USPS-FY14-39

FY 2014 Competitive Products Fund Reporting Materials

I. PREFACE

A. Purpose and Content

USPS-FY14-39, 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

USPS-FY13-39

C. Methodology

These materials draw upon cost and revenue data reported throughout the Postal Service's FY 2014 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 FY14 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-FY14-39 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 2014, Required by 39 U.S.C. § 2011(i)

CONTROLLER
FINANCE

UNITED STATES
POSTAL SERVICE

December 29, 2014

Mr. David Lebryk
Department of the Treasury
1500 Pennsylvania Avenue NW
Room 2112 MT
Washington, DC 20220-2112

Dear Mr. Lebryk:

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, 2014.

Additional information regarding the Postal Service is available elsewhere. The *2014 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.

Sincerely,

Jon Stratton, for

Maura McNerney
VP, Controller

Enclosures

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Competitive Products Fund Report
For Fiscal Year Ending
September 30, 2014

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, 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 2014, the Competitive Products Fund generated pretax earnings of $2.422 billion, which produced a tax obligation of $848 million. As required by law, this amount will be transferred to the Postal Service Fund by January 15, 2015.

As discussed in our *2014 United States Postal Service Annual Report on Form 10-K ("10-K"),* the law divides our services into two broad categories: Market-Dominant and Competitive. Market-Dominant services include, but are not limited to, First-Class Mail, Standard Mail, Periodicals, and certain parcel services. Price increases for these services are subject to a price cap by class of mail based on the Consumer Price Index–All Urban Consumers (CPI-U). Competitive services, such as Priority Mail, Priority Mail Express, Parcel Select and Parcel Return Service and some types of International Mail have greater pricing flexibility and are commonly referred to as "Shipping and Package Services."

On January 26, 2014, the Postal Service implemented a temporary exigent price increase on Market-Dominant services. The exigent price change, in conjunction with a simultaneous price cap change based on CPI-U, increased the price of a one ounce First-Class Mail single-piece letter from $0.46 to $0.49, and raised the other Market-Dominant rates as well. The exigent rate change was approved as a surcharge to be collected only until we recover a total amount of $3.2 billion of incremental revenue above what would otherwise have been recovered through a CPI-U increase alone, although court review of that limitation is pending. As of September 30, 2014, the Postal Service has collected approximately $1.4 billion in such incremental revenue.

Prices for Competitive services, by law, must cover costs attributable to each product, as well as an appropriate share of the institutional costs of the Postal Service. The required share of institutional costs to be covered by Competitive market services as determined by the PRC is 5.5% of total institutional costs. By law, changes in prices for our Competitive services must be announced at least 30 days prior to the implementation date. Prices for these Competitive services – including Priority Mail Express, Global Express Guaranteed, Express Mail International, Priority Mail, Priority Mail International, Parcel Select, and Parcel Return Service – increased an average of 2.4% in January, 2014. We offer contract prices, rebates, online price reductions, and other incentives to encourage customers to increase their volumes and in turn increase Postal Service revenue.

Reclassification of Certain Postal Services
Periodic reclassifications and expansions of services from Market-Dominant to Competitive, which require approval from the PRC, are necessary to rationalize service offerings. The additional flexibility provided in Competitive services allows us to better offer services that meet customer needs, to increase business for the Postal Service and to allow us to price our products and services competitively within the markets in which we operate. The Postal Service's Competitive services generally include most of our shipping, package, and expedited delivery services. Although there were reclassification dockets active before the Postal Regulatory Commission during FY 2014, none of them resulted in any reporting changes affecting the FY 2014 results reflected in this Report.

While there are distinct legal and regulatory classifications of postal services known as either Market-Dominant or Competitive which are required to be reported in the attachments to this document, Postal Service management utilizes the following broad service categories to evaluate performance and manage the business: First-Class Mail, Standard Mail, Shipping and Packages, International, Periodicals, and Other. Throughout our *Annual Report*, operational measurements and financial data, such as revenue and volume, are reported utilizing these categories.

RISK FACTORS

The risk factors identified in this section are discussed in our 10-K, and they are particularly relevant to our Shipping Services.

