchase commitments and other liabilities as of December 31, 2017, have not materially changed from those described in our Annual Report.

On September 30, 2012, we reported that we had reached the maximum borrowing amount allowed under our statutory debt ceiling, and the amount of debt we have reported each quarter has not changed since then. Our debt is borrowed from the Federal Financing Bank, a government-owned corporation under the general supervision of the Secretary of the Treasury, and consists of fixed-rate notes and two revolving credit facilities with various maturities with an aggregate principal balance of $15.0 billion as of December 31, 2017, and September 30, 2017.

The two revolving credit facilities have interest rates determined by the U.S. Department of the Treasury each business day and enable us to draw up to $4.0 billion in total. As of December 31, 2017, and September 30, 2017, these facilities were fully drawn and were included in the current portion of debt. These annually-renewable facilities were renewed on April 20, 2017, and are scheduled to expire and be renewed in April 2018.

***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 virtually eliminate 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 part of our rate base; and
3. Favorable outcome of the PRC's ten-year review, which would allow additional pricing flexibility.

Although we continue to inform the Administration, 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.

**2018 and Beyond**

We anticipate that given our ongoing liquidity concerns, and without legislative action and regulatory reform, we may not be able to pay all legally-required obligations and also invest in much-needed capital expenditures in 2018 and future years. Furthermore, we believe that continuing productivity improvements alone will not be sufficient to address the challenges presented by declining Market-Dominant volume and revenue, and that growth in operating revenue will unlikely be able to keep pace with increased costs.

***Legally-Required Obligations***
In addition to our previously discussed obligations for unfunded retirement and retiree health benefits due on September 30, 2018, we expect to pay the DOL approximately $1.4 billion in October 2018, representing the workers' compensation claims paid by DOL for the chargeback year July 1, 2017, to June 30, 2018, plus the estimated administrative fee.

***Capital Investments***
We currently estimate that our required cash outlays for necessary and overdue capital investments will amount to approximately $1.5 billion for the remainder of 2018, and an additional $9.4 billion for years 2019 through 2022, as we plan to invest in a new fleet of delivery vehicles and other capital expenditures. Although our future projections include these capital cash outlays, future cash flow from operations alone may not generate the cash needed to enable us to fully fund such necessary capital investments.

## LEGISLATIVE UPDATE

As a self-supporting independent establishment of the executive branch, our business model and operations are significantly influenced by congressional oversight and legislation. Additionally, we are intended 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. We have no presidentially appointed, Senate-confirmed Governors currently in office.

***LEGISLATION***
Several bills have been introduced that, if enacted, may have an impact on our financial condition. At this time, however, none of these bills have been scheduled for consideration by the full U.S. Senate or House of Representatives.

***APPROPRIATIONS***
On January 22, 2018, the House and Senate passed H.R. 195, *Making further continuing appropriations for the fiscal year ending September 30, 2018, and for other purposes*, to keep the government operating through February 8, 2018. The stopgap measure continues government funding at fiscal year 2017 levels, and continues the six-day mail delivery mandate. The measure was signed into law by the President on January 22, 2018, as Public Law 115-120.

***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. H.R. 756 continues to await action by the House Ways and Means Committee and Energy and Commerce Committee.

***BOARD OF GOVERNORS NOMINATIONS***
On October 26, 2017, the President announced the following nominations to serve on the Board of Governors of the United States Postal Service:

- Calvin R. Tucker for the remainder of a term expiring December 8, 2023.
- Robert M. Duncan for the remainder of a seven-year term expiring December 8, 2018, and an additional term expiring December 8, 2025.
- David Williams for the remainder of a seven-year term expiring December 8, 2019.

These nominations are pending consideration by the Senate Homeland Security and Governmental Affairs Committee.

## FAIR VALUE MEASUREMENTS

As required by authoritative accounting literature, certain fair value disclosures for the periods ended December 31, 2017, and September 30, 2017, are contained in *Item 1. Financial Statements*, *Notes to Unaudited Financial Statements*. We did not recognize gains as a result of valuation measurements during the three months ended December 31, 2017. All recognized losses have been incorporated into our financial statements as of December 31, 2017. See *Item 1. Financial Statements*, *Notes to Unaudited Financial Statements*, *Note 10 - Fair Value Measurement.*

## RELATED PARTY TRANSACTIONS

As disclosed throughout this quarterly report, we have significant transactions with other U.S. government entities, which are considered related parties for reporting purposes. For a more detailed description, see *Item 1. Financial Statements*, *Notes to Unaudited Financial Statements*, *Note 3 - Related Parties*.

