

USPS-FY10-39

FY 2010 Competitive Products Fund Reporting Materials

I. PREFACE**A. Purpose and Content**

USPS-FY10-39, Competitive Products Fund Reporting Materials, includes a copy of the Postal Service's annual report to the Secretary of the Treasury regarding the Competitive Products Fund, required by section 2011(i), and other Competitive Products Fund materials provided in accordance with Commission Rules 3060.20 through 3060.23. Specifically, this year that other material includes PRC Forms CP-01, CP-02, CP-03, and, for the first time, PRC Form CP-04 (Statement of Allocated Assets and Liabilities for Competitive Products), which was not required until after FY 2010.

B. Predecessor Document

Last year, predecessor materials were filed as USPS-FY09-39. Predecessor materials were not formally filed as part of Docket No. ACR2008. Instead, the Treasury Report for FY08 was filed by letter to the Commission dated December 30, 2008. The PRC Forms for FY08 were submitted by letter dated Jan. 15, 2009, although some of the figures reported in those forms were later superseded by figures in the Commission's ACD, as reflected in the Postal Service's letter of July 15, 2009, regarding calculation of the assumed income tax.

C. Methodology

These materials draw up cost and revenue data reported throughout the Postal Service's FY09 ACR, and therefore are implicitly based on the methodologies upon which the ACR is based. For purposes of specifically developing the PRC Forms, the procedures employed track those previously endorsed by the Commission.

D. Input/Output

For PRC Forms CP-01 and CP-02, inputs are this year's FY10 CRA and last year's PRC Forms CP-01 and CP-02 (albeit modified to reflect the Commission's FY09 ACD). Inputs for PRC Forms CP-03 and CP-04 come from accounting records.

II. ORGANIZATION

USPS-FY09-39 consists of one pdf file which includes this Preface, and four Excel files. Hardcopy printouts of those files are also provided.

**The Postal Service's Annual Report to the
Secretary of the Treasury
Regarding the Competitive Products Fund
For Fiscal Year 2010,
Required by 39 U.S.C. § 2011(i)**

CORPORATE TREASURY
FINANCE



December 29, 2010

Mr. Richard L. Gregg
Department of the Treasury
1500 Pennsylvania Avenue, NW
Room 2112 MT
Washington, DC 20220-2112

Dear Mr. Gregg:

Pursuant to 39 U.S.C. 2011(i)(1), the United States Postal Service hereby submits the enclosed *Competitive Products Fund Report* (CPFR) for the fiscal year ending September 30, 2010.

Additional information regarding the Postal Service is available elsewhere. The *2010 United States Postal Service Annual Report* is available on www.usps.com, as is our *2010 Comprehensive Statement on Postal Operations*. In addition, we file an *Annual Compliance Report* with the Postal Regulatory Commission within 90 days of the end of each fiscal year. We expect to discuss aspects of these reports with management of the Federal Financing Bank in the coming weeks.

Sincerely,

A handwritten signature in blue ink that reads "Robert J. Pedersen".

Robert J. Pedersen
Treasurer

Enclosures

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Competitive Products Fund Report For Fiscal Year Ending September 30, 2010

BACKGROUND

On December 18, 2008, the Postal Regulatory Commission (PRC) issued Order No. 151, Docket No. RM2008-5 Order Establishing Accounting Practices and Tax Rules for Competitive Products. With respect to the Competitive Products Fund (CPF), a fund established in the United States Treasury (listed in Table III of the Monthly Statement of the Public Debt as of September 30, 2010), the PRC rules are based on a theoretical, on-paper-only enterprise. Necessarily, the PRC's rules are distinct from generally accepted accounting principles (GAAP).

In Fiscal Year 2008, the Competitive Products Fund generated pretax earnings of \$14.4 million, which produced a tax obligation of \$4.9 million. As required by law, this amount was transferred to the Postal Service Fund on July 15, 2009.

In Fiscal Year 2009, the Competitive Products Fund generated pretax earnings of \$368.2 million, which produced a tax obligation of \$128.9 million. As required by law, this amount was transferred to the Postal Service Fund on January 15, 2010.