Adverse U.S. and global economic conditions directly impact our business, negatively affecting results of operations.

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 of our financial obligations or to carry out our strategy.

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

Adverse events may call into question our reputation for quality and reliability or our ability to deliver the mail, and could diminish the value of the Postal Service brand. This could potentially adversely affect our revenue and results of operations.

Our need to restructure our operations in response to declining mail volume may result in significant costs. It is possible that the measures being considered would be insufficient to reduce our workforce and physical infrastructure to a level commensurate with lower and declining mail volume.

Our business and results of operations are significantly affected by competition from both competitors in the marketplace as well as substitute products and channels provided by electronic communication services. If we do not compete effectively, operate efficiently, grow marketing mail and package services and increase revenue and profit margins from other sources, this adverse impact will become more substantial over time.

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

Slow market acceptance of new programs or product initiatives would adversely affect our results of operations.

An unduly burdensome union contract arrived at either through negotiation or arbitration could have a significant adverse impact on our future results of operations by impacting our control over wages and benefits and/or by limiting our ability to manage our workforce effectively.

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

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

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

Health and pension benefit costs represent a significant expense to us.

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

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 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.

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

Widespread outbreak of an illness or communicable disease, or any other public health crisis could reduce the demand for our products and services, which may adversely affect our revenue.

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, Competitive Mail and Services revenue totaled $15.3 billion in 2014 and volume totaled 3.4 billion pieces. In 2014, Competitive Mail and Services accounted for 2.2% of total Postal Service mail volume and 22.5% 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. The attributable costs of a product are the costs of the Postal Service determined through reliably identified causal relations to be directly or indirectly caused by the provision of that product. 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 FY2014, the Postal Service transferred $2.083 billion from the Competitive Products Fund to the Postal Service Fund. This transfer represented a prepayment of current and future year's institutional costs. Such prepayment transfers, however, in no way diminish the Postal Service's continuing obligation, in accord with 39 USC 3633(a)(3) and 39 CFR 3015.7(c), to ensure that revenues from Competitive products are sufficient to "collectively cover what the Commission determines to be an appropriate share of the institutional costs of the Postal Service."

In addition to covering attributable costs, Competitive Mail and Services are required by the PRC to bear 5.5% of postal-wide institutional costs. Total costs for Competitive Mail and Services are by definition equal to their attributable costs plus 5.5% of postal-wide institutional costs. In 2014, the contribution from Competitive Mail and Services equaled 12.59% of the institutional costs of the Postal Service. The difference between this 12.59% and the required 5.5% threshold is the "net income" for Competitive Mail and 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 2014, this regulatory-defined net income totaled $2.422 billion. Tax due will be transferred from the Competitive Products Fund to the Postal Service Fund by January 15, 2015.

USPS-FY14-39

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

For Fiscal Year 2014

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

PRC Form CP-01

	FY 2014	FY 2013	$ Change from SPLY	% Change from SPLY
Revenue				
(1) Mail and Services Revenues (a)	15,272,521	13,668,579	1,603,942	11.7%
(2) Investment Income	0	36	(36)	-100.0%
(3) Total Competitive Products Revenue	15,272,521	13,668,615	1,603,906	11.7%
Expenses				
(4) Volume Variable Costs	10,814,800	9,636,800	1,178,000	12.2%
(5) Product Specific Costs	155,100	125,300	29,800	23.8%
(6) Total Competitive Products Attributable Cost	10,969,900	9,762,100	1,207,800	12.4%
(7) Net Income Before Institutional Cost Contribution	4,302,621	3,906,515	396,106	
(8) Required Institutional Cost Contribution	1,880,285	1,823,217	57,068	3.1%
(9) Net Income Before Tax	2,422,336	2,083,298	339,038	
(10) Assumed Federal Income Tax *	847,818	729,154	118,663	16.3%
(11) Net Income After Tax	1,574,518	1,354,144	220,375	

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 gains from the sales and impairments of property and equipment. The loss for FY 14 was $43M with the amount allocated to Competitive Products (Building and Equipment allocation) of $7.479M. The gain for FY 13 was $53M with the amount allocated to Competitive Products (Building & Equipment allocation) of $7.779M.

