Postal Regulatory Commission
Submitted 5/9/2014 2:43:51 PM
Filing ID: 89757
Accepted 5/9/2014

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

FORM 10-Q

(Mark One)

☑ **QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934 FOR THE QUARTERLY PERIOD ENDED MARCH 31, 2014 OR**

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

Commission File Number: N/A

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

Washington, D.C.	41-0760000
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
475 L'Enfant Plaza, S.W. Washington, 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, or a smaller reporting company. See definition of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer ☐ Accelerated filer ☐

Non-accelerated filer ☐ (Do not check if a smaller reporting company) Smaller reporting company ☐

Not Applicable ☑

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes ☐ No ☑
Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date.

Common Stock	Outstanding Shares as of May 9, 2014
No Common Stock	N/A

Table of Contents

PART I. FINANCIAL INFORMATION

ITEM 1. Financial Statements

United States Postal Service
Condensed Statements of Operations
(Unaudited)
(in millions)

	Three Months Ended March 31,		Six Months Ended March 31,	
	2014	**2013**	**2014**	**2013**
Operating revenue	$ 16,727	$ 16,348	$ 34,721	$ 34,008
Operating expenses:				
Compensation and benefits	11,293	11,647	23,395	24,114
Retiree health benefits	2,170	2,109	4,323	4,187
Workers' compensation	1,022	429	1,022	753
Transportation	1,588	1,661	3,367	3,500
Other	2,486	2,327	4,758	4,499
Total operating expenses	18,559	18,173	36,865	37,053
Loss from operations	**(1,832)**	**(1,825)**	**(2,144)**	**(3,045)**
Interest and investment income	6	6	12	12
Interest expense	(46)	(47)	(94)	(97)
Net loss	**$ (1,872)**	**$ (1,866)**	**$ (2,226)**	**$ (3,130)**

See accompanying notes to the financial statements (unaudited).

United States Postal Service
Condensed Balance Sheets - Assets
(in millions)

	March 31, 2014	September 30, 2013
	(Unaudited)	
Current Assets		
Cash and cash equivalents	$ 3,736	$ 2,326
Restricted cash	273	312
Receivables:		
Foreign countries	650	618
U.S. government	57	118
Other	232	302
Receivables before allowances	939	1,038
Less allowances	56	54
Total receivables, net	883	984
Supplies, advances and prepayments	150	122
Total Current Assets	**5,042**	**3,744**
Noncurrent Assets		
Property and equipment, at cost:		
Buildings	24,533	24,452
Equipment	19,613	19,629
Land	2,890	2,895
Leasehold improvements	1,318	1,290
	48,354	48,266
Less allowances for depreciation and amortization	31,831	31,156
	16,523	17,110
Construction in progress	373	402
Total property and equipment, net	16,896	17,512
Other assets - principally revenue forgone receivable	409	385
Total Noncurrent Assets	**17,305**	**17,897**
Total Assets	**$ 22,347**	**$ 21,641**

See accompanying notes to the financial statements (unaudited).

United States Postal Service
Condensed Balance Sheets - Liabilities and Net Deficiency
(in millions)

	March 31, 2014 (Unaudited)	September 30, 2013
Current Liabilities		
Compensation and benefits	$ 1,608	$ 1,529
Retiree health benefits	19,565	16,766
Workers' compensation	1,309	1,322
Payables and accrued expenses:		
Trade payables and accrued expenses	1,385	1,237
Foreign countries	570	564
U.S. government	93	112
Total payables and accrued expenses	2,048	1,913
Deferred revenue-prepaid postage	3,407	2,993
Customer deposit accounts	1,188	1,229
Outstanding postal money orders	720	671
Prepaid box rent and other deferred revenue	513	460
Short-term portion of debt	9,800	9,800
Total Current Liabilities	**40,158**	**36,683**
Noncurrent Liabilities		
Workers' compensation	15,598	15,918
Employees' accumulated leave	1,913	1,982
Deferred appropriation and other revenue	85	159
Long-term portion capital lease obligations	323	354
Deferred gains on sales of property	302	308
Contingent liabilities and other	817	860
Long-term portion of debt	5,200	5,200
Total Noncurrent Liabilities	**24,238**	**24,781**
Total Liabilities	**64,396**	**61,464**
Net Deficiency		
Capital contributions of the U.S. government	3,132	3,132
Deficit since 1971 reorganization	(45,181)	(42,955)
Total Net Deficiency	**(42,049)**	**(39,823)**
Total Liabilities and Net Deficiency	**$ 22,347**	**$ 21,641**

See accompanying notes to the financial statements (unaudited).

United States Postal Service
Condensed Statement of Changes in Net Deficiency
(in millions)

	Capital Contributions of U.S. Government	Deficit Since Reorganization	Total Net Deficiency
Balance at September 30, 2012	**$ 3,132**	**$ (37,978)**	**$ (34,846)**
Net loss (unaudited)	—	(3,130)	(3,130)
Balance at March 31, 2013 (unaudited)	**$ 3,132**	**$ (41,108)**	**$ (37,976)**
Balance at September 30, 2013	**$ 3,132**	**$ (42,955)**	**$ (39,823)**
Net loss (unaudited)	—	(2,226)	(2,226)
Balance at March 31, 2014 (unaudited)	**$ 3,132**	**$ (45,181)**	**$ (42,049)**

See accompanying notes to the financial statements (unaudited).

United States Postal Service
Condensed Statements of Cash Flows
(Unaudited)
(in millions)

	Six Months Ended March 31, 2014	Six Months Ended March 31, 2013
Cash flows from operating activities:		
Net loss	$ (2,226)	$ (3,130)
Adjustments to reconcile net loss to cash provided by operations:		
Depreciation and amortization	929	968
(Gain) loss on disposals of property and equipment, net	(22)	20
Decrease in other assets - primarily appropriations receivable revenue forgone	(24)	(1)
Decrease in noncurrent workers' compensation	(320)	(576)
Decrease in noncurrent employees' accumulated leave	(69)	(48)
(Decrease) increase in noncurrent deferred appropriations and other revenue	(37)	14
(Decrease) increase in other noncurrent liabilities	(43)	110
Changes in current assets and liabilities:		
Receivables, net	101	78
Supplies, advances and prepayments	(28)	(27)
Compensation and benefits	79	359
Retiree health benefits	2,799	2,712
Workers' compensation	(13)	(42)
Payables and accrued expenses	134	(3)
Customer deposit accounts	(41)	(13)
Deferred revenue - prepaid postage	414	372
Outstanding postal money orders	49	27
Prepaid box rent and other deferred revenue	53	(17)
Net cash provided by operating activities	**1,735**	**803**
Cash flows from investing activities:		
Change in restricted cash requirements	39	(103)
Purchases of property and equipment	(333)	(309)
Proceeds from sales of property and equipment	35	30
Net cash used in investing activities	**(259)**	**(382)**
Cash flows from financing activities:		
Issuance of notes payable	3,000	2,700
Payments on notes payable	(3,000)	(2,700)
Payments on capital lease obligations	(29)	(29)
U.S. government appropriations - expensed	(37)	(24)
Net cash used in financing activities	**(66)**	**(53)**
Net increase in cash and cash equivalents	1,410	368
Cash and cash equivalents at beginning of year	2,326	2,087
Cash and cash equivalents at end of period	**$ 3,736**	**$ 2,455**
Supplemental cash flow disclosures:		
Cash paid for interest	$ 95	$ 96

See accompanying notes to the financial statements (unaudited).

Notes to Financial Statements (Unaudited)

Note 1 – Basis of Presentation

The accompanying unaudited financial statements have been prepared in accordance with United States (U.S.) generally accepted accounting principles (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. All material adjustments, including normal recurring adjustments, necessary for a fair presentation have been included. Where necessary, disclosure is made in the report for all other adjustments. Certain notes and other information normally included in the financial statements prepared in accordance with GAAP have been condensed or omitted pursuant to instructions, rules and regulations prescribed by the SEC. 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 2014 and 2013.

In the opinion of management, the accompanying unaudited interim financial statements reflect all adjustments necessary to fairly present the financial position as of March 31, 2014, the results of operations for the three and six month periods ended March 31, 2014 and 2013, and the cash flows for the six month periods ended March 31, 2014 and 2013. Operating results for the three and six month periods ended March 31, 2014, are not necessarily indicative of the results that may be expected for all of fiscal year 2014. Subsequent events have been evaluated through May 9, 2014, the date the Postal Service filed its Form 10-Q for the quarter ended March 31, 2014, with the Postal Regulatory Commission (PRC).

The Postal Service has significant transactions with other U.S. Government agencies, as disclosed throughout this report. In addition to the amounts disclosed elsewhere, deferred revenue of $38 million at March 31, 2014, and $37 million at September 30, 2013, related to government deposits are included in the Balance Sheets in “Customer deposit accounts.”

These financial statements should be read in conjunction with the Postal Service’s financial statements for the year ended September 30, 2013 filed as part of the Postal Service’s Annual Report on Form 10-K as filed with the PRC on November 15, 2013.

Note 2 – Liquidity
LIQUIDITY CONCERNS

The Postal Service continues to suffer from a lack of liquidity. The Postal Service held unrestricted cash of $3.7 billion and $2.3 billion as of March 31, 2014, and September 30, 2013, respectively, and had no remaining borrowing capacity on its $15 billion debt facility (See *Note 3, Debt*, for additional information). The increase in cash is largely attributable to the impact of holiday mailings during the first quarter of 2014 and the price increase implemented on January 26, 2014. The current positive cash balance would not exist if the Postal Service had paid the $16.7 billion of the legally-mandated prefunding payments that were due to the Postal Service Retiree Health Benefits Fund (PSRHBF) by September 30, 2013. Additionally, the Postal Service anticipates that it will be unable to make the $5.7 billion payment due by September 30, 2014. As of the date of this report, May 9, 2014, the Postal Service has incurred no penalties or negative consequences resulting from its inability to make these payments. The Postal Service does not have sufficient liquidity to make meaningful reductions in its debt or important investments in its infrastructure. Further, this level of cash could be insufficient to support operations in the event of another significant downturn in the U.S. economy. Current projections indicate that the Postal Service will continue to have a low level of liquidity throughout 2014 and for the foreseeable future.

The Postal Service incurred a net loss of $1,872 million and $2,226 million, respectively, for the three and six month periods ended March 31, 2014, which includes $1,425 million and $2,850 million of expense accrued for the legally-mandated prefunding payment for retiree health benefits, respectively. The requirement of the *Postal Accountability and Enhancement Act,* Public Law 109-435 (P.L. 109-435) to prefund retiree health benefit obligations, a requirement not imposed on most federal agencies or private sector businesses, the ongoing decline in First-Class Mail volume caused by changes in consumers’ and businesses' uses of mail resulting from the Great Recession and the continuing migration toward electronic communication and transactional alternatives, have been major factors contributing to Postal Service losses. Without structural change to the Postal Service’s business model, it will continue to be negatively impacted by these factors and, absent legislative change, it anticipates continuing quarterly losses for the remainder of 2014 and future periods.

In the event that circumstances leave the Postal Service with insufficient cash, the Postal Service would be required to implement contingency plans to ensure that mail deliveries continue. These measures could require the Postal Service to prioritize payments to its employees and suppliers ahead of some payments to the Federal Government, as has been done in the past.

POSTAL ACTIONS TAKEN TO IMPROVE LIQUIDITY

In 2013, the Postal Service accelerated the realignment of its operations to further reduce costs and strengthen its finances. These operational realignments included reductions in the number of mail processing facilities, realignment of retail office hours to match demand, reductions in the number of delivery routes, and consolidations of delivery offices. Additionally, the Postal Service leveraged employee attrition from the 2013 Voluntary Early Retirement (VER) and increased utilization of non-career employees, as provided by the new labor agreements, which allowed for better alignment of staffing and workload levels, resulting in reduced labor costs. The Postal Service continues to pursue legislation to transition to a new delivery schedule which would include package delivery Monday through Saturday (and on Sundays in some instances) and mail delivery Monday through Friday; however, changing the delivery schedule to eliminate Saturday delivery of mail is only possible if Congress refrains from blocking this change. Additionally, the Postal Service continues to seek a refund of the estimated overfunding of the Federal Employees' Retirement System (FERS).

