Postal Regulatory Commission
Submitted 8/11/2014 8:56:58 AM
Filing ID: 90139
Accepted 8/11/2014

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 JUNE 30, 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 August 11, 2014
No Common Stock	N/A

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PART I. FINANCIAL INFORMATION

ITEM 1. Financial Statements

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

	Three Months Ended June 30,		Nine Months Ended June 30,	
	2014	**2013**	**2014**	**2013**
Operating revenue	$ 16,504	$ 16,177	$ 51,225	$ 50,185
Operating expenses:				
Compensation and benefits	11,272	11,257	34,667	35,371
Retiree health benefits	2,181	2,129	6,504	6,316
Workers' compensation	933	(469)	1,955	284
Transportation	1,605	1,588	4,972	5,088
Other	2,430	2,371	7,188	6,870
Total operating expenses	18,421	16,876	55,286	53,929
Loss from operations	**(1,917)**	**(699)**	**(4,061)**	**(3,744)**
Interest income	6	6	18	18
Interest expense	(44)	(47)	(138)	(144)
Net loss	**$ (1,955)**	**$ (740)**	**$ (4,181)**	**$ (3,870)**

See accompanying notes to the financial statements (unaudited).

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

	June 30, 2014 (Unaudited)	September 30, 2013
Current Assets		
Cash and cash equivalents	$ 4,950	$ 2,326
Restricted cash	273	312
Receivables:		
Foreign countries	607	618
U.S. government	71	118
Other	241	302
Receivables before allowances	919	1,038
Less allowances	59	54
Total receivables, net	860	984
Supplies, advances and prepayments	126	122
Total Current Assets	**6,209**	**3,744**
Noncurrent Assets		
Property and equipment, at cost:		
Buildings	24,522	24,452
Equipment	19,504	19,629
Land	2,886	2,895
Leasehold improvements	1,338	1,290
Property and equipment, at cost before allowances	48,250	48,266
Less allowances for depreciation and amortization	32,083	31,156
	16,167	17,110
Construction in progress	366	402
Total property and equipment, net	16,533	17,512
Other assets - principally revenue forgone receivable	415	385
Total Noncurrent Assets	**16,948**	**17,897**
Total Assets	**$ 23,157**	**$ 21,641**

See accompanying notes to the financial statements (unaudited).

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

	June 30, 2014 (Unaudited)	September 30, 2013
Current Liabilities		
Compensation and benefits	$ 2,274	$ 1,529
Retiree health benefits	20,991	16,766
Workers' compensation	1,307	1,322
Payables and accrued expenses:		
Trade payables and accrued expenses	1,376	1,237
Foreign countries	575	564
U.S. government	81	112
Total payables and accrued expenses	2,032	1,913
Deferred revenue-prepaid postage	3,209	2,993
Customer deposit accounts	1,179	1,229
Outstanding postal money orders	667	671
Prepaid box rent and other deferred revenue	510	460
Current portion of debt	9,800	9,800
Total Current Liabilities	**41,969**	**36,683**
Noncurrent Liabilities		
Workers' compensation, net of current portion	16,516	15,918
Employees' accumulated leave	1,965	1,982
Deferred appropriation and other revenue	81	159
Noncurrent portion of capital lease obligations	307	354
Deferred gains on sales of property	301	308
Contingent liabilities and other	822	860
Noncurrent portion of debt	5,200	5,200
Total Noncurrent Liabilities	**25,192**	**24,781**
Total Liabilities	**67,161**	**61,464**
Net Deficiency		
Capital contributions of the U.S. government	3,132	3,132
Deficit since 1971 reorganization	(47,136)	(42,955)
Total Net Deficiency	**(44,004)**	**(39,823)**
Total Liabilities and Net Deficiency	**$ 23,157**	**$ 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)	—	(3,870)	(3,870)
Balance at June 30, 2013 (unaudited)	**$ 3,132**	**$ (41,848)**	**$ (38,716)**
Balance at September 30, 2013	**$ 3,132**	**$ (42,955)**	**$ (39,823)**
Net loss (unaudited)	—	(4,181)	(4,181)
Balance at June 30, 2014 (unaudited)	**$ 3,132**	**$ (47,136)**	**$ (44,004)**

See accompanying notes to the financial statements (unaudited).

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

	Nine Months Ended June 30, 2014	Nine Months Ended June 30, 2013
Cash flows from operating activities:		
Net loss	$ (4,181)	$ (3,870)
Adjustments to reconcile net loss to cash provided by operations:		
Depreciation and amortization	1,390	1,437
Loss (gain) on disposals of property and equipment, net	50	(51)
Increase in other assets - primarily appropriations receivable	(30)	(7)
Increase (decrease) in noncurrent workers' compensation liability	598	(1,072)
Increase (decrease) in noncurrent employees accumulated leave	(17)	10
Increase (decrease) in noncurrent deferred appropriations and other revenue	(15)	13
Increase (decrease) in other noncurrent liabilities	(38)	105
Changes in current assets and liabilities:		
Receivables, net	124	29
Supplies, advances and prepayments	(4)	(11)
Compensation and benefits	745	566
Retiree health benefits	4,225	4,140
Workers' compensation	(15)	(32)
Payables and accrued expenses	117	(72)
Customer deposit accounts	(50)	25
Deferred revenue-prepaid postage	216	125
Outstanding postal money orders	(4)	3
Prepaid box rent and other deferred revenue	50	3
Net cash provided by operating activities	**3,161**	**1,341**
Cash flows from investing activities:		
Change in restricted cash requirements	39	(105)
Purchases of property and equipment	(512)	(489)
Proceeds from sales of property and equipment	43	111
Net cash used in investing activities	**(430)**	**(483)**
Cash flows from financing activities:		
Issuance of notes payable	4,700	4,400
Payments on notes payable	(4,700)	(4,400)
Payments on capital lease obligations	(44)	(44)
U.S. government appropriations - expensed	(63)	(36)
Net cash used in financing activities	**(107)**	**(80)**
Net increase in cash and cash equivalents	2,624	778
Cash and cash equivalents at beginning of year	2,326	2,087
Cash and cash equivalents at end of period	**$ 4,950**	**$ 2,865**
Supplemental cash flow disclosures:		
Interest paid	$ 142	$ 144

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 June 30, 2014, the results of operations for the three and nine month periods ended June 30, 2014 and 2013 and the cash flows for the nine month periods ended June 30, 2014 and 2013. Operating results for the three and nine month periods ended June 30, 2014 are not necessarily indicative of the results that may be expected for all of fiscal year 2014. Subsequent events have been evaluated through August 11, 2014, the date the Postal Service filed its Form 10-Q for the quarter ended June 30, 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 $29 million at June 30, 2014, and $37 million at September 30, 2013, related to government deposits are included in the Condensed 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.

Recent Accounting Pronouncements

In May 2014, the Financial Accounting Standards Board issued Accounting Standards Update 2014-09 (ASU 2014-09), *"Revenue from Contracts with Customers."* The new standard outlines a single comprehensive model for entities to use in accounting for revenue arising from contracts with customers and supersedes most current revenue recognition guidance, including industry-specific guidance. ASU 2014-09 is effective for fiscals years, and interim periods within those years, beginning after December 15, 2016. Early adoption is not permitted. We are currently evaluating the impact of adoption of this standard on our financial statements.

