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

FORM 10-K

(Mark One)

☑ **ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the fiscal year ended SEPTEMBER 30, 2016

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, DC 20260
(202) 268-2000
(Address and telephone number, including area code, of registrant's principal executive offices)

Securities registered pursuant to Section 12(b) of the Act: None

Securities registered pursuant to Section 12(g) of the Act: None

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes ☐ No ☑

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Exchange Act. Yes ☑ No ☐

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 if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K (§229.405 of this chapter) is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. 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 the definitions 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 ☐ 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 ☑

The aggregate market value of shares of common stock held by non-affiliates as of March 31, 2016: N/A

The number of shares of common stock outstanding as of November 15, 2016: N/A

Documents Incorporated by Reference: None

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UNITED STATES POSTAL SERVICE

PART I

ITEM 1. BUSINESS

In accordance with the provisions of the *Postal Reorganization Act* ("PRA"), the United States Postal Service ("Postal Service," "USPS," "we," "our" and "us") began operations on July 1, 1971, succeeding the cabinet-level Post Office Department established in 1792. The PRA established us as an "independent establishment of the executive branch of the Government of the United States" with the mandate to offer a "fundamental service" to the nation "at fair and reasonable rates." We do not receive tax dollars for operating expenses and rely solely on the sale of postage, products and services to fund our operations.

We serve retail and commercial customers in the communications, distribution and delivery, advertising and retail markets throughout the nation and internationally. As a result, we maintain a very diverse customer base and are not dependent upon a single customer or small group of customers. No single customer represented more than 3% of operating revenue for the years ended September 30, 2016, 2015 and 2014.

As an establishment of the executive branch, we align specific objectives with those of the U.S. government. We are subject to numerous federal, state and local regulatory and reporting laws, as well as environmental laws and regulations. Our governing statute is codified in Title 39 of the U.S. Code. The *Postal Accountability and Enhancement Act of 2006, Public Law 109-435* ("PAEA") made revisions to the PRA and established the Postal Regulatory Commission ("PRC"), endowing it with regulatory and oversight obligations.

We operate and manage a very extensive and integrated retail, distribution, transportation and delivery network. Although PAEA divides our services into Market-Dominant and Competitive products, we monitor revenue by mail classes and weights, and we operate as a single segment throughout the U.S., including its possessions and territories.

As used herein, all references to years in this report, unless otherwise stated, refer to fiscal years beginning October 1 and ending September 30. All references to quarters, unless otherwise stated, refer to fiscal quarters.

GOVERNANCE

The law requires an eleven-seat Board of Governors ("Board") which generally consists of our Postmaster General, Deputy Postmaster General and nine independent governors ("Governors"). The Governors are appointed by the President of the United States ("President") with the advice and consent of the United States Senate ("Senate"). The Postmaster General is appointed by the Governors, and the Deputy Postmaster General is appointed by the Governors and the Postmaster General.

The Board is required by law to have a quorum of six members in order to take certain actions. In November 2014, while the Board still had a quorum, it issued a resolution that established a Temporary Emergency Committee of the Board ("TEC") to exercise certain powers reserved to the Board that are necessary for continuity of operations during a period in which it is unable to assemble a quorum.

Also in November 2014, the Governors issued a resolution regarding the exercise of those powers conferred by law solely to the Governors as distinguished from the full Board, which include the appointment and removal of the Postmaster General and the establishment of prices and classifications for our services. The Governors determined that their ability to exercise those powers reserved to the Governors' was not impacted by the loss of a Board quorum.

In December 2014, due to the term expiration of one Governor and Senate inaction on pending nominations, the number of sitting Board members dropped to five, thereby rendering the Board unable to assemble a quorum. The TEC has exercised its powers since that time.

We publicly announced the resolutions that established the TEC and the Board's exercise of power in a December 16, 2014, Federal Register notice.

On December 8, 2015, the terms of two of the remaining Governors expired, which reduced the number of sitting Board members to three, including only one Governor. As described later in *Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations - Legislative Update*, during 2015 and 2016, the President made six Governor nominations, and each of these awaits Senate confirmation. If the Senate does not confirm any of the Governor nominations prior to December 8, 2016, the date on which our remaining Governor's term expires, our Board will have lost all of its independent Governors and will consist of only our Postmaster General and Deputy Postmaster General.

The TEC currently consists of the remaining members of the Board and exercises those Board powers necessary for operational continuity. The TEC will continue in existence until the Board is again able to assemble a quorum.

SERVICES

We fulfill our legal mandate to provide universal service at a fair price by offering a variety of postal services to our many customers. Prices and fees are determined by our Governors, subject to a review process by the PRC. Services are sold by approximately 32,000 post offices, stations and branches, plus a large network of Contract Postal Units, Community Post Offices, Village Post Offices, commercial outlets which sell stamps and services on our behalf and through our website www.usps.com. Mail deliveries are made to approximately 156 million city, rural, *PO Box* and highway delivery points. Operations are conducted primarily in the domestic market, with international revenue representing approximately 4% of operating revenue for the year ended September 30, 2016.

CLASSIFICATION AND PRICING

Within *First-Class Mail*, *Standard Mail*, *Periodicals*, *International* and *Other* services, prices do not vary unreasonably by customer for the level of service provided. We offer contract prices, rebates, online price reductions and other incentives to encourage customers to increase their volume, which in turn increases our revenue. Although the PAEA classifies our services as Market-Dominant and Competitive "products," the term "services" is often used in this report for consistency with other descriptions of services we offer.

Periodic reclassification of services from Market-Dominant to Competitive, which requires PRC approval, is necessary to rationalize service offerings. The additional flexibility provided in Competitive services allows us to better offer services that meet customer needs, increase our business and allow us to price our services competitively within the markets in which we operate. Information regarding PRC decisions and pending dockets can be obtained on the PRC website: www.prc.gov.

Market-Dominant Services

Market-Dominant services account for approximately 74% of our annual operating revenues. Such services include, but are not limited to, *First-Class Mail*, *Standard Mail*, *Periodicals* and certain parcel services. Price increases for these services are generally subject to a price cap based on the Consumer Price Index for All Urban Consumers ("CPI-U"). Prices for Market-Dominant services are set by our Governors and reviewed by the PRC for legal compliance.

Prices for certain Market-Dominant services increased an average of 1.9% in May 2015 and 1.7% in January 2014. On October 12, 2016, we filed with the PRC a notice of our intent to increase prices for certain Market-Dominant services by an average of 0.9%. We also filed a request with the PRC to rename our *Standard Mail* service category and class of mail to *USPS Marketing Mail*. If approved, we expect these price increases and service category name change will go into effect in January 2017.

The PRC authorized us to collect an exigent surcharge on most Market-Dominant services beginning in January 2014 until it produced incremental revenue of just over $4.6 billion, a figure the PRC determined was lost due to the Great Recession's suppression of mail volume. The limit on the amount of the exigent surcharge that was imposed by the PRC was reached on April 10, 2016, and we therefore reduced the prices of applicable Market-Dominant services on that date.

As a result of the expiration of the surcharge, we estimate that our revenue and cash flow for 2016 was lower by approximately $1 billion than what it otherwise would have been. Going forward without the surcharge, we expect our revenue and cash flow to decline from what it otherwise would be by almost $2 billion per year, unless the PRC's decision to limit our recovery in the manner described above is modified again or reversed through a pending appeal.

Competitive Services

Competitive services, such as *Priority Mail*, *Priority Mail Express*, *Parcel Select* and *Parcel Return Service* and some types of *International* mail, have greater pricing flexibility. Prices for Competitive services are set by our Governor(s) and reviewed by the PRC for legal compliance. By law, prices must cover "costs attributable" (meaning the direct and indirect postal costs attributable to such product through reliably identified causal relationships) to each service and must contribute a reasonable share of the institutional costs of the Postal Service, currently 5.5%, as determined by the PRC.

Prices for certain Competitive services increased an average of 9.5% in January 2016, 3.5% in May 2015 and 2.4% in January 2014. On October 19, 2016, we filed with the PRC a notice of our intent to increase prices for certain Competitive services by an average of 3.9%. If approved, we expect these price increases will go into effect in January 2017.

The PAEA prohibits the subsidization of Competitive services costs by Market-Dominant services revenue. Accordingly, the PRC reviews our price increase notices, and we are diligent to ensure that each Competitive service covers its attributable costs and an appropriate share of our institutional costs.

SERVICE CATEGORIES

Although we operate as a single segment, we monitor revenue by mail classes, products and shapes. Our management uses the following broad service categories to describe and report on our performance:

- **First-Class Mail** - This category encompasses the *First-Class Mail* class of mail representing letters, postcards or any flat advertisement or merchandise destined for either domestic (up to 13 ounces) or international (up to 4 pounds) delivery. *First-Class Mail* letters include personal correspondence, bills or statements of account and payments.

- **Standard Mail** - This category encompasses the *Standard Mail* class of mail representing any item, including advertisements and marketing packages, weighing less than 16 ounces that is not required to be sent using *First-Class Mail*. *Standard Mail* is typically used for direct advertising to multiple delivery addresses. *Every Door Direct Mail* enables customers to prepare direct mailings without names and addresses for distribution to all business and residential customers on individual carrier routes. As mentioned above, we have filed a request with the PRC to change the name of this service category and class of mail from *Standard Mail* to *USPS Marketing Mail* effective in January 2017. This name change will aid our customers in understanding what *Standard Mail* is and how it can be used as part of their respective marketing strategies.

- **Shipping and Packages** - This category includes: *First-Class Package Service*, a shipping option for high-volume shippers of packages that weigh less than one pound and *First-Class Mail* parcels for shipment of boxes, thick envelopes or tubes of 13 ounces or less; *Package Services* for merchandise or printed matter, such as library and media mail weighing up to 70 pounds; *Parcels* - *Parcel Select*, *Parcel Return Service* and *Standard Mail Parcel Services* which provide commercial customers with a means of package shipment, typically “last-mile” products; *Priority Mail*, which is offered as a service both within the U.S. and abroad with the domestic service offering a 1-3 day specified (non-guaranteed) delivery; and *Priority Mail Express*, which provides an overnight, money-back guaranteed service which includes tracking, proof of delivery and basic insurance up to $100. *Priority Mail Express* delivery is offered to most U.S. destinations for delivery 365 days a year.

- **International** - This category offers international mail and shipping services with individual customer contracts and agreements with other postal administrations. *Priority Mail Express International* and *Priority Mail International* services compete in the e-commerce cross-border business. They provide an affordable option for our retail and business customers for much of their shipping needs to over 180 countries. *Global Express Guaranteed* is the premier international shipping option that offers reliable, date-certain delivery in 1 to 3 business days to major markets, with a money-back guarantee.

- **Periodicals** - This category encompasses the *Periodicals* class of mail offered for newspaper, magazine and newsletter distribution. This service requires prior authorization by the Postal Service.

- **Other** - This broad category includes: *PO Box* services, which provide customers an additional method for mail delivery that is private and convenient. *Money Orders* offer customers a safe, convenient and economical method for the remittance of payments. *Money Orders* are available for amounts up to $1,000, can be purchased and cashed at most post offices, or can be deposited or negotiated at financial institutions. USPS Extra Services offer a variety of service enhancements that provide security, proof of delivery or loss recovery. These services include: *Certified Mail*, *Registered Mail*, *Signature Confirmation*, *Adult Signature* and insurance up to $5,000 and are available online, at post offices or at automated postal centers.

For a discussion of economic and other factors affecting the volume of these services and our actions taken to address these factors, see *Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations*, *Results of Operations*, *Operating Revenue and Volume*.

RESEARCH AND DEVELOPMENT

We operate a research and development facility in Virginia for design, development and testing of postal equipment and operating systems. We also contract with independent suppliers to conduct research activities. While research and development activities are important to our business, these expenditures are not material to our results of operations or financial position.

INTELLECTUAL PROPERTY

We own intellectual property that includes trademarks, service marks, patents, copyrights, trade secrets and other proprietary information and routinely generate intellectual property in the course of developing and improving systems, services and operations. While legal protection for intellectual property and proprietary information is significant to our success, the knowledge, ability and experience of our employees and the timeliness and quality of service we provide are equally important.

MARKETING

Our marketing program seeks to capitalize on our industry standing, including our existing relationships and our reputation based on our service delivery performance every day. We have adjusted to changes in customer behaviors and demands to make accessing and using postal services more convenient. We have developed innovative mobile applications which enable customers to locate a post office, find a ZIP Code, track packages and shop online. Online service offerings available through www.usps.com have also enhanced the customer experience.

We believe that as we equip businesses with tools to reach our mutual customers, our revenue will grow. Our marketing approach highlights our value, our enhanced digital technologies and the linkages between them. Additionally, we seek to maintain our name recognition through the use of media advertising, trade shows, technical seminars and direct mailings.

We have key strategic alliances with large transportation corporations to provide distribution and delivery services allowing us to serve our respective customers' needs. Maintaining these alliances is crucial to sales development and growth as they often provide us with introductions into new markets.

COMPETITION

A wide variety of communications media compete for the same types of transactions and communications that historically were conducted using our services. These channels include, but are not limited to, newspapers, telecommunications, television, email, social networking and electronic funds transfers. The package and express delivery businesses are highly competitive. The primary competitors of our Shipping and Packages services are FedEx Corporation and United Parcel Service, as well as other regional and local delivery companies and leisure carriers. Our Shipping and Packages business competes on the basis of the breadth of our service network, convenience, reliability and economy of the service provided.

SEASONALITY

Mail volume and revenue are historically greatest in the first quarter of our fiscal year, which includes the holiday mailing season, and lowest in the third and fourth quarters of our fiscal year during the spring and summer. In national election years, direct mail may be heavily used by political organizations to reach their targeted audiences, thereby generating temporary volume and revenue increases during the months preceding an election.

EMPLOYEES

At September 30, 2016, we employed approximately 509,000 career employees and approximately 131,000 non-career employees, substantially all of whom reside in the U.S. For a more detailed discussion of items that impact our employees, see *Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations*, *Results of Operations*, *Operating Expenses*.

BARGAINING AGREEMENTS

Approximately 91% of career employees are covered by collective bargaining agreements. These agreements include provisions governing work rules and provide for general wage increases plus cost of living adjustments ("COLAs"), which are linked to the Consumer Price Index – Urban Wage Earners and Clerical Workers ("CPI-W"), as well as provisions that limit our ability to reduce the size of the labor force and restrict the number of non-career employees. Our 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").

By law, we must consult with management organizations representing most of our employees not covered by collective bargaining agreements. These consultations provide non-bargaining unit employees in the field with an opportunity to participate in the planning, development and implementation of certain programs and policies that affect them.

FEDERAL EMPLOYEE AND RETIREMENT BENEFIT PROGRAMS

We are required to participate in U.S. government pension and health and benefits programs for employees and retirees, including the Federal Employees Health Benefit ("FEHB") program, the Civil Service Retirement System ("CSRS") and the Federal Employees Retirement System ("FERS"). We have no control or influence over the benefits offered by these plans and we contribute to these plans as specified by law or contractual agreements with our employee unions (in the case of health benefits for most active employees).

We are legally-mandated to participate in the federal workers' compensation program that is managed by the Department of Labor's ("DOL") Office of Workers' Compensation Programs ("OWCP") and governed by the *Federal Employees' Compensation Act* ("FECA").

RETIREE HEALTH BENEFITS

The PAEA established the Postal Service Retiree Health Benefits Fund ("PSRHBF") in 2006. In accordance with applicable law, we are required to fund retiree health benefits using an accelerated prefunding payment schedule. Such a requirement to prefund retiree health benefits is not imposed on most other federal entities or private sector businesses that offer such benefits.

Since its enactment, the PSRHBF prefunding requirement has contributed significantly to our losses. As of September 30, 2016, we have contributed $20.9 billion to the PSRHBF and defaulted on additional prefunding amounts totaling $33.9 billion for the years 2012 through 2016 because we did not have sufficient funds to make the funding payments without adversely impacting our ability to continue operations. As of the date of this report, we have not incurred any penalties or negative financial consequences as a result of not making the PSRHBF prefunding payments. In 2017, the PSRHBF will begin funding the Postal Service's share of retiree health benefit premiums, and we will begin paying the "normal costs" of retiree health benefits (i.e., the present value of the estimated retiree health benefits attributable to active employees' current year of service), which we estimate will initially be approximately $2.9 billion per year, as well as an amortization payment of our unfunded liability, also estimated to initially be approximately $2.9 billion per year, based on preliminary valuations provided by OPM under the PAEA mandate.

OVERSIGHT AND REGULATION

As discussed throughout this report, we are subject to oversight by the United States Congress ("Congress") and regulation by the PRC and other government agencies. In addition to Senate confirmation of our Governors, Congress significantly influences how we conduct our business and operations through passage of laws. For example, unless and until new laws become effective, we are legally bound by annual *Financial Services and General Government* appropriations legislation, which is part of the larger U.S. government's budget and spending process each fiscal year for specific U.S. government departments, agencies and programs. Among other restrictions, such legislation requires us to maintain a six-day delivery schedule. We are also bound by postal-specific legislation, such as the PAEA, which impacts our financial performance and restricts our competitiveness by limiting our ability to grow our business, price our services and constrain our expenses. For a more detailed explanation, see *Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations*, *Legislative Update*.

ENVIRONMENTAL MATTERS

Although we are required to comply with various federal, state or local environmental laws and regulations, none of these has had a material impact on our financial results or competitive position, or resulted in material capital expenditures. However, the effect of possible future environmental legislation or regulations on operations cannot be predicted. New laws or regulations that regulate greenhouse gas emissions into the environment may increase our operating costs, including the cost of fuel, and possible retrofitting existing vehicles.

REGULATORY REPORTING

We are not a reporting company under the *Securities Exchange Act of 1934*, as amended ("Exchange Act"), and are not subject to regulation by the Securities and Exchange Commission ("SEC"). However, the PAEA requires us to file with the PRC certain financial reports containing information prescribed by the SEC under Sections 13 and 15(d) of the Exchange Act. These reports include annual reports on Form 10-K ("Annual Report"), quarterly reports on Form 10-Q and current reports on Form 8-K.

We are also required by law and regulations to disclose operational and financial information beyond what the law requires of most U.S. government entities and private-sector companies. Pursuant to Title 39 of the U.S. Code and PRC regulations, we must also file additional information with the PRC, including Cost and Revenue Analysis reports; Revenue, Pieces and Weight reports; financial and strategic plans and the *Comprehensive Statement on Postal Operations*.

All of these reports may be found online at www.about.usps.com/who-we-are/financials/welcome.htm, free of charge, as soon as reasonably practicable after we file them with the PRC. Information on our website is not incorporated by reference into this report. Requests for copies of our reports may also be sent to the following address: Corporate Communications, United States Postal Service, 475 L'Enfant Plaza, SW, Washington, DC 20260-3100.

ITEM 1A. RISK FACTORS

We are subject to various risks and uncertainties that could adversely affect our business, financial condition, results of operations and cash flows. In addition to the risks and uncertainties that are described below, others that we do not yet know of or that we currently believe are immaterial could arise or become material and may also impair our business.

Although the PRA established our eleven-seat Board with nine seats for independent Governors, the number of active Governors will likely be none if the Senate fails to confirm any of the President's nominations for Governor by December 8, 2016, restricting our ability to take certain important actions.

In 2014, the Senate failed to act on five Governor nominations, and those nominations expired upon the adjournment of Congress in December of 2014, causing our Board to lose its quorum. Because certain powers are reserved to the Board, it adopted a resolution, just prior to the loss of its quorum, delegating those powers needed to provide for continuity of operations to the TEC composed of the remaining members of the Board (*i.e.*, the Governors then in office, the Postmaster General and the Deputy Postmaster General).

Additionally, certain powers are reserved to the Governors. Although the inability of the Board to constitute a quorum does not inhibit or affect the authority of the Governors in office from exercising those powers vested solely in the Governors, it is not apparent how those powers could be exercised if no Governors are in place. The critical responsibilities reserved to the Governors are setting our prices, approving new services and appointing (and, if necessary, removing) our Postmaster General and Deputy Postmaster General. In the event that no Governors are in place, these critical duties may not be able to be executed, potentially leaving us without the ability to adjust our prices as needed, introduce new services or appoint or replace our two most senior executive officers.