The Postal Service continues to pursue the strategies within its control to increase operational efficiency and to improve liquidity. In April 2014, the Postal Service revised certain service standards for Standard Mail as part of an efficiency improvement effort known as "load leveling." With this change, delivery volume will be more evenly balanced across the workweek, which is expected to improve efficiency and reduce overtime pay and operating costs. This change did not affect the Postal Service's service standards for First-Class Mail or Periodicals. The Postal Service continues to pursue realignments in its delivery and retail operations, cost reductions throughout the organization, and revenue enhancement efforts, and continues to support comprehensive legislation to reform the Postal Service's current business model.

On January 26, 2014, the Postal Service implemented the PRC-approved price increases on Market-Dominant and Competitive products. The Market-Dominant increases include a 1.7% price increase based on the consumer price index for all urban consumers plus a 4.3% increase approved by the PRC in December 2013 as a temporary exigent rate change. The exigent price change was approved by the PRC as a surcharge to be collected only until the Postal Service recovers a total amount of $3.2 billion of incremental revenue above what it would otherwise have recovered through a Consumer Price Index (CPI) increase alone. The Postal Service has filed an appeal with the United States Court of Appeals for the District of Columbia Circuit arguing that the PRC erred in its decision to allow the exigent increase on only a temporary basis. Some mailers filed an appeal seeking relief from the PRC's decision to allow an exigent postage increase. Additionally, prices increased an average of 2.4% for Competitive products. These Market-Dominant and Competitive products changes are expected to generate approximately $2.7 billion of additional annualized revenue for the Postal Service.

MITIGATING CIRCUMSTANCES

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 revenue in excess of $67 billion, generated almost entirely through the sale of postage and delivery services, a financially sound Postal Service continues to be vital to American commerce. The U.S. economy benefits greatly from the Postal Service and the many businesses that provide the printing and mailing services that support it. Disruption of the mail would cause undue hardship to businesses and consumers. Therefore, it is unlikely that, in the event of a cash shortfall, the Federal Government would allow the Postal Service to significantly curtail or cease operations.

The Postal Service continues to inform the Administration, Congress, the PRC, and other stakeholders of the immediate and longer-term financial challenges it faces and the legislative changes that would help restore financial stability. The Postal Service will continue to pursue legislative changes, cost reductions, and additional ways to generate revenues. Many of the structural reforms needed to ensure long-term viability, such as adjustments to pension and health benefit funding schedules and changes to delivery standards, can only be achieved with legislative change. Given the vital role the Postal Service plays in the U.S. economy, it is hopeful that legislation will be enacted which will mitigate the Postal Service's short-term financial challenges and provide it with the authority to make needed changes to ensure long-term financial stability. However, there can be no assurances that the requests to restructure the pension and benefit payment schedules, or any other legislative changes, will be made in time to impact 2014, or any future period.

Note 3 – Debt

The Postal Service's debt consists of various fixed- and floating-rate notes with various maturities and an aggregate principal balance outstanding of $15 billion as of March 31, 2014 and September 30, 2013. All debt is borrowed from the Federal Financing Bank (FFB), a government-owned corporation under the general supervision of the Secretary of the Treasury. Of the $15 billion outstanding, $9.8 billion is due within 12 months from the balance sheet date and is classified as a current liability. The remaining $5.2 billion is classified as a noncurrent liability. The interest rates on the individual notes range from 0.145% to 3.790%, with maturities ranging from less than one month to 25 years. As of March 31, 2014, the premium associated with the prepayment of all debt is $291 million based upon current prevailing interest rates.

Included in short-term debt are two revolving credit line facilities, renewable annually, with the FFB, both of which are available through April 2015. These short-term credit lines enable the Postal Service to draw up to $4 billion. The interest rates for borrowings under these credit facilities are determined by the Treasury each business day. As of March 31, 2014 and September 30, 2013, these two revolving credit facilities were fully drawn.

The Postal Service's credit facilities and note arrangements provide the flexibility to borrow short- or long-term, using fixed- or floating-rate notes. As of March 31, 2014 and September 30, 2013, the Postal Service has reached its legally-mandated debt ceiling limitation of $15 billion.

Note 4 – Property and Equipment

Property and equipment are recorded at cost, less allowances for depreciation and amortization, which includes the interest on borrowings used to pay for the construction of major capital additions. Interest capitalized during both the three and six month periods ended March 31, 2014 and 2013 were not significant. Property and equipment are depreciated over estimated useful lives that range from 3 to 40 years, except for buildings with historic status, which are depreciated over 75 years, using the straight-line method.

Assets classified as held for sale of $56 million as of March 31, 2014, and $78 million as of September 30, 2013, are included on the Balance Sheets in "Land" and "Buildings." Impairment charges were de minimis during the three and six month periods ended March 31, 2014 and 2013.

Deferred gains on sales of property are recognized in income and the sold assets removed from the accounting records when any lease-backs or other conditions requiring continued Postal Service involvement in the properties have expired. Deferred gains recognized in income were de minimis for the three and six month periods ended March 31, 2014 and 2013, respectively.

Note 5 – Leases and Capital Commitments
Leases

Future minimum payments for all non-cancelable leases as of March 31, 2014, were as follows:

Lease Obligations (Dollars in millions)	Operating	Capital
(Unaudited)		
2014	$ 384	$ 46
2015	687	91
2016	619	87
2017	551	79
2018	500	64
Thereafter	3,773	150
Total lease obligations	$ 6,514	$ 517
Less interest		135
Total capital lease obligations		$ 382
Less current portion of capital lease obligations		59
Noncurrent portion of capital lease obligations		$ 323

The current portion of the capital lease obligation is included in "Trade payables and accrued expenses" on the Balance Sheets.

Rent expense consisting of non-cancelable real estate leases, facilities leased from the General Services Administration (GSA) and other equipment and short-term rentals for the three month periods ended March 31, 2014 and 2013, was $283 million and $290 million, respectively. Rent expense consisting of non-cancelable real estate leases, facilities leased from the GSA and other equipment and short-term rentals for the six month periods ended March 31, 2014 and 2013, was $565 million and $569 million, respectively.

Capital

Capital commitments consist primarily of equipment and building construction and improvements. At March 31, 2014, commitments to acquire capital assets were $620 million, compared to $708 million at September 30, 2013, a decrease of $88 million. Financial commitments for approved capital projects in progress were as follows:

Capital Commitments	As of			
(Dollars in millions)		March 31, 2014		September 30, 2013
		(Unaudited)		
Mail processing equipment	$	287	$	316
Building improvements, construction, and building purchases		263		329
Postal support equipment		65		50
Vehicles		5		13
Total capital commitments	$	620	$	708

Note 6 – Contingent Liabilities

Contingent liabilities consist primarily of claims and lawsuits resulting from labor, employment, environmental matters, property damage claims, injuries on postal properties, issues arising from postal contracts, personal claims, and traffic accidents.

Each quarter, significant new claims and litigation are evaluated for the probability of an adverse outcome. If the claim is deemed probable of an unfavorable outcome and the amount of the potential resolution is reasonably estimable, a liability for the loss is recorded. Each quarter, any pre-existing claims and litigation are reviewed and adjusted for resolutions or revisions to prior estimates. This evaluation of cases resulted in an increase of $145 million to the liability for the six months ended March 31, 2014.

As of March 31, 2014, contingent liabilities consisted of $957 million associated with Labor - employment, $48 million with Environmental, $48 million with Tort and $31 million with Contractual liabilities for a total of $1,084 million. As of September 30, 2013, contingent liabilities consisted of $809 million associated with Labor - employment, $48 million with Environmental, $49 million with Tort and $33 million with Contractual liabilities for a total of $939 million.

Based upon currently available information, adequate provision has been made for probable losses arising from claims and suits. The current portion of this liability of $295 million and $108 million as of March 31, 2014 and September 30, 2013, respectively, is included on the Balance Sheets in "Trade payables and accrued expenses." The long-term portion of this liability of $789 million and $831 million as of March 31, 2014 and September 30, 2013, respectively, is included on the Balance Sheets in "Contingent liabilities and other."

In addition to the amounts accrued in the financial statements, the Postal Service also has claims and lawsuits which it deems reasonably possible of unfavorable outcomes, which have an aggregate total range from $300 million to $1,000 million at March 31, 2014. At September 30, 2013, the range was $325 million to $925 million. No provisions for these reasonably possible losses are accrued or included in the financial statements.

Note 7 – Retirement Programs

The majority of employees participate in one of two Federal Government pension programs based on the starting date of their employment with the Federal Government. Employee and employer contributions are made to the Civil Service Retirement System (CSRS), or the FERS, all of which are administered by the OPM. As government-sponsored benefit plans, the CSRS and FERS are not subject to the provisions of the *Employee Retirement Income Security Act of 1974*, as amended. 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 cannot direct the costs, benefits, or funding requirements of the plans. Accordingly, the Postal Service's participation in the Federal retirement plans is accounted for using multiemployer plan accounting rules.

Retirement expense was $1,422 million and $1,421 million for the three month periods ended March 31, 2014 and 2013, respectively. Retirement expense was $2,884 million and $2,902 million for the six month periods ended March 31, 2014 and 2013, respectively. Retirement expense is recorded in "Compensation and benefits" in the Statements of Operations, and includes the costs of FERS, TSP and employer's share of Social Security taxes.

EMPLOYEE/EMPLOYER CONTRIBUTIONS

P.L. 109-435 suspended the employer contributions to CSRS that would otherwise have been required under Title 5, Section 8334(a)(1) of the United States Code until 2017. At that time, OPM will determine whether additional funding is required for the benefit of postal CSRS retirees. As a result, the Postal Service contribution rate for CSRS was zero for the three and six month periods ended March 31, 2014 and 2013.

As required by law, the Postal Service contribution rate was 11.9% of base salary for most current FERS employees for the three and six month periods ended March 31, 2014 and 2013. The Postal Service is required to contribute a minimum of 1% per year of the basic pay, and to match a voluntary employee contribution up to 3% of the employee's basic pay, and 50% of an employee's contribution of between 3% and 5% of basic pay to the TSP for FERS employees.

Note 8 – Health Benefit Plans

CURRENT EMPLOYEES

Substantially all career employees are covered by the Federal Employees' Health Benefits Program (FEHBP). This plan covers both active and retired employees. Health care benefits are available to all participants who meet certain eligibility requirements. In addition to administering the program, OPM allocates the cost of FEHBP to the various participating government agency employers. The Postal Service cannot direct the costs, benefits, or funding requirements of the plan and, therefore, accounts for program expenses using multiemployer plan accounting rules. Contributions to the plan are recorded as an expense in the period in which the contribution is due. The portion of the premium cost paid by the Postal Service for most active employees is determined through agreements with its unions.

Employees paid approximately 24% and 22% of the premium costs during the three month periods ended March 31, 2014 and 2013, respectively. Postal Service employee healthcare expense was $1,192 million, and $1,222 million during the three month periods ended March 31, 2014 and 2013, respectively. Employees paid approximately 23% and 22% of the premium costs during the six month periods ended March 31, 2014 and 2013, respectively. For the six month periods ended March 31, 2014 and 2013, employee healthcare expense was $2,414 million and $2,508 million, respectively. These expenses are included in "Compensation and benefits" in the Statements of Operations.

RETIREES

Employees who participate in the FEHBP for the five years immediately preceding their retirement may participate in the FEHBP during their retirement. The Postal Service is required to pay the employer's share of health insurance premiums for all retired postal employees and their survivors who participate in the FEHBP and who retire on or after July 1, 1971. The employer's share of premium costs for retirees (and their survivors) is set by law and is not subject to negotiation with the unions. Costs attributable to federal civil service before July 1, 1971 are not paid by the Postal Service.

The Postal Service is required to prefund retiree health benefits beginning in 2007, by depositing funds into the PSRHBF each year through 2016. This prefunding requirement is not imposed on most federal agencies or private sector businesses. The Postal Service has recorded $19.6 billion as a current liability for the PSRHBF prefunding requirements on its March 31, 2014 Balance Sheet. This includes payment defaults of $11.1 billion in 2012 and $5.6 billion in 2013, and $2.9 billion accrued for the 2014 payment of $5.7 billion due by September 30, 2014.

