USPS-FY11-39

FY 2011 Competitive Products Fund Reporting Materials

I. PREFACE

A. Purpose and Content

USPS-FY11-39, 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 CP-04.

B. Predecessor Document

Last year, predecessor materials were filed as USPS-FY10-39.

C. Methodology

These materials draw upon cost and revenue data reported throughout the Postal Service's FY11 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 from the FY11 CRA and last year's PRC Forms CP-01 and CP-02. Inputs for PRC Forms CP-03 and CP-04 come from accounting records.

II. ORGANIZATION

USPS-FY11-39 consists of one PDF file, which includes this Preface, and four Excel files.

The Postal Service's Annual Report to the

Secretary of the Treasury

Regarding the Competitive Products Fund

For Fiscal Year 2011,

Required by 39 U.S.C. § 2011(i)

CORPORATE TREASURY
FINANCE

UNITED STATES
POSTAL SERVICE

December 29, 2011

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, 2011.

Additional information regarding the Postal Service is available elsewhere. The *2011 United States Postal Service Annual Report* on form 10 – K is available on http://about.usps.com/who-we-are/financials/. 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,

EMSchafer

Elizabeth M. Schafer
Treasurer

Enclosures

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Competitive Products Fund Report
For Fiscal Year Ending
September 30, 2011

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, 2011), 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 was transferred to the Postal Service Fund on January 14, 2011.

In Fiscal Year 2011, the Competitive Products Fund generated pretax earnings of $691.1 million, which produced a tax obligation of $241.9 million. As required by law, this amount will be transferred to the Postal Service Fund by January 15, 2012.

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, 2011.

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 2011.[1] This Statement (attached) was produced in accordance with rules set forth by the PRC.

As discussed in our *2011 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*

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

includes financial statements for a single entity, the Postal Service, which are produced in accordance with GAAP.

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.
- Even with some regulatory and legislative changes, our ability to generate sufficient cash flows from current and future management actions to increase efficiency, reduce costs, and generate revenue may not be sufficient to meet all our financial obligations.
- 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.
- Adverse events may call into question our reputation for quality, reliability or our ability to deliver the mail, and could diminish the value of the Postal Service brand. This could potentially adversely affect our revenues and results of operations.
- Our need to restructure our operations in response to declining mail volumes may result in significant costs. It is possible that the measures being considered may be insufficient to reduce our workforce and physical infrastructure to a level commensurate with lower and declining mail volumes.
- Existing laws and regulations limit our ability to introduce new services or products, enter new markets, or generate new revenue streams, and thus grow and evolve as an important American institution.
- An unaffordable union contract arrived at either through negotiation or arbitration could have a significant impact on our future 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.
- We rely extensively on computer systems and technology to manage the delivery of mail, process transactions, summarize results and manage our business. Disruptions in both our primary and secondary (back-up) systems could harm our ability to run our business and potentially result in significant losses of revenue or additional operating costs. In addition, such disruptions could impair our reputation for reliable service, which would also adversely affect results of operations.

- Due to our current cash constraints, our operational performance in the future could be at risk as a result of inadequate capital investment in transportation equipment, mail processing equipment, facilities, or information technology which are either essential to operations or to improve the quality of our services.

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

- 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.

- International conflicts or terrorist activities and the effects of these events may have adverse impacts on business operations or our financial results. In addition, 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 product and service initiatives;
    - Adverse weather conditions or natural disasters, such as hurricanes, which can damage property and disrupt operations;
    - Widespread outbreak of an illness or any other communicable disease, or any other public health crisis; 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 $9 billion in 2011 and volume totaled 1.5 billion pieces. In 2011, Shipping Services accounted for 1% of total Postal Service mail volume and 14% 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 2011, the contribution from Shipping Services equaled 7.84% of the institutional costs of the Postal Service. The difference between this 7.84% 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 2011, this non-GAAP net income totaled $691.1 million. Tax due will be transferred from the Competitive Products Fund to the Postal Service Fund by January 15, 2012.

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

For Fiscal Year 2011

Table 1
Proposed Competitive Products Income Statement
($ in 000s)

PRC Form CP-01

	FY 2011	FY 2010	$ Change from SPLY	% Change from SPLY
Revenue				
(1) Mail and Services Revenues (a)	8,996,400	8,677,800	318,600	3.7%
(2) Investment Income	290	198	92	46.5%
(3) Total Competitive Products Revenue	8,996,690	8,677,998	318,692	3.7%
Expenses				
(4) Volume Variable Costs	6,508,700	6,092,700	416,000	6.8%
(5) Product Specific Costs	171,400	164,200	7,200	4.4%
(6) Total Competitive Products Attributable Cost	6,680,100	6,256,900	423,200	6.8%
(7) Net Income Before Institutional Cost Contribution	2,316,590	2,421,098	(104,508)	
(8) Required Institutional Cost Contribution	1,625,459	1,870,314	(244,855)	-13.1%
(9) Net Income (Loss) Before Tax	691,131	550,785	140,347	
(10) Assumed Federal Income Tax *	241,896	192,775	49,121	25.5%
(11) Net Income (Loss) After Tax	449,235	358,010	91,225	

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

(a) Note: Mail and Services revenues have been adjusted to include losses from the sales and impairments of property and equipment. The loss for FY 11 was $6M with the amount allocated to Competitive Products (Building and Equipment allocation) of $500k. The loss for FY10 was $8M with the amount allocated to Competitive Products (Building & Equipment allocation) of $7000k.