During 2015 and 2016, the President made six Governor nominations, and each of these awaits Senate confirmation. If the Senate does not confirm any of the Governor nominees prior to December 8, 2016, the date on which our remaining Governor's term expires, our Board will have lost all of its independent Governors and will consist of only our Postmaster General and Deputy Postmaster General.

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

The demand for our services is heavily influenced by the economy. Adverse economic conditions could negatively affect our business and results of operations, primarily through disrupting our customers' businesses. To the extent that the U.S. and other countries experience slow or negative economic growth, our business, financial position and results of operations will be adversely impacted.

Current and future management actions to generate cash flows by increasing efficiency, reducing costs and generating additional revenue may not be sufficient to meet all of our financial obligations or to carry out our strategy.
Our strategies to increase efficiency and reduce costs by adjusting our network, infrastructure and workforce and to retain and grow revenue are currently constrained by contractual, statutory, regulatory and political restrictions. Accordingly, our ability to react quickly to the changing economic climate and industry conditions is inhibited. We have also proposed legislative changes that are needed to provide us with the legal authority to implement additional measures to increase efficiency and cost savings and to grow revenue, but nothing we have proposed has become law.

We are subject to congressional oversight and regulation by the PRC and other government agencies. We have a wide variety of stakeholders whose interests and needs are sometimes in conflict.
We operate as an independent establishment of the executive branch of the U.S. government and as a result are subject to a variety of regulations and other limitations applicable to federal agencies. If the U.S. government curtails its spending due to debt ceiling or other constraints, we may be adversely impacted. Additionally, as an outgrowth of our unique status as a fundamental service provider to the nation, we attempt to balance the interests of many parties. Efforts to be responsive to various stakeholders sometimes adversely impact the speed with which we are able to respond to changes in mail volume or other operational needs. Limitations on our ability to take action could adversely affect operating and financial results.

Adverse events may call into question our reputation for quality and reliability or our ability to deliver the mail and could diminish the value of our brand. This could adversely affect our revenue and results of operations.
Our brand represents quality and reliable service, and therefore is a valuable asset. We use our brand extensively in sales and marketing initiatives and exercise care to defend and protect it. Any event, whether real or perceived, that calls into question our long-term existence, our ability to deliver mail, our quality or our reliability could diminish the value of our brand and reputation and could adversely affect our business operations and operating results.

The expiration of the exigent surcharge has had, and will continue to have, an adverse impact on our future operating revenue and liquidity.
In December 2013, the PRC ruled that we could collect a 4.3% exigent surcharge on Market-Dominant services beginning in January 2014, until such time as the surcharge produced $3.2 billion in incremental revenue, or $2.8 billion in contribution, a figure that the PRC determined was lost due to the Great Recession's suppression of mail volume.

We appealed the PRC's decision to the U.S. Court of Appeals for the District of Columbia Circuit (the "Court"), arguing that the PRC attributed to the Great Recession far too little lost mail volume and that the exigent surcharge should remain in effect for as long as it remained necessary. In June 2015, the Court ruled on the appeal and remanded the case back to the PRC for further review, primarily related to the PRC's methodology for calculating mail volume lost due to the Great Recession. Although the Court largely upheld the PRC's analytical framework, it vacated one key aspect of the methodology for calculating mail volume lost due to the Great Recession and suggested the PRC consider another element of its methodology.

On July 29, 2015, the PRC authorized us to collect over $1.4 billion in additional incremental revenue from the surcharge, bringing the total allowed to just over $4.6 billion. We also appealed that decision to the Court and it remains pending.

The limit on the amount of the exigent surcharge collected was reached on April 10, 2016, and we therefore reduced the prices of applicable Market-Dominant services on that date. As a result of the expiration of the surcharge, we estimate that our 2016 revenue and cash flow declined by approximately $1 billion from what it otherwise would have been, and is expected to continue to decline from what it otherwise would be by almost $2 billion per year going forward, unless the PRC's decision to limit our recovery in the manner described above is modified again or reversed through the pending appeal.

Our need to restructure our operations in response to declining mail volume may result in significant costs. It is possible that the measures being considered would be insufficient to reduce our workforce and physical infrastructure to a level commensurate with declining mail volume.
Our current network optimization plans include reviewing mail processing operations and reductions in lobby hours of many retail units, post offices and other facilities. Presently, our regular review of the carrying value of our assets has not resulted in significant impairment of our physical assets. However, future changes in business strategy, legislation, government regulations or economic or market conditions may result in material impairment write-downs of our assets.

In the future, we may also consider offering financial incentives to encourage employees to voluntarily end their employment, as has been done in the past. Any impairment, incentives or other related costs we incur associated with such separations would adversely impact our financial results in the short-term, although we would expect such actions to result in long-term savings. In addition, we can provide no assurance that the mechanisms available under existing law and contractual arrangements will be sufficient to reduce the workforce or facilities to a level that would allow a return to financial stability.

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

Our marketplace competitors primarily include providers of package delivery services. Our competitors have different cost structures and fewer regulatory restrictions than we do and are able to offer differing services and pricing, which may hinder our ability to remain competitive in these service areas. In addition, our competitors have access to public capital markets, which allows them greater freedom in their investments and expansion of their business.

Customer usage of postal services continues to shift to substitute products and channels provided by electronic communication services. *First-Class Mail*, such as the presentment and payment of bills, has been eroded by competition from electronic media, driven by some of our major commercial mailers which actively promote the use of online services. The volume of our *Periodicals* service continues to decline as consumers increasingly use electronic media for news and information. Periodical advertising has also experienced a decline as a result of the move to electronic media.

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

In order to offset declining volume and revenue caused by the changing economy and diversion to electronic media, our ability to sell new products and services in new or existing markets will be a key factor in returning to profitability. However, various laws and regulations significantly limit our ability to enter new markets and/or to provide new services and products as defined by traditional industry definitions.

Without legal or regulatory changes that allow us to introduce new products or services to take advantage of our assets, including our strong network and "last-mile" capabilities, we may be unable to respond adequately to consumers' changing needs and expectations. These limitations have the potential to adversely impact our results of operations and long-term financial viability. PAEA generally limits price increases on our Market-Dominant services to the rate of inflation as measured by the CPI-U. However, our costs are not similarly limited. A large portion of our cost structure cannot be altered expeditiously, and the number of our delivery points continues to grow. Accordingly, we may not be able to increase prices sufficiently to offset increased costs.

Because our services are provided primarily through our employees, our costs are heavily concentrated in wages and employee and retiree benefits. These costs are significantly impacted by wage inflation, health benefit premium increases, retirement and workers' compensation programs, and COLAs. Some of these costs have historically tended to increase at a higher rate than inflation as measured by the CPI-U. We believe that continuing productivity improvements alone will not be sufficient to address the challenges presented by declining volume and revenue and the regulatory price cap, nor will revenue enhancements keep pace with increased cost structures.

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

Our collective bargaining agreements currently in force include provisions for mandatory COLAs, which are linked to the CPI-W. Although CPI-W has been relatively low since 2008 when our employees received COLA-based pay increases of nearly $1.1 billion, a resurgence of consumer inflation could have a significant adverse impact on our labor costs. The agreements also contain provisions that limit our ability to reduce the size of the labor force and employ non-career personnel. Reductions in the size and cost of our labor force may be necessary to offset the effects of declining volume and revenue.

Our ability to negotiate contracts that control labor costs is essential to achieving financial stability. We have no assurance that we will be able to negotiate contracts in the future with our unions that will result in a cost structure that is sustainable within current and projected future revenue levels. In addition, if our future negotiations should fail and involved parties proceed to arbitration, the risk of an adverse outcome rises, as there is no current statutory mandate requiring an interest arbitrator to consider our financial health in issuing an award. An unfavorable award in arbitration could have significant adverse consequences on our ability to meet future financial obligations.

Furthermore, an increase in the CPI-W may not correspond to an equivalent increase in the CPI-U, which affects the prices of our Market-Dominant services, as the two indexes are calculated differently. Therefore, we may not be able to increase the prices of our services to keep up with increases in our wages.

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

Some of our suppliers and customers enter into long-term contracts with us to supply goods and services and to procure our services. These contracts are renegotiated from time to time and to the extent that contracts are not renewed, or are renewed with terms that may not sufficiently cover our costs or increase our costs, may have an adverse effect on our business. Certain vendors and customers are significant to the delivery of certain product lines, including a large courier service for air transportation. Otherwise no single customer or supplier is material to the Postal Service as a whole. Our ability to maintain current or improved contract terms with customers and suppliers is critical to our initiatives to return to financial sustainability.

We rely on third-parties for air transportation to deliver our mail throughout the nation and abroad. A significant disruption in air transportation service could adversely affect our business and results of operations.

We do not own or operate aircraft and we rely on third-parties for the air transportation service required to deliver our mail and packages to various destinations within the U.S. and abroad. We are therefore subject to the risk of our partners' business operations and also to the adoption of regulatory requirements and other events that affect specific airlines or the airline industry as a whole, which could affect air service or temporarily ground the fleets of our partners. We may also not be able to negotiate terms as favorable with replacement carriers should one or more of our existing partners experience a disruption.

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

We are exposed to changes in commodity prices, primarily for diesel fuel, unleaded gasoline and aircraft fuel for transportation of mail, and natural gas and heating oil for facilities. The price and availability of fuel can be unpredictable and is beyond our control. Unlike commercial entities, we are unable to institute fuel surcharges in our pricing model. Additionally, as we also use contracted carriers to transport the mail, we anticipate that increased operating costs for these independent carriers, including increased costs resulting from rising fuel prices, may ultimately be passed through to us.

A failure to protect the privacy of customer information could damage our reputation and result in a loss of business.

We have invested in and employ a variety of technology security initiatives aimed at protecting organizational information, as well as customer information. As one of the U.S. government entities most trusted by the nation, protecting the confidentiality of data that we obtain is paramount to us. However, should our information technology security initiatives not fully insulate us from a security breach or data loss, our reputation could be damaged, resulting in an adverse effect on our operations and financial results. Moreover, unlike other non-governmental entities in our industry, we must abide by the *Privacy Act of 1974*, which restricts how we can collect, use, maintain and disseminate personally-identifiable information and prescribes civil and criminal penalties for non-compliance.

We rely extensively on computer systems and technology to manage the delivery of mail, process transactions, summarize results and manage our business. In addition, we were subject to a major data breach in 2014, and while we have taken steps to prevent similar events going forward, we may be the target of future attacks.

Our operational and administrative information systems are among the largest and most complex systems maintained by any organization in the world. Any disruption to our infrastructure, including those impacting computer systems that facilitate mail handling and delivery and customer-utilized websites, could adversely impact customer service, mail volume and revenue, and result in significant increased costs. Any significant systems failure could cause delays in the processing and delivering of mail or result in the inability to process operational and financial data. Such disruptions could impair our reputation for reliable service, which would also adversely affect results of operations.

In the fourth quarter of 2014, we discovered a data breach that involved the theft of certain personally-identifiable information through unauthorized access to our network, and we have since remediated the condition and underlying controls. For more information, see *Item 7. Management's Discussion and Analysis of Financial Condition*, *Cyber Intrusion Incident*.

Reports of cyber incidents affecting national security, intellectual property and individuals have been widespread, with reported incidents involving data loss or theft, economic loss, computer intrusions and privacy breaches. The source of such threats is wide-ranging. The ability to maintain confidentiality, integrity and availability of information is critical to fulfilling our mission, and system failures resulting from these threats could damage our reputation, resulting in loss of business and increased costs.

Due to our recent and projected cash constraints, our operational performance in the future could be at risk as a result of inadequate capital investment in facilities, transportation equipment, mail processing equipment or information technology infrastructure, all of which are essential for our operations.
If our operations do not generate the liquidity we require, we may be forced to reduce, delay or cancel investments in technology, facilities and/or transportation equipment, as we have done in the recent past, while our competitors and other businesses are pursuing advanced, competing technologies and equipment.

Additionally, our aging facilities, equipment and transportation fleet could inhibit our ability to be competitive in the marketplace, deliver a high-quality service and meet the needs of the American public. The changes in the economic landscape in recent years have increased the importance for us to invest in our operations in order to remain competitive. Failure to anticipate or react to our competition, market demands and/or new technology due to inadequate cash reserves is a significant operational risk. An aging or potentially obsolete infrastructure could result in a loss of business and increased costs.

We have a substantial amount of indebtedness.
Since 2012, we have reported debt obligations to the Federal Financing Bank ("FFB") of $15 billion, the amount of our statutory debt limit. Our significant indebtedness has important consequences. It limits our flexibility in planning for, or reacting to, changes in the business environment or competition. It places us at a competitive disadvantage compared to commercial competitors that may have less debt and which have access to public capital markets. It also could require us to dedicate a substantial portion of our future cash flow from operations to payments on indebtedness, thus reducing the availability of cash flow to fund working capital, capital expenditures and other general organizational activities.

Health and pension benefit costs represent a significant expense to us.
With approximately 509,000 career employees and approximately 490,000 annuitants and survivors participating in FEHB as of September 30, 2016, our expenses relating to employee and retiree health and pension benefits are significant. We participate in U.S. government pension and health and benefits programs for employees and retirees, including FEHB, the CSRS and the FERS, as required by law. We have no control or influence over the benefits offered by these plans and make contributions to these plans as specified by law or contractual agreements with our unions (in the case of health benefits for most active employees). Several factors including participant mortality rates, return on investment, and inflation could require us to make significantly higher future contributions to these plans, and many of these factors are beyond our control.

In recent years, we have experienced significant increases in retiree health benefits costs, primarily as a result of PAEA, which obligates us to fully prefund, on an accelerated time frame, the health benefits of current Postal Service employees and retirees. Additionally, we are required to continue contributing to the FERS pension program at rates specified by the Office of Personnel Management ("OPM") and as soon as 2017, we will likely be required to resume contributions to the CSRS, which were suspended under PAEA through 2016, if OPM determines that a supplemental unfunded liability payment is necessary.

Workers' compensation insurance and claims expenses could have a material adverse effect on our business, financial condition and results of operations.
Workers' compensation expense accruals are established for estimates of cash outlays that we are expected to ultimately incur on reported claims, as well as estimates of the costs of claims that have been incurred but not yet reported. Trends in actual experience and management judgments about the present and expected levels of cost per claim are significant factors in the determination of such accruals. Several other factors which are beyond our control, such as discount and inflation rates, could cause us to incur higher workers' compensation expenses.

We believe our estimated accruals for such claims are adequate, but if actual experience in the number of claims, and/or severity of claims for which we retain risk increases, required accruals could materially differ from our estimates and adversely affect our financial condition and results of operations. In addition, our workers' compensation program is administered for us by the DOL, and as such, we do not have the same level of control over the execution of the program, including the costs we incur for certain medical and pharmacy costs, that a private company has with its workers' compensation insurance provider.

Additionally, our workers' compensation expenses have been increasingly impacted by costs associated with pharmaceutical compounding, which is the creation of a pharmaceutical product through the combination of various ingredients directly by a pharmacist. From 2013 to 2016, our compound pharmaceutical costs have experienced nearly a 1,800% increase, and in March 2016, the U.S. Postal Service Office of Inspector General issued a report concluding that those increases were attributable to DOL's failure to control the pharmacy-compound invoicing process. As the report recognized, we have no control over that process, which the DOL exclusively administers.

The potential liability associated with existing and future litigation against us could have a material adverse effect on our business, results of operations, financial condition and cash flows.
In the normal course of operations, we are subject to threatened and actual legal proceedings from time to time. Any litigation, regardless of its merits, could result in substantial legal fees and costs incurred by us. Further, actions that have been or will be brought against us may not be resolved in our favor and, if significant monetary judgments are rendered, we may not have the ability to pay them. Such disruptions, legal fees and any losses resulting from these claims could have a material adverse effect on our business, results of operations, financial condition and cash flows.

Natural disasters and adverse weather conditions that can damage property and disrupt business operations could have an adverse impact on our business operations and our financial results.
Natural disasters, such as hurricanes, earthquakes, tornadoes, floods and severe winter storms place our employees in harm's way and make it challenging to deliver mail under these unpredictable and dangerous conditions. Damage to our facilities could also have a negative impact on business operations. Significant additional operating costs may be incurred in order to maintain continuity in fulfilling our mission.

ITEM 1B. UNRESOLVED STAFF COMMENTS

None.

ITEM 2. PROPERTIES

We own nearly 8,500 and lease over 23,000 Postal Service facilities ranging in size from 60 square feet to 32 acres. Facilities support retail, delivery, mail processing, maintenance, administrative and support activities and are located in numerous communities throughout the U.S. and its territories. We believe our properties are generally in good physical condition and require only routine repairs and maintenance and periodic capital improvements. In addition, we monitor the productive capacity of our properties which has culminated in the consolidation of some of our facilities.

ITEM 3. LEGAL PROCEEDINGS

As previously reported, on January 14, 2010, the Equal Employment Opportunity Commission's Office of Federal Operations certified the case *McConnell v. Brennan* (first instituted in 2006 as *McConnell v. Potter*) as a class action against the Postal Service, with the class consisting of all permanent-rehabilitation and limited-duty Postal Service employees who were assessed under the Postal Service's National Reassessment Process ("NRP") between the dates of May 5, 2006, and July 1, 2011. The NRP was a program that we utilized to ensure that our records regarding employees injured on the job were correct and that employees receiving workers' compensation benefits were placed in jobs consistent with their abilities.

The case alleges violations of the *Rehabilitation Act of 1973* resulting from the NRP's failure to provide a reasonable accommodation, the NRP's wrongful disclosure of medical information, the creation by the NRP of a hostile work environment and the NRP's adverse impact on disabled employees. The class is seeking injunctive relief and damages of an uncertain amount. If the plaintiffs were able to prove their allegations in this matter and to establish the damages they assert, an adverse ruling could have a material impact on us. We continue to dispute the claims asserted in the case and are vigorously contesting the matter.

We are subject to other legal proceedings and claims that arise in the ordinary course of our business. For further discussion of the legal proceedings affecting us, see *Item 8. Financial Statements and Supplementary Data*, *Notes to Financial Statements*, *Note 8 - Commitments and Contingencies*.

ITEM 4. MINE SAFETY DISCLOSURES

Not applicable.

PART II

ITEM 5. MARKET FOR REGISTRANT'S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES

As an "independent establishment of the Executive Branch of the Government of the United States," we do not issue equity or other securities.

ITEM 6. SELECTED FINANCIAL DATA

The selected financial data presented below for each year ended September 30 is derived from our audited financial statements. The selected financial data should be read in conjunction with *Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations* and the related notes to the financial statements in *Item 8. Financial Statements and Supplementary Data*, *Notes to Financial Statements*:

(in millions)	2016	2015	2014	2013	2012
Operating Results					
Total revenue	**$ 71,498**	**$ 68,928**	**$ 67,830**	**$ 67,318**	**$ 65,223**
Operating expenses:					
Compensation and benefits	48,689	47,519	46,000	46,708	47,689
Retiree health benefits*	9,105	8,811	8,685	8,450	13,729
Workers' compensation	2,682	1,760	2,554	1,061	3,729
Transportation	6,992	6,579	6,586	6,735	6,630
All other operating expenses	9,431	9,157	9,353	9,174	9,187
Total operating expenses	**$ 76,899**	**$ 73,826**	**$ 73,178**	**$ 72,128**	**$ 80,964**
Loss from operations	**$ (5,401)**	**$ (4,898)**	**$ (5,348)**	**$ (4,810)**	**$(15,741)**
Net loss	**$ (5,591)**	**$ (5,060)**	**$ (5,508)**	**$ (4,977)**	**$(15,906)**
Financial Position					
Assets:					
Cash and cash equivalents	$ 8,077	$ 6,634	$ 4,906	$ 2,326	$ 2,087
Property and equipment, net	15,296	15,686	16,338	17,512	18,863
All other assets	1,846	1,694	1,718	1,803	1,661
Total Assets	**$ 25,219**	**$ 24,014**	**$ 22,962**	**$ 21,641**	**$ 22,611**
Liabilities:					
Accrued retiree health benefits	$ 33,900	$ 28,100	$ 22,417	$ 16,766	$ 11,205
Workers' compensation liability	20,039	18,811	18,422	17,240	17,567
Debt	15,000	15,000	15,000	15,000	15,000
All other liabilities	12,262	12,494	12,454	12,458	13,685
Total Liabilities	**$ 81,201**	**$ 74,405**	**$ 68,293**	**$ 61,464**	**$ 57,457**
Total Net Deficiency	**$(55,982)**	**$(50,391)**	**$(45,331)**	**$(39,823)**	**$(34,846)**

*PSRHBF expenses in 2012 totaled $11.1 billion which included $5.5 billion for a postponed 2011 amount and $5.6 billion for the scheduled 2012 amount.

ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

CAUTIONARY STATEMENTS

The following *Management's Discussion and Analysis of Financial Condition and Results of Operations* and other parts of this report describe the principal factors affecting our financial results, liquidity, capital resources and critical accounting estimates. Our results of operations may be impacted by risks and uncertainties, many of which we cannot control or influence, and may cause actual results to differ materially from those currently contemplated.

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 forward-looking statements, which involve a number of risks and uncertainties, reflect current expectations regarding future events and operating performance as of the date of this report.

We have no obligation to publicly update or revise any forward-looking statements, whether as a result of new information, future events or otherwise. Important factors that could cause actual results to differ materially from those anticipated in our forward-looking statements include, but are not limited to, those described under *Item 1A. Risk Factors*.

OVERVIEW

With our mandate to provide universal postal services to the nation, we serve retail and commercial customers in the U.S. as well as internationally. Our operations include an extensive and integrated retail, distribution, transportation and delivery network, and we operate as a single segment throughout the U.S., its possessions and territories.

We have successfully implemented initiatives that have reduced our costs by billions of dollars while offering broader services. However, legal restrictions on pricing, service diversification and operations restrict our ability to fully implement our strategic objectives and cover our costs to provide secure, reliable and affordable postal services to the nation. We have established a core set of goals that drive our strategic initiatives and continuous improvement efforts:

1. Deliver a world-class customer experience,
2. Equip, empower and engage employees,
3. Innovate faster to deliver value, and
4. Invest in our future platforms.

As part of these efforts, we aim to achieve long-term financial stability, as well as a reduction in our debt. Our focus on maintaining liquidity and reducing operating expenses reflects current trends, as well as projected future volume of mail and packages. We believe that consistent revenue growth is within reach as we continue to identify and create innovative and affordable services, and deliver high levels of performance and capabilities.

RESULTS OF OPERATIONS

SUMMARY

The major factors that impact our operating results include overall customer demand, the mix of postal services and contribution associated with those services, volume of mail and packages processed through our network and our ability to manage our cost structure in line with declining levels of mail volume, growth in more labor-intensive Shipping and Packages volume and an increasing number of delivery points. We operate as a single segment and report our performance as such.

2016 Compared with 2015

Our reported operating revenue was $71.4 billion in 2016, an increase of $2.6 billion, or 3.8%, from the prior year. Excluding the effect of a nearly $1.1 billion non-cash adjustment for deferred revenue, discussed below in *Change in Accounting Estimate*, operating revenue was nearly $70.4 billion for 2016, an increase of $1.6 billion, or 2.3%, from the prior year.

As more fully described below in *Operating Revenue and Volume*, this increase in our operating revenue was driven by an increase in our Shipping and Packages revenue of $2.4 billion, or 15.8%, although this was partially offset by a decline in *First-Class Mail* of $925 million, and the April 10, 2016, expiration of the exigent surcharge, which reduced 2016 operating revenue by approximately $1 billion from what it otherwise would have been. The expiration of the surcharge most significantly impacted revenue associated with *First-Class Mail* and *Standard Mail*, impacting certain other Market-Dominant services to a lesser extent.

As more fully described below in *Operating Expenses*, 2016 operating expenses increased $3.1 billion, or 4.2%, compared to the prior year. The increase in operating expenses was due to increased compensation and benefits expense of $1.2 billion, resulting primarily from an increase in labor hours used to support higher package volumes, and an increase in workers' compensation expense of $922 million as discount rates declined in 2016 compared to the prior year. Additionally, transportation costs grew by $413 million, driven by an increase in both air and highway transportation in support of the Shipping and Packages volume growth and our strategic efforts to continue to improve our delivery service.

This resulted in a net loss of $5.6 billion for the year ended September 30, 2016, compared to a net loss of $5.1 billion for 2015, an increase in net loss of $531 million, or 10.5%. Although Shipping and Packages drove the growth in operating revenue, these gains were outpaced by increases in operating expenses, driven by compensation and benefits, and to a lesser extent, workers' compensation expenses largely outside of management's control.

2015 Compared with 2014

As more fully described below in *Operating Revenue and Volume*, operating revenue was $68.8 billion in 2015, an increase of $1.0 billion from the prior year. Revenue in 2015 benefited by an estimated $2.1 billion from a full year of the exigent surcharge that went into effect in January 2014, and to a lesser extent, price increases implemented in May 2015. Also contributing to the increase, Shipping and Packages revenue was $14.9 billion, an increase of $1.4 billion, or 10.3%, compared to 2014, driven by a 13.6% increase in volume.

As more fully described below in *Operating Expenses*, 2015 operating expenses increased $648 million, or 0.9%, compared to the prior year. The net $794 million reduction in our workers' compensation expense, mainly the result of changes in assumptions and actuarial valuation and revaluation of new and existing workers' compensation cases, was more than offset by an increase for the year in compensation and benefits expense of $1.5 billion, attributable to contractually-obligated salary escalations, higher FERS contribution rates mandated by OPM and an increase in labor hours, primarily resulting from higher Shipping and Packages volume.

This resulted in a net loss of $5.1 billion for the year ended September 30, 2015, compared to a net loss of $5.5 billion for 2014, a decrease in net loss of $448 million. While both operating revenue and total operating expenses increased in 2015, the reduction in net loss was largely driven by a decrease in workers' compensation expense of $794 million resulting from changes in assumptions and actuarial valuation and revaluation of new and existing workers' compensation cases.

Change in Accounting Estimate

We recognize revenue for postage at the time a piece of mail is processed and delivered, not when we receive cash for the sale of postage. We estimate the amount of postage that we have sold, but customers have not yet used, and include this amount as a liability in our Balance Sheets as *Deferred revenue-prepaid postage*. The majority of this liability consists of our estimate of sold, but unused, *Forever Stamps*, the non-denominated postage stamps we introduced in 2007. Since their introduction through September 30, 2016, we sold approximately $48 billion in *Forever Stamps* to the public.

We have developed and validated the usage portion of our deferred revenue estimate through complex mathematical and statistical methods of postage stamp usage trends. Small differences in inputs can lead to significant differences in our estimate of the liability. "Breakage" represents the portion of sold *Forever Stamps* that we estimate will never be used by customers due to loss, damage or stamp collection. Assumptions regarding estimated usage and breakage of a particular postage stamp issue cannot be refined until each "series" of postage stamps nears the end of its life cycle.

During 2016, we revised the estimation technique utilized to estimate our *Deferred revenue-prepaid postage* liability for *Forever Stamps*. The change resulted from new information regarding customer's retention and usage habits of applicable postage, and enabled the Postal Service to update its estimate of stamps that will never be used for mailing. As a result of this change, *Deferred revenue-prepaid postage* was decreased by nearly $1.1 billion. In accordance with accounting principles generally accepted in the U.S. ("GAAP"), the change was accounted for as a change in accounting estimate, and was reflected in operating results as an increase to revenue and a decrease in net loss by the same amount in the year ended September 30, 2016. This adjustment had no impact on our current liquidity nor did it lessen the severity of our liquidity outlook.

Non-GAAP Controllable Income

In the day-to-day operation of our business, we focus on costs within our control, such as work hours and transportation. We calculate controllable income, a non-GAAP measure, by excluding items we cannot control, such as PSRHBF prefunding expenses, workers' compensation expenses caused by actuarial revaluation and discount rate changes, retirement expenses caused by actuarial revaluation, and adjustments for non-recurring items, such as the change in accounting estimate for *Deferred revenue-prepaid postage*. Controllable income should not be considered a substitute for net income and other GAAP reporting measures. The following table reconciles our GAAP net loss to controllable income for the years ended September 30, 2016, 2015 and 2014:

(in millions)	2016	2015	2014
Net loss	**$ (5,591)**	**$ (5,060)**	**$ (5,508)**
PSRHBF prefunding expense	5,800	5,700	5,700
Change in workers' compensation liability due to fluctuations in discount rates	1,026	809	485
Other change in workers' compensation liability[1]	188	(502)	673
Actuarial revaluation of retirement liability[2]	248	241	7
Change in accounting estimate	(1,061)	—	—
Controllable income	**$ 610**	**$ 1,188**	**$ 1,357**

1 This is a net amount that includes changes in assumptions, as well as the valuation of new claims and revaluation of existing claims, less current year claim payments.

2 Determined by OPM in 2015 to amortize the $3.6 billion unfunded FERS retirement obligation based on actuarial valuations and assumptions. Payments are to be made in equal installments through 2046.

OPERATING REVENUE AND VOLUME

First-Class Mail and *Standard Mail* continued to provide the majority of our operating revenue despite customers' continuing migration to electronic communication and transactional alternatives. As a percentage of operating revenue, *First-Class Mail* and *Standard Mail* combined represented 63.4%, 67.2% and 67.6% (before the change in accounting estimate) for the years ended September 30, 2016, 2015 and 2014, respectively. *First-Class Mail* and *Standard Mail* combined volume represented 92.1%, 92.4% and 92.7% in 2016, 2015 and 2014, respectively. We anticipate that *First-Class Mail* volume will continue to decline in future years with the migration to electronic alternatives resulting from technological changes.

While we continue to experience strong results in our Shipping and Packages business, it represented only 24% of our revenues for the year ended September 30, 2016, compared to *First-Class Mail*, which represented 38%. Furthermore, Shipping and Packages generated only 3% of our volume for the year ended September 30, 2016, and we need to generate approximately $2.50 in Shipping and Packages revenue to replace the contribution from each $1 of lost *First-Class Mail* revenue, as the costs to process and deliver Shipping and Packages services were, and continue to be, substantially higher than the costs associated with *First-Class Mail*.

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 proactively targeted opportunities to grow our business. We continue to concentrate on our customers' needs and have increased our marketing investment and focus on mail and package innovation. However, revenue growth is constrained by laws and regulations restricting the types of products, services and pricing we may offer to our customers and the speed with which we can bring them to market.

To address the long-term trend that technological change and the lingering effects of the Great Recession have had on our *First-Class Mail* revenue and volume, we have focused on providing new services to the extent we are allowed, growing e-commerce and implementing marketing campaigns that have helped us grow our Shipping and Packages business. By offering day-specific delivery, improved tracking and text alerts and up to $50 of free insurance on most *Priority Mail* packages, we have demonstrated our responsiveness to our customers.

As described below, we implemented price increases on various Market-Dominant and Competitive services in January 2014, May 2015, January 2016 and August 2016. We have filed with the PRC notices of our intent to increase prices for certain Market-Dominant and Competitive services by an average of 0.9% and 3.9%, respectively. If approved, these price increases would go into effect in January 2017.

As referenced throughout this report, the PRC authorized us to collect an exigent surcharge on most Market-Dominant services beginning in January 2014 until it produced incremental revenue of just over $4.6 billion, a figure the PRC determined was lost due to the Great Recession's suppression of mail volume. The limit on the amount of the exigent surcharge collected was reached on April 10, 2016, and we therefore reduced the prices of applicable Market-Dominant services on that date. As a result of the expiration of the surcharge, we estimate that our revenue and cash flow was lower than what they otherwise would have been by approximately $1 billion for 2016, and will continue to be lower by almost $2 billion per year going forward, unless the PRC's decision to limit our recovery in the manner described above is modified again or reversed through the pending appeal.

The following table details our operating revenue and volume for the years ended September 30, 2016, 2015 and 2014 by service category:

(in millions)	2016	2015	2014
Operating Revenue:			
First-Class Mail[1]	$ 27,281	$ 28,206	$ 28,409
Standard Mail[2]	17,982	17,992	17,426
Shipping and Packages[3]	17,307	14,942	13,543
International	2,695	2,702	2,923
Periodicals	1,507	1,589	1,625
Other[4]	3,596	3,359	3,838
Total operating revenue before change in accounting estimate	**$ 70,368**	**$ 68,790**	**$ 67,764**
Change in accounting estimate	1,061	—	—
Total operating revenue	**$ 71,429**	**$ 68,790**	**$ 67,764**
Volume:			
First-Class Mail[1]	60,922	62,353	63,839
Standard Mail[2]	80,885	80,030	80,308
Shipping and Packages[3]	5,134	4,510	3,969
International	1,006	913	893
Periodicals	5,544	5,838	6,045
Other[5]	450	391	485
Total volume	**153,941**	**154,035**	**155,539**

Note: The totals for certain mail categories for prior years have been reclassified to conform to classifications used in the current year. Non-operating revenue is no longer included in this schedule.

[1] Excludes *First-Class Mail Parcels*.

[2] Excludes *Standard Mail Parcels*.

[3] Includes *Priority Mail*, *Priority Mail Express, USPS Retail Ground*, *Parcel Select*, *Parcel Return Service*, *Standard Parcels*, Package Services, *First-Class Mail Parcels* and *First-Class Package Service.* Excludes International packages.

[4] Includes *PO Box* services, *Certified Mail*, Return Receipts, Insurance, Other Ancillary Services, Shipping and Mailing Supplies, Collect on Delivery, Registered Mail, sales of envelopes and cards, money orders and Other services.

[5] Volume includes U.S. Postal Service internal mail and free mail provided to certain groups.

First-Class Mail

First-Class Mail, presented in this report as a mail class and a service category, includes cards, letters and flats, and is priced the same regardless of the distance the mail travels. The volume of *First-Class Mail*, our most profitable service category, continues to decline, although at a slower pace than in previous years, with decreases of 2.3% in 2016 and 2.3% in 2015, due to the continuing migration toward electronic communication and electronic transaction alternatives.

For the year ended September 30, 2016, *First-Class Mail* revenue fell by $925 million, or 3.3%, on a volume decline of 2.3%, compared to the prior year. The decline in revenue was greater than the decline in volume for the year due to the April 10, 2016, expiration of the exigent surcharge. We estimate that approximately $550 million of the decline in *First-Class Mail* revenue during 2016 was attributable to the surcharge expiration.

For the year ended September 30, 2015, *First-Class Mail* revenue decreased by $203 million, or 0.7%, on a volume decline of 2.3%, compared to the prior year. The increase in our 2015 revenue compared to a reduction in volume was primarily due to the exigent surcharge that we implemented in January 2014, as the incremental revenue from the surcharge was an estimated $1.2 billion and $793 million for the years ended September 30, 2015, and 2014, respectively.

Standard Mail

Standard Mail, presented as a mail class and a service category, is mail not required to be mailed as *First-Class Mail* or *Periodicals*, and may include advertising, newsletters, catalogs, small marketing parcels and other printed matter. *Standard Mail* volume is reflective of the cyclical nature of the U.S. economy and competition from other forms of advertising. Price increases for *Standard Mail* are generally capped at the rate of inflation because they are classified by law as Market-Dominant. As previously mentioned, we have filed a request with the PRC to change the name of this service category and class of mail from *Standard Mail* to *USPS Marketing Mail* effective in January 2017. This name change will aid our customers in understanding what *Standard Mail* is and how it can be used as part of their respective marketing strategies.

Standard Mail generated approximately 53% of the total volume, but represented approximately 25% of operating revenue for each of the three years ended September 30, 2016, 2015 and 2014. *Standard Mail* had experienced relatively stagnant volume and a declining share of the advertising market due to the continued migration toward electronic communication. Nonetheless, the utilization of *Standard Mail* by our commercial customers has proven to be a relatively resilient marketing channel, and its value to U.S. businesses is increasing due to better data and technology integration.

For the year ended September 30, 2016, *Standard Mail* revenue decreased slightly during 2016. We estimate that the incremental revenue decline in *Standard Mail* due to the expiration of the exigent surcharge was approximately $335 million during 2016.

For the year ended September 30, 2015, *Standard Mail* revenue increased by $566 million, or 3.2%, despite volume decrease of 0.3%, compared to the prior year. The incremental revenue for *Standard Mail* generated from the exigent price increase was an estimated $731 million and $482 million for the years ended September 30, 2015, and 2014, respectively.

Shipping and Packages

Our Shipping and Packages category consists largely of Competitive services that can be priced to reflect current market conditions. These include *Priority Mail* and *Priority Mail Express,* as well as business-oriented services such as *Parcel Select* and *Parcel Return*. *First-Class Parcels* and certain other package delivery classes are also part of Shipping and Packages, but are considered Market-Dominant services and are therefore subject to price caps.

As a percentage of operating revenue, Shipping and Packages generated 24.2%, 21.7% and 20.0% for the years ended 2016, 2015 and 2014, respectively. As a percentage of total volume, Shipping and Packages represented 3.3%, 2.9% and 2.6% for the years ended 2016, 2015 and 2014, respectively. Prices for these Competitive services increased an average of 9.5% in January 2016, 3.5% in May 2015 and 2.4% in January 2014.

For the year ended September 30, 2016, Shipping and Packages revenue grew by 15.8% on volume growth of 13.8%, compared to the prior year. For the year ended September 30, 2015, Shipping and Packages revenue grew by 10.3% on volume growth of 13.6%, compared to the prior year.

Our Shipping and Packages revenue continues to show strong year-over-year growth as a result of our successful efforts to compete in the shipping services and the "last-mile" e-commerce fulfillment markets, including through Sunday deliveries. Volume has also experienced end-to-end growth as we have responded to customers' increased use of online shopping, which provided a surge in package volume with a record number of packages delivered during the calendar year 2015 holiday season. To accommodate the surge in volume and to minimize service disruptions during the holiday season, we have increased Sunday delivery service and added non-career employees for the holiday season in accordance with our labor agreements.

The following table details our operating revenue and volume for Shipping and Packages for the years ended September 30, 2016, 2015 and 2014 by each service:

(in millions)	2016	2015	2014
Shipping and Packages Revenue:			
Priority Mail Services[1]	$ 8,943	$ 8,380	$ 7,993
Parcel Services[2]	4,833	3,519	2,736
First-Class Packages[3]	2,739	2,262	2,002
Package Services	792	781	812
Total Shipping and Packages revenue	**$ 17,307**	**$ 14,942**	**$ 13,543**
Shipping and Packages Volume:			
Priority Mail Services[1]	1,055	1,030	970
Parcel Services[2]	2,478	1,997	1,605
First-Class Packages[3]	1,011	919	847
Package Services	590	564	547
Total Shipping and Packages volume	**5,134**	**4,510**	**3,969**

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 Shipping and Packages revenue for the prior years.

[1] Includes *Priority Mail*, a 1-3 business day delivery service; *Priority Mail Express*, an overnight delivery service available 365 days per year; and *USPS Retail Ground,* a retail-only Market-Dominant service priced identically and functionally equivalent to *Priority Mail* for Zones 1-4.

[2] Includes *Parcel Select*, *Parcel Return* and *Standard Parcels*.

[3] Includes *First-Class Mail Parcels* and *First-Class Package Services*.

Priority Mail Services

Priority Mail Services includes *Priority Mail*, *Priority Mail Express* and *Retail Ground*, and allows customers the ability to send documents and packages requiring expedited transportation and handling. As our flagship Shipping and Packages subcategory for retail and commercial customers, Priority Mail Services accounted for 51.7%, 56.1% and 59.0% of Shipping and Packages revenue for the years ended 2016, 2015 and 2014, respectively. While Priority Mail Services continues to grow year-over-year, it is somewhat price sensitive, particularly with retail customers, and its growth rate is lower than some other Shipping and Packages subcategories used by commercial customers.

For the year ended September 30, 2016, Priority Mail Services revenue grew by 6.7% on volume growth of 2.4%, compared to the prior year. The January 2016 price increase in Competitive services contributed to higher growth in revenue versus volume for the year ended September 30, 2016.

For the year ended September 30, 2015, Priority Mail Service revenue grew by 4.8% on volume growth of 6.2%, compared to the prior year. The increase in year-over-year growth of Priority Mail Services revenue and volume is the result of growth in e-commerce and the success of our sales and marketing initiatives.