Note 2 – Liquidity

LIQUIDITY CONCERNS

The Postal Service continues to suffer from a lack of liquidity. Cash balances remain insufficient to support an organization with approximately $72 billion in annual operating expenses as the present cash balance can fund less than one month of operating activity and remains insufficient to cover the legally-required retiree health benefits prefunding payment due by September 30, 2014. The Postal Service held cash and cash equivalents of $5.0 billion and $2.3 billion as of June 30, 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 seasonal impact of holiday mailings during the first quarter of 2014 and the temporary exigent price increase on Market-Dominant products implemented on January 26, 2014. This 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, August 11, 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 cash balances to meet all of its existing legal obligations, make meaningful reductions in its debt and make important investments in its infrastructure. Annual capital expenditures have declined from $2 billion in 2008 to less than $700 million in 2013 to conserve cash. For the nine months ended June 30, 2014, capital expenditures totaled approximately $500 million. The present level of capital expenditures is not sustainable. The Postal Service's delivery fleet includes approximately 140,000 vehicles that are at least 20 years old and nearing the end of their useful life. Repair and maintenance costs for these vehicles have risen significantly in recent years. Some facilities maintenance has been deferred in recent years to save cash and the backlog needs to be addressed. Investments in package sorting and handling equipment are needed to fully capitalize on business opportunities in the growing package delivery market and other letter sorting equipment must be updated. Further, the existing level of cash could be insufficient to support operations in the event of another significant downturn in the U.S. economy. Absent legislative change, 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 net losses of $1,955 million and $4,181 million, respectively, for the three and nine month periods ended June 30, 2014, which includes $1,425 million and $4,275 million of expense accrued for the legally-mandated prefunding payment for retiree health benefits, respectively. This was the 21st quarterly loss in the past 23 quarters, and continues the trend of steady losses at the Postal Service. 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 foreseeable future.

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 may 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 implemented a 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. In June 2014, it announced that a second phase of mail processing realignments would begin in January 2015, culminating in the consolidation of up to 82 more processing locations. Additionally, the Postal Service continues to leverage employee attrition, Voluntary Early Retirement (VER) and increased utilization of non-career employees. In July 2014, the Postal Service announced that a VER would be offered to approximately 3,900 Postmasters who were impacted by reductions in retail hours at certain postal facilities. There is no financial statement impact to the three months ended June 30, 2014 for this offer.

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 delivery days, which is expected to improve efficiency and reduce overtime pay and operating costs. The Postal Service also announced its intent to continue the consolidation of its mail processing operations beginning in January 2015.

On January 26, 2014, the Postal Service implemented price increases on Market-Dominant and Competitive products. The Market-Dominant increases included a 1.7% price increase based on the Consumer Price Index for All Urban Consumers (CPI-U) plus a temporary 4.3% increase approved by the PRC in December 2013 as an exigent rate change. The exigent rate change was approved 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 CPI-U 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 have also filed an appeal seeking relief from the PRC's decision to allow any exigent rate increase. Additionally, the Postal Service increased prices an average of 2.4% for Competitive products. Including the exigent rate change, these Market-Dominant and Competitive products changes are projected to generate approximately $2.7 billion of additional annualized revenue for the Postal Service.

The Postal Service has conserved capital by spending only what is believed essential to maintain its existing facilities and service levels. However, an increase of capital investment is necessary to upgrade its existing fleet of vehicles and processing equipment in order to remain operationally competitive.

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 with a change in existing law. The Postal Service also continues to seek reforms that would establish a set of health care plans within the Federal Employees' Health Benefits Program (FEHBP) that would fully integrate with Medicare for current and future Postal Service retirees, largely eliminating the current unfunded liability. In addition, it seeks reforms to the workers' compensation system, and a refund of the estimated overfunding of the Federal Employees' Retirement System (FERS), each of which requires legislative action.

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 postal products and 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 long-term financial challenges it faces and the legislative changes that are required to restore 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.

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 June 30, 2014 and September 30, 2013, which is the maximum amount allowed under the legally-mandated debt ceiling. 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 0.135% to 3.790%, with maturities ranging from less than one month to 25 years. As of June 30, 2014, the premium associated with the prepayment of all debt is $370 million based upon current prevailing interest rates.

Included in the current portion of debt are two revolving credit line facilities, renewable annually, with the FFB, both of which are available through April 2015. These current 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 June 30, 2014 and September 30, 2013, these two revolving credit facilities were fully drawn.

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 nine month periods ended June 30, 2014 and 2013 was 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 $75 million as of June 30, 2014, and $78 million as of September 30, 2013, are included on the Condensed Balance Sheets in "Land" and "Buildings." Impairment charges were $54 million for the three months ended June 30, 2014 and not significant for the three months ended June 30, 2013. Impairment charges were $59 million and $21 million for the nine month periods ended June 30, 2014 and 2013, respectively. Depreciation expense was $420 million and $1,262 million for the three and nine month periods ended June 30, 2014, respectively. Depreciation expense was $424 million and $1,298 million for the three and nine month periods ended June 30, 2013, respectively.

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 nine month periods ended June 30, 2014 and 2013, respectively.

Note 5 – Leases and Capital Commitments

Leases

Future minimum payments for all non-cancelable leases as of June 30, 2014, were as follows:

Lease Obligations (Dollars in millions)	Operating	Capital
(Unaudited)		
Less than one year	$ 740	$ 91
One to less than two years	681	88
Two to less than three years	614	81
Three to less than four years	558	68
Four to less than five years	502	53
Thereafter	3,657	112
Total lease obligations	$ 6,752	$ 493
Less interest		126
Total capital lease obligations		$ 367
Less current portion of capital lease obligations		60
Noncurrent portion of capital lease obligations		$ 307

The current portion of the capital lease obligation is included in "Trade payables and accrued expenses" on the Condensed 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 June 30, 2014 and 2013, were $256 million and $270 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 nine month periods ended June 30, 2014 and 2013, were $821 million and $839 million, respectively.

Capital

Capital commitments consist primarily of equipment and building construction and improvements. At June 30, 2014 and September 30, 2013, commitments to acquire capital assets were $690 million and $708 million, respectively. Financial commitments for approved capital projects in progress were as follows:

Capital Commitments	As of	
(Dollars in millions)	**June 30, 2014**	**September 30, 2013**
	(Unaudited)	
Mail processing equipment	$ 281	$ 316
Building improvements, construction, and building purchases	281	329
Postal support equipment	53	50
Vehicles and other	75	13
Total capital commitments	$ 690	$ 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 $185 million to the liability for the nine months ended June 30, 2014 and is included in “Operating expenses: Other" on the Condensed Statements of Operations.

As of June 30, 2014, contingent liabilities consisted of $995 million associated with Labor/Employment, $48 million with Environmental, $49 million with Tort and $32 million with Contractual liabilities for a total of $1,124 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 $331 million and $108 million as of June 30, 2014 and September 30, 2013, respectively, is included on the Condensed Balance Sheets in “Trade payables and accrued expenses.” The noncurrent portion of this liability of $793 million and $831 million as of June 30, 2014 and September 30, 2013, respectively, is included on the Condensed 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 June 30, 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 Office of Personnel Management (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 $1,426 million and $1,413 million for the three month periods ended June 30, 2014 and 2013, respectively. For the nine month periods ended June 30, 2014 and 2013, the retirement expense was $4,309 million and $4,315 million, respectively. Retirement expense is recorded in “Compensation and benefits” in the Condensed Statements of Operations, and includes the costs of FERS, TSP and employer's share of Social Security taxes.