* Note: 2011 Assumed Federal Income Tax is estimated based on the 2011 and 2010 Federal corporate tax rates respectively.

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 *	$655,934	$449,235	$1,105,169
(2)	Total Financial Obligations (List of Financial Obligations)	$0	$0	$0
(3)	Total Financial Investments (List of Financial Investments)	$248,998	$358,301	$607,299
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: 2011 Assumed Federal Income Tax is estimated based on the 2011 Federal corporate tax rate.

Table 3
Competitive Products Property and Equipment Assets (FY 2011)
(Actual $)

PRC Form CP-03

Finance Number	Finance Location	Asset Identifier	Asset Description	Cost	Accumulated Depreciation	Net Book Value
ClickNShip	475 L'Enfant Plaza, Wash, Dc 20260	1916084	Shredder	$3,673.92	$275.54	$3,398.38
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	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	$87,601.92	$84,203.54	$3,398.38

Table 4
Statement of Allocated Assets and Liabilities for Competitive Products
($ in thousands)

	FY2011		FY 2010	PRC Form CP-04
Total Net Assets	USPS Annual Report	Corp. Fin. Reporting - Competitive Products	Corp. Fin. Reporting - Competitive Products	Distributed on Basis of:
Cash and Cash Equivalents	1,488,000	203,707	150,233	Revenue
Net Accounts Receivable	1,041,000	142,513	139,623	Revenue
Supplies, Advances, and Prepayments	120,000	16,428	14,752	Revenue
Total Current Assets	2,649,000	362,648	304,608	
Property and Equipment				
Buildings	24,263,000	2,744,145	2,537,043	Depreciation cost for Buildings
Leasehold Improvements	1,112,000	125,656	109,269	Depreciation cost for Leasehold Improvements
Equipment	20,409,000	1,079,636	1,180,951	Depreciation cost for Equipment
Land	2,952,000	333,871	316,731	Depreciation cost for Buildings
Accumulated Depreciation	29,023,000	2,604,101	2,519,221	Depreciation cost for Bld/Eq/Leasehold/Vehicle
Construction in Progress	624,000	70,549	155,518	Depreciation cost for Buildings & Leaseholds
Total Property and Equipment, Net	20,337,000	1,749,757	1,780,291	
Appropriations and Receivables - Revenue Forgone	427,000	0	0	Non Competitive
Total Assets	23,413,000	2,112,405	2,084,898	
Total Assets Determined from Section 2011(e)(5)		3,205,240	3,147,784	
Total Net Liabilities	USPS Annual Report	Competitive Products	Competitive Products	Distributed on Basis of:
Liabilities:				
Current Liabilities				
Compensation and Benefits	2,338,000	231,228	273,686	Labor
Retire Health Benefits	7,000	692	0	Labor
Workers' Compensation	1,255,000	124,371	104,699	Workers' Comp Expense
Payables and Accrued Expenses	1,812,000	248,063	263,070	Revenue
Customer Deposit Accounts	1,386,000	189,743	184,913	Revenue
Deferred Revenue-Prepaid Postage	3,497,000	478,739	334,370	Revenue
Outstanding Postal Money Orders	688,000	6,545	3,400	Actual International Money Orders Outstanding
Prepaid Box Rent and Other Deferred Revenue	502,000	2,729	2,510	Actual Competitive Deferred Box Rents
Debt	7,500,000	679,500	674,250	Volume Variable Interest Expense
Non-Current Liabilities				
Workers' Compensation	13,887,000	1,376,202	1,077,409	Workers' Comp Expense
Employee Accumulated Leave	2,082,000	206,326	196,063	Repriced Annual Leave
Deferred Appropriation and Other Revenue	326,000	0	0	Non Competitive
Long-Term Portion of Capital Lease Obligation	460,000	51,980	54,528	Leasehold Depreciation
Deferred Gains on Sales of Property	345,000	29,365	26,284	Depreciation cost for Buildings & Equipment
Contingent Liabilities and Other	768,000	75,955	23,213	Labor
Long-Term Portion Notes Payables	5,500,000	0	0	Non Competitive
Total Liabilities	42,353,000	3,701,439	3,218,393	