Parcel Services

The Parcel Services subcategory includes *Parcel Select*, *Parcel Return* and *Standard Parcels*, which are Competitive services largely consisting of "last-mile" deliveries. Parcel Services accounting for 27.9%, 23.6% and 20.2% of Shipping and Packages revenue for the years ended 2016, 2015 and 2014, respectively. Parcel Services showed strong revenue growth of 37.3% and 28.6% and volume growth of 24.1% and 24.4% for the years ended September 30, 2016, and 2015, respectively.

The increase in year-over-year growth for Parcel Services revenue and volume were driven largely by the continuing growth of e-commerce, which largely affects our *Parcel Select* service, and our competitive pricing on these services. This high-growth subcategory has rapidly become a significant contributor to our overall Shipping and Packages growth. However, *Parcel Services* includes some of our lowest-priced services that have historically provided a relatively lower contribution margin compared to others.

First-Class Packages

The First-Class Packages subcategory includes the competitively priced *First-Class Packages Service*, an under one-pound Competitive service targeted to commercial customers, and *First-Class Parcels*, a Market-Dominant, under 13-ounce retail package service. First-Class Packages offers commercial customers that ship primarily lightweight fulfillment parcels the lowest priced expedited end-to-end shipping option in the marketplace. First-Class Packages revenue and volume performance continues to experience strong increases for the past three years, primarily attributable to growth in e-commerce.

For the year ended September 30, 2016, First-Class Packages revenue increased 21.1% on volume growth of 10.0%, compared to the prior year. The higher growth in revenue was due in large part to the January 2016 price increase in Competitive services. For the year ended September 30, 2015, First-Class Packages revenue grew by 13.0% on volume growth of 8.5%, compared to the prior year.

Package Services

Customers use our Package Services subcategory for shipping merchandise or bound printed matter, including library and media mail, weighing up to 70 pounds. For the year ended September 30, 2016, Package Services revenue increased by 1.4%, on volume growth of 4.6%, compared to the prior year. For the year ended September 30, 2015, Package Services revenue decreased by 3.8% on volume growth of 3.1%, compared to the prior year. This category has been affected by certain large mailers' increased use of drop shipments offset by a lower price per piece on bound printed matter.

International Mail

Our International Mail category includes several services that enable customers, both domestic and abroad, to send international mail and packages, including postcards, envelopes, flats and packages, with either standard or express delivery options. Our revenue from International Mail, the majority of which is generated from "outbound services" that allow customers in the U.S. to send mail and packages to other countries, was 3.8%, 3.9% and 4.3% of total operating revenue for 2016, 2015 and 2014, respectively. For the past several years, we have experienced an increase in lower-priced inbound mail volume, much of that from tracked letter packets and parcels related to international e-commerce.

For the year ended September 30, 2016, International Mail revenue decreased by 0.3% on volume growth of 10.2%, compared to the prior year. The January 2016 price increases positively affected revenue from *First-Class International Package Service* and other international Competitive services, which almost offset the revenue lost from declines in higher-priced outbound volume. For the year ended September 30, 2015, International Mail revenue decreased by 7.6% while volume increased by 2.2%, compared to the prior year, as the ongoing increase in lower-priced inbound mail volume was not enough to offset the revenue lost from declines in higher-priced outbound volume.

Periodicals

Periodicals, also presented as a mail class and a service category, is designed for newspapers, magazines and other periodical publications whose primary purpose is transmitting information to an established list of subscribers or requesters. For the year ended September 30, 2016, *Periodicals* revenue decreased by 5.2% and volume decreased by 5.0%, compared to the prior year. For the year ended September 30, 2015, *Periodicals* revenue decreased by 2.2% and volume decreased by 3.4%, compared to the prior year.

Periodicals provides our lowest percentage of total operating revenue and has continued to decline over the past three years given recent trends in hard-copy reading behavior and advertising shifts from print to other media. We do not expect *Periodicals* to rebound as e-readers and electronic content continue to grow in popularity with the public.

Other

Other services include ancillary services such as *Certified Mail*, *PO Box* services and *Return Receipt* services. Also included in this category are money orders and passport services. For the year ended September 30, 2016, Other services revenue increased by 7.1% on volume growth of 15.1%, compared to the prior year. For the year ended September 30, 2015, Other services revenue decreased by 12.5% and volume decreased by 19.4%, compared to the prior year. In each of these years, decreases were due to an increase in volume of services that produce no revenue for us, including "signature on delivery" services, insurance, and our own mail that we send internally.

OPERATING EXPENSES

In an effort to align our resources with anticipated types of services and mail volume, we continue to aggressively manage operating expenditures under management's control.

As described above in *Operating Revenue and Volume*, we anticipate that migration of hard copy mail will continue to reduce *First-Class Mail* volume and revenue for the foreseeable future. Although increased Shipping and Packages volume has offset some of these declines, we must earn approximately $2.50 in Shipping and Packages revenue to replace the contribution lost from each $1 of *First-Class Mail* revenue because the costs of transporting and delivering packages are significantly higher than letters.

Our challenge to contain costs is compounded by the continuing increase in the number of delivery points, which, when combined with the impact of lower hard copy mail volume, has resulted in a drop in the average number of pieces delivered per delivery point per day from approximately 5.5 pieces in 2007 to 3.7 pieces in 2016, a reduction of approximately 32%.

Furthermore, our mail processing and distribution network was originally designed to provide overnight delivery service of *First-Class Mail* within specified delivery areas for a much higher volume of mail than what we process and deliver today, and therefore the network's legacy capabilities are excessive relative to today's mail volume. Consequently, many of our processing and distribution facilities continue to operate at much less than full capacity.

Compensation and Benefits

Our compensation and benefits expenses, our largest operating expense category, represented approximately 63%, 64% and 63% of our total operating expenses for the years ended September 30, 2016, 2015 and 2014, and consist of costs related to our active career and non-career employees. The following table provides the components of compensation and benefits expense for active employees as of September 30, 2016, 2015 and 2014:

(in millions)	**2016**	**2015**	**2014**
Compensation	$ 36,634	$ 35,931	$ 35,113
Retirement	6,757	6,480	5,758
Employee health benefits	4,972	4,774	4,804
Other	326	334	325
Total compensation and benefits expense	**$ 48,689**	**$ 47,519**	**$ 46,000**

Compensation

During the year ended September 30, 2016, compensation expense increased $703 million, or 2.0%, compared to 2015. During the year ended September 30, 2015, compensation expense increased $818 million, or 2.3%, compared to 2014. These increases were attributable to contractually-obligated salary escalations and additional work hours associated in large part with growth in the more labor-intensive Shipping and Packages business, partially offset by newly converted career employees and non-career employees earning lower wages.

During the year ended September 30, 2016, total work hours increased by approximately 30 million, or 2.6%, compared to the prior year. During the year ended September 30, 2015, total work hours increased by approximately 21 million, or 1.9%, compared to the prior year. These increases in work hours were in large part associated with growth in the more labor-intensive Shipping and Packages business along with growth in the number of delivery points.

During 2016 and 2015, we converted approximately 44,000 and 35,000 employees, respectively, from non-career to career status, as dictated by our operational needs and contractual provisions. These conversions were necessary to offset attrition of career employees, primarily through retirement. Although career employees are more costly than non-career, these converted employees represent a significant savings relative to the career employees they replace.

Workforce Composition

The composition of our workforce is a significant factor of our compensation expense. As of September 30, 2016, our workforce consisted of approximately 640,000 career and non-career employees, an increase of 18,000, or 2.9%, compared to the prior year. This increase is the result of an increase in career employees needed to support the continuing growth in our Shipping and Packages business and the continuing growth in the delivery network.

The number of total employees increased slightly from 2014 to 2015. Beginning in 2013, our labor contracts permitted us to use more non-career employees, allowing us to replace career work hours with non-career work hours at reduced rates.

The following table provides the totals of career and non-career employees as of September 30, 2016, 2015 and 2014:

	2016	2015	2014
Career employees	509,000	492,000	488,000
Non-career employees	131,000	130,000	130,000
Total employees	**640,000**	**622,000**	**618,000**

Work Hours

Work hours are an important component of compensation expense. Total work hours increased by approximately 30 million, or 2.6%, between 2016 and 2015, and increased by approximately 21 million, or 1.9%, between 2015 and 2014. These increases were in part due to the increase in work hours for city delivery and customer service operations related to the growth of our more labor-intensive Shipping and Packages business. Also influencing work hours is the growth in the number of delivery points and the variations in products and services sold. The number of delivery points increased by approximately 1.1 million in 2016 and 1.1 million in 2015.

Collective Bargaining Agreements and Non-bargaining Salaries

As indicated previously in this report, as of September 30, 2016, approximately 91% of our career employees are covered by collective bargaining agreements. The contracts with the four labor unions representing the majority of our employees include provisions granting annual increases and COLAs, which are linked to the CPI-W.

On May 23, 2011, a contract with the APWU became effective and it extended through May 20, 2015. The contract included a wage freeze for the first two years, with general wage increases over the life of the contract, totaling 3.5%. The agreement also established a new career pay schedule that on average was 10.2% lower than the previous pay schedule.

On July 3, 2012, a final award was rendered in the arbitration case between the NRLCA and us, resulting in a new NRLCA contract that extended through May 20, 2015. The contract included a two-year wage freeze followed by modest increases and a lower wage scale for both new career and non-career employees. The contract also included a reduction in health benefits employer contribution rate.

On January 10, 2013, a final award was rendered in the arbitration case between the Postal Service and the NALC, resulting in a new NALC contract. The contract with the NALC became effective on November 21, 2011, and it extended through May 20, 2016. The NALC contract had no retroactive payments, included general wage increases in 2014 through 2016, stipulated that the 2013 COLA be deferred until 2014 and reduced the employer contribution to the funding of health benefits.

On February 15, 2013, a final award was rendered in the arbitration case between the NPMHU and us, resulting in a new NPMHU contract. The contract became effective on November 21, 2011, and it extended through May 20, 2016. The NPMHU contract had no retroactive payments, included general wage increases in 2014 through 2016, stipulated that the 2013 COLA be deferred until 2014 and reduced the employer contribution of the funding of health benefits.

In 2014, employees represented by the APWU and NRLCA received a 1.5% general wage increase and 2014 COLAs. Employees represented by the NALC and NPMHU received a 1.0% general wage increase, 2014 COLAs and COLAs deferred from 2013. Employees represented by the NALC and NPMHU received neither a COLA or general wage increase in 2013, although the 2013 COLA was earned and deferred until 2014.

In 2015, employees represented by the APWU and NRLCA received a 1.0% general wage increase, and employees represented by the NALC and NPMHU received a 1.5% general wage increase. Employees represented by the APWU, NALC, NRLCA and NPMHU did not receive COLAs in 2015.

In April 2016, we reached a new three-year collective bargaining agreement with the NRLCA which was ratified by the NRLCA membership. The new contract includes general wage increases totaling 3.8% (1.2% of which was retroactive to November 2015) with a COLA base month of July 2014 (no retroactive COLA payments), a reduction in the employer share of health insurance premiums, beginning in the 2017 plan year, and the creation of a new non-career employee category to provide weekend and holiday parcel deliveries. The contract will expire on May 20, 2018.

In July 2016, an interest arbitration decision was issued that resulted in an award which established a collective bargaining agreement between the APWU and us. The award, which will expire on September 20, 2018, was the result of a legally-mandated binding arbitration process that was required when the parties reached impasse in negotiating a new collective bargaining agreement after the prior agreement expired in May 2015. The contract includes general wage increases totaling 3.8% (1.2% of which was retroactive to November 2015) with a COLA base month of July 2014 (no retroactive COLA payments), a reduction in the employer share of health insurance premiums, beginning in the 2017 plan year, and annual increases in uniform and work clothes allowances. The award also converted approximately 5,000 non-career positions to career positions.

In May 2016, we agreed to extend contract negotiations on new collective bargaining agreements with both the NALC and the NPMHU. Our contracts with NALC and NPMHU each expired on May 20, 2016, and the respective parties mutually agreed to extend negotiations beyond the deadline, and these negotiations were continuing as of September 30, 2016.

Annual salary increases for non-bargaining unit employees only occur through a Pay-For-Performance ("PFP") system. With only minor exceptions, no COLA or locality pay programs apply to non-bargaining unit employees. PFP salary increases averaged 1.0% for 2013 (implemented in January 2014), 2.1% for 2014 (implemented in January 2015), and 1.6% for 2015 (implemented in January 2016).

Separation Incentives

We have periodically offered targeted separation incentives to employees who agreed to retire or resign within a specified time period. These separation incentives encourage attrition and help us to reduce our career complement to better match workload and reduce costs. These incentives have been targeted to postmasters, clerks, mail handlers and administrative employees, and are utilized only when work has been eliminated. No separation incentives were offered during the years ended September 30, 2016, and 2015. During the year ended September 30, 2014, separation incentives of $10,000 each were accepted by 1,380 postmasters and we recorded a charge of approximately $15 million.

Retirement Expense

The majority of our employees participate in either CSRS or FERS based on the starting date of employment with us or another U.S. government employer. Employees may also participate in the Thrift Savings Plan ("TSP"), a defined contribution savings and investment plan administered by the Federal Retirement Thrift Investment Board. For additional information, see *Item 8. Financial Statements and Supplementary Data*, *Notes to Financial Statements*, *Note 9 - Retirement Plans*.

We record our contributions to the plans as an expense in the period during which the contribution is due. The expense is reported within *Compensation and benefits* under *Operating expenses* in the accompanying Statements of Operations. We recognize expense for the legally required contribution for each period and record a liability for any contributions due and unpaid at the end of each reporting period. The table below details the components of total retirement expense for the years ended September 30, 2016, 2015 and 2014:

(in millions)	2016	2015	2014
FERS	$ 3,684	$ 3,499	$ 2,888
Social security	2,009	1,956	1,881
TSP	1,064	1,025	989
Total retirement expense	**$ 6,757**	**$ 6,480**	**$ 5,758**

Retirement expense increased 4.3% in 2016 primarily due to the increase in our employer contribution rate from 13.2% to 13.7% of basic pay for most employees who participated in FERS during the year. This rate increase became effective October 1, 2015, and increased our annual retirement expense by approximately $140 million for the year ended September 30, 2016. OPM announced that FERS employer contributions as a percentage of employee basic pay will continue to be 13.7% in 2017.

Retirement expense increased 12.5% in 2015 primarily due to the increase in our employer contribution rate from 11.9% to 13.2% of basic pay for most employees who participated in FERS during 2015. This rate increase became effective October 1, 2014, and increased our annual retirement expense by approximately $500 million for the year ended September 30, 2015.

Also contributing to the increase in our FERS expense for 2015 was an increase in the supplemental expense related to the actuarial revaluation of our FERS liability. In September 30, 2015, OPM notified us that our FERS account for our retirees was underfunded by $3.6 billion as of September 30, 2014. To fund this, OPM directed us to make additional payments to FERS of $241 million per year for 30 years beginning in 2015, and revised the amount to $248 million per year beginning in 2016. This revaluation caused our supplemental expense to increase by $7 million in 2016 and $234 million in 2015, compared to their respective prior years. Pending our review of OPM's underlying calculation, we have not made payments for any of the years 2016, 2015 or 2014, and have accrued the combined unpaid obligation of $496 million as a current liability.

OPM calculates our FERS liability using government-wide salary growth and demographic data, rather than Postal Service-specific demographics and salary growth assumptions. We believe that the OPM methodology unfairly increases our present and future costs. Experience over the past decade demonstrates that average salary increases of our employees are lower than the government-wide estimates that OPM currently uses.

As described elsewhere in this report, OPM calculated that our portion of the FERS plan was underfunded by $3.6 billion as of September 30, 2014. We continue to request that OPM reconsider its use of such government-wide factors and instead apply Postal Service-specific economic and demographic assumptions, which we believe would have resulted in a surplus of approximately $1.2 billion as of September 30, 2014, the most recent period in which such comparisons have been calculated.

In addition to OPM's use of government-wide statistics to calculate our liability and contribution rates to the plans, we are subject to the following constraints and risks that would otherwise not apply with a Postal Service-specific structure:

- Assets contributed to the plans by a single participating U.S. government employer may be used to provide benefits to employees of other participating employers.
- If a participating U.S. government employer ceases contributing to a plan, any unfunded obligations of the plan may be borne by the remaining participating employers.
- Federal law mandates our participation in the plans. If a change in the law permitted us to discontinue this participation, we may be required to contribute to the discontinued plan(s) an amount based on any underfunded status, referred to as a withdrawal liability, if such a liability exists at that time.

<u>Funded Status</u>

OPM administers the CSRS and FERS plans via the Civil Service Retirement and Disability Fund ("CSRDF"). Although CSRDF is a single fund that does not maintain a separate account for each participating U.S. government employer, PAEA requires certain disclosures regarding obligations and changes in net assets as if the funds were separate. Because CSRS and FERS are not subject to the rules and regulations of the *Pension Protection Act of 2006*, typical plan measurements such as zone status and financial improvement plan status, or rehabilitation plan status are not available for these plans.

For the years 2016, 2015 and 2014, we provided more than 5% of the total plan contributions for FERS from all employers (as disclosed in OPM's *Civil Service Retirement and Disability Fund Annual Report*). According to OPM, our portion of the FERS liability had been overfunded from 1992 through the year ended September 30, 2012, when our estimated surplus was approximately $900 million. Because of revisions to OPM's government-wide economic and demographic assumptions, this surplus reversed to a deficit of $3.8 billion and $3.6 billion for the years ended September 30, 2015, and 2014, respectively.

As a result of the deficit, OPM calculated an amortization schedule to pay down the deficit over 30 years, and, accordingly, billed us $248 million, $241 million and $7 million for 2016, 2015 and 2014, respectively, all of which are included within *Payables and accrued expenses* in the accompanying Balance Sheets. OPM currently estimates that the FERS deficit will remain at approximately $3.8 billion by September 30, 2016.

Under current law, no mechanism exists for us to address a FERS surplus when it occurs, and while we may submit a "request for redetermination" of OPM's valuation of our FERS liability or the statistics used to determine our required contributions, no mechanism exists for us to formally appeal OPM's determination. However, in the event that OPM publishes new government-wide contribution rates, any participating U.S. government employer may request that OPM use such employer's specific data if it estimates that its normal cost percentage is at least 10% lower than OPM's calculation. Legislation that would allow OPM to refund any estimated FERS surplus and requiring use of Postal Service-specific economic and demographic assumptions has in the past been considered in Congress; however no such legislation has reached the floor of either the U.S. House of Representatives ("House") or the Senate.

The following table provides OPM's calculations of the funded status of CSRS and FERS for our employees as of September 30, 2016, (projected), 2015 and 2014 and represents the most recent data available:

(in billions)	Projected* 2016	Actual 2015	Actual 2014
CSRS			
Actuarial Liability as of September 30	$ 191.9	$ 194.1	$ 201.5
Current Fund Balance	174.4	177.4	182.1
Unfunded	**$ (17.5)**	**$ (16.7)**	**$ (19.4)**
FERS			
Actuarial Liability as of September 30	$ 115.9	$ 109.0	$ 104.5
Current Fund Balance	112.1	105.2	100.9
Unfunded	**$ (3.8)**	**$ (3.8)**	**$ (3.6)**
Total CSRS and FERS			
Actuarial Liability as of September 30	$ 307.8	$ 303.1	$ 306.0
Current Fund Balance	286.5	282.6	283.0
Unfunded	**$ (21.3)**	**$ (20.5)**	**$ (23.0)**

* The most current actual data is as of September 30, 2015.

We have reported this information based on the same valuations that are used by the Civil Service Retirement System Board of Actuaries ("Board of Actuaries") to establish the normal cost and funding requirements for the plans. OPM actuarial valuations utilize the long-term economic assumptions established by the Board of Actuaries. These assumptions are prepared for U.S. government employers as a whole and based upon assumptions from government-wide employee demographics, rather than those specific to our workforce. As of September 30, 2014, the most recent date of available data, the CSRS plan for U.S. government employers, taken as a whole, was less than 35% funded, although the FERS plan was greater than 90% funded.