Current law also obligates the Postal Service to make additional annual payments of $5.7 billion in 2014 and 2015, and $5.8 billion in 2016, due by September 30 of each respective year. Although P.L. 109-435 dictates the annual prefunding requirements through 2016, these amounts and the timing of funding could be changed at any time with enactment of a new law or an amendment of existing law. To date, no law changes have addressed these required payments. However, given its low levels of liquidity, the Postal Service will likely be forced to default on these prepayments in order to ensure that it continues to be able to fulfill its other statutory obligations, including the obligation to provide universal mail service to the nation (as discussed in *Note 2, Liquidity*). P.L. 109-435, the statutory requirement establishing the payment schedule, contains no provisions addressing a payment default.

At March 31, 2014, scheduled prefunding payments to the PSRHBF are:

PSRHBF Commitment (Dollars in millions)		**P.L. 109-435** **Requirement**
2014*	**$**	**22,400**
2015		**5,700**
2016		**5,800**
Thereafter		**—**
Total PSRHBF commitment	**$**	**33,900**

*This amount includes defaults on $16.7 billion due to the PSRHBF as of September 30, 2013 and $5.7 billion due by September 30, 2014. Amortization of the unfunded liability at September 30, 2016 is not reflected above.

These annual prefunding payments are in addition to the regularly allocated cost of premiums for current retirees, which continue to be payable through 2016. The law requires that OPM perform an actuarial valuation to determine if additional payments into the PSRHBF are required no later than 2017. If required, OPM will design an amortization schedule to fully fund any remaining liability by 2056. Starting in 2017, the Postal Service's share of the health insurance premiums for current and future Postal Service retirees will be paid from the PSRHBF. Also, beginning in 2017, the Postal Service will fund the actuarially determined normal cost attributable to that year's service for employees who will retire in the future.

Retiree Health Benefits	**Three Months Ended March 31,**				**Six Months Ended March 31,**			
(Dollars in millions)		**2014**		**2013**		**2014**		**2013**
(Unaudited)								
Employer premium expense	**$**	**745**	**$**	**709**	**$**	**1,473**	**$**	**1,387**
Accrual for P.L. 109-435 payment to PSRHBF		**1,425**		**1,400**		**2,850**		**2,800**
Total retiree health benefits expense	**$**	**2,170**	**$**	**2,109**	**$**	**4,323**	**$**	**4,187**

These costs, which are reflected as "Retiree health benefits" in the Condensed Statements of Operations, consist of payments to OPM for the Postal Service's share of FEHBP retiree premiums currently being paid, plus accrued prefunding payments to the PSRHBF for current employees who will retire in the future. Because the amounts to be paid into the PSRHBF are set by legislation, the Postal Service retiree health expense may represent more or less than the full cost of the benefits earned by Postal Service employees.

Note 9 – Workers' Compensation

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

An estimation model that combines four generally accepted actuarial valuation techniques is used to project future claim payments based upon past claim-payment experience and exposure to claims as measured by total hours worked by Postal Service employees. A liability is recorded for the present value of estimated future payments to postal employees, or their qualified survivors, who have been injured through the end of the reporting period. The estimated total cost of a claim is based on the date of the injury, pattern of historical payments, frequency or severity of the claim-related injury or injuries, and the expected trend in future costs. The Postal Service uses the average rate of medical inflation experienced by its workers' compensation claimants over the past five years as an estimate for future medical inflation. An inflation factor based upon the Consumer Price Index - Urban Wage Earners and Clerical Workers (CPI-W) index is utilized in calculating inflation related to compensation claims. The liability for claims arising more than 10 years ago is determined by an independent actuary.

The FECA benefit program is often superior to benefits available under federal retirement, and these more lucrative payments will, in some cases, be for the rest of the claimants' lives. Under the FECA program, this benefit may cause an undue financial burden on the Postal Service.

The liability for estimated future workers' compensation payments is recorded at its present value. To record the liability and annual expense, an estimate is made of the amount of funding that would need to be invested at current interest rates in order to fully fund all estimated future payments. Inflation and discount (interest) rates are updated as of the date of the financial statements to determine the present value of the workers' compensation liability at fair value in accordance with GAAP. The impact of changes in the discount and inflation rates is accounted for as a change in accounting estimate and included in operating expenses.

The estimation of the liability is highly sensitive to changes in inflation and discount rates. An increase of 1% in the discount rate would decrease the liability by approximately $1.7 billion as of March 31, 2014 and decrease the related expense by approximately $1.7 billion during the six months ended March 31, 2014. A decrease of 1% in the discount rate would increase the liability by approximately $2.1 billion as of March 31, 2014 and increase the related expense by approximately $2.1 billion during the six months ended March 31, 2014.

The inflation and discount rates used to estimate the workers' compensation liability and related expense are shown in the following table:

Workers' Compensation Liability Inflation and Discount Rates	**Quarter Ended**			
	March 31, 2014	**September 30, 2013**	**March 31, 2013**	**September 30, 2012**
	(Unaudited)		(Unaudited)	
Compensations claims liability:				
Discount rate	**3.0%**	**3.0%**	**2.4%**	**2.1%**
Wage inflation	**2.9%**	**2.9%**	**2.9%**	**2.9%**
Medical claims liability:				
Discount rate	**3.0%**	**3.0%**	**2.4%**	**2.2%**
Medical inflation	**8.9%**	**9.1%**	**9.0%**	**8.9%**

The present value of the liability for future workers' compensation payments was $16,907 million and $17,240 million as of March 31, 2014 and September 30, 2013, respectively. On October 15, 2013, the Postal Service made the scheduled annual payment to the DOL of $1,372 million, which included $50 million of prepaid administrative fees. The current portion of the liability was $1,309 million and $1,322 million as of March 31, 2014 and September 30, 2013, respectively.

Changes in the workers' compensation liability are attributable to the combined impact of changes in the discount and inflation rates, routine changes in actuarial estimation, new compensation and medical cases, and the progression of existing cases. Workers' compensation expense, including the impact of changes in the discount rates, for the three and six month periods ended March 31, 2014 and 2013, were as follows:

Workers' Compensation Expense (Dollars in millions)	Three Months Ended March 31, 2014	Three Months Ended March 31, 2013	Six Months Ended March 31, 2014	Six Months Ended March 31, 2013
(Unaudited)				
Impact of discount rate changes	$ 541	$ (229)	$ —	$ (455)
Actuarial valuation of new cases and revaluation of existing cases	$ 464	$ 641	$ 988	$ 1,174
Subtotal	1,005	412	988	719
Administrative Fee	17	17	34	34
Total workers' compensation expense	$ 1,022	$ 429	$ 1,022	$ 753

Note 10 – Fair Value Measurements

The Postal Service estimates that the carrying value of current assets and liabilities approximates fair values. The Postal Service also has non-current financial instruments, such as the long-term portion of debt (see *Note 3-Debt*) and long-term receivables (see *Note 11-Revenue Forgone*), that must be measured for disclosure purposes on a recurring basis following authoritative accounting literature in GAAP. The Postal Service also applies these requirements to various non-recurring measurements of financial and non-financial assets and liabilities, such as the impairment of property and equipment. Measurement of assets and liabilities at fair value is performed using inputs from the following three levels of the fair value hierarchy as defined in the authoritative literature:

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

Because no active market exists for the debt with the FFB, the fair value of the noncurrent portion of these notes has been estimated using prices provided by the FFB, a Level 3 input.

The fair value of revenue forgone has been estimated using the income method and discount rates on similar assets, such as noncurrent U.S. Treasury securities that have a similar maturity, a level 2 input.

The carrying values of current assets and liabilities approximate their fair values due to the short-term maturity of those financial instruments. The carrying values and the fair values of noncurrent assets and liabilities that qualify as financial instruments in accordance with the accounting literature are as indicated in the table below. This table is presented for disclosure purposes only. The Postal Service has not recorded a gain or loss to its operations for the differences between carrying and fair values of the above assets and liabilities.

Fair Value of Long-Term Financial Assets and Liabilities (Dollars in millions)	March 31, 2014 Carrying Amount	March 31, 2014 Fair Value	September 30, 2013 Carrying Amount	September 30, 2013 Fair Value
	(Unaudited)			
Revenue forgone	$ 408	$ 485	$ 385	$ 461
Total long-term financial assets	$ 408	$ 485	$ 385	$ 461
Long-term portion of debt	$ 5,200	$ 5,488	$ 5,200	$ 5,517
Total long-term financial liabilities	$ 5,200	$ 5,488	$ 5,200	$ 5,517

For the three and six month periods ended March 31, 2014, there were no transfers between Level 1, Level 2 or Level 3 assets or liabilities.

Non-financial assets, such as property and equipment, are measured at fair value when there is an indicator of impairment or when a decision is made to dispose of an asset, and recorded at fair value only when impairment is recognized. Impairment analyses of property and equipment were performed in each quarter of 2013 and the first two quarters of 2014. Impairment charges were de minimis for the three and six month periods ended March 31, 2014 or 2013. Independent appraisals, adjusted for estimated selling costs, are used to determine the fair value of non-financial assets deemed impaired or being held for sale. Independent third party appraisals are deemed Level 2 inputs as defined above.

Note 11 – Revenue Forgone

Revenue forgone is an appropriation received from the U.S. Government that is intended to reimburse the Postal Service for statutorily-required free and reduced rate mailing services provided to specified groups. It also includes amounts authorized in the *Revenue Forgone Reform Act of 1993* for services performed and revenue forgone for the years 1991 through 1998, which was scheduled to be reimbursed at a rate of $29 million each year from 1993 through 2035.

P.L. 113-76, *Consolidated Appropriations Act, 2014*, which funded the Government for 2014, did not contain a provision for funds to be paid to the Postal Service regarding these amounts due under the *Revenue Forgone Reform Act of 1993*. The Postal Service last received a contribution for the *Revenue Forgone Reform Act of 1993* of $12 million in 2011 and has received none of the combined total of $87 million due for years 2012 through 2014. However, there was no impact to the Condensed Statements of Operations as a result of the shortfall in Congressional appropriations for these years because the revenue was previously recognized upon the enactment of the *Revenue Forgone Reform Act of 1993*. The impact of not fully funding these obligations only represents a change in the timing of the funding but not a change to the legal requirement for reimbursement. The unfunded amounts will be included as part of the 2015 and 2016 appropriations requests.

For the three months ended March 31, 2014, the Postal Service recognized revenue of $19 million, including $5 million of imputed interest income from these appropriations, compared to recognized revenue of $20 million, including $5 million of imputed interest, for the three months ended March 31, 2013. For the six months ended March 31, 2014, the Postal Service recognized revenue of $39 million, including $11 million of imputed interest, compared to recognized revenue of $29 million, including $11 million of imputed interest for the six months ended March 31, 2013.

The related amount of the noncurrent receivable as of March 31, 2014 and September 30, 2013 was $408 million and $385 million, respectively. The current portion of this receivable as of March 31, 2014 and September 30, 2013 was $26 million and $68 million, respectively, and is recorded under "Receivables – U.S. Government" on the Balance Sheets while the noncurrent portions are shown as "Other Assets."

Item 2 – Management's Discussion and Analysis of Financial Condition and Results of Operations

Cautionary Statements

Forward-looking statements contained in this report represent our best estimates of known and anticipated trends believed relevant to future operations. However, actual results may differ significantly from current estimates. Certain forward-looking statements are included in this report and use such words as "may," "will," "could," "expect," "believe," "plan," "estimate," "project," or other similar terminology. These statements reflect current expectations regarding future events and operating performance as of the date of this report. These forward-looking statements involve a number of risks and uncertainties.