In Fiscal Year 2010, the Competitive Products Fund generated pretax earnings of \$550.8 million, which produced a tax obligation of \$192.8 million. As required by law, this amount will be transferred to the Postal Service Fund by January 15, 2011.

The Postal Service Fund is also held within the U.S. Treasury and is listed in Table III of the Monthly Statement of the Public Debt as of September 30, 2010.

The PRC's Order No. 151 also directed the Postal Service to produce its first Statement of Allocated Assets and Liabilities for Competitive Products within 90 days of the close of Fiscal Year 2010.¹ This Statement (attached) was produced in accordance with rules set forth by the PRC.

As discussed in our *2010 United States Postal Service Annual Report ("Annual Report")*, the law divides our services into two broad categories: market-dominant and competitive (or "Competitive Products Fund"). Throughout this document and in the day-to-day operation of the organization, we refer to market-dominant services as "Mailing Services" and competitive services as "Shipping Services". Mailing Services include, First-Class Mail, Standard Mail, Periodicals, and Package Services. Price increases for these services are subject to a price cap based on the Consumer Price Index — All Urban Consumers (CPI-U). Shipping Services include, but are not limited to Priority Mail, Express Mail, Bulk Parcel Post, and Bulk International Mail. The regulations for Shipping Services place no upper limit on price changes but do set a price floor.

Although the law divides our services into market-dominant and competitive categories, and revenue is monitored by category and class, we operate one fully-integrated network, which is one segment throughout the United States, its possessions and territories. Our *Annual Report* includes financial statements for a single entity, the Postal Service, which are produced in accordance with GAAP.

¹ Hereafter, all years referenced are government fiscal years unless otherwise noted.

RISK FACTORS

The risk factors identified in this section are discussed in our *Annual Report*, and they are particularly relevant to our Shipping Services.

- Adverse changes in the economy directly impact our business, negatively affecting our results of operations.
- Our ability to generate sufficient cash flows is substantially dependent on our ability to increase efficiency, reduce costs, and generate revenue, as well as on legislative change.
- Our business and results of operations are adversely affected by electronic diversion. If we do not compete effectively with electronic communications services, or grow marketing mail, package services, or revenue from other sources, this adverse impact will become more substantial over time.
- While the Postal Act of 2006 (P.L. 109-435) limited price increases on our Mailing Services to the rate of inflation, our costs are not similarly limited. Accordingly, we may not be able to increase prices sufficiently to offset increased costs. This would adversely affect our results of operations.
- Adverse events may call into question our reputation for quality and reliability, which could diminish the value of the Postal Service brand and potentially adversely affect our business and results of operations.
- Fuel expenses are a material part of our operating costs. A significant increase in fuel prices could adversely affect our costs and results of operations.
- We are subject to Congressional oversight and regulation from the Postal Regulatory Commission and other government agencies. We have a wide variety of stakeholders whose interests and needs are sometimes in conflict. If we cannot successfully address the various, and sometimes conflicting, concerns of our stakeholders, we may be subject to greater legislation and regulation, which could increase costs or otherwise place additional burdens on operations.
- We rely extensively on technology to operate our systems. A significant failure in a material system could impair our reputation for reliable service and adversely affect our results of operations.
- A failure on our part to protect the privacy of information we obtain from customers could damage our reputation and result in a loss of business.
- We are subject to the risk of biohazards and other threats placed in the mail.
- We may be adversely impacted by the legal or regulatory responses to actual or perceived global climate change.
- We are also subject to risks and uncertainties that affect many other businesses, including:
 - market acceptance of new service and growth initiatives;
 - adverse weather conditions or natural disasters, such as hurricanes, which can damage property and disrupt our operations;

- international conflicts or terrorist activities and the effects these events may have on business or results of operations; and
- Changes in interest rates and foreign currency exchange rates.

These risks and others could clearly affect the liquidity of the Competitive Products Fund that is held within the U.S. Treasury.

RESULTS OF OPERATIONS

Using PRC methodology, Shipping Services revenue totaled \$8.68 billion in 2010 and volume totaled 1.4 billion pieces. In 2010, Shipping Services accounted for 1% of total Postal Service mail volume and 13% of total revenue.