When CSRS and FERS data for the Postal Service were excluded from the data for U.S. government employers, taken as a whole, the CSRS plan was less than 20% funded, while the FERS plan was approximately 90% funded. This is because the Postal Service funding of CSRS and FERS was greater than 90% and 96%, respectively.

Cost Methods and Assumptions

The Board of Actuaries recommended revisions to certain demographic assumptions including additional future mortality improvement, effective for the September 30, 2013, valuation. The following table details the long-term economic assumptions recommended by the Board of Actuaries in July 2012, and revised in June 2013:

	2016		**2015**	
	CSRS	**FERS**	**CSRS**	**FERS**
Rate of Inflation	3.00%	3.00%	3.00%	3.00%
Long-term COLA	3.00%	2.40%	3.00%	2.40%
Actual COLA applied	0.00%	0.00%	1.70%	1.70%
Long-term salary increase	3.25%	3.25%	3.25%	3.25%
Actual salary increase	1.30%	1.30%	1.00%	1.00%
Long-term interest rate	5.25%	5.25%	5.25%	5.25%

Net Periodic Costs

The following, provided by OPM, details the net periodic costs and the changes in the actuarial liability for CSRS and FERS:

(in billions)	Projected[1] 2016	Actual 2015
CSRS		
Actuarial liability as of October 1	$ 194.1	$ 201.5
+ Contributions[2]	0.1	0.2
- Benefit disbursements	(12.2)	(12.3)
+ Interest expense	9.9	10.3
+ Total actuarial loss	—	(5.6)
Actuarial liability as of September 30	**$ 191.9**	**$ 194.1**
FERS		
Actuarial liability as of October 1	$ 109.0	$ 104.5
+ Normal costs	3.7	3.5
- Benefit disbursements	(2.6)	(2.3)
+ Interest expense	5.8	5.5
+ Total actuarial loss	—	(2.2)
Actuarial liability as of September 30	**$ 115.9**	**$ 109.0**
Total actuarial liability as of September 30	**$ 307.8**	**$ 303.1**

[1] The most current actual data is as of September 30, 2015.

[2] Contributions for CSRS consist of employee contributions only.

Components of Net Change in Plan Assets

As described above, CSRDF is a single fund and does not maintain separate accounts for CSRS and FERS or for individual U.S. government employers. The investment holdings of the CSRDF consist entirely of long-term special-issue U.S. Treasury securities with maturities of up to 15 years. The long-term securities bear interest rates ranging from 1.38% to 5.25%.

The assumed rate of return on the CSRS fund balance was 5.25% for both 2016 and 2015, and the actual rates of return were 4.04% and 4.11%, respectively. For the FERS fund, the assumed rate of return was 5.25% for 2016 and 2015, while the actual rates of return were 3.04% and 3.47%, respectively. The projected long-term rate of return for both the CSRS and FERS fund balances for 2016 was 5.25%.

The following table details OPM's 5-year estimates for CSRS and FERS contributions and benefit payments:

(in billions)	CSRS		FERS	
Year	**Contributions**	**Total Benefit Payments**	**Contributions**	**Total Benefit Payments**
2017	$ 0.1	$ 12.4	$ 3.6	$ 2.9
2018	0.1	12.6	3.6	3.2
2019	0.1	12.8	3.5	3.6
2020	0.1	13.0	3.5	4.0
2021	0.1	13.1	3.4	4.5

The following information, provided by OPM, details the components of the net change in plan assets for CSRS and FERS:

(in billions)		Actual* 2015		Actual 2014
CSRS				
Net assets as of October 1	$	182.4	$	186.9
+ Contributions		0.2		0.2
- Benefit disbursements		(12.3)		(12.1)
+ Investment income		7.1		7.4
CSRS net assets as of September 30	**$**	**177.4**	**$**	**182.4**
FERS				
Net assets as of October 1	$	100.9	$	96.5
+ Contributions		3.5		3.1
- Benefit disbursements		(2.3)		(2.1)
+ Investment income		3.1		3.4
FERS net assets as of September 30	**$**	**105.2**	**$**	**100.9**

* The most current actual data is as of September 30, 2015.

Employee Health Benefits Expense

Health benefits expense is most significantly impacted by the number of employees electing coverage and the premium costs of the selected plans. Our active employees may participate in FEHB, which is administered by OPM. We account for employee benefit costs as an expense in the period in which our contributions to the plans under the program are due. Average premium increases were 3.8% in 2016, 3.2% in 2015 and 3.7% in 2014. OPM has announced average increases of 4.4% for 2017.

Employee health benefits expense was $5.0 billion for the year ended September 30, 2016. For the year ended September 30, 2015, the expense was $4.8 billion, essentially unchanged from the 2014 expense.

Our employer contribution rates for the majority of our employees are subject to collective bargaining agreements. Our share of healthcare premiums for employees represented approximately 74%, 75% and 76% of premiums for 2016, 2015 and 2014, respectively. Employee health benefits expense was 10.2%, 10.0% and 10.4% of total compensation and benefits expense for the years ended September 30, 2016, 2015 and 2014, respectively.

Retiree Health Benefits

Retirees who participated in FEHB for the five years immediately preceding their retirement may continue to participate in the plan during retirement. Qualifying survivors of retirees are also eligible to receive benefits. Under PAEA, we are obligated to fully prefund the PSRHBF with the employer's portion of the established health benefits of retirees and our current employees. Our total cost for retiree health benefits consists of two components: 1) our portion of the current premium expense for beneficiaries, and 2) the legally-mandated PSRHBF prefunding payments, which we recognize as an expense when due.

In addition to changes in premium amounts each year, several other factors could significantly affect our future retiree health benefits expenses, including investment performance of the PSRHBF, changes in demographics, changes in actuarial assumptions and increased or decreased benefits to participants. See *Item 8. Financial Statements and Supplementary Data*, *Notes to Financial Statements*, *Note 10 - Health Benefits Plans*, *Retiree Health Benefits* for additional information.

Retiree Health Benefits Premiums

Retiree health benefits premium expense, which does not include PSRHBF prefunding, increased 6.2%, 4.2% and 4.8% for the years ended September 30, 2016, 2015 and 2014, respectively. The number of retiree health beneficiaries was approximately 490,000 for each of the years ended September 30, 2016, 2015 and 2014, respectively.

PSRHBF Funded Status

OPM valuations of post-retirement health liabilities and normal costs were prepared in accordance with Federal Accounting Standards Advisory Board Statement of Federal Financial Accounting Standards ("SFFAS") No. 5 and SFFAS No. 33, which require the use of the aggregate entry age normal actuarial cost method. Demographic assumptions are consistent with the pension valuation assumptions, but decrements are based upon counts or number rather than dollars. The following information, provided by OPM, details the PSRHBF funded status and components of net periodic costs:

(in millions)		2016		2015
Beginning actuarial liability at October 1	$	105,162	$	97,740
- Actuarial (gain) loss		(4,555)		3,525
+ Normal costs		2,755		2,852
+ Interest @ 3.9% and 4.1%, respectively		3,924		4,152
Subtotal net periodic costs		2,124		10,529
- Premium payments		(3,305)		(3,107)
Actuarial liability at September 30		103,981		105,162
- Fund balance at September 30		(51,862)		(50,345)
Unfunded obligations at September 30	**$**	**52,119**	**$**	**54,817**

The determination of the liability assumes a single discount rate of 3.9% equivalent to the most recent ten year historical average yield curve. The normal cost, which is on a per-participant basis, is computed to increase annually by a variable medical inflation rate which is assumed to be 5.5% per annum as of the valuation date, grading down to an ultimate value of 3.5% in 2075. Past-year medical inflation was assumed to be 5.0%. Normal costs are derived from the current FEHB on-rolls population with an accrual period from entry into FEHB to assumed retirement. The amounts and variables used to determine the liability are the same the assumptions used under OPM's methodology, except that the average government share of premium payments for annuitants is substituted for annuitant medical costs less annuitant premium payments.

Because calculation of the PSRHBF liability involves several areas of judgment, estimates of the liability could vary significantly depending on the assumptions used. Utilizing the same underlying data that was used in preparing the estimate in the table above, the September 30, 2016, unfunded obligation could range from $39 billion to $68 billion, solely by varying the inflation rate by plus or minus 1%, and the September 30, 2015 unfunded obligation would range from $41 billion to $72 billion. If the actuarial liability had been calculated using the Board of Actuaries long-term rate assumption of 5.25%, the liability would have been approximately $86 billion, or 17% lower, as of September 30, 2016, and approximately $89 billion, or 15% lower, as of September 30, 2015.

For our current annuitants, the government share of premium payments is adjusted to reflect the pro rata share of civilian service to total service for which we are responsible. The pro rata adjustment is made by applying calculated factors based upon actual payments that vary by the age and Medicare status of enrollees. For our active employees, the pro-rata share in retirement is assumed to be 93% of the total.

PSRHBF assets are comprised entirely of long-term, special-issue U.S. Treasury securities with maturities of up to 15 years bearing interest rates from 1.38% to 5.0%. The following table details the fund balance of the PSRHBF, as reported by OPM:

(in millions)		2016		2015
Beginning balance at October 1	$	50,345	$	48,850
Contributions and transfers		—		—
Earnings at 3.1% and 3.3%, respectively		1,517		1,495
Net increase		1,517		1,495
Fund balance at September 30	**$**	**51,862**	**$**	**50,345**

Although PAEA dictated the annual prefunding requirements through 2016, these amounts and the timing of funding could change at any time with enactment of a new law or an amendment of existing law. The total amount of defaulted payments due to the PSRHBF through 2016 is $33.9 billion. No additional payments have been included beyond 2016.

The following information, provided under the PAEA mandate, details OPM's preliminary 5-year estimates for payments into the PSRHBF for normal costs and amortization of unfunded liability, and payments out of the PSRHBF for annuitant premiums:

(in billions)	**Estimated Payments into the PSRHBF***			**Estimated Payments out of the PSRHBF**
Year	**Normal Costs**	**Amortization of Unfunded Liability**	**Total**	**Annuitant Premiums**
2017	$ 2.9	$ 2.9	$ 5.8	$ 3.9
2018	3.1	2.9	6.0	4.1
2019	3.3	2.9	6.2	4.4
2020	3.5	2.9	6.4	4.6
2021	3.6	2.9	6.5	4.9

* Assumes no portion of the $33.9 billion in defaulted payments as of September 30, 2016, will be made to the PSRHBF.

Workers' Compensation

Our employees who are injured on the job are covered by FECA, administered by the DOL's OWCP, which makes all decisions regarding injured workers' eligibility for benefits. We are legally mandated to participate in the federal workers' compensation program. Additionally, we reimburse the DOL for all workers' compensation benefits paid to or on behalf of our employees.

Under FECA, workers' compensation claims cannot be settled through lump-sum payments, and in some instances with regard to those claims, compensation may be paid over many years. Federal law grants COLA adjustments to those claims, and this results in substantially higher costs to us than would likely result if we managed our own claims. Additionally, since we do not manage the FECA program, we have no ability to control the significant administrative costs associated with managing the claims and payments process.

Workers' Compensation Expense

Our workers' compensation expense reflects the impacts of changes in discount rates as well as the actuarial valuation of new workers' compensation cases and revaluation of existing ones. The expense also includes an administrative fee paid to DOL.

For the year ended September 30, 2016, workers' compensation expense was nearly $2.7 billion, an increase of $922 million, or 52.4%, from the prior year. This was most significantly affected by the combined costs of new cases and actuarial revaluation of existing cases, which were nearly $1.6 billion for 2016, compared to $881 million for 2015, an increase of $703 million. The increase is related to changes in the valuation assumptions associated with COLA, medical trend and compensation severity rates, along with the impact of a first quarter 2015 change in accounting estimate, discussed below and in *Item 8. Financial Statements and Supplementary Data, Notes to Financial Statements*, *Note 11 - Workers' Compensation*. The portion of 2016 workers' compensation expense attributable to the impact of discount rate changes was $1.0 billion, compared to $809 million for the prior year, an increase of $217 million. This portion of workers' compensation expense was affected by activity outside of management's control, specifically interest rates declining slightly more during the year ended September 30, 2016, compared to the prior year.

For the year ended September 30, 2015, workers' compensation expense was nearly $1.8 billion, a decrease of $795 million, or 31.1%, from the prior year. The decrease was the result of several factors, most notably a reduction of $1.1 billion in the combined costs of new cases and actuarial revaluation of existing cases. This reduction was partially offset by an increase of $324 million in the expense due to the impact of discount rate changes, which were the result of interest rate fluctuations outside of management's control.

The 2015 workers' compensation expense also reflected a one-time change in accounting estimate under GAAP that was recognized, reducing workers' compensation expense by $353 million. We believe the change allows greater flexibility to select factors reflecting the best and most current injury trends and provides the best estimate when determining the actuarial revaluation of existing cases.

Compound Pharmaceutical Costs

Medical claims payments are impacted by costs associated with pharmaceutical compounding, which is the creation of a pharmaceutical product through the combination of various ingredients directly by a pharmacist. These expenses are included within the combined costs of new cases and actuarial revaluation of existing cases.

In 2013, our compound pharmaceutical costs totaled $9 million. However, in 2015, these costs increased to $99 million, an eleven-fold increase in only two years. In March 2016, the U.S. Postal Service Office of Inspector General issued a report concluding that those increases were attributable to DOL's failure to control the pharmacy-compound invoicing process. As the report recognized, we have no control over that process, which the DOL exclusively administers.

We have, however, repeatedly urged DOL to address the problem. In October 2015, we formally requested DOL to adjust its annual charge-back invoice and we withheld a $69 million payment for new compound-drug costs. DOL ultimately refused to adjust the bill, and we paid the $69 million as we were legally required to do. Nevertheless, we have continued to press DOL to adopt additional safeguards over the billing process and to reign in compound-drug costs.

For the 2016 charge-back year (July 1, 2015 - June 30, 2016), DOL paid approximately $173 million in compound-drug costs on behalf of Postal Service claimants. This represents a 76% increase over 2015 costs and an approximately 1,800% increase over the $9 million cost in 2013. In October 2016, we again formally requested DOL to adjust its annual charge-back invoice and we withheld $151 million from the payment for new compound-drug costs and the associated administrative fee. We are currently awaiting a response from DOL.

Transportation

Transportation expense includes only the costs we incur to transport mail and other products between our facilities, not our costs of transportation to delivery points, which costs are included in *Other operating expenses.* Transportation expenses are primarily comprised of contracted highway, air and international transportation costs. Variations in the volume and weight of mail being transported and the mode of transportation used have significant impact on transportation expenses. The table below details the components of transportation expense for the years ended September 30, 2016, 2015 and 2014:

(in millions)	2016	2015	2014
Highway	$ 3,827	$ 3,638	$ 3,531
Air	2,469	2,151	2,092
International	642	773	934
Other	54	17	29
Total transportation expense	**$ 6,992**	**$ 6,579**	**$ 6,586**

Highway and air transportation expenses increased approximately 5% and 15%, respectively, in 2016 compared to 2015 due in large part to volume growth in our Shipping and Packages business and our strategic efforts to continue to improve our delivery service results. These increased transportation costs were buffered by an approximately 24% reduction in average diesel fuel prices, affecting our highway network, and an approximately 29% reduction in average jet fuel prices, affecting our air network, yielding approximately $170 million and $153 million in annual savings, respectively. International transportation expenses, which represent expenses related only to outbound services, decreased primarily due to a decline in *Priority Mail International* and *Priority Mail Express International* volumes.

Total transportation expenses were essentially unchanged in 2015 compared to 2014. While our overall transportation expenses benefited from lower fuel costs, our transportation fleet was utilized for more trips between facilities during the year. Highway and air transportation costs increased due to the increase in volume of mail classes that utilize our highway and air networks. These increased costs were offset by an approximately 34% reduction in average diesel fuel prices, affecting our highway network, and approximately a 45% reduction in average jet fuel prices, affecting our air network. International transportation costs decreased primarily due to the decrease in international outbound mail volume.

Other Operating Expenses

The following table details other operating expenses for the periods ended September 30, 2016, 2015 and 2014:

(in millions)	2016	2015	2014
Supplies and services	$ 2,755	$ 2,705	$ 2,550
Depreciation and amortization	1,740	1,769	1,843
Rent and utilities	1,560	1,613	1,613
Vehicle maintenance service	624	617	556
Delivery vehicle fuel	359	436	552
Information technology and communications	852	784	791
Rural carrier equipment maintenance	484	514	556
Miscellaneous other	1,057	719	892
Total other operating expenses	**$ 9,431**	**$ 9,157**	**$ 9,353**

While most of the components within other operating expenses either declined slightly or remained nearly the same in 2016 compared to 2015, the miscellaneous other component had a more significant increase which led to the overall 3.0% growth of other operating expenses during 2016 compared to 2015. Expenses associated with contingent liabilities, which is included within the miscellaneous other category, experienced a decline in 2015 pertaining to labor and employment matters, resulting in a larger increase in miscellaneous other between 2015 and 2016. See *Item 8. Financial Statements and Supplementary Data, Notes to Financial Statements*, *Note 8 - Commitments and Contingencies* for further details regarding our contingent liabilities and provision for probable losses arising from claims and lawsuits.

While most of the components within other operating expenses declined or remained the same in 2015 compared to 2014, supplies and services increased and had the most significant change, due most notably to debit and credit card merchant fees and our implementation of certain new technology for our retail operations. While we benefited from lower delivery vehicle fuel costs, this was somewhat offset by higher vehicle maintenance and service costs on our aging vehicle fleet. The miscellaneous other component had the most significant decrease, due to a reduction in contingent liabilities associated with labor and employment matters when compared to 2014. See *Item 8. Financial Statements and Supplementary Data, Notes to Financial Statements*, *Note 8 - Commitments and Contingencies* for further details regarding our contingent liabilities and provision for probable losses arising from claims and lawsuits.

NON-OPERATING REVENUES AND EXPENSES

Interest and Investment Income

The majority of our interest income is derived from the imputed interest we recognize on the future installment payments that are owed to us under the *Revenue Forgone Reform Act of 1993* (the "RFA"). Under the RFA, Congress agreed to reimburse us $1.2 billion in 42 annual installments of $29 million each through 2035 for services we performed in prior years. Imputed interest for the future revenue forgone installments was $22 million, $22 million and $22 million for the years ended September 30, 2016, 2015 and 2014, respectively. See *Item 8. Financial Statements and Supplementary Data*, *Notes to Financial Statements*, *Note 12 - Revenue Forgone* for additional information. Investment income was immaterial for the years ended September 30, 2016, 2015 and 2014.

Interest Expense

Interest expense was $222 million, $185 million and $184 million, for the years ended September 30, 2016, 2015 and 2014, respectively. Although long-term debt generally carries higher interest rates than short-term debt, financing a portion of our debt at longer-term fixed rates decreases our interest rate risk and interest expense volatility in subsequent years.

LIQUIDITY AND CAPITAL RESOURCES

We held cash and cash equivalents of $8.1 billion and $6.6 billion as of September 30, 2016, and September 30, 2015, respectively. Our average daily cash balance during the year ended September 30, 2016, was $8.2 billion, which represents approximately 30 days of operating cash. We define days of cash available as unrestricted cash divided by estimated average cash disbursements (including capital expenditures) per business day (usually 251 cash disbursement days per year). See *Item 8. Financial Statements and Supplementary Data*, *Notes to Financial Statements*, *Note 2 - Liquidity* for additional information.

CASH FLOW ANALYSIS

Our cash balances have increased by approximately $6 billion from the reported low in 2012. This improvement would not have occurred had the Postal Service not defaulted on the annual PSRHBF prefunding payments in 2012 and subsequent years. Aside from the defaults, the improvement is largely attributable to the temporary exigent surcharge (discussed in greater detail below) which generated approximately $4.6 billion in incremental revenue from January 2014 through April 10, 2016.

However, our cash balances remain insufficient to support an organization with approximately $77 billion in annual operating expenses. We continue to face challenges from the ongoing migration of mail to electronic alternatives, and we are legally limited in how we can price our products and streamline our legacy business model. We are further challenged by onerous payment requirements for legacy retirement and PSRHBF obligations that, barring legislative reform, will continue indefinitely.