Management's Discussion and Analysis of Financial Condition and Results of Operations and other parts of this report include statements representing expectations about the United States Postal Service business and financial results. These may be impacted by risks and uncertainties discussed here and in the Annual Report on Form 10-K for the year ended September 30, 2013, such as, but not limited to, effectiveness of operating initiatives; rate of electronic diversion; changes in laws and regulations; costs and delays associated with new regulations imposed by the Postal Regulatory Commission (PRC) or other regulatory bodies; the amount of required prefunding payments to the Postal Service Retiree Health Benefits Fund (PSRHBF); success in advertising and promotional efforts; changes in national and local business and economic conditions, including their impact on consumer and business confidence; fluctuations in currency exchange and interest rates; labor and other operating costs; oil, fuel, and other transportation costs; the effects of war and terrorist activities; competition, including pricing and marketing initiatives and new service offerings by our competitors; consumer preferences or perceptions concerning our service offerings; spending patterns and demographic trends; availability of qualified personnel; severe weather conditions; labor relations, particularly the results of collective bargaining; effects of legal claims; cost and deployment of capital; and changes in applicable accounting policies and practices. The foregoing list of important factors is not all-inclusive. Some of these and other factors, many of which we cannot control or influence, may cause actual results to differ materially from those currently contemplated. We have no obligation to publicly update or revise any forward-looking statements, whether as a result of new information, future events, or otherwise. Operating results for the three and six month periods ended March 31, 2014 are not necessarily indicative of the results to be expected for the year ending September 30, 2014. This report should be read in conjunction with the United States Postal Service Annual Report on Form 10-K for the year ended September 30, 2013. As in that report, all references to years, unless otherwise stated, refer to the fiscal year beginning October 1 and ending September 30. All references to quarters, unless otherwise noted, refer to quarters within fiscal years 2014 and 2013.

Introduction

The United States Postal Service commenced operations on July 1, 1971 as an "independent establishment of the executive branch of the Government of the United States." We are governed by an eleven-member Board of Governors (the Board). Nine independent Governors are appointed by the President of the United States with the advice and consent of the Senate. The Postmaster General, who is appointed by the independent Board members, also serves on the Board, as does the Deputy Postmaster General, who is appointed by the independent Board members and the Postmaster General. Under the *Postal Reorganization Act*, Public Law 91-375 (P.L. 91-375) and its successor, the *Postal Accountability and Enhancement Act*, Public Law 109-435 (P.L. 109-435), we have a legal mandate to offer a "fundamental service" to the American people "at fair and reasonable rates." We fulfill this legal mandate to provide universal service at a fair price by offering a variety of classes of mail services without undue discrimination among our customers. This means that, within each class of mail service, prices do not vary unreasonably by customer for the level of service provided. However, P.L. 109-435 provides greater flexibility in the pricing of Shipping Services, as discussed below.

We serve individual and commercial customers in the communications, distribution and delivery, advertising and retail markets throughout the nation and internationally. As a result, we have a very diverse customer base and are not dependent upon a single customer or small group of customers. No single customer represents more than 2.1% of operating revenue.

Prices and fees are subject to a review process by the Board and by the independent PRC.

P.L. 109-435 classifies postal services into two broad categories: Market-Dominant and Competitive "products"; however, the term "services" is often used in this document for consistency with other descriptions of "services" offered by the Postal Service. Price increases for those services classified as Market-Dominant are subject to a price cap based on the Consumer Price Index — All Urban Consumers (CPI-U). The regulations for Competitive services place no upper limit on price changes but do set a price floor. Throughout this document and in the day-to-day operations of the organization, we refer to our major service categories as the following: First-Class Mail, Standard Mail, Shipping and Packages, International, Periodicals, and Other. Most services in the First-Class Mail, Standard Mail, and Periodicals are in the Market-Dominant category. Shipping and Package Services and International Mail, which are predominantly Competitive services, include, but are not limited to, First-Class and Standard Mail Parcels, Priority Mail, Priority Mail Express, Parcel

Select and Parcel Return Service, Bulk Standard Post, and Bulk International Mail. A price increase that was approved by the PRC became effective on January 26, 2014. The Market-Dominant price included a 1.7% increase based on the consumer price index plus a 4.3% increase approved as a temporary exigent rate change. The exigent price change is approved as a surcharge to be collected only until the Postal Service recovers $3.2 billion of incremental revenue above what it would otherwise have recovered through a CPI increase alone. The decision by the PRC to limit the duration of the exigent rate increase is the subject of an appeal to the United States Court of Appeals for the District of Columbia Circuit. Additionally, prices increased an average of 2.4% for Competitive service products.

Mailing and Shipping Services are sold through a network of nearly 32,000 postal-managed Post Offices, stations, and branches, plus thousands of contract postal units, community post offices, Village Post Offices, retail establishments that sell postage stamps and other services, and our website, *http://www.usps.com*. Mail deliveries are made to over 153 million city, rural, Post Office box, and highway delivery points. Operations are conducted primarily in the domestic market, with international sales representing approximately 5% of total revenue.

We operate and manage a very extensive and integrated retail, distribution, transportation and delivery network. As such, the physical infrastructure and labor force are not, with limited exceptions, dedicated to individual business lines. Expenses are incurred and managed by functional groupings that align with the integrated network structure. Reporting of expenses on a functional basis in this report conforms to the management and structure of expense incurrence within the organization.

The labor force is primarily represented by the American Postal Workers Union, AFL-CIO (APWU), the National Association of Letter Carriers, AFL-CIO (NALC), the National Postal Mail Handlers Union, AFL-CIO (NPMHU), and the National Rural Letter Carriers Association (NRLCA). Approximately 86% of career employees are covered by collective bargaining agreements.

We are required by law to consult with management associations representing supervisory and managerial employees and postmasters prior to making final decisions concerning changes to pay and benefits for such employees.

The Postal Service is not a reporting company under the Securities Exchange Act of 1934, as amended, and is not subject to regulation by the Securities and Exchange Commission (SEC). However, it is required under P.L.109-435 to file with the PRC certain financial reports containing information prescribed by the SEC under Section 13 of the Securities Exchange Act of 1934. These reports include annual reports on Form 10-K, quarterly reports on Form 10-Q, and current reports on Form 8-K, which are available at *http://about.usps.com/who-we-are/financials/welcome.htm*. The Postal Service is required by law and regulations to disclose operational and financial information well beyond what the law requires of other government agencies and most private sector companies.

Pursuant to Title 39 and PRC regulations, additional disclosures on the organization and finances, including Cost and Revenue Analysis reports, Revenue, Pieces, and Weight reports, financial and strategic plans, and the *Comprehensive Statement on Postal Operations* are filed with the PRC and may also be found online at *http://about.usps.com*. Information on the website is not incorporated by reference into this document.

Critical Accounting Policies and Estimates

The preparation of financial statements in accordance with United States (U.S.) generally accepted accounting principles (GAAP) requires management to make significant judgments and estimates to develop certain amounts reflected and disclosed in the financial statements. In many cases, there are alternative policies or estimation techniques that could 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 on Form 10-K for the year ended September 30, 2013. Management discusses the development and selection of accounting policies and estimates with the Audit and Finance Committee of the Board of Governors. There have been no significant changes or updates to our critical accounting policies and estimates since our last report.

Recent Accounting Standards

There were no new accounting standards issued or adopted during the three and six month periods ended March 31, 2014 that had or will have a material impact on our financial statements.

Results of Operations

Three and Six Months Ended March 31, 2014 and March 31, 2013

Our net loss was $1,872 million for the three months ended March 31, 2014, compared to a net loss of $1,866 million for the same period last year, an increase in the net loss of $6 million. Operating revenue increased $379 million, or 2.3%, compared to the same period last year. This increase in operating revenue is primarily due to an increase in our Shipping and Packages volume and the approved price increases that became effective January 26, 2014. Operating expenses increased $386 million, or 2.1%, compared to the same period last year. The increase in operating expenses is primarily due to an increase in workers' compensation expense of $593 million, offset by a reduction in compensation and benefits of $354 million, or 3.0%.

Our net loss was $2,226 million and $3,130 million for the six months ended March 31, 2014 and 2013, respectively. This represents a favorable decrease in our net loss of $904 million. Operating revenue increased $713 million, or 2.1%, compared to the same period last year. This increase in operating revenue is primarily due to an increase in our Shipping and Packages volume and the approved price increases that became effective January 26, 2014. Operating expenses decreased $188 million, or 0.5%, compared to the same period last year. The decrease in operating expenses is primarily due to reduced compensation and benefits expense of $719 million, or 3.0%, which includes the 2013 Voluntary Early Retirement (VER) incentive of $351 million. This is offset by an increase in workers' compensation expense of $269 million, or 35.7% and in other operating expenses of $259 million, or 5.8%.

Although significant efforts continue to be made to increase revenues and reduce costs under management's control, we have not been able to completely offset the impact of declining First-Class Mail volume and the ongoing effects of the Great Recession. In addition, the PSRHBF prefunding requirement, continuation of legally-mandated six-days-per-week delivery and continued high fuel costs have adversely affected our financial results.

The following table summarizes key operating statistics for the three and six month periods ended March 31, 2014 and 2013:

Key Operating Statistics	**Three Months Ended March 31,**		**Six Months Ended March 31,**	
(Dollars and mail volume in millions)	**2014**	**2013**	**2014**	**2013**
Operating revenue	**$ 16,727**	**$ 16,348**	**$ 34,721**	**$ 34,008**
PSRHBF expense	**$ 1,425**	**$ 1,400**	**$ 2,850**	**$ 2,800**
Net loss	**$ (1,872)**	**$ (1,866)**	**$ (2,226)**	**$ (3,130)**
Total mail volume	**38,098**	**38,774**	**80,137**	**82,249**
Average mail volume per day	**515**	**524**	**538**	**552**

As explained further in the Revenue and Volume section, we continue to make efforts to offset declining First-Class Mail volume. Continuing development of new products and enhancements to existing products, successful marketing campaigns, and growing consumer e-commerce contribute to the growth in our package business. By introducing new services and supporting them with better educational marketing information, we are showing customers new ways that the mail can be used in conjunction with current technologies. We continue to encourage mailers to try new products and services that can add value to their mail and allow them to connect with customers in a more individualized way. Products and services, such as Every Door Direct Mail offer new ways of doing business with us.

Our net losses include expenses of $2,447 million and $3,872 million for the three and six month periods ended March 31, 2014, respectively, for the legally-mandated prefunding of retiree health benefits, as well as the legally-mandated participation in the federal workers' compensation program that is managed by the Department of Labor's (DOL's) Office of Workers' Compensation Programs (OWCP) and governed by the Federal Employees' Compensation Act (FECA). As the Postal Service does not manage the FECA program, we have no ability to control its significant costs. These factors, compounded by cost of living adjustments (COLA) granted by Federal Law to those claims, result in substantially higher costs to the Postal Service than would likely be the case if claims management decisions were made by the Postal Service. In addition to the constraints imposed by the legally-mandated FECA program, actuarial estimations and projected cash payments that will be paid well into the future also have substantial impact on our reported workers' compensation liability. Future cash payments must be converted to present-day dollars, or discounted, by applying current rates at which the liability could theoretically be settled. Discount rates can fluctuate significantly from period to period, with changes in the economic and interest rate environment. Even a small change in discount rates can have a large impact on the workers' compensation liability and expense, as a 1% decrease in rates at March 31, 2014, would have resulted in approximately a $2.1 billion increase of the liability. This results in significant differences between the GAAP workers' compensation expense and our cash outlays.

Because the legislative mandates for prefunding of retiree health benefits and the participation in the FECA are not subject to management's control, we believe that analyzing operating results without the impact of certain of these charges provides a more meaningful insight into current operations. In the day-to-day operation of our business, we exclude these items from our internal financial analyses in order to direct focus upon relevant expenses that management can control and include only those workers' compensation costs representing current year payments on behalf of postal claimants. The following table illustrates the net income or loss for the three and six month periods ended March 31, 2014 and 2013 from ongoing business activities when these charges are not considered, and reconciles this amount to our GAAP net loss. Enhancements implemented in our business operations, as more fully described in the sections below, have yielded improvements to our non-GAAP operating net income (loss), for the three and six month periods ended March 31, 2014 when compared to the same period last year.