EMPLOYER CONTRIBUTIONS

P.L. 109-435 suspended the employer contributions to CSRS until 2017 that would otherwise have been required under Title 5, Section 8334(a)(1) of the United States Code. At that time, the 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 nine month periods ended June 30, 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 nine month periods ended June 30, 2014 and 2013. The Postal Service is also required to contribute to the TSP for FERS employees by contributing 1% per year of basic pay, and to match voluntary employee contributions by up to an additional 4% of the employee’s basic pay.

Note 8 – Health Benefit Plans

CURRENT EMPLOYEES

Substantially all career employees are covered by the 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 23% of the premium costs during the three month periods ended June 30, 2014 and 2013, respectively. Postal Service employee healthcare expense was $1,191 million, and $1,215 million during the three month periods ended June 30, 2014 and 2013, respectively. Employees paid approximately 24% and 22% of the premium costs during the nine month periods ended June 30, 2014 and 2013, respectively. For the nine month periods ended June 30, 2014 and 2013, employee healthcare expense was $3,605 million and $3,723 million, respectively. These expenses are included in “Compensation and benefits” in the Condensed 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 a portion of the health insurance premiums, based on the length of federal civilian service occurring after July 1, 1971, for all retired postal employees and their survivors who participate in the FEHBP and who retired 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.

Since 2007, the Postal Service has been required to prefund retiree health benefits by depositing funds into the PSRHBF. Payments are mandated to be made each year through 2016. This prefunding requirement is not imposed on most federal agencies or private sector businesses. The Postal Service has recorded $21.0 billion as a current liability for the PSRHBF prefunding requirements on its June 30, 2014 Condensed Balance Sheet. This includes payment defaults of $11.1 billion in 2012 and $5.6 billion in 2013, and $4.3 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 (as noted above) and 2015, and $5.8 billion in 2016, due by September 30 of each respective year. The total unfunded PSRHBF commitment including past defaulted amounts and future obligations is $33.9 billion. Statutorily required payments to amortize any unfunded liability remaining at September 30, 2016 over 40 years are not reflected in this amount. 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 liquidity concerns, the Postal Service will likely 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.

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 no later than 2017 to determine if additional payments into the PSRHBF are required. 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 June 30,		Nine Months Ended June 30,	
(Dollars in millions)	2014	2013	2014	2013
(Unaudited)				
Employer premium expense	**$ 756**	**$ 729**	**$ 2,229**	**$ 2,116**
Accrual for P.L. 109-435 payment to PSRHBF	**1,425**	**1,400**	**4,275**	**4,200**
Total retiree health benefits expense	**$ 2,181**	**$ 2,129**	**$ 6,504**	**$ 6,316**

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 scheduled 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 Department of Labor's (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.

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 included in operating expenses.

The estimation of the liability is highly sensitive to changes in inflation and discount rates. As of June 30, 2014, an increase of 1% in the discount rate would decrease the liability and related expense by approximately $1.8 billion. As of June 30, 2014, a decrease of 1% in the discount rate would increase the liability and related expense by approximately $2.2 billion.

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	As of		
	June 30, 2014	September 30, 2013	June 30, 2013
	(Unaudited)		(Unaudited)
Compensation claims liability:			
Discount rate	2.8%	3.0%	2.8%
Wage inflation	2.9%	2.9%	2.9%
Medical claims liability:			
Discount rate	2.8%	3.0%	2.9%
Medical inflation	8.8%	9.1%	9.0%

The present value of the liability for future workers' compensation payments was $17,823 million and $17,240 million as of June 30, 2014 and September 30, 2013, respectively. On October 15, 2013, the Postal Service made its annual payment to the DOL of $1,372 million, which included $50 million of prepaid administrative fees. The current portion of the liability was $1,307 million and $1,322 million as of June 30, 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 nine month periods ended June 30, 2014 and 2013, were as follows:

Workers' Compensation Expense	Three Months Ended June 30,		Nine Months Ended June 30,	
(Dollars in millions)	2014	2013	2014	2013
(Unaudited)				
Impact of discount rate changes	$ 379	$ (918)	$ 379	$ (1,373)
Actuarial valuation of new cases, revaluation of existing cases, and inflation rate changes	537	432	1,525	1,606
Subtotal	916	(486)	1,904	233
Administrative fee	17	17	51	51
Total workers' compensation expense (benefit)	$ 933	$ (469)	$ 1,955	$ 284

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 current portion of debt approximates fair value.

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 Noncurrent Financial Assets and Liabilities	As of			
	June 30, 2014		September 30, 2013	
(Dollars in millions)	Carrying Amount	Fair Value	Carrying Amount	Fair Value
	(Unaudited)			
Revenue forgone	$ 414	$ 513	$ 385	$ 461
Total noncurrent financial assets	$ 414	$ 513	$ 385	$ 461
Noncurrent portion of debt	$ 5,200	$ 5,567	$ 5,200	$ 5,517
Total noncurrent financial liabilities	$ 5,200	$ 5,567	$ 5,200	$ 5,517

For the three and nine month periods ended June 30, 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 three quarters of 2014. Impairment charges were $54 million for the three month period ended June 30, 2014 and not significant for the three month period ended June 30, 2013. Impairment charges were $59 million and $21 million for the nine month periods ended June 30, 2014 and 2013, respectively. 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 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 June 30, 2014, the Postal Service recognized revenue of $17 million, including $6 million of imputed interest income from these appropriations, compared to recognized revenue of $20 million, including $6 million of imputed interest, for the three months ended June 30, 2013. For the nine months ended June 30, 2014, the Postal Service recognized revenue of $57 million, including $17 million of imputed interest, compared to recognized revenue of $49 million, including $17 million of imputed interest for the nine months ended June 30, 2013.

The related amount of the noncurrent receivable as of June 30, 2014 and September 30, 2013 was $414 million and $385 million, respectively. The current portion of this receivable as of June 30, 2014 and September 30, 2013 was $38 million and $68 million, respectively, and is recorded under "Receivables – U.S. Government" on the Condensed 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. We have no obligation to publicly update or revise any forward-looking statements, whether as a result of new information, future events, or otherwise.

Management's Discussion and Analysis of Financial Condition and Results of Operations and other parts of this report describes the principal factors affecting the results of operations, liquidity, capital resources and critical accounting estimates of 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. Operating results for the three and nine month periods ended June 30, 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 change included a 1.7% increase based on the CPI-U index, plus a 4.3% increase approved as a temporary exigent rate change. The exigent price change was 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-U increase alone. The decision by the PRC to limit the duration of the exigent price 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 services 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 nearly 154 million city, rural, Post Office box, and highway delivery points. Operations are conducted primarily in the domestic market, with international sales representing approximately 4% 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. There have been no significant changes or updates to our critical accounting policies and estimates since our last report.

Recent Accounting Standards

In May 2014, the Financial Accounting Standards Board issued Accounting Standards Update 2014-09 (ASU 2014-09), *"Revenue from Contracts with Customers."* The new standard outlines a single comprehensive model for entities to use in accounting for revenue arising from contracts with customers and supersedes most current revenue recognition guidance, including industry-specific guidance. The standard's core principle is that an entity will recognize revenue when the transfer of promised goods or services to a customer is complete. Revenue will be recognized in an amount that reflects the consideration to which an entity expects to be entitled for those goods and services. The standard is designed to create greater comparability for financial statement users across industries as well as requiring informative enhanced disclosures. ASU 2014-09 is effective for fiscals years, and interim periods within those years, beginning after December 15, 2016. Early adoption is not permitted. We are currently evaluating the impact of adoption of this standard on our financial statements.