Our operations will require significant capital investment over the next few years to modernize and improve our processing and delivery infrastructure and update our delivery fleet in order continue to meet our statutory obligation to provide prompt, efficient and reliable postal services to the nation. Furthermore, given our inability to raise cash through the issuance of additional debt, we do not have sufficient cash balances to meet all of our existing legal obligations, pay down our debt and make all of the critical investments in our infrastructure that have been deferred in recent years.

Operating Activities

Cash provided by operating activities decreased by $143 million, or 5.0%, for the year ended September 30, 2016, compared to the previous year. As more fully described in *Results of Operations*, our operating revenue increased during the year ended September 30, 2016, as we benefited from a full year of a price increase on certain Market-Dominant services that went into effect in May 2015 and by a price increase on certain Competitive services that went into effect in January 2016. These increases were offset, however, by an increase in cash used for operating expenses and by the expiration of the exigent surcharge on April 10, 2016, which resulted in a price reduction of certain Market-Dominant services from that date forward. Given the volume of our cash activity from operations during the year, the change in cash provided by operating activities was immaterial.

Cash provided by operating activities decreased by $435 million in 2015, compared to the previous year, primarily due to cash paid for compensation and benefits increasing more than the increase in operating revenue. This was offset slightly by higher accrued liabilities for payroll as of September 30, 2015, versus the prior year end due to timing differences.

Our cash balance was not sufficient to pay the legally-mandated PSRHBF prefunding payments of $5.7 billion that were due by September 30, 2015, and 2014. Although our cash balance was higher than our 2016 payment of $5.8 billion due by September 30, 2016, doing so would have made it impossible to maintain a prudent level of liquidity and to adequately fund our normal operations and necessary capital investments necessary to fulfill our fundamental service mandate. As of September 30, 2016, the total PSRHBF obligation of $33.9 billion remains outstanding; however, we have incurred no penalties or negative consequences resulting from our inability to make these payments.

Exigent Surcharge

As described in *Operating Revenue and Volume*, we collected an exigent surcharge on most Market-Dominant services beginning in January 2014 until it produced incremental revenue of just over $4.6 billion, a figure the PRC determined was lost due to the Great Recession's suppression of mail volume. This limit was reached on April 10, 2016, and we therefore reduced the prices of applicable Market-Dominant services on that date.

As a result of the expiration of the surcharge, we estimate that our revenue and cash flow for 2016 was lower by approximately $1 billion than what it otherwise would have been. Going forward without the surcharge, we expect our revenue and cash flow to be reduced from what it otherwise would be by almost $2 billion per year, unless the PRC's decision to limit our recovery in the manner described above is modified again or reversed through the pending appeal.

Price Increases

On May 31, 2015, a price increase averaging slightly below the CPI-U price cap of 1.966% took place for certain Market-Dominant services. We estimate this price increase generates $750 million in annualized revenue and cash flow.

On October 16, 2015, we filed a notice with the PRC of our intent to increase certain Competitive services prices by an average of 9.5%. The PRC approved this plan and the increase went into effect on January 17, 2016. We estimate that this price increase generates approximately $1 billion in annualized revenue and cash flow.

On October 12, 2016, we filed a notice with the PRC of our intent to increase prices for certain Market-Dominant services by an average of 0.9%. If approved, we expect this price increase to go into effect in January 2017, and would generate approximately $430 million in annualized revenue.

On October 19, 2016, we filed a notice with the PRC of our intent to increase prices for certain Competitive services by an average of 3.9%. If approved, this price increase would likely also go into effect in January 2017, and would generate approximately $507 million in annualized revenue.

Investing Activities

In 2016, we invested $1.4 billion in the purchase of property and equipment, an increase of $206 million over 2015, as we used additional cash on hand to fund some of our much-needed investments in building improvements, vehicles, equipment and other capital projects. In 2015, we invested $1.2 billion in the purchase of property and equipment, an increase of $441 million over 2014.

To conserve cash, we have reduced our capital expenditures from an annual average of approximately $1.5 billion in years 2009 through 2011 to an annual average of approximately $960 million in years 2012 through 2016, a reduction of approximately 35%. However, we will need to increase our capital expenditures in order to address our aging facilities and delivery fleet and to upgrade our equipment to remain competitive in the marketplace and to ensure that we will be able to continue to meet our statutory obligation to provide prompt, efficient and reliable postal services to the nation. The source of funds needed to fulfill these commitments has been generated from our operating activities, as we have not raised capital through the net increase in debt since September 2012.

We assign priority to proposed capital investments based on the following factors:

1. Needed for safety and/or health or legal requirements;
2. Required to provide service to our customers; and
3. Initiatives with a high return on investment and a short payback period.

Our delivery fleet includes approximately 145,000 vehicles that are at least 20 years old and need additional maintenance to continue, therefore repair and maintenance costs have risen significantly in recent years. Additionally, we must invest in upgrades of letter sorting equipment that is at or near the end of its useful life, and also invest in sorting and handling equipment to fully capitalize on business opportunities in the growing package delivery market. To conserve cash, we have also deferred facilities maintenance in instances where this could be done without adversely impacting employee health or safety issues.

Financing Activities

As an "independent establishment of the Executive Branch of the Government of the United States," we receive no tax dollars for ongoing operations and have not received an appropriation for operational costs since 1982. We fund our operations chiefly through cash generated from operations and by borrowing from the FFB, a government-owned corporation under the general supervision of the Secretary of the Treasury. See *Item 8. Financial Statements and Supplementary Data*, *Notes to Financial Statements*, *Note 7 - Debt* for additional information.

We have not increased our debt since September 2012 when we reached the maximum borrowing amount allowed under our statutory debt ceiling. Our debt consists of fixed-rate notes and two revolving credit facilities with various maturities with an aggregate principal balance of $15.0 billion as of September 30, 2016, and September 30, 2015.

The two revolving credit facilities have interest rates determined by the U.S. Department of Treasury each business day and enable us to draw up to $4.0 billion in total. As of September 30, 2016, and September 30, 2015, these facilities were fully drawn and are included in the current portion of debt in the accompanying Balance Sheets. The facilities currently have maturity dates in April 2017.

Net cash used in financing activities, for the periods ended September 30, 2016, 2015 and 2014 were $51 million, $62 million and $148 million, respectively, consisting primarily of cash payments on capital lease obligations.

LIQUIDITY OUTLOOK

With the anticipated continued migration to electronic communication and transactional alternatives, we continue to pursue legislation to reform our business model and streamline our burdensome regulatory structure. Such changes might include the adoption of USPS-specific economic and demographic assumptions for calculating our pension liabilities, restoring the exigent rate surcharge by making it a part of our rate base, and giving us some additional product flexibility.

Additionally, reform is needed to establish a set of healthcare plans within FEHB that would fully integrate with Medicare for current and future retirees. We believe such reform would make our retiree health benefits system affordable by virtually eliminating the unfunded liability previously noted. Although we continue to inform the Administration, Congress, the PRC and other stakeholders of the immediate and long-term financial challenges we face, we have no assurances that our requests will result in meaningful reform in the foreseeable future.

2017 and Beyond

The following table provides details of estimated future cash obligations as of September 30, 2016:

(in millions)	Total	Less than 1 Year	1-3 Years	3-5 Years	After 5 Years
Debt[1]	$ 15,000	$ 10,100	$ 2,700	$ 1,000	$ 1,200
Interest on debt[1]	1,419	195	299	133	792
CSRS amortization of unfunded liability[2]	33,219	1,230	2,461	2,461	27,067
FERS supplemental liability	7,428	496	495	495	5,942
PSRHBF amortization of unfunded liability[3]	113,600	2,840	5,680	5,680	99,400
Workers' compensation[4]	25,913	1,483	2,588	2,140	19,702
Capital lease obligations	326	82	121	64	59
Operating leases	7,429	781	1,472	1,266	3,910
Capital cash outlays[5]	17,070	1,887	3,298	4,153	7,732
Purchase obligations[5]	3,998	1,537	1,517	189	755
Employees' leave[6]	2,057	131	230	224	1,472
Total commitments	**$ 227,459**	**$ 20,762**	**$ 20,861**	**$ 17,805**	**$ 168,031**

[1] For overnight and short-term debt, the table assumes the balance as of period end remains outstanding for all periods presented.

[2] Represents OPM's calculation of annual payments for the amortization of the unfunded liability that we are obligated to begin paying as soon as 2017.

[3] Represents estimated annual payments of $2.84 billion for 40 years that we are obligated to begin paying as soon as 2017.

[4] Represents the undiscounted expected future workers' compensation payments plus $75 million in administrative fees due October 15, 2016, and assumes no new cases in future years. The obligation to pay administrative fees in future years as determined by DOL is currently not estimated.

[5] Capital cash outlays pertain to planned purchases of equipment, building improvements and vehicles per the 2017 Integrated Financial Plan. Purchase obligations pertain to items that are expensed when received or amortized over a short period of time. These are not reflected on the *Balance Sheets*.

[6] Employees' leave includes both annual and holiday leave.

According to law, our obligations pertaining to CSRS will change in 2017 and OPM will determine the amount of annual payments we will need to make to amortize the CSRS unfunded liabilities. We estimate this payment obligation will be approximately $1.2 billion beginning as soon as 2017. This matter is under review by the Office of Legal Counsel at the U.S. Department of Justice, to confirm whether these payments should begin in 2017 or 2018.

Also in 2017, our retiree health benefit obligations will change according to law. The PSRHBF will begin funding the Postal Service's share of retiree health benefit premiums, and we will begin paying the normal costs of retiree health benefits, which we estimate will be approximately $2.9 billion per year. Additionally, OPM will determine the amount of annual payments we will need to make to amortize the PSRHBF unfunded liabilities, which we estimate will be approximately $2.9 billion.

Although the total amount of these CSRS and PSRHBF projected cash outlays on our 2017 obligations is estimated to be approximately $2.1 billion less than our 2016 mandated obligations for these items, we anticipate that without legislative action, it is unlikely that we will be able to make all legally-required payments in 2017, given our liquidity concerns.

We also estimate that our cash outlays for capital assets will amount to $1.9 billion in 2017 and an additional $7.5 billion for the periods of 2018 through 2021. Although our future projections include these capital cash outlays, future cash flow from operations alone may not generate the cash needed for such necessary capital expenditures.

Contingency Plans

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 of approximately $71 billion, generated almost entirely through the sale of postal services, a financially-sound Postal Service continues to be vital to U.S. commerce. The U.S. economy benefits greatly from the Postal Service and the many businesses that provide the printing and mailing services that we support, and disruption of the mail would cause undue hardship to businesses and consumers.

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 suppliers ahead of some payments to U.S. government entities, as has been done in the past. Without structural change to our business model and legislative change, the factors discussed above will continue to negatively impact us resulting in continuing losses and liquidity challenges for the foreseeable future.

LEGISLATIVE UPDATE

LEGISLATION

On July 12, 2016, the House Oversight and Government Reform Committee passed the *Postal Service Financial Improvement Act of 2016* (H.R. 5707), which would require a percentage of the PSRHBF to invest in certain types of index fund investments using one or more qualified professional asset managers. The measure would also establish a PSRHBF Investment Committee to advise the Secretary of the Treasury in setting investment guidelines and selecting professional asset managers.

Also on July 12, 2016, the House Oversight and Government Reform Committee unanimously passed the *Postal Service Reform Act of 2016* (H.R. 5714). The bipartisan measure would institute separate, Postal Service-only plans within FEHB that are fully integrated with Medicare, require Postal Service-specific demographic and economic assumptions in calculating pension liabilities, reinstate half of the exigent surcharge and authorize us to provide non-postal services to state, local and tribal governments. The measure would also reduce the number of Governors from nine to five and empower the Postmaster General to implement our strategic direction and pricing and product strategy, as approved by the Governors.

Both measures continue to await consideration by the full House.

APPROPRIATIONS

On July 7, 2016, the House passed the *Fiscal 2017 Financial Services and General Government Appropriations* bill (H.R. 5485), which includes $41 million in appropriated funds to us for revenue forgone on “free and reduced mail” for the blind and for overseas absentee ballots. A provision requiring six-day mail delivery frequency remains in the bill. Our 2017 appropriations request to Congress was $170 million. The amounts requested represent accounts receivable from the U.S. government for postal services provided and/or mandated by law.

BOARD OF GOVERNORS NOMINATIONS

As previously reported, the President has nominated six individuals to serve on our Board of Governors, and the Senate Homeland Security and Governmental Affairs Committee has voted to advance each of these nominations. These six nominations continue to await a confirmation vote by the full Senate, the timing of which remains uncertain.

CYBER INTRUSION INCIDENT

As previously disclosed, during the fourth quarter of 2014 we learned of a cyber intrusion into some of our information systems. The intrusion compromised files containing data submitted by customers who contacted our customer care center with inquiries via telephone or email between January 1, 2014, and August 16, 2014. Our transactional revenue systems were not affected, and we believe that no customer credit or debit card information from retail or online purchases was compromised. The compromised files also contained personally identifiable information of individuals we employed from May 2012 through the fourth quarter of 2014, when we learned of the breach. We are unaware of any evidence that the compromised employee information was used to engage in malicious activity. Following the incident, we worked with both public and private-sector forensic specialists to investigate the matter and to strengthen the security of our systems against future cyber intrusions.

FAIR VALUE MEASUREMENTS

We did not have any recognized gains as a result of fair valuation measurements in the years ended September 30, 2016, 2015 and 2014. All recognized losses have been incorporated into our financial statements and the unrecognized gains and losses are not considered to have a significant impact upon our operations. See *Item 8. Financial Statements and Supplementary Data*, *Notes to Financial Statements*, *Note 13 - Fair Value Measurement* for additional information.

RELATED PARTY TRANSACTIONS

We have significant transactions with other U.S. government entities, which are considered related parties for reporting purposes. See *Item 8. Financial Statements and Supplementary Data*, *Notes to Financial Statements*, *Note 3 - Related Parties*

CRITICAL ACCOUNTING POLICIES AND ESTIMATES

The preparation of financial statements in accordance with GAAP requires management to make significant judgments and estimates to develop certain amounts reflected and disclosed in the financial statements. In many cases, alternative policies or estimation techniques may 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. Management discusses the development and selection of these accounting policies and estimates with the Audit and Finance Committee of the Board. However, even under optimal circumstances, estimates routinely require adjustment based on changing circumstances and new or better information.

The three accounting policies that are considered either the most judgmental, or involve the selection or application of alternative accounting policies, and are material to the financial statements, are those related to the recording of workers' compensation costs, deferred revenue-prepaid postage and contingent liabilities. For further information, see *Item 8. Financial Statements and Supplementary Data*, *Notes to Financial Statements*, *Note 1 - Organization and Summary of Significant Accounting Policies*, *Note 11 - Workers' Compensation* and *Note 8 - Commitments and Contingencies*.

WORKERS' COMPENSATION

Workers' compensation costs reflected in our accompanying Statements of Operations are subject to actuarial estimates of future claim payments based upon past claim payment experience. Workers' compensation costs are highly sensitive to discount and inflation rates, which are updated on a quarterly basis and the length of time recipients are expected to stay on the compensation rolls. However, the annual cash payment for claims is relatively stable and predictable.

The discount rate reflects the current rate at which the workers' compensation liabilities could be effectively settled at the measurement date (e.g., the end of the accounting period). In setting the discount rates, we use the current yield, as of the measurement date, on U.S. Treasury securities that are matched to the expected duration of both the medical and compensation payments. Expected inflation in compensation claim obligations are estimated using the Philadelphia Fed Consensus Inflation Forecast. For medical claims, we use the average rate of medical cost increases experienced by our workers' compensation claimants over the past five years as an estimate for future medical inflation. Workers' compensation liabilities are recorded in the Balance Sheets as *Workers' compensation costs* with both current and noncurrent components.

DEFERRED REVENUE-PREPAID POSTAGE

Deferred revenue-prepaid postage is an estimate of postage that has been sold, but not yet used by customers. Revenue is recognized only when mail is delivered, not when postage is purchased, and revenue is deferred and reflected in the Balance Sheets as *Deferred revenue-prepaid postage.* The deferred revenue estimate is developed and validated through complex mathematical and statistical methods of stamp usage trends. Small differences in inputs can lead to significant differences in the estimate of the liability. Three categories of postage sales account for the majority of *Deferred revenue-prepaid postage*: *Forever stamp* sales, metered postage and mail-in-transit, which is mail that has not reached its final destination.

During 2016, we revised the estimation technique utilized to estimate our *Deferred revenue-prepaid postage* liability for *Forever Stamps*. The change resulted from new information regarding customer's retention and usage habits of applicable postage, and enabled the Postal Service to update its estimate of stamps that will never be used for mailing. As a result of this change, *Deferred revenue-prepaid postage* was decreased by nearly $1.1 billion. In accordance with GAAP, the change was accounted for as a change in accounting estimate, and was reflected in operating results as an increase to revenue and a decrease to net loss by the same amount in the year ended September 30, 2016.

CONTINGENT LIABILITIES

The recording of contingent liabilities requires significant judgment in estimating potential losses for legal and other claims. Each quarter, significant new claims and litigation are evaluated for the probability of an adverse outcome. Liabilities are recorded in the Balance Sheets within *Trade payables and accrued expenses* and *Other noncurrent liabilities* when amounts are deemed both probable and estimable.

In addition, any prior claims and litigation are reviewed and, when necessary, the liability balances are adjusted for resolutions or revisions to prior estimates. Estimates of loss can therefore change as individual claims develop and additional information becomes available. We disclose the range of amounts for pending claims and litigations that are deemed to be reasonably possible of an unfavorable outcome, but do not accrue for or include such provisions in our financial statements.

RECENT ACCOUNTING STANDARDS

See *Item 8. Financial Statements and Supplementary Data*, *Notes to Financial Statements*, *Note 1 - Organization and Summary of Significant Accounting Policies*, *Summary of Significant Accounting Policies*, *Recent Accounting Standards*.

ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

The market rate risks we encounter are primarily related to foreign currency exchange rate fluctuations, interest rates and commodity prices. Historically, we have not entered into derivatives contracts or commodity instruments for trading or speculative purposes or to manage market risks.

FOREIGN EXCHANGE RISK

While we operate outside of the U.S., and foreign currency fluctuations may favorably or unfavorably impact our reported earnings, we believe that foreign exchange risk is not a material amount since the vast majority of our business transactions are denominated in U.S. dollars. Because of this, we estimate that a 1% increase or decrease in foreign exchange rates would not have a material impact on our financial statements.

INTEREST RATE RISK

We are impacted by changes in interest rates in the normal course of our business operations as a result of our ongoing investing and financing activities which include our revolving credit line facilities and floating note purchase agreements as well as our cash and cash equivalents. We assess our interest rate risks on a regular basis and currently estimate that a 1% increase in interest rates would have resulted in approximately a $38 million increase in interest expense.

We currently have no significant exposure to changing interest rates on our noncurrent debt as interest rates are fixed on such debt. As disclosed in the accompanying notes to the financial statements, see *Item 8. Financial Statements and Supplementary Data*, *Notes to Financial Statements*, *Note 13 - Fair Value Measurement*, the fair value of our noncurrent debt, exclusive of capital leases, was $5.5 billion and $5.4 billion for the years ended September 30, 2016, and 2015, respectively. The underlying fair value of our noncurrent debt was estimated using prices provided by the FFB.

We also have interest rate risk associated with our workers' compensation liability, which is highly sensitive to changes in discount rates. An increase of 1% in the interest rates would decrease the liability at September 30, 2016, and 2016 expense by approximately $2.2 billion. A decrease of 1% would increase the liability at September 30, 2016, and 2016 expense by approximately $2.7 billion. See *Item 8. Financial Statements and Supplementary Data*, *Notes to Financial Statements*, *Note 11 - Workers' Compensation* for further explanation.

COMMODITY PRICES RISK

We currently have market risk for changes in fuel and natural gas costs. As of September 30, 2016, we estimated that a 1% increase in fuel and natural gas would have resulted in a $19 million increase in 2016 expense.

ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

The Temporary Emergency Committee of the Board of Governors of the United States Postal Service

We have audited the accompanying balance sheets of the United States Postal Service as of September 30, 2016 and 2015, and the related statements of operations, changes in net deficiency, and cash flows for each of the three years in the period ended September 30, 2016. These financial statements are the responsibility of the United States Postal Service's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States), the auditing standards generally accepted in the United States of America, and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the United States Postal Service at September 30, 2016 and 2015, and the results of its operations and its cash flows for each of the three years in the period ended September 30, 2016, in conformity with U.S. generally accepted accounting principles.