Net Income before Impact of Expense Related to the Long-term Portion of Workers' Compensation and PSRHBF Expense

(Dollars in millions)	Three Months Ended March 31, 2014	Three Months Ended March 31, 2013	Six Months Ended March 31, 2014	Six Months Ended March 31, 2013
Net loss	**$ (1,872)**	**$ (1,866)**	**$ (2,226)**	**$ (3,130)**
Impact of:				
Change related to the long-term portion of workers' compensation	**708**	**120**	**402**	**128**
PSRHBF expense	**1,425**	**1,400**	**2,850**	**2,800**
Net income (loss) before the impact of expense related to long-term portion of workers' compensation and PSRHBF expense	**$ 261**	**$ (346)**	**$ 1,026**	**$ (202)**

Revenue and Volume

Revenue and volume are closely linked to the strength of the U.S. economy and changes in how our customers use the mail. 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 them to market.

As discussed in detail below, the resulting effects of the Great Recession and the ongoing technological change have impacted our First-Class Mail volume and revenue, which continues to decline even as new services, the growth of e-commerce, and successful marketing campaigns, have helped us grow the Shipping and Packages business. However, because Shipping and Packages represents only 18.6% of our total annual revenues, compared to First-Class Mail, which represents 42%, growth in Shipping and Packages, by itself, cannot fully offset the declines in First-Class Mail. Furthermore, the profit contribution for First-Class Mail is greater than that of Shipping and Packages. As a result, revenues from Shipping and Package Services would have to grow at a substantially higher rate than the decline in First-Class Mail revenues in order to replace the lost profit contribution of First-Class Mail.

Summary of Revenue and Volume Results

For the three months ended March 31, 2014, operating revenue was $16,727 million, an increase of $379 million, or 2.3%, compared to the same period last year. We implemented the PRC-approved price increases on Market-Dominant and Competitive products during the three months ended March 31, 2014. The Market-Dominant price increase included an exigent price increase of 4.3%, which is being assessed as a surcharge in addition to the 1.7% CPI price increase. The PRC's decision, authorizing the exigent surcharge, specifies that it shall remain in effect only until an additional $3.2 billion in revenue has been raised. We have filed an appeal with the United States Court of Appeals for the District of Columbia Circuit arguing that the PRC erred in its decision to allow the exigent increase on only a temporary basis. The outcome of this appeal cannot be determined at this time. Some mailers filed an appeal seeking relief from the PRC's decision to allow an exigent postage increase.

Shipping and Packages revenue of $3,384 million increased $252 million, or 8.0%, compared to the same period last year, aided by the price increases implemented in January 2014. Shipping and Packages volume was 986 million pieces for the three months ended March 31, 2014, an increase of 67 million pieces, or 7.3%, compared to the same period last year. Increased consumer spending, especially e-commerce retail sales, were responsible for the growth in Shipping and Packages revenue and volume during the three months ended March 31, 2014.

For the six months ended March 31, 2014, operating revenue was $34,721 million, an increase of $713 million, or 2.1%, compared to the same period last year. Shipping and Packages revenue of $7,265 million increased $730 million, or 11.2%, compared to the same period last year. Shipping and Packages volume was 2,100 million pieces for the six months ended March 31, 2014, an increase of 170 million pieces, or 8.8%, compared to the same period last year. Increased consumer spending, growing e-commerce retail sales, and increasingly effective marketing efforts were responsible for the growth in Shipping and Packages revenue and volume during the six months ended March 31, 2014.

The following table summarizes our revenue and volume for the three and six month periods ended March 31, 2014 and 2013, by major service line:

Operating Revenue and Volume by Service Line*	Three Months Ended March 31,			Six Months Ended March 31,		
(Dollars and pieces in millions)	2014	2013	% Change	2014	2013	% Change
Revenue:						
First-Class Mail[1]	$ 7,133	$ 7,131	— %	$ 14,424	$ 14,630	(1.4)%
Standard Mail[2]	4,213	4,041	4.3 %	8,841	8,675	1.9 %
Shipping and Packages[3]	3,384	3,132	8.0 %	7,265	6,535	11.2 %
International	717	762	(5.9)%	1,583	1,593	(0.6)%
Periodicals	394	416	(5.3)%	803	842	(4.6)%
Other[4]	886	866	2.3 %	1,805	1,733	4.2 %
Total revenue	**$ 16,727**	**$ 16,348**	**2.3 %**	**$ 34,721**	**$ 34,008**	**2.1 %**
Volume:						
First-Class Mail[1]	16,026	16,708	(4.1)%	32,906	34,407	(4.4)%
Standard Mail[2]	19,313	19,216	0.5 %	41,307	41,837	(1.3)%
Shipping and Packages[3]	986	919	7.3 %	2,100	1,930	8.8 %
International	209	225	(7.1)%	476	495	(3.8)%
Periodicals	1,479	1,604	(7.8)%	3,044	3,245	(6.2)%
Other[5]	85	102	(16.7)%	304	335	(9.3)%
Total volume	**38,098**	**38,774**	**(1.7)%**	**80,137**	**82,249**	**(2.6)%**

*Note: The totals for certain mail categories for the prior year have been reclassified to better reflect classifications used in the current year. These reclassifications did not impact total operating revenue for the prior year.

[1] Excludes First-Class Mail Parcels.

[2] Excludes Standard Mail Parcels.

[3] Includes Priority Mail, Standard Post, Parcel Select, Parcel Return Service, Standard Mail Parcels, Package Service, First-Class Mail Parcels, First-Class Package Service, and Priority Mail Express.

[4] Includes P.O. Box Services, Certified Mail, Return Receipts, Insurance, Other Ancillary Fees, Shipping and Mailing Supplies, and other operating revenue.

[5] Includes Postal Service Mail and Free and Reduced Mail.

First-Class Mail and Standard Mail continue to provide the majority of our revenue for the three and six month periods ended March 31, 2014, despite trends away from hard copy to electronic media. Year to date First-Class Mail represented 41.5% of our revenue and accounted for 41.1% of the mail volume while Standard Mail generated 25.5% of revenue, but 51.5% of volume. Shipping and Packages generated approximately 20.9% of our revenue despite representing only 2.6% of our volume.

FIRST-CLASS MAIL

First-Class Mail volume, our most profitable service category, declined 682 million pieces, or 4.1%, for the three months ended March 31, 2014. The most significant factors contributing to this decline in volume were the continuation of trends associated with changes in the behavior of consumers and businesses emanating from the Great Recession, and the continuing migration toward electronic communication and electronic transaction alternatives. First-Class Mail had revenue of $7,133 million for the three months ended March 31, 2014, an increase of $2 million, relatively unchanged compared to the same period last year. The relatively flat revenue in the current period compared to the same period last year was primarily due to the price increase that went into effect during the current period, offset by the decline in volume as noted above.

First-Class Mail had revenue of $14,424 million for the six months ended March 31, 2014, a decrease of $206 million, or 1.4%, compared to the same period last year. The corresponding volume decrease was 1,501 million pieces, or 4.4%. As noted above, the most significant factors contributing to this decline were the continuation of trends associated with changes in the behavior of consumers and businesses.

STANDARD MAIL

Standard Mail had revenue of $4,213 million for the three months ended March 31, 2014, an increase of $172 million, or 4.3%, compared to the same period last year. Standard Mail revenues also benefited from the price increase implemented in January 2014. The corresponding volume increase was 97 million pieces, or 0.5%. The increase in volume is reflective of the cyclical nature of Standard Mail which increases as the economy expands and decreases as the economy contracts.

Standard Mail had revenue of $8,841 million for the six months ended March 31, 2014, an increase of $166 million, or 1.9%, compared to the same period last year, primarily due to the January 2014 price increase. However, volume decreased 530 million pieces, or 1.3%. The decline in volume primarily reflects the results in the first quarter of 2014 which was not a national election year compared to the 2012 election year in which significant political mail volume was delivered in the first quarter of 2013.

SHIPPING AND PACKAGES

The following table summarizes our revenue and volume for Shipping and Packages for the three and six month periods ended March 31, 2014, and 2013, by service line:

Shipping & Packages Revenue and Volume*	Three Months Ended March 31,			Six Months Ended March 31,		
(Dollars and pieces in millions)	2014	2013	% Change	2014	2013	% Change
Revenue:						
Priority Mail[1]	$ 1,815	1,769	2.6 %	$ 3,975	$ 3,732	6.5 %
Parcel Select, Parcel Return and Standard Parcels	643	515	24.9 %	1,401	1,092	28.3 %
Package Services	209	208	0.5 %	418	416	0.5 %
First-Class Packages[2]	526	444	18.5 %	1,084	892	21.5 %
Priority Mail Express	191	196	(2.6)%	387	403	(4.0)%
Total revenue	**$ 3,384**	**$ 3,132**	**8.0 %**	**$ 7,265**	**$ 6,535**	**11.2 %**
Volume:						
Priority Mail[1]	240	234	2.6 %	514	489	5.1 %
Parcel Select, Parcel Returns and Standard Parcels	377	340	10.9 %	823	734	12.1 %
Package Services	138	137	0.7 %	289	284	1.8 %
First-Class Packages[2]	222	198	12.1 %	456	403	13.2 %
Priority Mail Express	9	10	(10.0)%	18	20	(10.0)%
Total volume	**$ 986**	**$ 919**	**7.3 %**	**$ 2,100**	**$ 1,930**	**8.8 %**

*Note: The totals for certain mail categories for the prior year have been reclassified to better reflect classifications used in the current year.
[1] Includes Standard Post.
[2] Includes First-Class Mail Parcels and First-Class Package Services.

Shipping and Packages revenue continued to show solid volume growth as a result of our successful efforts to compete in the ground shipping services and "last mile" e-commerce fulfillment markets. Additionally, the 2013 holiday season provided a surge in package volume, as we took advantage of consumers' continued growth in online shopping. In order to accommodate this surge in volume, and avoid service disruptions, we implemented Sunday delivery service for some of our customers in limited U.S. markets.

Shipping and Packages revenue increased $252 million, or 8.0% from $3,132 million for the three months ended March 31, 2013, to $3,384 million for the three months ended March 31, 2014. Shipping and Packages volume increased 67 million pieces, or 7.3%, for the three months ended March 31, 2014, compared to the same period last year. For the six months ended March 31, 2014, Shipping and Packages revenue increased $730 million, or 11.2%, compared to the same period last year. Shipping and Packages volume increased 170 million pieces, or 8.8%, for the six months ended March 31, 2014, compared to the same period last year.

Priority Mail

We continue to simplify our Priority Mail service to better meet the needs of the public and introduced the new *"Priority You"* marketing campaign in 2013. E-commerce has grown at a higher rate than traditional retail sales, which has helped to boost Priority Mail revenues.

Priority Mail represented approximately 54% of our total Shipping and Packages Service revenue for the three and six month periods ended March 31, 2014. Priority Mail revenue increased $46 million, or 2.6%, for the three months ended March 31, 2014, compared to the same period last year. For the six months ended March 31, 2014 Priority Mail revenue increased $243 million, or 6.5%, compared to the same period last year.

Parcel Services

Parcel Services had revenue of $643 million for the three months ended March 31, 2014, an increase of $128 million, or 24.9%, compared to the same period last year. This category includes Parcel Select revenue of $593 million, Parcel Returns revenue of $35 million, and Standard Mail Parcels revenue of $15 million. These services continue to show strong volume growth of 10.9% for the three months ended March 31, 2014, compared to the same period last year. However, this category represents one of our lowest available priced services, and as a result, provides a relatively low level of profitability compared to many of our other services.

Parcel Services had revenue of $1,401 million for the six months ended March 31, 2014, comprised of Parcel Select revenue of $1,299 million, Parcel Returns revenue of $69 million, and Standard Mail Parcels revenue of $33 million. Revenue increased $309 million, or 28.3%, compared to the same period of the prior year. Parcel Services volume increased 89 million pieces, or 12.1%, during the six month period, compared to the same period last year.

Package Services

This category includes Parcel Post, Bound Printed Matter, Library Mail and Media Mail weighing up to 70 pounds. Because all services in this category are classified as Market-Dominant, price increases for these services are capped.

Package Services revenue of $209 million for the three months ended March 31, 2014, remained unchanged compared to the same period last year. Package Services revenue was $418 million for the six months ended March 31, 2014, an increase of $2 million, or 0.5%, compared to the same period last year.