Results of Operations

Three and Nine Months Ended June 30, 2014 and June 30, 2013

Our net loss was $1,955 million for the three months ended June 30, 2014, compared to a net loss of $740 million for the same period last year, an increase in the net loss of $1,215 million. Operating revenue increased $327 million, or 2.0%, 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 were implemented on January 26, 2014. Operating expenses increased $1,545 million, or 9.2%, compared to the same period last year. The increase in operating expenses is primarily due to the fair value adjustment associated with the decline in interest rates in workers' compensation expense of $1,298 million.

Our net loss was $4,181 million and $3,870 million for the nine months ended June 30, 2014 and 2013, respectively. This represents an increase in our net loss of $311 million. Operating revenue increased $1,040 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 increased $1,357 million, or 2.5%, compared to the same period last year. The increase in operating expenses is primarily due to an increase in workers' compensation expense of $1,671 million, offset by reduced compensation and benefits expense of $704 million, which includes the expense associated with the 2013 Voluntary Early Retirement (VER) incentive of $353 million incurred in 2013.

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. However, the magnitude of First-Class Mail and total volume declines have decreased from the trend observed in prior years. In addition, the Postal Service Retiree Health Benefits Fund (PSRHBF) prefunding requirement, continuation of legally-mandated six-days-per-week delivery and continued high fuel and employee benefits costs have adversely affected our financial results.

The following table summarizes key operating statistics for the three and nine month periods ended June 30, 2014 and 2013:

Key Operating Statistics	Three Months Ended June 30,		Nine Months Ended June 30,	
(Dollars and mail volume in millions)	2014	2013	2014	2013
Operating revenue	**$ 16,504**	**$ 16,177**	**$ 51,225**	**$ 50,185**
PSRHBF expense	**$ 1,425**	**$ 1,400**	**$ 4,275**	**$ 4,200**
Net loss	**$ (1,955)**	**$ (740)**	**$ (4,181)**	**$ (3,870)**
Total mail volume	**37,745**	**37,802**	**117,883**	**120,051**
Average mail volume per day	**490**	**491**	**522**	**531**

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. Services, such as Every Door Direct Mail, offer new ways of doing business with us.

Our net losses include expenses of $2,358 million and $6,230 million for the three and nine month periods ended June 30, 2014, respectively, for the expenses incurred and accrued related to the legally-mandated PSRHBF prefunding of retiree health benefits ($1,425 million and $4,275 million, respectively), as well as the change in value of the liability associated with 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) ($933 million and $1,955 million, respectively.) 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) required by Federal Law for 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 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 June 30, 2014, would have resulted in approximately a $2.2 billion increase of the liability and related expense. This results in significant differences between the GAAP workers' compensation expense and our cash outlays.

Because the legislative mandates for the PSRHBF 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 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 nine month periods ended June 30, 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 nine month periods ended June 30, 2014 when compared to the same period last year.

Net Income (Loss) Before Expense Impact Related to Noncurrent Portion of Workers' Compensation and PSRHBF Expense

(Dollars in millions)	Three Months Ended June 30, 2014	Three Months Ended June 30, 2013	Nine Months Ended June 30, 2014	Nine Months Ended June 30, 2013
Net loss	**$ (1,955)**	**$ (740)**	**$ (4,181)**	**$ (3,870)**
Impact of:				
Change related to the noncurrent portion of workers' compensation	**540**	**(813)**	**911**	**(698)**
PSRHBF expense	**1,425**	**1,400**	**4,275**	**4,200**
Net income (loss) before expense impact related to noncurrent portion of workers' compensation and PSRHBF expense	**$ 10**	**$ (153)**	**$ 1,005**	**$ (368)**

*Note: The totals for certain amounts for the prior year have been reclassified to conform with classifications used in the current year. These reclassifications did not impact our operating results for the prior year.

Revenue and Volume

Although revenue and volume are closely linked to the strength of the U.S. economy and changes in how our customers use the mail, we have been proactive in addressing how to develop growth in these areas. We continue to concentrate on our customers' needs and have increased our marketing investment, as well as focusing on mail and package innovation. However, we also recognize that 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 revenue and volume, 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. The *Priority: You* campaign is just one example of how we are making the most of this trend. By offering day specific delivery, improved tracking and text alerts, and up to $50 free insurance on most Priority Mail® packages, we have demonstrated our responsiveness to our customers. However, because Shipping and Packages represents only 20% of our year-to-date 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 contribution for First-Class Mail is greater than that of Shipping and Packages. As a result, revenues from Shipping and Packages would have to grow at a substantially higher rate than the decline in First-Class Mail revenues in order to replace the lost contribution of First-Class Mail.

Summary of Revenue and Volume Results

For the three months ended June 30, 2014, operating revenue was $16,504 million, an increase of $327 million, or 2.0%, compared to the same period last year. We implemented price increases on Market-Dominant and Competitive products during the second quarter of 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-U 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 limit 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 any exigent postage increase.

Shipping and Packages revenue was $3,185 million for the three months ended June 30, 2014, an increase of $196 million, or 6.6%, compared to the same period last year, aided by the price increases implemented in January 2014. Shipping and Packages volume was 941 million pieces for the three months ended June 30, 2014, an increase of 67 million pieces, or 7.7%, compared to the same period last year.

For the nine months ended June 30, 2014, operating revenue was $51,225 million, an increase of $1,040 million, or 2.1%, compared to the same period last year. Shipping and Packages revenue of $10,450 million increased $926 million, or 9.7%, compared to the same period last year. Shipping and Packages volume was 3,041 million pieces for the nine months ended June 30, 2014, an increase of 237 million pieces, or 8.5%, 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 nine months ended June 30, 2014.

The following table summarizes our revenue and volume for the three and nine month periods ended June 30, 2014 and 2013, by major service line:

Operating Revenue and Volume by Service Line*						
	Three Months Ended June 30,			Nine Months Ended June 30,		
(Dollars and pieces in millions)	2014	2013	% Change	2014	2013	% Change
Revenue:						
First-Class Mail[1]	$ 7,120	$ 6,899	3.2 %	$ 21,544	$ 21,530	0.1 %
Standard Mail[2]	4,220	4,017	5.1 %	13,062	12,692	2.9 %
Shipping and Packages[3]	3,185	2,989	6.6 %	10,450	9,524	9.7 %
International Mail	706	730	(3.3)%	2,289	2,323	(1.5)%
Periodicals	418	418	— %	1,220	1,260	(3.2)%
Other[4]	855	1,124	(23.9)%	2,660	2,856	(6.9)%
Total revenue	**$ 16,504**	**$ 16,177**	**2.0 %**	**$ 51,225**	**$ 50,185**	**2.1 %**
Volume:						
First-Class Mail[1]	15,749	15,965	(1.4)%	48,655	50,372	(3.4)%
Standard Mail[2]	19,205	19,039	0.9 %	60,512	60,877	(0.6)%
Shipping and Packages[3]	941	874	7.7 %	3,041	2,804	8.5 %
International Mail	204	219	(6.8)%	680	713	(4.6)%
Periodicals	1,535	1,612	(4.8)%	4,579	4,857	(5.7)%
Other[5]	111	93	19.4 %	416	428	(2.8)%
Total volume	**37,745**	**37,802**	**(0.2)%**	**117,883**	**120,051**	**(1.8)%**

*Note: The totals for certain mail categories for the prior year have been reclassified to conform with 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 continued to provide the majority of our revenue for the three and nine month periods ended June 30, 2014, despite trends away from hard copy to electronic media. Year to date First-Class Mail represented 42.1% of our revenue and accounted for 41.3% of the mail volume while Standard Mail generated 25.5% of revenue and 51.3% of volume. Shipping and Packages generated approximately 20.4% of our revenue despite representing only 2.6% of our volume.