Before further discussion, it may be useful to define several terms that are part of our regulatory lexicon. Coverage is defined as the ratio of revenue to attributable costs, using PRC-determined methodology. Institutional costs are those costs that are not attributable. When a product's revenue exceeds its attributable costs, the difference represents contribution toward covering institutional costs.

In addition to covering attributable costs, Shipping Services are required, by the PRC, to bear 5.5% of postal-wide institutional costs. Total costs for Shipping Services are by definition equal to their attributable costs plus 5.5% of postal-wide institutional costs. In 2010, the contribution from Shipping Services equaled 7.12% of the institutional costs of the Postal Service. The difference between this 7.12% and the required 5.5% threshold is the "net income" for Shipping Services, and it is used to calculate the required tax transfer from the Competitive Products Fund in the U.S. Treasury to the Postal Service Fund, also within the Treasury. For 2010, this non-GAAP net income totaled \$550.8 million. Tax due will be transferred from the Competitive Products Fund to the Postal Service Fund by January 15, 2011.

PRC Forms CP-01, CP-02, CP-03, and CP-04

For Fiscal Year 2010

Table 1 Competitive Products Income Statement (\$ in 000s)				
			PRC Form CP-01	
	FY 2010	FY 2009	\$ Change from SPLY	% Change from SPLY
Revenue				
(1) Mail and Services Revenues @	8,677,800	8,132,800	545,000	6.7%
(2) Investment Income	198	2	196	N/A
(3) Total Competitive Products Revenue	8,677,998	8,132,802	545,196	6.7%
Expenses				
(4) Volume Variable Costs	6,092,700	6,093,400	(700)	0.0%
(5) Product Specific Costs	164,200	81,300	82,900	102.0%
(6) Total Competitive Products Attributable Cost	6,256,900	6,174,700	82,200	1.3%
(7) Net Income Before Institutional Cost Contribution	2,421,098	1,958,102	462,996	
(8) Required Institutional Cost Contribution	1,870,314	1,589,874	280,440	17.6%
(9) Net Income (Loss) Before Tax	550,785	368,228	182,557	
(10) Assumed Federal Income Tax *	192,775	128,880	63,895	49.6%
(11) Net Income (Loss) After Tax	358,010	239,348	118,662	
Line (1): Total revenues from Competitive Products volumes and Ancillary Services				
Line (2): Income provided from investment of surplus Competitive Products revenues				
Line (3): Sum total of revenues from Competitive Products volumes, services, and investments				
Line (4): Total Competitive Products volume variable costs as shown in the Cost and Revenue Analysis (CRA) report				
Line (5): Total Competitive Products product specific costs as shown in the CRA report				
Line (6): Sum total of Competitive Products costs (sum of lines 4-5)				
Line (7): Difference between Competitive Products total revenues and attributable costs (line 3 less line 6)				
Line (8): Minimum amount of Institutional Cost contribution required under 39 CFR 3015.7 of this chapter.				
Line (9): Line 7 less line 8				
Line (10): Total assumed Federal income tax as calculated under 39 CFR 3060.40				
Line (11): Line 9 less line 10				

@ Note: Mail and Services revenues have been adjusted to include losses from the sales and impairments of property and equipment, in accordance with Order No. 479 (June 25, 2010). The loss for FY 10 was \$8M, with the amount allocated to Competitive Products (Building and Equipment allocation) of \$700k.

* Note: 2010 Assumed Federal Income Tax is estimated based on the 2010 Federal corporate tax rate.