## CRITICAL ACCOUNTING POLICIES AND ESTIMATES

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

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

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

## RECENT ACCOUNTING STANDARDS

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

## ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

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

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

We also have provisions in our debt agreements that allow us to prepay our $15.0 billion debt at any time at a price determined by the Secretary of the Treasury, based on prevailing interest rates in the U.S. Treasury market at the time of repayment.

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

## ITEM 4. CONTROLS AND PROCEDURES

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

## DISCLOSURE CONTROLS

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

We carried out an evaluation under the supervision and with the participation of management, including the Postmaster General and the Chief Financial Officer, of the effectiveness of the design and operation of disclosure controls and procedures as of

December 31, 2017. Based upon and as of the date of the evaluation, the Postmaster General and the Chief Financial Officer concluded that our disclosure controls and procedures were effective.

**INTERNAL CONTROLS**

We have made no changes in our internal control over financial reporting during the three months ended December 31, 2017, that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

## PART II. OTHER INFORMATION

### ITEM 1. LEGAL PROCEEDINGS

For a discussion of legal proceedings affecting us, please refer to *Item 1. Financial Statements*, *Notes to Unaudited Financial Statements* and *Note 6 - Commitments and Contingencies*, as well as our Annual Report.

### ITEM 1A. RISK FACTORS

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

### ITEM 6. EXHIBITS

| Exhibit Number | Description |
|---|---|
| 31.1 | Certification of Principal Executive Officer Pursuant to Rules 13a-14(a) and 15d-14(a) under the *Securities and Exchange Act of 1934*, as Adopted Pursuant to Section 302 of the *Sarbanes-Oxley Act of 2002*. |
| 31.2 | Certification of Principal Financial Officer 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*. |
| 32.1 | Certification of Principal Executive Officer Pursuant to *18 U.S.C. Section 1350*, as Adopted Pursuant to Section 906 of the *Sarbanes-Oxley Act of 2002*. |
| 32.2 | Certification of Principal Financial Officer Pursuant to *18 U.S.C. Section 1350*, as 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: February 8, 2018

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

Date: February 8, 2018

**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 quarterly report on Form 10-Q of the United States Postal Service ("Postal Service");

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the Postal Service as of, and for, the periods presented in this report;

4. The Postal Service's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the Postal Service and have:

    a. Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the Postal Service, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

    b. Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

    c. Evaluated the effectiveness of the Postal Service's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

    d. Disclosed in this report any change in the Postal Service's internal control over financial reporting that occurred during the Postal Service's most recent fiscal quarter (the Postal Service's fourth fiscal quarter in the case of an Annual Report) that has materially affected, or is reasonably likely to materially affect, the Postal Service's internal control over financial reporting; and

5. The Postal Service's other certifying officer and I have disclosed based on our most recent evaluation of internal control over financial reporting, to the Postal Service's independent registered accounting firm and the Audit and Finance Committee of the Postal Service's Board of Governors (or persons performing the equivalent functions):

    a. All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the Postal Service's ability to record, process, summarize and report financial information; and

    b. Any fraud, whether or not material, that involves management or other employees who have significant role in the Postal Service's internal control over financial reporting.

Date: February 8, 2018

/s/Megan J. Brennan

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

Date: February 8, 2018

/s/Joseph Corbett

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 Quarterly Report of the United States Postal Service ("Postal Service") on Form 10-Q for the period ended December 31, 2017, (the "Report"), I, Megan J. Brennan, certify, pursuant to *18 U.S.C. Section 1350*, as adopted pursuant to Section 906 of the *Sarbanes-Oxley Act of 2002* that:

(1) The Report fully complies with the requirements of Section 13(a) or 15(d) of the *Securities Exchange Act of 1934*; and

(2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Postal Service.

Dated: February 8, 2018

/s/Megan J. Brennan

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 Quarterly Report of the United States Postal Service ("Postal Service") on Form 10-Q for the period ended December 31, 2017, (the "Report"), I, Joseph Corbett, certify, pursuant to *18 U.S.C. Section 1350*, as adopted pursuant to Section 906 of the *Sarbanes-Oxley Act of 2002* that:

(1) The Report fully complies with the requirements of Section 13(a) or 15(d) of the *Securities Exchange Act of 1934*; and

(2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Postal Service.

Dated: February 8, 2018

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