FIRST-CLASS MAIL

First-Class Mail volume, our most profitable service category, declined 216 million pieces, or 1.4%, for the three months ended June 30, 2014 compared to the same period last year. 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 provided revenue of $7,120 million for the three months ended June 30, 2014, an increase of $221 million, compared to the same period last year. The increase in revenue was primarily due to the price increase that went into effect during the second quarter of our fiscal year, offset by the decline in volume as noted above.

First-Class Mail provided revenue of $21,544 million for the nine months ended June 30, 2014, an increase of $14 million, or 0.1%, compared to the same period last year. The corresponding volume decrease was 1,717 million pieces, or 3.4%. The most significant factor contributing to the increase in revenue was the price increase that was implemented in January 2014. The increase is offset by a decrease in volume. However, the magnitude of First-Class Mail and total volume declines have decreased from the trend observed in prior years.

STANDARD MAIL

Standard Mail provided revenue of $4,220 million for the three months ended June 30, 2014, an increase of $203 million, or 5.1%, compared to the same period last year. Standard Mail revenues benefited from the price increase that went into effect during the second quarter of this fiscal year. The corresponding volume increase was 166 million pieces, or 0.9%. The increase in volume is reflective of the cyclical nature of Standard Mail, targeted sales advertising campaigns and the positive improvements in the labor market which stimulate demand for standard mail.

Standard Mail provided revenue of $13,062 million for the nine months ended June 30, 2014, an increase of $370 million, or 2.9%, compared to the same period last year, primarily due to the price increase that went into effect during the second quarter of our fiscal year. However, volume decreased 365 million pieces, or 0.6%. 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 nine month periods ended June 30, 2014, and 2013, by product:

Shipping & Packages Revenue and Volume*	Three Months Ended June 30,			Nine Months Ended June 30,		
(Dollars and pieces in millions)	2014	2013	% Change	2014	2013	% Change
Revenue:						
Priority Mail[1]	$ 1,657	$ 1,632	1.5 %	$ 5,632	$ 5,364	5.0 %
Parcel Select, Parcel Return and Standard Parcels	658	543	21.2 %	2,059	1,635	25.9 %
Package Services	180	182	(1.1)%	598	598	— %
First-Class Packages[2]	497	428	16.1 %	1,581	1,320	19.8 %
Priority Mail Express	193	204	(5.4)%	580	607	(4.4)%
Total revenue	**$ 3,185**	**$ 2,989**	**6.6 %**	**$ 10,450**	**$ 9,524**	**9.7 %**
Volume:						
Priority Mail[1]	222	217	2.3 %	736	706	4.2 %
Parcel Select, Parcel Returns and Standard Parcels	386	339	13.9 %	1,209	1,072	12.8 %
Package Services	118	120	(1.7)%	407	404	0.7 %
First-Class Packages[2]	206	188	9.6 %	661	592	11.7 %
Priority Mail Express	9	10	(10.0)%	28	30	(6.7)%
Total volume	**941**	**874**	**7.7 %**	**3,041**	**2,804**	**8.5 %**

*Note: The totals for certain mail categories for the prior year have been reclassified to conform with classifications used in the current year. These reclassifications did not impact total operating revenue for the prior 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 of $3,185 million increased $196 million, or 6.6% for the three months ended June 30, 2014, compared to the same period last year. Shipping and Packages volume increased 67 million pieces, or 7.7%, for the three months ended June 30, 2014, compared to the same period last year. Shipping and Packages revenue increased $926 million, or 9.7%, for the nine months ended June 30, 2014, compared to the same period last year. Shipping and Packages volume increased 237 million pieces, or 8.5%, for the nine months ended June 30, 2014, compared to the same period last year.

Priority Mail

We continue to improve our Priority Mail service to better meet the needs of consumers and business mailers. E-commerce transactions have grown at a higher rate than traditional retail sales, which has helped to boost Priority Mail revenues.

Priority Mail represented approximately 52% of our total Shipping and Packages revenue for the three and nine month periods ended June 30, 2014. Priority Mail revenue increased $25 million, or 1.5%, for the three months ended June 30, 2014, compared to the same period last year. For the nine months ended June 30, 2014 Priority Mail revenue increased $268 million, or 5.0%, compared to the same period last year.

Parcel Services

Parcel Services provided revenue of $658 million for the three months ended June 30, 2014, an increase of $115 million, or 21.2%, compared to the same period last year. This category includes Parcel Select revenue of $605 million, Parcel Returns revenue of $36 million and Standard Mail Parcels revenue of $17 million. These services continue to show strong volume growth of 13.9% for the three months ended June 30, 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 contribution compared to many of our other services.

Parcel Services provided revenue of $2,059 million for the nine months ended June 30, 2014, comprised of Parcel Select revenue of $1,904 million, Parcel Returns revenue of $105 million, and Standard Mail Parcels revenue of $50 million. Revenue increased $424 million, or 25.9%, compared to the same period of the prior year. Parcel Services volume increased 137 million pieces, or 12.8%, during the nine 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 $180 million for the three months ended June 30, 2014, decreased $2 million, or 1.1%, compared to the same period last year. Package Services revenue was $598 million for the nine months ended June 30, 2014, remained unchanged, 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 $497 million for the three months ended June 30, 2014, an increase of $69 million, or 16.1%, compared to the same period last year. Volume increased 18 million pieces, or 9.6%, for the three months ended June 30, 2014, compared to the same period last year.

First-Class Packages revenue was $1,581 million for the nine months ended June 30, 2014, an increase of $261 million, or 19.8%, compared to the same period last year. Volume increased 69 million pieces, or 11.7%, for the nine months ended June 30, 2014, compared to the same period last year.