Table 2 Annual Summary of Competitive Products Financials (\$ in 000s)				
PRC Form CP-02				
		Beginning Value	Change from Prior Year	Ending Value
(1)	Cumulative Net Income (Loss) After Assumed Federal Income Tax *	\$297,924	\$358,010	\$655,934
(2)	Total Financial Obligations (List of Financial Obligations)	\$0	\$0	\$0
(3)	Total Financial Investments (List of Financial Investments)	\$9,452	\$239,546	\$248,998
Line 1:	Beginning Value: Sum total of Net Income (Loss) as of October 1 of Reportable Fiscal Year			
	Change from Prior Year: Amount of Net Income (Loss) of Reportable Fiscal Year			
	Ending Value: Sum of Beginning Value and the Change from Prior Year			
Line 2:	Beginning Value: Sum total of Financial Obligations as of October 1 of Reportable Fiscal Year			
	Change from Prior Year: Amount of Net Financial Obligations of Reportable Fiscal Year			
	Ending Value: Sum of Beginning Value and the Change from Prior Year			
Line 3:	Beginning Value: Sum total of Financial Investments as of October 1 of Reportable Fiscal Year			
	Change from Prior Year: Amount of Net Financial Investments of Reportable Fiscal Year			
	Ending Value: Sum of Beginning Value and the Change from Prior Year			

* Note: 2010 Assumed Federal Income Tax is estimated based on the 2010 Federal corporate tax rate.

Table 3
Competitive Products Property and Equipment Assets (FY 2010)
(Actual \$)

PRC Form CP-03

Finance Number	Finance Location	Asset Identifier	Asset Description	Cost	Accumulated Depreciation	Net Book Value
VP Shipping	475 L'Enfant Plaza, Wash, Dc 20260	1597470	Copying Machine	\$10,543.00	\$10,543.00	\$0.00
ClickNShip	475 L'Enfant Plaza, Wash, Dc 20260	1057123	Micro Computer System	\$4,812.00	\$4,812.00	\$0.00
ClickNShip	475 L'Enfant Plaza, Wash, Dc 20260	1138602	Micro Computer System	\$11,610.00	\$11,610.00	\$0.00
ClickNShip	475 L'Enfant Plaza, Wash, Dc 20260	1138603	Micro Computer System	\$5,290.00	\$5,290.00	\$0.00
ClickNShip	475 L'Enfant Plaza, Wash, Dc 20260	1147567	Micro Computer System	\$23,138.00	\$23,138.00	\$0.00
ClickNShip	475 L'Enfant Plaza, Wash, Dc 20260	1147568	Micro Computer System	\$23,138.00	\$23,138.00	\$0.00
ClickNShip	475 L'Enfant Plaza, Wash, Dc 20260	1147569	Micro Computer System	\$23,138.00	\$23,138.00	\$0.00
ClickNShip	475 L'Enfant Plaza, Wash, Dc 20260	1602540	Micro Computer System	\$9,702.00	\$9,702.00	\$0.00
Total			Total	\$111,371.00	\$111,371.00	\$0.00

Table 4			
Statement of Allocated Assets and Liabilities for Competitive Products			
(\$ in thousands)			
FY2010			PRC Form CP-04
	USPS Annual Report	Corp. Fin. Reporting - Competitive Products	Distributed on Basis of:
Total Net Assets			
Cash and Cash Equivalents	1,161,000	150,233	Revenue
Net Accounts Receivable	1,079,000	139,623	Revenue
Supplies, Advances, and Prepayments	114,000	14,752	Revenue
Appropriations and Receivables - Revenue Forgone	377,000	0	Non Competitive
Total Current Assets	2,731,000	304,608	
Property and Equipment			
Buildings	23,822,000	2,537,043	Depreciation cost for Buildings
Leasehold Improvements	1,026,000	109,269	Depreciation cost for Leasehold Improvements
Equipment	20,646,000	1,180,951	Depreciation cost for Equipment
Land	2,974,000	316,731	Depreciation cost for Buildings
Accumulated Depreciation	28,333,000	2,519,221	Depreciation cost for Bld/Eq/Leasehold/Vehicle
Construction in Progress	1,460,000	155,518	Depreciation cost for Buildings & Leaseholds
Total Property and Equipment, Net	21,595,000	1,780,291	
Total Assets	24,326,000	2,084,898	
Total Assets Determined from Section 2011(e)(5)		3,147,784	
Total Net Liabilities	USPS Annual Report	Competitive Products	Distributed on Basis of:
Liabilities:			
Current Liabilities			
Compensation and Benefits	2,924,000	273,686	Labor
Workers' Compensation	1,115,000	104,699	Workers' Comp Expense
Payables and Accrued Expenses	2,033,000	263,070	Revenue
Customer Deposit Accounts	1,429,000	184,913	Revenue
Deferred Revenue-Prepaid Postage	2,584,000	334,370	Revenue
Outstanding Postal Money Orders	639,000	3,400	Actual International Money Orders Outstanding
Prepaid Box Rent and Other Deferred Revenue	452,000	2,510	Actual Money Order Allocation
Debt	7,500,000	674,250	Volume Variable Interest Expense
Non-Current Liabilities			
Workers' Compensation	11,474,000	1,077,409	Workers' Comp Expense
Employee Accumulated Leave	2,088,000	196,063	Repriced Annual Leave
Deferred Appropriation and Other Revenue	392,000	0	Non Competitive
Long-Term Portion of Capital Lease Obligation	512,000	54,528	Leasehold Depreciation
Deferred Gains on Sales of Property	309,000	26,284	Depreciation cost for Buildings & Equipment
Contingent Liabilities and Other	248,000	23,213	Labor
Long-Term Portion Notes Payables	4,500,000	0	Non Competitive
Total Liabilities	38,199,000	3,218,393	