First-Class Packages

The First-Class Packages category was introduced in 2012. This reliable package service offers commercial customers that ship primarily lightweight fulfillment parcels, the lowest priced end-to-end package option in the marketplace. First-Class Packages, which include the competitively priced First-Class Package Services, and under one pound commercial package product, and First-Class Mail Parcels, a Market-Dominant under 13 ounce package product, generated revenue of $526 million for the three months ended March 31, 2014, an increase of $82 million, or 18.5%, compared to the same period last year. Volume increased 24 million pieces, or 12.1%, for the three months ended March 31, 2014, compared to the same period last year.

First-Class Packages revenue was $1,084 million for the six months ended March 31, 2014, an increase of $192 million, or 21.5%, compared to the same period last year. Volume increased 53 million pieces, or 13.2%, for the six months ended March 31, 2014, compared to the same period last year.

INTERNATIONAL MAIL

International mail revenue was $717 million for the three month period ended March 31, 2014, a decrease of $45 million, or 5.9%, compared to the same period last year. Revenue was $1,583 million for the six month period ended March 31, 2014, a decrease of $10 million, or 0.6%, compared to the same period last year. A weaker global economy was the primary factor contributing to the decline in international mail revenues and volumes.

PERIODICALS

Trends in hard-copy reading behavior and shifts of advertising away from print have been depressing this segment for years. Periodicals are not expected to rebound as e-readers and electronic content continue to grow in popularity with the public.

Periodicals revenue was $394 million for the three months ended March 31, 2014, a decrease of $22 million, or 5.3%, compared to the same period last year. Periodicals volume decreased by 125 million pieces for the three months ended March 31, 2014, or 7.8%, compared to the same period last year. Periodicals revenue was $803 million for the six months ended March 31, 2014, a decrease of $39 million, or 4.6%, compared to the same period last year. Periodicals volume decreased by 201 million pieces, or 6.2% for the six months ended March 31, 2014, compared to the same period last year.

OTHER

Other revenue includes both Market-Dominant and Competitive ancillary services such as Certified Mail, P.O. Box services, return receipts, delivery confirmation, and shipping supplies. In addition, other revenue generated from miscellaneous items such as the sales of money orders, passport services, and gains from the sale of real estate are also included in this category.

Operating Expenses

The following table summarizes our major categories of operating expenses for the three and six month periods ended March 31, 2014 and 2013:

Operating Expenses	Three Months Ended March 31,		Six Months Ended March 31,	
(Dollars in millions)	2014	2013	2014	2013
Compensation and benefits	$ 11,293	$ 11,647	$ 23,395	$ 24,114
Retiree health benefit premiums	745	709	1,473	1,387
PSRHBF prefunding	1,425	1,400	2,850	2,800
Workers' compensation	1,022	429	1,022	753
Transportation	1,588	1,661	3,367	3,500
Other expenses	2,486	2,327	4,758	4,499
Total operating expenses	$ 18,559	$ 18,173	$ 36,865	$ 37,053

COMPENSATION AND BENEFITS

Compensation and benefits expenses consist of costs related to our active career and non-career employees including compensation expense, retirement expense, health benefits expense and other compensation expenses more fully described below in the sections *Compensation expense, Retirement expense and Health benefits expense*.

Compensation expense. Compensation expense was $8,610 million for the three months ended March 31, 2014, compared to $8,919 million in the same period last year, a decrease of $309 million, or 3.5%. During the three months ended March 31, 2013, we recorded an expense of $259 million related to the 2013 VER incentive offer. Excluding the impact of the additional expense related to the incentive offer, compensation expense would have decreased by $50 million, or 0.6% for that period. Compensation expense was $17,930 million for the six months ended March 31, 2014, compared to $18,518 million in the same period last year, a decrease of $588 million, or 3.2%. During the six months ended March 31, 2013, we recorded an expense of $351 million related to the VER incentive offer. Excluding the impact of the additional expense related to the incentive offer, compensation expense would have decreased by $237 million, or 1.3%. There were no incentives offered during the six months ended March 31, 2014.

The decrease in compensation expense is primarily driven by changes in the staffing composition between career and non-career employees in the workforce. As of March 31, 2014, the number of career employees was reduced by approximately 14,000, or 3%, compared to March 31, 2013. These reductions have been accomplished primarily through attrition and retirements. The number of non-career employees increased by approximately 12,000, or 10%, since March 31, 2013 as a result of the increased workforce flexibility available under the new collective bargaining agreements. This increased flexibility allowed us to more efficiently manage the workforce and reduce the average cost per work hour by $0.51, or 1.2% to $41.75 for the six months ended March 31, 2014 from $42.26 for the same period last year. These compensation expense decreases were partially offset by increases in compensation required under collective bargaining agreements.

Retirement expense. The majority of employees participate in one of two Federal Government pension programs based on the starting date of their employment with the Federal Government, see Note 7, *Retirement Programs*, in the Notes to the Financial Statements. All expenses of the retirement programs, except for retiree health benefits, are included in compensation and benefits expense. Retirement expense was $1,422 million for the three months ended March 31, 2014, compared to $1,421 million for the same period last year, an increase of $1 million, or 0.1%. Retirement expense was $2,884 million for the six months ended March 31, 2014, compared to $2,902 million for the same period last year, a decrease of $18 million, or 0.6%. The six month decrease is primarily due to the reduced number of career employees when compared to the same periods last year.

Health benefits expense. Health benefits expense was $1,192 million for the three months ended March 31, 2014, compared to $1,222 million for the same period last year, a decrease of $30 million, or 2.5%. Our share of the health care premiums for our employees represents 76% and 78% of the total health care premium cost for the three months ended March 31, 2014 and 2013, respectively. Health benefits expense was $2,414 million for the six months ended March 31, 2014, compared to $2,508 million for the same period last year, a decrease of $94 million, or 3.7%. Our share of the health care premiums for our employees represents 77% and 78% of the total health care premium cost for the six months ended March 31, 2014 and 2013, respectively. The decrease in health benefits expense was driven by a reduction in the number of career employees, as noted above, and lower health care contribution percentages for certain categories of employees, consistent with our contractual agreements. However, these savings were partially offset by increases in retiree health benefits and an average premium increase of 3.4% for employees participating in the FEHB.

RETIREE HEALTH BENEFIT PREMIUMS AND PSRHBF PREFUNDING

We participate in federal employee benefit programs for retirement, health and workers' compensation benefits. United States Code Section 8909a requires us to fully fund the employer's portion of the retiree health benefits of current retirees and current postal employees who have not yet retired. The law established the Postal Service Retiree Health Benefits Fund (PSRHBF) and requires us to pay into the PSRHBF, $51.8 billion in 10 annual installments, beginning in 2007 each year through 2016. While USC 8909a dictates the amounts and timing of payments, the amounts to be paid and the timing of the payments can be rescheduled at any time with the passage of a new law, or amendment of the existing law.

As previously reported in our Annual Report on Form 10-K for the year ended September 30, 2013, we defaulted on the legally required PSRHBF payments due in 2013 and 2012 of $16.7 billion in total. We have recorded $19.6 billion as a current liability for the PSRHBF prefunding requirements. This includes the $16.7 billion due for defaulted payments and an accrual of $2.9 billion related to the $5.7 billion payment due by September 30, 2014. Absent legislative change, we anticipate that we will be forced to default on the $5.7 billion payment due by September 30, 2014.

Current law further obligates us to make additional payments of $5.7 billion in 2015 and $5.8 billion in 2016, due by September 30 of each respective year. However, given the low levels of our cash resources, we expect to be forced to default on these prefunding payments and to prioritize payments to our employees and our suppliers, in order to ensure that we will continue to be able to fulfill our other statutory obligations, including our obligation to provide universal mail service to the nation (as discussed in *Note 2, Liquidity,* in the Notes to the Financial Statements). The statutory requirement establishing the payment schedule contains no provisions addressing a payment default. As of May 9, 2014, no penalties or adverse consequences have resulted.

Under current law, not later than 2017, the Office of Personnel Management (OPM) will conduct an actuarial valuation and determine whether any further payments into the PSRHBF are required. If additional payments are required, OPM will design a schedule to fully amortize the remaining liability, by 2056. Beginning in 2017, the PSRHBF will begin to pay the Postal Service's portion of the retiree health premiums. Also beginning in 2017, we are required to fund the actuarially determined normal cost, plus any required amortization of the unfunded liability.

Under the current law, we pay the premiums for postal retirees participating in the Federal Employees' Health Benefits Program (FEHBP) through 2016. We continue to expense these payments as they become due, at a cost of $745 million and $1,473 million for the three and six month periods ended March 31, 2014, an increase of $36 million, or 5.1% and $86 million, or 6.2% from the same periods last year, respectively. The major drivers of retiree health benefits premium costs are the number of retirees and survivors receiving health benefits, the mix of plans selected by retirees, the premium costs of those plans, and the portion of premium costs allocated to the Federal Government for retiree service prior to 1971. As of March 31, 2014, there were approximately 489,000 retirees and survivors participating in FEHBP, a net increase of approximately 12,000 since March 31, 2013. In addition to the growth in the number of plan participants, retiree health benefit premium expense also increased due to an increase in the cost of premiums which averaged 3.7% beginning in January 2014 and changes in the cost sharing of premium expenses based on retiree service periods. For the six months ended March 31, 2014, retiree health benefits premiums accounted for 4.0% of our total operating expenses, compared to 3.7% for the comparable period last year. When prefunding accruals are included, retiree health benefits expenses represented 11.7% of total operating expenses, compared to 11.3% for the same period last year.

The components of retiree health benefits expense for the three and six month periods ended March 31, 2014, and 2013, are as follows:

Retiree Health Benefits	Three Months Ended March 31,				Six Months Ended March 31,			
(Dollars in millions)		2014		2013		2014		2013
(Unaudited)								
Employer premium expense	$	745	$	709	$	1,473	$	1,387
Accrual for P.L. 109-435 payment to PSRHBF		1,425		1,400		2,850		2,800
Total retiree health benefits expense	$	2,170	$	2,109	$	4,323	$	4,187

Although no PSRHBF prepayments were made during the first six months of the year, the expense has been accrued, in order to properly reflect the portion of the required annual payment allocable to this period.

WORKERS' COMPENSATION

Postal employees injured on the job are covered by the FECA, administered by DOL's OWCP. The DOL makes all decisions regarding injured workers' eligibility for benefits and we annually reimburse the DOL for all workers' compensation benefits paid to or on behalf of postal employees, including an administrative fee to the DOL.

An estimation model that combines four generally accepted actuarial valuation techniques is used to project future claim payments based upon past claim-payment experience and exposure to claims as measured by total hours worked by our employees. A liability is recorded for the present value of the estimated future payments to employees, or their qualified survivors, who have been injured through the end of the reporting period. The estimated total cost of a claim is based on the date of the injury, pattern of historical payments, frequency or severity of the claim-related injury or injuries, and the expected trend in future costs. We use the average rate of medical inflation experienced by our workers' compensation claimants over the past five years as an estimate for future medical inflation. An inflation factor based upon the Consumer Price Index - Urban Wage Earners and Clerical Workers (CPI-W) index is utilized in calculating inflation related to compensation claims. The liability for claims arising more than ten years ago is determined by an independent actuary.

The liability for estimated future workers' compensation payments is recorded at its present value. To record the liability and annual expense, an estimate is made of the amount of funding that would need to be invested at current interest rates in order to fully fund all estimated future payments. Inflation and discount (interest) rates are updated as of the date of the financial statements to determine the present value of the workers' compensation liability at fair value in accordance with GAAP. The impact of changes in the discount and inflation rates is accounted for as a change in accounting estimate and included in operating expenses.

The estimation of the liability is highly sensitive to changes in inflation and discount rates. An increase of 1% in the discount rate would decrease the liability by approximately $1.7 billion as of March 31, 2014 and decrease the related expense by approximately $1.7 billion during the six months ended March 31, 2014. A decrease of 1% in the discount rate would increase the liability by approximately $2.1 billion and increase the related expense by approximately $2.1 billion during the six months ended March 31, 2014.