* Note: 2014 Assumed Federal Income Tax is estimated based on the 2014 and 2013 Federal corporate tax rates respectively.

Table 2
Annual Summary of Competitive Products Financials (FY 2014)
($ in 000s)

PRC Form CP-02

		Beginning Value	Change from Prior Year	Ending Value
(1)	Cumulative Net Income (Loss) After Assumed Federal Income Tax *	$2,984,877	$1,574,518	$4,559,395
(2)	Total Financial Obligations (List of Financial Obligations)	$0	$0	$0
(3)	Total Financial Investments (List of Financial Investments)	$0	$0	$0
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: 2014 Assumed Federal Income Tax is estimated based on the 2014 Federal corporate tax rate.

Table 3
Competitive Products Property and Equipment Assets (FY 2014)
(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	$1,377.71	$2,296.21
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	1147569	Micro Computer System	$23,138.00	$23,138.00	$0.00
Total			**Total**	**$54,761.92**	**$52,465.71**	**$2,296.21**

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

	FY2014		FY 2013	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	5,152,000	1,159,715	535,514	Revenue
Net Accounts Receivable	930,000	209,343	199,752	Revenue
Supplies, Advances, and Prepayments	122,000	27,462	24,766	Revenue
Total Current Assets	6,204,000	1,396,520	760,032	
Property and Equipment				
Buildings	24,593,000	4,916,141	4,232,641	Depreciation cost for Buildings
Leasehold Improvements	1,357,000	271,129	223,299	Depreciation cost for Leasehold Improvements
Equipment	19,375,000	2,565,250	1,960,937	Depreciation cost for Equipment
Land	2,886,000	576,911	501,125	Depreciation cost for Buildings
Accumulated Depreciation	32,288,000	5,724,438	4,735,718	Depreciation cost for Bld/Eq/Leasehold/Vehicle
Construction in Progress	415,000	82,944	69,597	Depreciation cost for Buildings & Leaseholds
Total Property and Equipment, Net	16,338,000	2,687,937	2,251,881	
Appropriations and Receivables - Revenue Forgone	420,000	0	0	Non Competitive
Total Assets	22,962,000	4,084,457	3,011,913	
Total Assets Determined from Section 2011(e)(5)		5,168,746	4,393,123	
Total Net Liabilities	**USPS Annual Report**	**Competitive Products**	**Competitive Products**	**Distributed on Basis of:**
Liabilities:				
Current Liabilities				
Compensation and Benefits	1,506,000	289,754	244,793	Labor
Retire Health Benefits	22,417,000	4,313,031	2,684,237	Labor
Workers' Compensation	1,320,000	254,496	211,917	Workers' Comp Expense
Payables and Accrued Expenses	2,023,000	455,377	388,339	Revenue
Customer Deposit Accounts	1,191,000	268,094	249,487	Revenue
Deferred Revenue-Prepaid Postage	3,064,000	689,706	607,579	Revenue
Outstanding Postal Money Orders	628,000	918	5,744	Actual International Money Orders Outstanding
Prepaid Box Rent and Other Deferred Revenue	593,000	205,470	188,457	Actual Competitive Deferred Box Rents
Debt	9,800,000	1,737,540	1,491,560	Volume Variable Interest Expense
Non-Current Liabilities				
Workers' Compensation	17,102,000	3,297,266	2,551,655	Workers' Comp Expense
Employee Accumulated Leave	1,982,000	382,130	317,715	Repriced Annual Leave
Deferred Appropriation and Other Revenue	65,000	0	0	Non Competitive
Long-Term Portion of Capital Lease Obligation	294,000	58,741	61,277	Leasehold Depreciation
Deferred Gains on Sales of Property	301,000	52,351	45,206	Depreciation cost for Buildings & Equipment
Contingent Liabilities and Other	807,000	155,267	137,686	Labor
Long-Term Portion Notes Payables	5,200,000	0	0	Non Competitive
Total Liabilities	68,293,000	12,160,141	9,185,652	