Competitive Mail Revenue Allocation Keys

	Revenue (\$ 000)
Competitive Mail %:	
Competitive Mail (A)	8,678.5
All Mail (B)	67,076.6
Percent of Total	12.94%

CRA Based Allocation Keys

Allocation Keys:	Equipment (\$ 000)	Depreciation		Leasehold (\$ 000)	Repriced Annual Leave (\$ 000)	Workers Comp (\$ 000)	Interest Expense (\$ 000)	Total Labor (\$ 000)
		Vehicle (\$ 000)	Building (\$ 000)					
Competitive Mail:								
Domestic Competitive Mail (C)	39,431	7,604	95,520	15,868	4,507	58,162	9,776	2,424,154
International Competitive Mail (D)	4,548	336	10,527	1,749	483	6,239	1,180	252,669
Total Competitive Mail	43,979	7,940	106,047	17,617	4,990	64,401	10,956	2,676,823
Total USPS Volume Variable Costs (C)	768,194	45,575	995,568	165,386	53,164	686,121	121,865	28,596,863
Competitive Products Share	5.72%	17.42%	10.65%	10.65%	9.39%	9.39%	8.99%	9.36%

(A) Source: Docket No. ACR 2010, USPS-FY10-NP11

	(in millions)
Mail and Services Revenues	8,678.5
Investment Income	0.0
Total Competitive Products	8,678.5

(B) Source: Public Cost and Revenue Analysis

	(in millions)
Total All Mail and Services	66,407.2
Miscellaneous	556.2
Transit Revenue	0.1
Appropriation Rrevenue Foregone	88.9
Total Operating Revenue	67,052.5
Investment Income	24.1
Total All	67,076.6

(C) Source: Docket No. ACR 2010, USPS-FY10-NP13

(FY08.Crpt.xls, FY08.Brpt.xls, FY08.Krpt.xls)

	Equipment (\$ 000)	Vehicle (\$ 000)	Depreciation Building (\$ 000)	Leasehold (\$ 000)	Repriced Annual Leave (\$ 000)	Workers Comp (\$ 000)	Interest Expense (\$ 000)	Total Labor (\$ 000)
Total USPS Volume Variable Costs	768,194.4	45,575.2	995,568.4	165,386.2	53,163.8	686,120.7	121,865.0	28,596,862.7
Domestic Competitive Mail	39,430.7	7,603.5	95,519.9	15,868.0	4,506.7	58,162.4	9,775.9	2,424,153.6
International			22,255	3,697				
			85.75%	14.25%				

(D) Source: Docket No. ACR 2010, USPS-FY10-NP3, FY10ICRA CRpt.xls, FY10ICRA KRpt.xls

	Equipment (\$ 000)	Vehicle (\$ 000)	Depreciation Building and Leasehold (\$ 000)	Repriced Annual Leave (\$ 000)	Workers Comp (\$ 000)	Interest Expense (\$ 000)	Total Labor (\$ 000)
International Competitive Mail	4,548	336	12,276	483	6,239	1,180	252,669