As discussed more fully in Note 2 to the financial statements, the United States Postal Service, an independent establishment of the executive branch of the Government of the United States, is dependent upon future actions of the Government to continue its operations in the ordinary course as a result of continuing operating losses and statutory funding requirements for employee benefit obligations. The Postal Service has incurred recurring losses from its operations primarily due to sustained declines in mail volume, and statutory and regulatory restrictions have constrained the ability of the Postal Service to implement strategies to improve efficiency, reduce costs and increase revenues. Due to these conditions, during fiscal year 2016, the Postal Service defaulted on a $5.8 billion prefunding payment required to be paid to the Postal Service Retiree Health Benefits Fund by Public Law (P.L.) 109-435, the Postal Accountability and Enhancement Act, by September 30, 2016 and has not satisfied $28.1 billion of required prefunding payments due in previous years. The Postal Service does not expect to have sufficient cash to satisfy these obligations. The statutory requirement establishing the payments required by P.L. 109-435 contains no provisions addressing a payment default. The Postal Service does not, at this time, anticipate any legal consequences, under current law, from its inability to make the required payments. Management expects, but no assurances can be given, that additional legislation will be enacted to address the short-term funding requirements of the United States Postal Service and to address regulatory restrictions that have not allowed the Postal Service to adjust its operations to levels commensurate with its current revenue base.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States) and in accordance with attestation standards established by the American Institute of Certified Public Accountants, the United States Postal Service's internal control over financial reporting as of September 30, 2016, based on criteria established in Internal Control-Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (2013 framework) and our report dated November 15, 2016 expressed an unqualified opinion thereon.

In accordance with *Government Auditing Standards*, we also have issued our report dated November 15, 2016 on our consideration of the United States Postal Service's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, and contracts and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

/s/ Ernst & Young LLP

McLean, Virginia
November 15, 2016

UNITED STATES POSTAL SERVICE
STATEMENTS OF OPERATIONS

(in millions)	Year Ended September 30, 2016	2015	2014
Revenue			
Operating revenue	$ 71,429	$ 68,790	$ 67,764
Other revenue	69	138	66
Total revenue	**71,498**	**68,928**	**67,830**
Operating expenses			
Compensation and benefits	48,689	47,519	46,000
Retiree health benefits	9,105	8,811	8,685
Workers' compensation	2,682	1,760	2,554
Transportation	6,992	6,579	6,586
Other operating expenses	9,431	9,157	9,353
Total operating expenses	**76,899**	**73,826**	**73,178**
Loss from operations	**(5,401)**	**(4,898)**	**(5,348)**
Interest and investment income	32	23	24
Interest expense	(222)	(185)	(184)
Net loss	**$ (5,591)**	**$ (5,060)**	**$ (5,508)**

See accompanying notes to the financial statements.

UNITED STATES POSTAL SERVICE
BALANCE SHEETS

(in millions)	September 30, 2016	September 30, 2015
Current Assets:		
Cash and cash equivalents	$ 8,077	$ 6,634
Restricted cash	253	233
Receivables, net	1,042	930
Supplies, advances and prepayments	140	118
Total current assets	**9,512**	**7,915**
Property and equipment, net	15,296	15,686
Other assets	411	413
Total assets	**$ 25,219**	**$ 24,014**
Current Liabilities:		
Compensation and benefits	$ 2,669	$ 1,899
Retiree health benefits	33,900	28,100
Workers' compensation costs	1,427	1,401
Payables and accrued expenses	1,892	1,853
Deferred revenue-prepaid postage	2,253	3,304
Customer deposit accounts	1,246	1,201
Other current liabilities	1,128	1,053
Current portion of debt	10,100	10,100
Total current liabilities	**54,615**	**48,911**
Workers' compensation costs, noncurrent	18,612	17,410
Employees' accumulated leave, noncurrent	1,926	1,951
Other noncurrent liabilities	1,148	1,233
Noncurrent portion of debt	4,900	4,900
Total liabilities	**81,201**	**74,405**
Net Deficiency:		
Capital contributions of the U.S. government	3,132	3,132
Deficit since 1971 reorganization	(59,114)	(53,523)
Total net deficiency	**(55,982)**	**(50,391)**
Total liabilities and net deficiency	**$ 25,219**	**$ 24,014**

See accompanying notes to the financial statements.

UNITED STATES POSTAL SERVICE
STATEMENTS OF CHANGES IN NET DEFICIENCY

(in millions)	Capital Contributions of U.S. Government	Accumulated Deficit Since Reorganization	Total Net Deficiency
Balance, September 30, 2013	**$ 3,132**	**$ (42,955)**	**$ (39,823)**
Net loss	—	(5,508)	(5,508)
Balance, September 30, 2014	**$ 3,132**	**$ (48,463)**	**$ (45,331)**
Net loss	—	(5,060)	(5,060)
Balance, September 30, 2015	**$ 3,132**	**$ (53,523)**	**$ (50,391)**
Net loss	—	(5,591)	(5,591)
Balance, September 30, 2016	**$ 3,132**	**$ (59,114)**	**$ (55,982)**

See accompanying notes to the financial statements.

UNITED STATES POSTAL SERVICE
STATEMENTS OF CASH FLOWS

(in millions)	Years Ended September 30, 2016	2015	2014
Cash flows from operating activities:			
Net loss	$ (5,591)	$ (5,060)	$ (5,508)
Adjustments to reconcile net loss to cash provided by operations:			
Depreciation and amortization	1,740	1,769	1,843
(Gain) loss on disposals of property and equipment, net	(11)	(59)	43
Decrease (increase) in other assets	2	7	(35)
Increase in noncurrent workers' compensation	1,202	308	1,184
Decrease in noncurrent deferred appropriations and other revenue	(40)	(8)	(5)
Decrease in other noncurrent liabilities	(122)	(215)	(53)
Changes in current assets and liabilities:			
Receivables, net	(112)	—	54
Other assets	(22)	4	—
Retiree health benefits	5,800	5,683	5,651
Payables, accrued expenses and other	935	306	1
Deferred revenue-prepaid postage, prepaid box rents and other	(1,045)	144	139
Net cash provided by operating activities	**2,736**	**2,879**	**3,314**
Cash flows from investing activities:			
Change in restricted cash	(20)	13	66
Purchases of property and equipment	(1,428)	(1,222)	(781)
Proceeds from sales of property and equipment	206	120	129
Net cash used in investing activities	**(1,242)**	**(1,089)**	**(586)**
Cash flows from financing activities:			
Issuance of notes payable	7,600	5,800	5,800
Payments on notes payable	(7,600)	(5,800)	(5,800)
Changes in capital lease obligations and other	(51)	(62)	(148)
Net cash used in financing activities	**(51)**	**(62)**	**(148)**
Net increase in cash and cash equivalents	1,443	1,728	2,580
Cash and cash equivalents at beginning of year	6,634	4,906	2,326
Cash and cash equivalents at end of year	**$ 8,077**	**$ 6,634**	**$ 4,906**
Supplemental cash flow disclosures:			
Cash paid for interest	$ 188	$ 179	$ 184

See accompanying notes to the financial statements.

NOTES TO FINANCIAL STATEMENTS

NOTE 1 - ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Organization

The United States Postal Service (the "Postal Service") provides postage, mail delivery and shipping services to retail and commercial customers in the communications, distribution and delivery, advertising and retail markets throughout the nation and internationally. As a result, the Postal Service maintains a very diverse customer base and is not dependent upon a single customer or small group of customers. No single customer represented more than 3% of operating revenue for the years ended September 30, 2016, 2015 and 2014. The Postal Service is subject to congressional oversight and regulation by the Postal Regulatory Commission ("PRC"), but does not receive tax dollars for operating expenses, relying solely on the sale of postage, products and services to fund its operations.

Postal Service products are classified as either Market-Dominant or Competitive; however, the term "services" is used in this report for consistency with other descriptions of services the Postal Service offers. Services are sold by approximately 32,000 post offices, stations and branches, plus a large network of Contract Postal Units, Community Post Offices, Village Post Offices, commercial outlets which sell stamps and services on the Postal Service's behalf and through its website www.usps.com. The Postal Service delivers to approximately 156 million city, rural, *PO Box* and highway delivery points. Operations are conducted primarily in the domestic market, with international revenue representing approximately 4% of operating revenue.

Approximately 91% of career employees are covered by collective bargaining agreements and are 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"). The contracts with the four labor unions representing the majority of Postal Service employees include provisions granting annual increases and cost-of-living adjustments ("COLAs"), which are linked to the CPI-W. For further information on collective bargaining agreements, see *Note 8 - Commitments and Contingencies.*

By law, the Postal Service must consult with management organizations representing most of its employees not covered by collective bargaining agreements. These consultations provide non-bargaining unit employees in the field with an opportunity to participate in the planning, development and implementation of certain programs and policies that affect them.

Summary of Significant Accounting Policies

The preparation of financial statements in accordance with accounting principles generally accepted in the U.S. ("GAAP") requires management to make estimates and judgments that affect the reported amounts of assets, liabilities, revenue and expenses and related disclosure of contingent assets and liabilities. On an ongoing basis, management evaluates its estimates which are based on historical experience and various other assumptions that management believes are reasonable under the circumstances, the results of which form a basis for making judgments about the carrying value of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates; however, management believes that its estimates are reasonable and that the actual results will not vary significantly from the estimated amounts.

All references to years in this report, unless otherwise stated, refer to fiscal years beginning October 1 and ending September 30. All references to quarters, unless otherwise stated, refer to fiscal quarters.

Cash and Cash Equivalents

Cash and Cash Equivalents consists of cash and short-term, highly-liquid investments with maturities of 90 days or less.

Restricted Cash

Restricted Cash represents Postal Service cash that is not available for general use. This may include cash originated from forfeitures or seizures related to consumer fraud or other criminal activity related to the mail and either held for third-party beneficiaries or awaiting disposition. *Restricted Cash* also includes funds designated for specific use due to congressional appropriation for our obligations to the PRC and the United States Postal Service Office of Inspector General, or other restriction.

Receivables, net

Receivables, net represents Postal Service receivables recorded at the amount invoiced, net of allowances. Allowances for potential credit losses are recognized at each balance sheet date. These estimates are determined based on historical collection experience, trends in customer payment frequency and judgments about the probable effects on observable data, including present economic conditions and the financial health of specific customers and market sectors.

Property and Equipment, net

Property and Equipment, net represents property and equipment recorded at cost, including the interest on borrowings used to pay for the construction of major capital additions, less accumulated depreciation. Depreciation expense is recorded using the straight-line method over estimated useful life, which ranges from 3 to 40 years. Depreciation expense is included within *Other operating expenses* in the accompanying Statements of Operations. The costs and accumulated depreciation of assets sold or retired are removed from balance sheet accounts in the period in which the transaction occurred. General maintenance and repair costs are charged to expense as incurred. See *Note 5 - Property and Equipment, net* for additional information.

Software Capitalization

Software costs, including internal development costs, are capitalized when they meet certain criteria including, most significantly, when the software is for internal use, whether acquired or internally developed or modified to meet the Postal Service's internal needs. Costs to be capitalized include both contracted resources and employee labor costs involved in the development. Interest costs incurred while developing internal-use software are also capitalized. Costs are accumulated until the software is put into production, at which time amortization of the internal-use software begins for a period not to exceed 3 years. See *Note 5 - Property and Equipment, net* for additional information.

Leases

The Postal Service leases over 23,000 real properties. As the lessee, the Postal Service classifies a lease which has substantially all the risks and rewards of ownership as a capital lease. These leases are capitalized on the lease commencement date at the lower of the fair value of the leased assets and the present value of the minimum lease payments. The discount rate used to determine the present value is based on average U.S. Treasury rates. Property acquired under a capital lease is depreciated over the lease term. Capital leases are included within *Property and equipment, net* in the accompanying Balance Sheets.

Other lease arrangements in which substantially all risks and rewards of ownership are retained by the lessor are classified as operating leases. Rent expense for operating leases is included in *Other operating expenses* in the accompanying Statements of Operations on a straight-line basis over the term of the lease.

Impaired Assets

Impairment losses on long-lived assets are recorded when events or circumstances indicate that an asset's fair value is less than its carrying value. When such a determination is made, the carrying values of the assets are written down to fair value. Fair value is determined by independent appraisals for real property. Due to the absence of a market for most types of mailing equipment, impaired equipment assets are typically assigned a fair value of zero. See *Note 5 - Property and Equipment, net* for additional information.

Employees' Accumulated Leave

Employees' accumulated leave represents leave earned as of the balance sheet date and is recorded net of advances. Employees earn annual leave based on the number of creditable years of service with the Postal Service. The Postal Service advances annual leave to employees at the beginning of each calendar year for the value of leave they will earn for the current year. Leave taken by employees before it is earned is considered an advance. Advances were $149 million and $156 million at September 30, 2016, and 2015, respectively. The current portion of employees' accumulated leave is included under *Current liabilities* within *Compensation and benefits* in the accompanying Balance Sheets. *Employees' accumulated leave, noncurrent* is also recorded in the accompanying Balance Sheets.

Retiree Benefits

Employees are eligible to participate in the U.S. government pension and retiree health benefits programs. The Postal Service is required to provide funding for these plans as determined by the Office of Personnel Management ("OPM"), the administrator of the plans. The Postal Service cannot direct the costs, benefits or funding requirements of the plans. Accordingly, the plans are accounted for using multiemployer plan accounting rules, and expenses are recorded in the period in which the contributions are due and payable. These amounts can fluctuate significantly from year to year if funding requirements change. See *Note 9 - Retirement Plans* and *Note 10 - Health Benefits Plans* for additional information.

Workers' Compensation

Postal Service employees are covered by the *Federal Employees' Compensation Act* ("FECA"), administered by the Department of Labor ("DOL") Office of Workers' Compensation Programs ("OWCP"). The Postal Service uses an estimation model to forecast and record the workers' compensation liability for the present value of estimated future payments. See *Note 11 - Workers' Compensation* for additional information.

Deferred Revenue–Prepaid Postage

Deferred revenue–prepaid postage is an estimate of postage that the Postal Service has sold but customers have not yet used. Revenue is recognized when mail is delivered. Because payments for postage are collected in advance of services being performed, revenue is deferred and reflected as *Deferred revenue–prepaid postage* in the accompanying Balance Sheets. Stamp sales and metered postage account for the majority of *Deferred revenue–prepaid postage*. Included in the estimate of the liability is an estimate for mail that is in-transit within the Postal Service network. See *Note 6 - Payables, Accrued Expenses and Deferred Revenue* for additional information.

Contingent Liabilities

The Postal Service is a party to various legal proceedings and claims in the normal conduct of its operations. Contingent liabilities require significant judgment in estimating potential losses. Each quarter, significant new claims and litigation are evaluated for the probability of an adverse outcome. Any prior claims and litigation are also reviewed, and when necessary, the liability balance is adjusted for resolutions or revisions to prior estimates. Estimates of loss can therefore change as additional information becomes available. See *Note 8 - Commitments and Contingencies* for additional information.

Revenue Forgone

Under the *Revenue Forgone Reform Act of 1993*, Congress agreed to reimburse the Postal Service $1.2 billion in 42 annual "installments" of $29 million through 2035 for certain services the Postal Service performed during years 1991 through 1998. Additionally, each year the Postal Service estimates the costs it incurs to provide "free and reduced mail" services to groups of mailers that Congress has determined should be subsidized, and the Postal Service submits these estimates annually to Congress. Congress then considers this for funding, which may be modified and approved or denied, under an appropriation for both of these components of revenue forgone. See *Note 12 - Revenue Forgone* for additional information.

Emergency Preparedness Plan

As a result of an act of biological terrorism, Congress appropriated funds to the Postal Service in 2001 and 2002 to support the costs of maintaining the safety of Postal Service employees and customers, as well as mail and packages in transit. These appropriated funds were accounted for as deferred revenue upon receipt and were generally used to procure capital equipment.

When the Postal Service records depreciation expense for equipment purchased with funds from the Emergency Preparedness Fund appropriation, it recognizes revenue for emergency preparedness appropriations concurrently. The emergency preparedness appropriations revenue recognized was zero for September 30, 2016, as all equipment purchased with these funds is now fully depreciated. For the years ended September 30, 2015, and 2014, the revenue recognized was $86 million and $90 million, respectively. These amounts are included within *Operating revenue* in the accompanying Statements of Operations.

Advertising

Advertising costs, which the Postal Service expenses as they are incurred, were $163 million, $160 million and $175 million for the years ended September 30, 2016, 2015 and 2014, respectively, and are included within *Other operating expenses* in the accompanying Statements of Operations.

Foreign Currency Translation

Foreign currency translation risk can arise from international mail transactions related to settlements of receivables and payables with foreign postal administrations. The majority of international accounts are denominated in special drawing rights, based on a group of currencies comprised of the Euro, Japanese yen, British pound sterling and the U.S. dollar, which fluctuate daily. Changes in the relative value of these currencies increase or decrease the value of the settlement accounts and result in a gain or loss that is included in operating results. The impact of foreign currency translation on operating results was not material for the years ended September 30, 2016, 2015 and 2014.

Segment Information

The Postal Service operates as one segment throughout the U.S., its possessions and territories.

Related Parties
As disclosed throughout this report, the Postal Service conducts significant transactions with other U.S. government entities. See *Note 3 - Related Parties* for additional information.

Change in Accounting Estimate
During 2016, the Postal Service revised the estimation technique utilized to estimate its *Deferred revenue-prepaid postage* liability for *Forever Stamps*. The change resulted from new information regarding customer's retention and usage habits of applicable postage, and enabled the Postal Service to update its estimate of stamps that will never be used for mailing. As a result of this change, *Deferred revenue-prepaid postage* was decreased by nearly $1.1 billion. In accordance with GAAP, the change was accounted for as a change in accounting estimate, and was reflected in operating results as an increase to revenue and a decrease to net loss by the same amount in the year ended September 30, 2016.

Recent Accounting Standards

Accounting Standards Update 2014-09 Revenue from Contracts with Customers
In May 2014, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update 2014-09 *Revenue from Contracts with Customers* ("ASU 2014-09"). 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. As originally issued, ASU 2014-09 was effective for fiscal years and interim periods within those years beginning after December 15, 2016, with early adoption not permitted.

In July 2015, the FASB voted for a one-year deferral of the effective date of the standard to annual reporting periods beginning after December 15, 2017, with an option that would permit reporting entities to adopt the standard as early as the original effective date. The new standard may be adopted either retrospectively or on a modified retrospective basis whereby the new standard would be applied to new and existing contracts with remaining performance obligations as of the effective date, with a cumulative catch-up adjustment recorded to beginning retained earnings or net deficiency at the effective date for existing contracts with remaining performance obligations. The Postal Service is currently evaluating the impact of adopting this standard retrospectively on its financial statements, which is not known or reasonably estimable at this time.

Accounting Standards Update 2014-15 Disclosure of Uncertainties about an Entity's Ability to Continue as a Going Concern
In August 2014, the FASB issued Accounting Standards Update 2014-15 *Disclosure of Uncertainties about an Entity's Ability to Continue as a Going Concern* ("ASU 2014-15"). The new standard requires an entity to perform interim and annual assessments of its ability to continue to meet obligations as they become due within one year after the date that the financial statements are issued. ASU 2014-15 is effective for annual periods ending after December 15, 2016, and interim periods thereafter, with early adoption permitted. The Postal Service does not believe the adoption of the new standard will have a significant impact on its reported disclosures.

Accounting Standards Update 2016-02 Leases
In February 2016, the FASB issued Accounting Standards Update 2016-02 *Leases* ("ASU 2016-02"). The new standard requires an entity to record most leases on its balance sheets but continue to recognize expenses in the statements of operations in a manner similar to current accounting practices. The new standard states that a lessee will recognize a lease liability for the obligation to make lease payments and a right-of-use asset for the right to use the underlying asset for the lease term. Expenses related to leases determined to be operating leases will be recognized on a straight-line basis, while those determined to be capital leases will generally have higher expense in the earlier periods of the lease and both interest and amortization are presented separately in the statements of operations.