At March 31, 2014, the present value of the liability for future workers' compensation payments was $16,907 million, after making the scheduled annual payment of $1,372 million on October 15, 2013, which included $50 million of prepaid administrative fees. The liability at September 30, 2013 was $17,240 million. The current portion of the liability was $1,309 million at March 31, 2014, compared to $1,322 million at September 30, 2013.

Changes in the workers' compensation liability are attributable to the combined impact of changes in the discount and inflation rates, routine changes in actuarial estimation, new compensation and medical cases, and the progression of existing cases. Workers' compensation expense, including the impact of changes in the discount rates, was $1,022 million and $429 million for the three months ended March 31, 2014 and 2013, respectively, and was $1,022 million and $753 million for the six months ended March 31, 2014 and 2013, respectively.

On a quarterly basis, changes in the number of claims and amounts paid are highly volatile and depend on a number of factors including, but not limited to, the following: the number of and timing and severity of injuries; the number of new claims and closed claims within the period; and the amount and timing of payments made by the OWCP on our behalf. Medical and compensation claims payments fluctuate significantly from quarter to quarter, so the change in the number of paid medical and compensation claims for any quarter compared to the same period last year may not necessarily be representative of the results to be expected for the full year. We experienced a $3 million, or 1.1%, decrease in compensation and medical claim payments for the three months ended March 31, 2014, compared to the same period last year. We experienced a $1 million, or 0.2%, increase in compensation and medical claim payments for the six months ended March 31, 2014, compared to the same period last year. Additional information regarding the inputs, assumptions, estimates and historical information for workers' compensation are available in *Note 9 – Workers' Compensation*.

As noted above, we are legally-mandated to participate in the federal workers' compensation program that is managed by the DOL OWCP and governed by FECA. Under FECA, workers' compensation claims for many types of injuries cannot be settled through lump-sum payments. Rather, compensation may be paid over many years. As we do not manage the FECA program, we have no ability to control the significant claims and administrative costs. These factors, compounded by COLA adjustments granted by Federal Law to those claims, results in substantially higher costs to the Postal Service than would likely be the case if claims management decisions were made by us. In addition to the constraints imposed due to the legally-mandated FECA program, actuarial estimations and projected cash payments that will be paid many years into the future also have substantial impact on our reported workers' compensation liability and expense. Future cash payments must be converted to present-day dollars, or discounted, by applying the current rates at which the liability could theoretically be settled. Discount rates can fluctuate significantly from period to period with changes in the economic and interest rate environment.

For the periods shown, the table below highlights the often significant differences between actual claims paid on behalf of Postal Service workers' compensation obligations compared to the total workers' compensation expense shown on our Condensed Statements of Operations. Total workers' compensation expense includes fluctuations in discount rates, inflation rate increases, and amounts that may not be paid until well into the future.

Workers' Compensation Expense				
	Three Months Ended March 31,		Six Months Ended March 31,	
(Dollars in millions)	2014	2013	2014	2013
(Unaudited)				
Total workers' compensation expense	$ 1,022	$ 429	$ 1,022	$ 753
Claims paid on behalf of Postal Service's workers' compensation obligations	(314)	(309)	(620)	(625)
Expense related to the long-term portion of workers' compensation	$ 708	$ 120	$ 402	$ 128

TRANSPORTATION

Transportation expense consists primarily of highway, air, and international transportation costs. Transportation expense for the three months ended March 31, 2014, was $1,588 million, a decrease of $73 million, or 4.4%, compared to $1,661 million for the same period last year. Transportation expense for the six months ended March 31, 2014, was $3,367 million, a decrease of $133 million, or 3.8%, compared to $3,500 million for the same period last year.

The following table summarizes the components of transportation expense for the three and six month periods ended March 31, 2014 and 2013:

Transportation Expense				
	Three Months Ended March 31,		Six Months Ended March 31,	
(Dollars in millions)	2014	2013	2014	2013
(Unaudited)				
Highway transportation	$ 863	$ 831	$ 1,802	$ 1,739
Air transportation	496	594	1,060	1,235
International transportation	218	227	482	506
Other transportation	11	9	23	20
Total transportation expense	$ 1,588	$ 1,661	$ 3,367	$ 3,500

Highway transportation expenses were $863 million for the three months ended March 31, 2014, compared to $831 million for the same period last year, an increase of $32 million, or 3.9%. For the six months ended March 31, 2014, highway transportation expenses were

$1,802 million, compared to $1,739 million for the same period last year, an increase of $63 million, or 3.6%. These increases are attributable to the greater use of ground transportation in lieu of air transportation during the first six months of 2014.

Air transportation expenses were $496 million for the three months ended March 31, 2014, compared to $594 million for the same period last year, a decrease of $98 million, or 16.5%. Air transportation expenses were $1,060 million for the six months ended March 31, 2014, compared to $1,235 million for the same period last year, a decrease of $175 million, or 14.2%. The decline in air transportation expenses is primarily attributable to the new air cargo contract that was implemented in October of 2013 and lower courier rates resulting from that agreement.

International transportation expenses were $218 million for the three months ended March 31, 2014, compared to $227 million for the same period last year, a decrease of $9 million, or 4.0%. International transportation expenses were $482 million for the six months ended March 31, 2014, compared to $506 million for the same period last year, a decrease of $24 million, or 4.7%. The decreases are attributable to a decline in the International Express and International Priority volumes.

OTHER EXPENSES

Other operating expenses were $2,486 million for the three months ended March 31, 2014, compared to $2,327 million for the same period last year, an increase of $159 million, or 6.8%. These expense increases were largely due to changes in the estimate of new and existing contingent liabilities as a result of the ongoing estimation evaluation process. Postal supplies expenses of $37 million and advertising expenses of $12 million associated with our advertising campaigns were also drivers of this expense. Other operating expenses were $4,758 million for the six months ended March 31, 2014, compared to $4,499 million for the same period last year, an increase of $259 million, or 5.8%. The expense increases for the six months ended March 31, 2014 were primarily related to $63 million for postal supplies and $42 million for advertising expenses, changes related to the estimate of new and existing contingent liabilities and other related costs.

In addition, we had increases in vehicle maintenance service of $12 million and $30 million for the three and six month periods ended March 31, 2014, respectively, resulting from our aging fleet of vehicles, and expenditures relating to continued improvements in technology and communications were responsible for increases of $19 million and $44 million.

These increases were offset in part by a decrease in depreciation and amortization of $19 million and $39 million for the three and six month periods ended March 31, 2014, respectively. The decrease in depreciation and amortization expense is the result of lower levels of capital investment in recent years.

Liquidity and Capital Resources
CASH FLOW ACTIVITY

Unrestricted Cash and cash equivalents totaled $3,736 million at March 31, 2014, compared to $2,326 million at September 30, 2013, respectively, an increase of $1,410 million.

The following table provides a summary of our cash flows for the six month periods ended March 31, 2014, and 2013:

Cash Flow Statement (Dollars in millions)	**Six Months Ended March 31,** **2014**	**2013**
(Unaudited)		
Operating activities:		
Net loss	**$ (2,226)**	**$ (3,130)**
Noncash depreciation and gains on sales	**907**	**988**
Prefunding of retiree health benefits	**2,799**	**2,712**
Other changes in assets and liabilities	**255**	**233**
Net cash provided by operating activities	**1,735**	**803**
Investing activities:		
Capital expenditures, net of proceeds	**(298)**	**(279)**
Other	**39**	**(103)**
Net cash used in investing activities	**(259)**	**(382)**
Financing activities:		
Other	**(66)**	**(53)**
Net cash used in financing activities	**(66)**	**(53)**
Net increase in cash and cash equivalents	**$ 1,410**	**$ 368**

Operating Activities. Operating activities generated $1,735 million of cash during the six months ended March 31, 2014, compared to $803 million for the six months ended March 31, 2013, an increase of $932 million. The increase in cash generated from operating activities was primarily due to the increased volumes of our Shipping and Packages and First-Class Packages service offerings, including the impact of holiday mailings in the first quarter of 2014, as well as price increases on Market-Dominant and Competitive products during the current period. In addition to increased revenues, reduced operating expenses, primarily compensation and benefits, contributed to the increase in net cash from operating activities during the period.

Investing Activities. Purchases of property and equipment were $333 million for the six months ended March 31, 2014, compared to $309 million in the same period last year, a decrease of $24 million, or 7.8%. Proceeds from the sale of property and equipment were $35 million and $30 million for the six months ended March 31, 2014 and 2013, respectively.

Financing Activities. In addition to the cash generated by operations, we use credit lines and notes payable to the Federal Financing Bank to help fund operations. During the six months ended March 31, 2014 and 2013, we issued and repaid $3,000 million and $2,700 million in notes payable, respectively, resulting in zero net issuance. There was no change in our revolving credit line from our September 30, 2013 balance of $4,000 million.

LIQUIDITY CHALLENGES
LIQUIDITY CONCERNS

We continue to suffer from a lack of liquidity. We held unrestricted cash of $3.7 billion and $2.3 billion as of March 31, 2014, and September 30, 2013, respectively, and had no remaining borrowing capacity on our $15 billion debt facility (See *Note 3, Debt*, for additional information). The increase in our cash balance is largely attributable to the impact of holiday mailings during the first quarter of 2014 and the price increase implemented on January 26, 2014. The current positive cash balance would not exist had we paid the $16.7 billion of the legally-mandated prefunding payments that were due to the PSRHBF by September 30, 2013. Additionally, we anticipate that we will be unable to make our next $5.7 billion payment due by September 30, 2014. As of the date of this report, May 9, 2014, we have incurred no penalties or negative consequences resulting from our inability to make these payments. We do not have sufficient liquidity to make meaningful reductions in our debt or important investments in our infrastructure. Further, this level of cash could be insufficient to support operations in the event of another significant downturn in the U.S. economy. Current projections indicate that we will continue to have a low level of liquidity throughout 2014 and for the foreseeable future.

Our net loss of $1,872 million and $2,226 million, respectively, for the three and six month periods ended March 31, 2014, which includes $1,425 million and $2,850 million of expense accrued for the legally-mandated prefunding payment for retiree health benefits, respectively.

The requirement of the *Postal Accountability and Enhancement Act,* Public Law 109-435 (P.L. 109-435) to prefund our retiree health benefit obligations, a requirement not imposed on most federal agencies or private sector businesses, the ongoing decline in First-Class Mail volume caused by changes in consumers' and businesses' uses of mail resulting from the Great Recession and the continuing migration toward electronic communication and transactional alternatives, have been major factors contributing to our losses. Without structural change to our business model, we will continue to be negatively impacted by these factors and, absent legislative change, we anticipate continuing quarterly losses for the remainder of 2014 and future periods.

In the event that circumstances leave us with insufficient cash, we would be required to implement contingency plans to ensure that mail deliveries continue. These measures could require us to prioritize payments to our employees and to our suppliers ahead of some payments to the Federal Government, as has been done in the past.

POSTAL ACTIONS TAKEN TO IMPROVE LIQUIDITY

In 2013, we accelerated the realignment of our operations to further reduce costs in order to strengthen our finances. These operational realignments included reductions in the number of mail processing facilities, realignment of retail office hours to match demand, reductions in the number of delivery routes, and consolidations of delivery offices. Additionally, we leveraged employee attrition from the 2013 VER and increased utilization of non-career employees, as provided by the new labor agreements, which allowed for better alignment of staffing and workload levels, resulting in reduced labor costs. We continue to pursue legislation to transition to a new delivery schedule, which would include package delivery Monday through Saturday (and on Sundays in some instances) and mail delivery Monday through Friday; however, changing the delivery schedule to eliminate Saturday delivery of mail is only possible if Congress refrains from blocking this change. Additionally, we continue to seek a refund of the estimated overfunding of the Federal Employees' Retirement System (FERS).

We continue to pursue the strategies within our control to increase operational efficiency and to improve liquidity. In April 2014, we revised certain service standards for Standard Mail as part of an efficiency improvement effort known as "load leveling". With this change, delivery volume will be more evenly balanced across the workweek, which is expected to improve efficiency and reduce overtime pay and operating costs. This change did not affect our service standards for First-Class Mail or Periodicals. We continue to pursue realignments in our delivery and retail operations, cost reductions throughout the organization, and revenue enhancement efforts, and continue to support comprehensive legislation to reform our current business model.