INTERNATIONAL MAIL

International mail revenue was $706 million for the three month period ended June 30, 2014, a decrease of $24 million, or 3.3%, compared to the same period last year. Revenue was $2,289 million for the nine month period ended June 30, 2014, a decrease of $34 million, or 1.5%, compared to the same period last year. A weaker global economy continues to be 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 of $418 million for the three months ended June 30, 2014, remained unchanged, compared to the same period last year. Periodicals volume decreased by 77 million pieces for the three months ended June 30, 2014, or 4.8%, compared to the same period last year. Periodicals revenue was $1,220 million for the nine months ended June 30, 2014, a decrease of $40 million, or 3.2%, compared to the same period last year. Periodicals volume decreased by 278 million pieces, or 5.7%, for the nine months ended June 30, 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 nine month periods ended June 30, 2014 and 2013:

Operating Expenses	Three Months Ended June 30,		Nine Months Ended June 30,	
(Dollars in millions)	2014	2013	2014	2013
Compensation and benefits	$ 11,272	$ 11,257	$ 34,667	$ 35,371
Retiree health benefit premiums	756	729	2,229	2,116
PSRHBF prefunding	1,425	1,400	4,275	4,200
Workers' compensation	933	(469)	1,955	284
Transportation	1,605	1,588	4,972	5,088
Other expenses	2,430	2,371	7,188	6,870
Total operating expenses	$ 18,421	$ 16,876	$ 55,286	$ 53,929

COMPENSATION AND BENEFITS

Compensation and benefits expenses consist of costs related to our 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 $8,578 million for the three months ended June 30, 2014, compared to $8,551 million in the same period last year, an increase of $27 million, or 0.3%. This increase is driven by wage increases mandated by our collective bargaining agreements, offset by increased utilization of lower-cost non-career employees. The quarter ended June 30, 2014 was the first full quarter impacted by the March 2014 COLA increases mandated in collective bargaining agreements. For the three months ended June 30, 2014, the average cost per work hour increased by $0.11, or 0.3%, to $40.94 from $40.83 for the same period last year. Compensation expense was $26,508 million for the nine months ended June 30, 2014, compared to $27,069 million in the same period last year, a decrease of $561 million, or 2.1%. During the nine months ended June 30, 2013, we recorded an expense of $353 million related to the VER offer. Excluding the impact of the additional expense related to the incentive offer, compensation expense would have decreased by $208 million, or 0.8%, for the nine months ended June 30, 2014. There were no VER incentives offered during the nine months ended June 30, 2014.

As of June 30, 2014, the number of career employees was reduced by approximately 8,000, or 2%, compared to June 30, 2013. These reductions have been accomplished primarily through attrition and retirements. The number of non-career employees increased by approximately 7,000, or 6%, since June 30, 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 $0.30, or 0.7%, to $41.49 for the nine month period ended June 30, 2014 from $41.79 for the same period last year.

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 Item 1. Financial Statements, *Note 7, Retirement Programs*. All expenses of the retirement programs, except for retiree health benefits, are included in compensation and benefits expense. Retirement expense was $1,426 million for the three months ended June 30, 2014, compared to $1,413 million for the same period last year, an increase of $13 million, or 0.9%. Retirement expense was $4,309 million for the nine months ended June 30, 2014, compared to $4,315 million for the same period last year, a decrease of $6 million, or 0.1%. The nine month decrease is primarily due to the reduced number of career employees when compared to the same period last year.

Effective October 1, 2014, our employer contribution rate for most current Federal Employees' Retirement System (FERS) employees' increases from 11.9% to 13.2% of basic pay. This is a government-wide increase determined by the Office of Personnel Management (OPM), which further underscores the need for postal-specific calculations of our retirement costs. This contribution increase is expected to result in an annual increase in our retirement expense of approximately $300 million.

Health benefits expense. Health benefits expense was $1,191 million for the three months ended June 30, 2014, compared to $1,215 million for the same period last year, a decrease of $24 million, or 2.0%. Our share of the health care premiums for our employees represents 76% and 77% of the total health care premium cost for the three months ended June 30, 2014 and 2013, respectively. Health benefits expense was $3,605 million for the nine months ended June 30, 2014, compared to $3,723 million for the same period last year, a decrease of $118 million, or 3.2%. Our share of the health care premiums for our employees represents 76% and 78% of the total health care premium cost for the nine months ended June 30, 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 Federal Employees' Health Benefits Program (FEHBP).

RETIREE HEALTH BENEFIT PREMIUMS AND PSRHBF PREFUNDING

We participate in federal employee benefit programs for retirement, health and workers' compensation. United States Code Section 8909a (USC8909a) 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, which began in 2007 and continues 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. As of June 30, 2014, we have recorded $21.0 billion as a current liability for the PSRHBF prefunding requirements. This includes the $16.7 billion due for defaulted payments and an accrual of $4.3 billion related to the $5.7 billion payment due by September 30, 2014. Absent legislative change, we anticipate that we will 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 default on these prefunding payments. This may require us 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 Item 1. Financial Statements, *Note 2, Liquidity*). The statutory requirement establishing the payment schedule contains no provisions addressing a payment default. As of August 11, 2014, no penalties or adverse consequences have resulted.

Under current law, not later than 2017, the 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 continue to pay the premiums for postal retirees participating in the FEHBP through 2016. We expense these payments as they become due, at a cost of $756 million for the three months ended June 30, 2014, an increase of $27 million, or 3.7%, from the same period last year. For the nine months ended June 30, 2014, the cost was $2,229 million, an increase of $113 million, or 5.3%, from the same period last year. 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 June 30, 2014, there were approximately 490,000 postal retirees and survivors participating in FEHBP, a net increase of approximately 2,000 since June 30, 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. Our pro-rata share of premium expenses based on retiree service periods also increased. For the nine months ended June 30, 2014, retiree health benefits premiums accounted for 4.0% of our total operating expenses, compared to 3.9% for the comparable period last year. When prefunding accruals are included, retiree health benefits expenses represented 11.8% of total operating expenses, compared to 11.7% for the same period last year.

The components of retiree health benefits expense for the three and nine month periods ended June 30, 2014, and 2013, are as follows:

Retiree Health Benefits	Three Months Ended June 30,		Nine Months Ended June 30,	
(Dollars in millions)	2014	2013	2014	2013
(Unaudited)				
Employer premium expense	**$ 756**	**$ 729**	**$ 2,229**	**$ 2,116**
Accrual for P.L. 109-435 payment to PSRHBF	**1,425**	**1,400**	**4,275**	**4,200**
Total retiree health benefits expense	**$ 2,181**	**$ 2,129**	**$ 6,504**	**$ 6,316**

Although no PSRHBF prepayments were made during the first nine 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. The liability and annual expense is estimated for the amount of funding that would need to be invested at current interest rates in order to fully fund all future estimated 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. As of June 30, 2014, an increase of 1% in the discount rate would decrease the liability and related expense by approximately $1.8 billion. A decrease of 1% in the discount rate would increase the liability and related expense by approximately $2.2 billion.

At June 30, 2014, the present value of the liability for future workers' compensation payments was $17,823 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 $1,307 million at June 30, 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 $933 million and a benefit of $469 million for the three months ended June 30, 2014 and 2013, respectively, and was $1,955 million and $284 million for the nine months ended June 30, 2014 and 2013, respectively. The increases of $1,402 million for the three months ended June 30, 2014, and $1,671 million for the nine months ended June 30, 2014, are primarily due to the impact of discount rate changes from the prior periods.

On a quarterly basis, changes in the number of claims and amounts paid can be highly volatile and depend on a number of factors including, but not limited to, the following: the number of, 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 $49 million, or 14.3%, increase in compensation and medical claims for the three months ended June 30, 2014, compared to the same period last year. We experienced a $63 million, or 6.4%, increase in compensation and medical claims for the nine months ended June 30, 2014, compared to the same period last year. Additional information regarding the inputs, assumptions, estimates and historical information for workers' compensation are available in Item 1. Financial Statements, *Note 9 – Workers' Compensation*.

For the periods shown, the table below highlights the 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 June 30,		Nine Months Ended June 30,	
(Dollars in millions)	2014	2013	2014	2013
(Unaudited)				
Total workers' compensation expense	$ 933	$ (469)	$ 1,955	$ 284
Claims paid on behalf of Postal Service's workers' compensation obligations	(393)	(344)	(1,044)	(982)
Expense related to the noncurrent portion of workers' compensation	$ 540	$ (813)	$ 911	$ (698)

*Note: The totals for certain amounts for the prior year have been reclassified to conform with classifications used in the current year. These reclassifications did not impact our operating results for the prior year.