On January 26, 2014, we implemented the PRC approved price increases on Market-Dominant and Competitive products. The Market-Dominant increases include a 1.7% price increase based on the consumer price index plus a 4.3% increase approved by the PRC in December 2013 as a temporary price increase. The exigent change was approved by the PRC as a surcharge to be collected only until we recover a total amount of $3.2 billion of incremental revenue above what we would otherwise have recovered through a CPI increase alone. The Postal Service has filed an appeal with the United States Court of Appeals for the District of Columbia Circuit arguing that the PRC erred in its decision to allow the exigent increase on only a temporary basis. Some mailers filed an appeal seeking relief from the PRC's decision to allow an exigent postal increase. Additionally, prices increased an average of 2.4% for Competitive products. These Market-Dominant and Competitive products changes went into effect on January 26, 2014 and are expected to generate approximately $2.7 billion of additional annualized revenue for the Postal Service.

MITIGATING CIRCUMSTANCES

Our status as an independent establishment of the executive branch that does not receive tax dollars for our operations presents unique requirements and restrictions, but also potentially mitigates some of the financial risk that would otherwise be associated with a cash shortfall. With annual revenue in excess of $67 billion, generated almost entirely through the sale of postage and delivery services, a financially sound Postal Service continues to be vital to American commerce. The U.S. economy benefits greatly from the Postal Service and the many businesses that provide the printing and mailing services that support it. Disruption of the mail would cause undue hardship to businesses and consumers. Therefore, it is unlikely that, in the event of a cash shortfall, the Federal Government would allow us to significantly curtail or cease operations.

We continue to inform the Administration, Congress, the PRC, and other stakeholders of the immediate and longer-term financial challenges we face and the legislative changes that would help restore financial stability. We will continue to pursue legislative changes, cost reductions, and additional ways to generate revenues. Many of the structural reforms needed to ensure long-term viability, such as adjustments to pension and health benefit funding schedules and changes to delivery standards, can only be achieved with legislative change. Given the vital role that we play in the U.S. economy, we are hopeful that legislation will be enacted which will mitigate our short-term financial challenges and provide us with the authority to make needed changes to ensure long-term financial stability. However, there can be no assurances that the requests to restructure the pension and benefit payment schedules, or any other legislative changes, will be made in time to impact 2014, or any future period.

Legal Matters and Contingent Liabilities

An estimated loss contingency is accrued in our financial statements if it is probable that a liability has been incurred and the amount of the loss can be reasonably estimated. Assessing contingencies is highly subjective and requires judgments about future events. We regularly review loss contingencies to determine the adequacy of our accruals and related disclosures. The amount of the actual loss may differ significantly from these estimates. As of March 31, 2014, our estimate of our liability for material claims increased by $145 million to $1,084 million from $939 million at September 30, 2013.

Fair Value Measurements

As required by authoritative accounting literature, certain fair value disclosures for the three months ended March 31, 2014 are contained in the Notes to the Financial Statements. We did not recognize gains as a result of valuation measurements during the three and six month periods ended, March 31, 2014. All recognized losses have been incorporated into our financial statements as of March 31, 2014. See *Note 10-Fair Value Measurements.*

LEGISLATIVE UPDATE

Our legislative update section provides ongoing insights into the legislative and policy processes that may affect the Postal Service and its operations. Please also refer to the Legislative Update contained in our financial statements for the year ended September 30, 2013 filed as part of the Postal Service's Annual Report on Form 10-K as filed with the PRC on November 15, 2013.

As the debate on postal reform legislation continues in the 113th Congress, a number of reforms are urgently needed. The Postal Service's legislative requirements include:

- Require a set of specific health care plans within the Federal Employees Health Benefit (FEHB) Program that would fully integrate with Medicare and virtually eliminate the retiree health benefits (RHB) unfunded liability.
- Refund Federal Employees Retirement System (FERS) Overpayment and Adjust the FERS Normal Cost Contribution
- Adjust Delivery Frequency (Six-Day Package/Five-Day Mail Delivery)
- Streamline Governance Model (Eliminate Duplicative Oversight)
- Provide Authority to Expand Products and Services
- Require Defined Contribution Retirement System for Future Postal Employees
- Require Arbitrators to Consider Financial Condition of Postal Service
- Reform Workers' Compensation
- Right to Appeal EEOC Class Action Decisions to Federal Court

HOUSE OF REPRESENTATIVES BUDGET PROPOSAL

On April 10, 2014, the full House passed H. Con Res 96, the Fiscal Year 2015 House Budget Resolution. The measure was introduced on April 1 and marked up on April 2. The resolution would establish the budget for the United States Government for fiscal year 2015 and set appropriate budgetary levels for fiscal years 2016 through 2024. The Committee's accompanying report, "The Path to Prosperity: Fiscal Year 2015 Budget Resolution," notes that the Postal Service is unable to meet its financial obligations and in desperate need of structural reforms. Further, the report:

- Recommends giving the Postal Service the flexibility that any business needs to respond to changing market conditions, including declining mail volume, which has declined by more than 25 percent since 2006.
- Suggests the need to reform compensation of postal employees who currently pay a smaller share of the costs of their health and life insurance premiums than other federal employees.
- Concludes that the combined recommendations would save an estimated $19 billion over ten years and help restore the Postal Service to solvency.

The budget resolution was approved by roll call vote 219-205.

PRESIDENT'S FISCAL YEAR 2015 BUDGET PROPOSAL

On March 4, 2014, the President released his Fiscal Year 2015 Budget Proposal for the U.S. Government. The President's proposal is one component of the budgeting process. The President proposed a comprehensive postal reform package that would:

- Refund to the Postal Service, over a period of two years the FERS surplus and require that the Office of Personnel Management (OPM) calculate future costs using factors specific to the demographics and salary assumptions of the Postal Service workforce.
- Defer the 2014 RHB prefunding payment, and reduce the fixed payments due in 2015 and 2016 by one half.
- Shift to paying an estimate of how much the Postal Service needs to set aside annually to fund retirement health care benefits for current employees (normal cost) beginning in 2014 rather than 2017 as in current law. The missed RHB payments in 2012 (totaling $11.1 billion) and 2013 ($5.6 billion) would be incorporated into the 40-year amortization schedule for the remaining unfunded liability starting in 2017.

In addition, the Budget proposes reforms to reduce Postal Service costs and improve its revenue, including:

- Authorizing the Postal Service to adjust mail delivery frequency from six days to five-days per week upon enactment.
- Allowing the Postal Service to leverage its resources by increasing collaboration with state and local governments.
- Allowing the Postal Service to begin shifting to centralized and curbside delivery where appropriate.
- Codifying the current administrative plan (POSTPlan) to avoid small and rural Post Office closures.
- Permanently extending the January 2014 exigent price increase beyond two years, as limited by the Postal Regulatory Commission.

The President's Budget reflects reimbursement to the Postal Service in the amount of $70.8 million for free mail for the blind and overseas voting; however, the proposal contained no provisions related to the *Revenue Forgone Reform Act of 1993*, which authorizes the Postal Service to receive $29 million annually through 2035 as reimbursement for services it provided from FY 1991 through FY 1998.

CONGRESSIONAL PROPOSALS

A number of bills that could affect the Postal Service were introduced and/or considered during committee markup during the second quarter of FY 2014. A description of the bills and current status follows:

Major Congressional Postal Reform Proposals

Postal Reform Act of 2014, S. 1486

On February 6, 2014, the Senate Homeland Security and Governmental Affairs Committee held a business meeting to complete the markup of S. 1486, the *Postal Reform Act of 2014*, which began on January 29, 2014. The bill was introduced on August 1, 2013, and provides for reform on a variety of issues, including Postal Service pensions, health care, workers' compensation, operations, ratemaking, governance, innovation, and other areas. The Committee passed S. 1486, as amended, by a strong bipartisan margin of 9-1. The measure is pending consideration by the full Senate.

Other Significant Postal Legislation Proposals

There are other bills that were introduced and/or considered that could have a significant impact on the Postal Service, including:

Alaska Bypass Modernization Act of 2014, H.R. 4174

On March 12, 2014, The House Oversight and Government Reform Committee held a markup of H.R. 4174, the *Alaska Bypass Modernization Act of 2014*, which was introduced on March 6. H.R. 4174 would improve the cost coverage for Alaska bypass mail, and was approved by the Committee. The bill is now pending consideration by the full House.

Victory for Veterans Stamp Act of 2014, H.R. 4175

On March 6, 2014, H.R. 4175, the *Victory for Veterans Stamp Act of 2014*, was introduced in the House to provide for the issuance of a Victory for Veterans semipostal stamp. The proceeds from the proposed $1 dollar stamp would be divided equally, with one-third going to the Department of Veterans Affairs to fund vocational rehabilitation programs, one-third to the U.S. Treasury for Federal deficit reduction, and one-third to the U.S. Postal Service to reduce debt. The bill was referred to the House Oversight and Government Reform Committee.

Federal Leadership in Energy Efficient Transportation Act of 2014, H.R. 3963

On January 29, 2014, H.R. 3963, the *Federal Leadership in Energy Efficient Transportation Act of 2014,* or FLEET Act, was introduced in the House. The FLEET Act would require the Postal Service to reduce petroleum consumption over a 10-year period, and set minimum fuel efficiency and emission standards for all new fleet vehicles. It also directs the Postal Service to replace older vehicles. H.R. 3963 was referred to the House Oversight and Government Reform and the House Energy and Commerce Committees.

BOARD OF GOVERNORS NOMINATIONS

On February 12, 2014, President Obama announced his nomination of Victoria Reggie Kennedy, of Massachusetts, to serve on the Board of Governors of the United States Postal Service for a term expiring on December 8, 2016. This nomination brought to four the total number of Board of Governors nominations pending before the Senate. On January 6, the President resubmitted the following nominations to the Senate for consideration during the Second Session of the 113th Congress: James C. Miller, III, for a term expiring December 8, 2017, Stephen Crawford, for a term expiring December 8, 2015, and David Michael Bennett, for a term expiring December 8, 2018.

As of the date of this report no action has been taken on these nominations. The Board of Governors currently has only 4 of the 9 authorized seats filled.

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 rate fluctuations 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.

See our 2013 Annual Report on Form 10-K, Financial Section Part II, Item 7A-*Quantitative and Qualitative Disclosures about Market Risk*.

Item 4 – Controls and Procedures

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

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 P.L. 109-435, 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 Chief Financial Officer, of the effectiveness of the design and operation of disclosure controls and procedures as of March 31, 2014. Based upon, and as of the date of, the evaluation, the Postmaster General and Chief Financial Officer concluded that our disclosure controls and procedures were effective.

Internal Controls
There have been no changes in the Postal Service's internal controls over financial reporting during the quarter ended March 31, 2014, that have materially affected, or are reasonably likely to materially affect, the Postal Service's internal control over financial reporting.

Part II. OTHER INFORMATION

Item 1 – Legal Proceedings

For a discussion of legal proceedings affecting us, please refer to our annual report Form 10-K, filed on November 15, 2013, as well as the information under the caption "*Legal Matters and Contingent Liabilities*" within *Item 2 - "Management's Discussion and Analysis of Financial Condition and Results of Operations"* included in this report.

Item 1A – Risk Factors

There have been no material changes in risk factors from those disclosed in Part I, Item 1A of our Annual Report on Form 10-K for the year ended September 30, 2013.

Item 4 – Mine Safety Disclosures

Not applicable.

Item 6 – Exhibits

Exhibit Number	Description of Exhibit
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/Patrick R. Donahoe

Patrick R. Donahoe

Postmaster General and Chief Executive Officer

Date: May 9, 2014

/s/Joseph Corbett

Joseph Corbett

Chief Financial Officer and Executive Vice President

Date: May 9, 2014

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, Patrick R. Donahoe, 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 auditors and the audit 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: May 9, 2014

/s/Patrick R. Donahoe

Patrick R. Donahoe

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 auditors and the audit 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: May 9, 2014

/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 March 31, 2014, (the Report), I, Patrick R. Donahoe, 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: May 9, 2014

/s/Patrick R. Donahoe

Patrick R. Donahoe

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 March 31, 2014 (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: May 9, 2014

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