TRANSPORTATION

Transportation expense consists primarily of highway, air, and international transportation costs. Transportation expense for the three months ended June 30, 2014, was $1,605 million, an increase of $17 million, or 1.1%, compared to $1,588 million for the same period last year. Transportation expense for the nine months ended June 30, 2014, was $4,972 million, a decrease of $116 million, or 2.3%, compared to $5,088 million for the same period last year.

The following table summarizes the components of transportation expense for the three and nine month periods ended June 30, 2014 and 2013:

Transportation Expense	Three Months Ended June 30,		Nine Months Ended June 30,	
(Dollars in millions)	2014	2013	2014	2013
(Unaudited)				
Highway transportation	$ 854	$ 812	$ 2,656	$ 2,551
Air transportation	515	565	1,575	1,800
International transportation	229	200	711	706
Other transportation	7	11	30	31
Total transportation expense	$ 1,605	$ 1,588	$ 4,972	$ 5,088

Highway transportation expenses were $854 million for the three months ended June 30, 2014, compared to $812 million for the same period last year, an increase of $42 million, or 5.2%. For the nine months ended June 30, 2014, highway transportation expenses were $2,656 million, compared to $2,551 million for the same period last year, an increase of $105 million, or 4.1%. These increases are attributable to the greater use of ground transportation in lieu of air transportation during the first nine months of 2014, as part of a continuing initiative to provide a cost-effective service and responsive transportation throughout the network.

Air transportation expenses were $515 million for the three months ended June 30, 2014, compared to $565 million for the same period last year, a decrease of $50 million, or 8.8%. Air transportation expenses were $1,575 million for the nine months ended June 30, 2014, compared to $1,800 million for the same period last year, a decrease of $225 million, or 12.5%. The decline in air transportation expenses is primarily attributable to the new air cargo contract with lower courier rates that was implemented in October of 2013. Additional savings were achieved through identification and transition of transportation modes from air to ground.

International transportation expenses were $229 million for the three months ended June 30, 2014, compared to $200 million for the same period last year, an increase of $29 million, or 14.5%. International transportation expenses were $711 million for the nine months ended June 30, 2014, compared to $706 million for the same period last year, an increase of $5 million, or 0.7%. The increases are attributable to increases in terminal dues fees.

OTHER EXPENSES

Other operating expenses were $2,430 million for the three months ended June 30, 2014, compared to $2,371 million for the same period last year, an increase of $59 million, or 2.5%. The increase is primarily due to vehicle maintenance service resulting from our aging fleet, and impairments and net gains/losses of equipment and vehicles.

Other operating expenses were $7,188 million for the nine months ended June 30, 2014, compared to $6,870 million for the same period last year, an increase of $318 million, or 4.6%. The increase is primarily due to vehicles maintenance of $52 million, supplies of $80 million, building maintenance of $36 million, impairments and net gains/losses of equipment and vehicles of $51 million, advertising and promotions campaigns of $50 million and technology and communication of $49 million. These increases were offset in part by decreases in depreciation and amortization expenses of $46 million.

Liquidity and Capital Resources

CASH FLOW ACTIVITY

Unrestricted Cash and cash equivalents totaled $4,950 million at June 30, 2014, compared to $2,326 million at September 30, 2013, an increase of $2,624 million.

The following table provides a summary of our cash flows for the nine month periods ended June 30, 2014, and 2013:

Cash Flow Statement (Dollars in millions)	Nine Months Ended June 30, 2014	2013
(Unaudited)		
Operating activities:		
Net loss	**$ (4,181)**	**$ (3,870)**
Noncash depreciation and gains on sales	**1,440**	**1,386**
Prefunding of retiree health benefits	**4,225**	**4,140**
Other changes in assets and liabilities	**1,677**	**(315)**
Net cash provided by operating activities	**3,161**	**1,341**
Investing activities:		
Capital expenditures, net of proceeds	**(469)**	**(378)**
Other	**39**	**(105)**
Net cash used in investing activities	**(430)**	**(483)**
Financing activities:		
Other	**(107)**	**(80)**
Net cash used in financing activities	**(107)**	**(80)**
Net increase in cash and cash equivalents	**$ 2,624**	**$ 778**

Operating Activities. Operating activities generated $3,161 million of cash during the nine months ended June 30, 2014, compared to $1,341 million for the nine months ended June 30, 2013, an increase of $1,820 million. The increase is due to timing differences for payroll related costs of $1,710 million incurred at June 30, 2014 but not disbursed until July. In addition, the increase in cash generated from operating activities was 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 and price increases on Market-Dominant and Competitive products which became effective on January 26, 2014.

Investing Activities. Purchases of property and equipment were $512 million for the nine months ended June 30, 2014, compared to $489 million in the same period last year, an increase of $23 million, or 4.7%. Proceeds from the sale of property and equipment were $43 million and $111 million for the nine months ended June 30, 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 nine months ended June 30, 2014 and 2013, we issued and repaid $4,700 million and $4,400 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 CONCERNS

We continue to suffer from a lack of liquidity. Cash balances remain insufficient to operate an organization with approximately $72 billion in annual operating expenses as its present balance can only fund less than one month of operating activity and remains insufficient to cover the legally-required retiree health benefits prefunding payment due by September 30, 2014. We held cash and cash equivalents of $5.0 billion and $2.3 billion as of June 30, 2014, and September 30, 2013, respectively, and had no remaining borrowing capacity on our $15 billion debt facility (See Item 1. Financial Statements, *Note 3 Debt*, for additional information). The increase in cash is largely attributable to the seasonal impact of holiday mailings during the first quarter of 2014 and the temporary exigent price increase on Market-Dominant products implemented on January 26, 2014. This 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, August 11, 2014, we have incurred no penalties or negative consequences resulting from our inability to make these payments.

We do not have sufficient cash balances to meet all of our existing legal obligations, make meaningful reductions in our debt and make important investments in our infrastructure. Annual capital expenditures have declined from almost $2 billion in 2008 to less than $700 million in 2013 to conserve cash. For the nine months ended June 30, 2014, capital expenditures totaled approximately $500 million. The present level of capital expenditures is not sustainable. Our delivery fleet includes approximately 140,000 vehicles that are at least 20 years old and nearing the end of their useful life. Repair and maintenance costs for these vehicles have risen significantly in recent years. Some facilities maintenance has been deferred in recent years to save cash and the backlog needs to be addressed. Investments in package sorting and handling equipment are needed to fully capitalize on business opportunities in the growing package delivery market and other letter sorting equipment must be updated. Further, the existing level of cash could be insufficient to support operations in the event of another significant downturn in the U.S. economy. Absent legislative change, current projections indicate that we will continue to have a low level of liquidity throughout 2014 and for the foreseeable future.

Our net losses of $1,955 million and $4,181 million, respectively, for the three and nine month periods ended June 30, 2014, includes $1,425 million and $4,275 million of expense accrued for the legally-mandated prefunding payment for retiree health benefits, respectively. This was the 21st quarterly loss in the past 23 quarters, and continues the trend of steady losses at the Postal Service. The requirement of 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 foreseeable future.

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 may 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 implemented a realignment of our operations to further reduce costs and 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. In July 2014, we announced that a second phase of mail processing realignments would begin in January 2015, culminating in the consolidation of up to 82 more processing locations. Additionally, we continue to leverage employee attrition, VER and increased utilization of non-career employees. In July 2014, we announced that a VER would be offered to approximately 3,900 Postmasters that were impacted by reductions in retail hours at certain postal facilities. There is no financial statement impact to the three months ended June 30, 2014 for this offer.

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 delivery days, which is expected to improve efficiency and reduce overtime pay and operating costs. We also announced our intent to continue the consolidation of its mail processing operations beginning in January 2015.

On January 26, 2014, we implemented price increases on Market-Dominant and Competitive products. The Market-Dominant increases included a 1.7% price increase based on the CPI-U plus a temporary 4.3% increase approved by the PRC in December 2013 as an exigent rate change. 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 we would otherwise have recovered through a CPI-U increase alone. 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. Some mailers have also filed an appeal seeking relief from the PRC's decision to allow an exigent rate increase. Additionally, we increased prices an average of 2.4% for Competitive products. Including the exigent rate change, these Market-Dominant and Competitive products changes are projected to generate approximately $2.7 billion of additional annualized revenue for the Postal Service.

We conserved capital by spending only what is believed essential to maintain our existing facilities and service levels. However, an increase of capital investment is necessary to upgrade our existing fleet of vehicles and processing equipment in order to remain operationally competitive.

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 with a change in existing law. We also continue to seek reforms that would establish a set of health care plans within FEHBP that would fully integrate with Medicare for current and future Postal Service retirees, largely eliminating the current unfunded liability. In addition, we seek reforms to the workers’ compensation system, and a refund of the estimated overfunding of the FERS, each of which requires legislative action.

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 postal products and 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 long-term financial challenges we face and the legislative changes that are required to restore 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.

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 June 30, 2014, the estimate of our liability for material claims increased by $185 million to $1,124 million from $939 million at September 30, 2013 based upon our evaluation of new and existing claims.

Fair Value Measurements

As required by authoritative accounting literature, certain fair value disclosures for the three months ended June 30, 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 nine month periods ended, June 30, 2014. All recognized losses have been incorporated into our financial statements as of June 30, 2014. See Item 1. Financial Statements, *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 and the Form 10-Q for the quarters ending December 31, 2013, and March 31, 2014.

As the debate on postal reform legislation continues in the 113th Congress, a number of reforms are urgently needed. Our key legislative requirements include:

- Require a set of specific health care plans within the FEHBP that would fully integrate with Medicare and largely eliminate the retiree health benefits unfunded liability.
- Refund the FERS Overfunding and Adjust the FERS Normal Cost Contribution.
- Adjust Delivery Frequency (Six-Day Packages/Five-Day Mail).
- Streamline the Governance Model (Eliminate Duplicative Oversight).
- Provide Authority to Expand Products and Services.
- Require a 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.

APPROPRIATIONS

On July 16, 2014, the House passed H.R. 5016, the *Financial Services and General Government Appropriations Act, 2015*. The bill includes $58.3 million in funding for revenue forgone and for free mail for the blind and overseas voting. The Postal Service requested $162.6 million, which included past revenue forgone debt repayments that had not been funded in past appropriations bills. A provision requiring six-day delivery of mail was included in the bill.

On June 24, 2014, the Senate Appropriations Subcommittee on Financial Services and General Government approved its fiscal year 2015 Financial Services bill. The bill includes $70.4 million in funding for free mail for the blind and overseas voting. The bill contains no provisions related to the Revenue Forgone Act of 1993, which authorizes the Postal Service to receive $29 million annually through 2035 as reimbursement for services it provided from fiscal years 1991 through 1998. A provision requiring six-day delivery of mail remains in the bill. It is uncertain when the full Senate Appropriations Committee will mark up the bill.

SIGNIFICANT POSTAL LEGISLATION

On June 17, 2014, H.R. 4872, the *Ending Special Mail Privileges for Congress Act of 2014*, was introduced in the House. The measure would amend several sections of Title 39, U.S. Code, as well as several other statutes, to repeal the franking privilege for Congressional mail and to strike all mention of franking and Congressional mail. The Postal Service would be instructed to revise its regulations governing the treatment of Congressional mail. If enacted, the changes would be effective at the beginning of calendar year 2015, coinciding with the start of the 114th Congress. The measure was referred to the House Oversight and Government Reform and the House Administration Committees.

On May 21, 2014, the House Oversight and Government Reform Committee held a markup meeting of H.R. 4670, the *Secure Delivery for America Act of 2014.* H.R.4670 was introduced on May 19, 2014, and it directs the Postal Service to provide the most cost effective primary mode of delivery feasible for postal customers. H.R. 4670 (as amended) was voted favorable by the Committee and was referred to the full House for consideration.

BOARD OF GOVERNORS NOMINATIONS

On July 30, 2014, the Senate Homeland Security and Governmental Affairs Committee held a business meeting to consider the nominations of James C. Miller III, Stephen D. Crawford, David Michael Bennett, and Victoria Reggie Kennedy, to be named Governors of the United States Postal Service. The Committee reported the nominations favorably. The nominations now await consideration by the full Senate.

On July 17, 2014, President Obama nominated Mickey D. Barnett to serve on the Board of Governors of the United States Postal Service for a term expiring December 8, 2020. Mr. Barnett was first appointed to the Board in 2006, and currently serves as Chairman. The nomination awaits consideration by the Senate Homeland Security and Governmental Affairs Committee.

PRC NOMINATIONS

On May 21, 2014, the Senate Homeland Security and Governmental Affairs Committee considered the nominations of Tony Hammond, of Missouri, to be a Commissioner of the Postal Regulatory Commission for a term expiring October 14, 2018, and Nanci E. Langley, of Hawaii, to be a Commissioner of the Postal Regulatory Commission for a term expiring November 22, 2018. Both nominations were reported favorably by the Committee. The nominations were sent to the full Senate for consideration.

CONGRESSIONAL HEARING

On April 8, 2013, the Deputy Director of the Office of Management and Budget (OMB) testified before the House Oversight and Government Reform Committee at a hearing entitled, "The President's Fiscal Year 2015 Budget Proposal for the Postal Service." The hearing was held to examine the Administration's proposals to improve the financial viability of the Postal Service and to compare the proposals against current postal reform legislation. The President's FY 2015 Budget offered several proposals on the Postal Service as follows:

- Refund the projected FERS overpayment to the Postal Service, over a 2-year period, and use postal-specific assumptions to calculate payments.
- Permit the Postal Service to shift to curbside and centralized delivery; and codify the Post Plan.
- Extend the exigent rate increase permanently.
- Recalculate the Retiree Health Benefits liability and restructure prepayments by forgiving the FY14 payment, cutting in half the payments due in FY15 and FY16, and then making payments based on a 40-year amortization schedule for 100 percent of the remaining liability.
- Provide the Postal Service with the authority to reduce mail frequency to 5 days per week.
- Allow the Postal Service the ability to increase collaboration with state and local governments, and allow beer and wine sales through the mail.

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 June 30, 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 June 30, 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 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: August 11, 2014

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

Date: August 11, 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: August 11, 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: August 11, 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 June 30, 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: August 11, 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 June 30, 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: August 11, 2014

/s/Joseph Corbett

Joseph Corbett

Chief Financial Officer and Executive Vice President