ASU 2016-02 is effective for annual periods beginning after December 15, 2018, and interim periods within those years, with early adoption permitted. Entities are required to use a modified retrospective approach for leases that exist or are entered into after the beginning of the earliest comparative period in the financial statements. The Postal Service is currently evaluating the impact of adopting this standard on its financial statements and disclosures, but given the significant number of leases in place, the Postal Service expects that the adoption will have a material effect on its financial statements and disclosures.

Accounting Standards Update 2016-04 Liabilities - Extinguishments of Liabilities
In March 2016, the FASB issued Accounting Standards Update 2016-04 *Liabilities - Extinguishments of Liabilities* ("ASU 2016-04"). The new standard requires entities that sell prepaid stored-value products redeemable for goods, services or cash

at third-party merchants to recognize "breakage" (i.e., the value that is ultimately not redeemed by the consumer) in a way that is consistent with how gift card breakage will be recognized under ASU 2014-09, discussed earlier.

ASU 2016-04 is effective for annual and interim periods beginning after December 15, 2017, with early adoption permitted. The new standard may be adopted either retrospectively or on a modified retrospective basis with a cumulative catch-up adjustment recorded to beginning retained earnings or net deficiency as of the beginning of the fiscal year the standard is effective. The standard is applicable to the Postal Service's determination of money orders and related breakage. The Postal Service is currently evaluating the impact of adopting this standard on its financial statements and disclosures.

NOTE 2 - LIQUIDITY

The Postal Service generates its cash almost entirely through the sale of postage and other services. It holds its cash with the Federal Reserve Bank of New York and invests its excess cash, when available, in highly-liquid, short-term investments issued by the U.S. Department of Treasury. As of September 30, 2016, and 2015, the Postal Service held unrestricted cash and cash equivalents of $8.1 billion and $6.6 billion, respectively. The Postal Service had no remaining borrowing capacity under its statutory debt ceiling. See *Note 7 - Debt* for additional information.

Liquidity Concerns

The Postal Service is constrained by laws and regulations, including the *Postal Accountability and Enhancement Act of 2006*, Public Law 109-435 ("PAEA"), which restricts revenue sources and mandates certain expenses, including prefunding of the Postal Service Retiree Health Benefits Fund ("PSRHBF"). Additionally, as noted above, it has reached the maximum borrowing capacity under its statutory debt ceiling.

Available liquidity (cash and short term investments, plus available borrowing capacity) has increased by approximately $6 billion from the reported 2012 low. This improvement would not have occurred had the Postal Service not defaulted on the annual PSRHBF prefunding payments in 2012 and subsequent years. Aside from the defaults, the improvement is largely attributable to the temporary exigent surcharge (discussed in greater detail below) which generated approximately $4.6 billion in incremental revenue from January 2014 through April 10, 2016, as well as to aggressively managing capital expenditures and operating expenses under management's control. Despite this increase in the Postal Service's liquidity, unrestricted cash remains insufficient to support an organization that has already defaulted on $33.9 billion in PSRHBF payments, projects continuing losses and has approximately $77 billion in annual operating expenses.

The Postal Service incurred a net loss of $5.6 billion for the year ended September 30, 2016, and has incurred cumulative net losses of $62.4 billion since 2007. As a result of these losses and its liquidity concerns, the Postal Service does not have sufficient cash balances to meet all of its existing legal obligations, pay down its debt and make all of the critical investments in its infrastructure that have been deferred in recent years.

In the event that circumstances leave the Postal Service with insufficient cash, it 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 other U.S. government entities, as has been done in the past.

Mail Migration to Alternatives

A significant factor contributing to Postal Service losses is the ongoing decline in the volume of *First-Class Mail*, which generates a higher contribution than other classes of mail. This decline is largely the result of changes in consumers' and businesses' use of mail resulting from the continuing migration to electronic communication and transactional alternatives, which was exacerbated by the Great Recession. Also contributing to losses is the increase in the number of delivery points, which, when combined with the impact of the reduction in hard-copy mail volume, has resulted in a drop in the average number of pieces delivered per delivery point per day from approximately 5.5 pieces in 2007 to 3.7 pieces in 2016, a decline of approximately 32%.

Expiration of Exigent Surcharge

In December 2013, after a successful appeal by the Postal Service to the U.S. Court of Appeals for the District of Columbia Circuit (the "Court") of an earlier decision in which the PRC denied outright the request of the Postal Service for exigent price relief, the PRC decided that the Postal Service could collect a 4.3% exigent surcharge on most Market-Dominant services beginning in January 2014. This original authorization by the PRC allowed the Postal Service to collect the exigent surcharge until such time as it produced $3.2 billion in incremental revenue, a figure the PRC determined was lost due to the Great Recession's suppression of mail volume.

The Postal Service again appealed the PRC's decision to the Court, arguing that the PRC attributed far too little lost mail volume to the Great Recession and that the surcharge should remain in effect for a longer period of time. In June 2015, the Court issued its decision and remanded the case back to the PRC for further review. Although the Court largely upheld the PRC's analytical framework, it vacated one key aspect of the methodology for calculating mail volume lost due to the Great Recession and suggested the PRC could reconsider another element of its methodology. On July 29, 2015, the PRC announced that it had authorized the Postal Service to collect over $1.4 billion in additional incremental revenue from the surcharge, bringing the total allowed to just over $4.6 billion. That decision was also appealed to the Court and remains pending.

The Postal Service reduced the prices of applicable Market-Dominant services on April 10, 2016, the date the limit on the amount of exigent surcharge collected was reached.

Business Model Challenges/Constraints

The Postal Service continues to incur significant losses, in part due to the PAEA-mandated PSRHBF prefunding requirement. Such a requirement to prefund retiree healthcare obligations is not imposed on most other federal entities or private-sector businesses that even offer retiree health benefits.

As of September 30, 2016, the Postal Service has accrued $33.9 billion of prefunding payments that were due but not paid since 2012 due to insufficient liquidity. As of the date of this report, the Postal Service has not incurred any penalties or negative consequences as a result of not making the PSRHBF prefunding payments. In addition to the prefunding requirement, the Postal Service continues to pay and expense the employer share of health insurance premiums for its retirees, which was $3.3 billion, $3.1 billion and $3.0 billion for the years ended September 30, 2016, 2015 and 2014, respectively.

With the exception of the exigent surcharge discussed above, Market-Dominant services, which account for approximately 74% of the Postal Service's annual operating revenues, are subject to a price cap based on the Consumer Price Index for All Urban Consumers ("CPI-U"). While the vast majority of revenues are constrained by the price cap, costs are not statutorily constrained. Contractual obligations granting general wage increases, step increases, COLAs, along with increases in costs for mandatory federal benefits programs, such as health and retirement benefits, have continued to escalate, thereby increasing expenses. Increases in retirement costs and retiree health benefits, excluding FERS supplemental liability payment, added approximately $600 million to 2016 annual expenses. Additionally, the Postal Service adds approximately one million delivery points each year which drives up our delivery costs.

Not later than September 30, 2017, the Postal Service will begin paying the "normal costs" of retiree health benefits (i.e., the present value of the estimated retiree health benefits attributable to active employees' current year of service). Although 2016 was the final year of statutorily-fixed amounts of PSRHBF prefunding payments, the statute requires that OPM perform an actuarial valuation no later than June 30, 2017, to determine the amount of additional payments into the fund that will be required to amortize the unfunded liability of the PSRHBF by 2056. The Postal Service is also obligated to begin paying any required amortization of the unfunded PSRHBF liability by September 30, 2017. The Postal Service estimates that the obligation for normal costs and the amortization of the unfunded PSRHBF liability will be at least $5.8 billion annually. The Postal Service also estimates that it may be required to pay approximately $1.2 billion annually to amortize the unfunded liability of the CSRS beginning as soon as 2017. This matter is under review by the Office of Legal Counsel at the U.S. Department of Justice, to confirm whether the CSRS payments should begin in 2017 or 2018. Given Postal Service's limited liquidity, it may be forced to default on some or all of these obligations in order to continue to fulfill its mandate to provide postal services to the nation.

Postal Service Actions Taken to Improve Liquidity

The Postal Service continues to pursue strategies within its control to increase operational efficiency and improve liquidity. The Postal Service has conserved capital in recent years by spending only what it believed essential to maintain its existing facilities and service levels. However, an increase of capital investment is necessary to upgrade its facilities, its existing fleet of vehicles, and its processing equipment in order to remain operationally viable.

The Postal Service continues to pursue legislation that will enable it to increase revenue and reduce costs. Initiatives include reforms that would establish a set of health care plans that would fully integrate with Medicare for current and future Postal Service retirees, largely eliminating the current unfunded liability and the necessity for the prefunding requirement.

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 of approximately $71 billion, a financially-sound Postal Service continues to be vital to U.S. commerce.

The U.S. economy benefits greatly from the Postal Service and the many businesses that provide the printing and mailing services that it supports. Disruption of the mail would cause undue hardship to businesses and consumers, and in the event of a cash shortfall, the U.S. government would likely prevent the Postal Service from significantly curtailing or ceasing 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 its financial stability.

NOTE 3 - RELATED PARTIES

The Postal Service conducts significant transactions with other U.S. government entities, which are considered related parties.

The following table presents related-party assets and liabilities as of September 30, 2016, and 2015:

(in millions)	September 30, 2016	September 30, 2015
Related-party assets:		
Receivables and advances[1]	$ 40	$ 100
Carrying amount of revenue forgone installment receivable[2]	405	413
Related-party liabilities:		
Current portion of debt	$ 10,100	$ 10,100
Other current liabilities[3]	36,509	29,871
Noncurrent portion of debt	4,900	4,900
Other noncurrent liabilities[4]	18,638	17,473

[1] Included within *Receivables, net* in the accompanying Balance Sheets.
[2] Included within *Other assets* in the accompanying Balance Sheets.
[3] Amounts include PSRHBF obligations and current workers' compensation obligations.
[4] Amounts include noncurrent workers' compensation obligations.

The following table presents related-party revenue and expenses for the years ended September 30, 2016, 2015 and 2014:

(in millions)	2016	2015	2014
Related-party operating revenue[1]	$ 1,054	$ 999	$ 918
Related-party operating expenses[2]	18,830	18,136	17,271
Related-party interest income[3]	31	23	23
Related-party interest expenses[4]	195	182	182

[1] Included within *Operating revenue* in the accompanying Statements of Operations.
[2] Included within *Operating expenses* in the accompanying Statements of Operations.
[3] Imputed on the revenue forgone installment receivable or generated on cash equivalents held with the Federal Reserve Bank of New York or short-term investments in U.S. Treasury instruments. Included within *Interest and investment income* in the accompanying Statements of Operations.
[4] Incurred on debt issued to the Federal Financing Bank, and included within *Interest expense* in the accompanying Statements of Operations.

NOTE 4 - RECEIVABLES AND MAJOR CUSTOMERS

The Postal Service's operations are conducted primarily in the domestic market, with international revenue representing 3.8%, 3.9% and 4.3% of operating revenue for the years ended September 30, 2016, 2015 and 2014, respectively. For the years ended September 30, 2016, 2015 and 2014, combined revenue from the Postal Service's three largest customers (excluding mail service providers) represented approximately 5.8%, 5.1% and 4.1% of operating revenue, respectively.

The following table details *Receivables, net* from the accompanying Balance Sheets as of September 30, 2016, and 2015:

(in millions)	2016	2015
Foreign countries	$ 776	$ 585
U.S. government	34	100
Other	302	302
Receivables before allowances	1,112	987
Less: Allowances	70	57
Receivables, net	**$ 1,042**	**$ 930**

Receivables from foreign countries were 69.8% and 59.3% of the total receivables before allowances as of September 30, 2016, and 2015, respectively. The largest receivable was from China, which represented 36.2% and 34.0% of the total foreign balance outstanding in 2016 and 2015, respectively. U.S. government receivables consist primarily of appropriations receivables of $14 million and $57 million, and military and official mail receivables of $24 million and $41 million as of September 30, 2016, and 2015, respectively.

Total provisions for allowances charged to expense for the years ended September 30, 2016, 2015 and 2014 were $22 million, $10 million and $11 million, respectively, and are included within *Other operating expenses* in the accompanying Statements of Operations.

NOTE 5 - PROPERTY AND EQUIPMENT, NET

Assets within *Property and equipment, net* are recorded at cost, which includes the interest on borrowings used to pay for the construction of major capital additions, less allowances for depreciation and amortization. Interest capitalized during the years ended September 30, 2016, and 2015, was not significant. Assets within *Property and equipment, net* are depreciated over estimated useful lives that range from 3 to 40 years using the straight-line method.

The following table provides details for *Property and equipment, net* from the accompanying Balance Sheets as of September 30, 2016, and 2015:

(in millions, except years)	Estimated Life in Years	2016	2015
Buildings	3 - 40	$ 24,704	$ 24,622
Equipment	3 - 20	15,626	15,990
Vehicles	5 - 24	4,098	3,702
Land	-	2,840	2,850
Leasehold improvements	3 - 20	1,443	1,404
Property and equipment, at cost		**$ 48,711**	**$ 48,568**
Less: Accumulated depreciation and amortization		34,210	33,403
Construction in progress		795	521
Property and equipment, net		**$ 15,296**	**$ 15,686**

Gains recognized on assets sold are reported in *Other revenue* within the accompanying Statements of Operations. For the years ended September 30, 2016, 2015 and 2014, total gains, including the amortization of deferred gains noted below, were approximately $58 million, $124 million and $53 million, respectively.

The Postal Service defers gains when it enters into any lease-back arrangements or contractual obligations requiring continued Postal Service involvement with the property. Total deferred gains on the sale of property were $404 million and $301 million as of September 30, 2016, and 2015, respectively. The current portions of deferred gains were $11 million and $2 million as of September 30, 2016, and 2015, respectively, and are included within *Other current liabilities* in the accompanying Balance

Sheets. The noncurrent portions of deferred gains were $393 million and $299 million as of September 30, 2016, and 2015, respectively, and are included within *Other noncurrent liabilities* in the accompanying Balance Sheets.

Deferred gains are amortized over the periods during which the Postal Service has continuing involvement with the applicable properties. The amounts amortized, included within *Other revenue* in the accompanying Statements of Operations, were $9 million, $49 million and $8 million for the years ended September 30, 2016, 2015 and 2014, respectively.

Impairment charges were $17 million, $19 million and $62 million for the years ended September 30, 2016, 2015 and 2014, respectively, and are included in *Other operating expenses* in the accompanying Statements of Operations.

Depreciation and amortization expenses were approximately $1.7 billion, $1.8 billion and $1.8 billion for the years ended September 30, 2016, 2015 and 2014, respectively, and are included within *Other operating expenses* in the accompanying Statements of Operations.

Capitalized software totaled $98 million and $43 million as of September 30, 2016, and 2015, respectively. No software costs were capitalized in 2014. Amortized costs were $6 million as of September 30, 2016. The Postal Service did not amortize any costs associated with capitalized software during 2015 or 2014, as no capitalized software was put into production during those years.

Assets classified as held for sale were approximately $43 million and $65 million as of September 30, 2016, and 2015, respectively, and are included within both *Land* and *Buildings* in the table above.

NOTE 6 - PAYABLES, ACCRUED EXPENSES AND DEFERRED REVENUE

Payables and Accrued Expenses

The following table provides details for *Payables and accrued expenses* from the accompanying Balance Sheets as of September 30, 2016, and 2015:

(in millions)	2016	2015
Trade payables	$ 707	$ 663
Foreign countries	453	498
U.S. government	96	95
Other accrued expenses	636	597
Total payables and accrued expenses	**$ 1,892**	**$ 1,853**

Deferred Revenue–Prepaid Postage

Deferred revenue for postage sales is developed and validated through complex mathematical and statistical sampling methods for estimating postage stamp usage. The estimated postage stamp usage is subtracted from stamp sales with the difference representing the Postal Service's obligation to perform future services. That obligation is reduced by recognizing a provision for postage sold that may never be used, either through loss, damage or stamp-collecting activity.

Metered postage is primarily used by businesses. Deferred revenue related to meters is estimated by monitoring the actual usage of all postage meters that had postage added during the month preceding the financial measurement date. The information from the two most recent meter readings is used to derive a deferral percentage, which is applied to all postage meter receipts for the month.

During 2016, the Postal Service revised the estimation technique utilized to estimate its *Deferred revenue-prepaid postage* liability for *Forever Stamps*. The change resulted from new information regarding customer's retention and usage habits of applicable postage, and enabled the Postal Service to update its estimate of stamps that will never be used for mailing. As a result of this change, *Deferred revenue-prepaid postage* was decreased by nearly $1.1 billion. In accordance with GAAP, the change was accounted for as a change in accounting estimate, and was reflected in operating results as an increase to revenue and a decrease to net loss by the same amount in the year ended September 30, 2016.

Included in the estimate of *Deferred revenue–prepaid postage* is an estimate for mail that is in-transit within the Postal Service processing and delivery network. The following table provides details for *Deferred revenue–prepaid postage* from the accompanying Balance Sheets as of September 30, 2016, and 2015:

(in millions)		2016		2015
Forever stamps	$	1,253	$	2,304
Mail in-transit		506		520
Meters		380		349
Other		114		131
Total deferred revenue-prepaid postage	**$**	**2,253**	**$**	**3,304**

NOTE 7 - DEBT

Under the *Postal Reorganization Act*, as amended by Public Laws 101-227 and 109-435, the Postal Service can issue debt obligations. The Postal Service is limited by statute to net annual debt increases of $3.0 billion, and total debt may not exceed $15.0 billion. Postal Service debt is issued to the Federal Financing Bank ("FFB"), a government-owned corporation under the general supervision of the Secretary of the Treasury.

The Postal Service has two revolving credit line facilities, renewable annually with the FFB, both of which have been extended until April 2017. One facility, a short-term credit line, enables the Postal Service to draw up to $3.4 billion with two days prior notice. Borrowings under this credit line are typically on an overnight basis, but can have a maximum term of up to one year. The second credit line, which only allows for borrowings on an overnight basis, enables borrowings of up to $600 million on the same business day that funds are requested. The interest rates for borrowings under these credit facilities are determined by the U.S. Treasury each business day. As of September 30, 2016, these two revolving credit facilities were fully drawn.

Additionally, under the provisions of a note purchase agreement with the FFB, the Postal Service can issue a series of notes with varying provisions with two days prior notice. The note purchase agreement, renewable annually, was extended to September 30, 2017.

These credit line facilities and note arrangements provide the flexibility to borrow short or long-term, using floating or fixed-rate instruments. Fixed-rate notes can be either callable or non-callable at the option of the Postal Service. All of the Postal Service's debt is unsecured, not subject to sinking fund requirements and can be repaid at any time at a price determined by the Secretary of the Treasury based on prevailing interest rates in the U.S. Treasury security market at the time of repayment. As of September 30, 2016, the premium associated with a prepayment of all debt was $598 million based on prevailing interest rates. The weighted average interest rate for all outstanding debt was 1.395% as of September 30, 2016.

The following table provides details for *Current portion of debt* and *Noncurrent portion of debt* from the accompanying Balance Sheets as of September 30, 2016, and 2015:

(in millions, except percentages)	2016		2015	
Maturity	**Balance**	**Rate %**	**Balance**	**Rate %**
Current portion of debt:				
Fixed rate notes:				
October 15, 2015	$ —		$ 700	0.219
November 12, 2015	—		1,300	0.248
December 10, 2015	—		700	0.359
January 7, 2016	—		300	0.278
March 24, 2016	—		500	0.221
April 28, 2016	—		1,200	0.379
May 2, 2016	—		300	2.844
June 23, 2016	—		500	0.413
June 23, 2016	—		600	0.413
October 13, 2016	700	0.425	—	
November 10, 2016	1,300	0.603	—	
December 8, 2016	700	0.773	—	
January 5, 2017	300	0.588	—	
January 26, 2017	500	0.547	—	
March 2, 2017	500	0.757	—	
April 27, 2017	700	0.737	—	
May 25, 2017	300	0.782	—	
June 22, 2017	600	0.593	—	
August 17, 2017	500	0.732	—	
Current revolving credit line:				
October 3, 2016	3,400	0.267	3,400	0.125
Overnight revolving credit line:				
October 3, 2016	600	0.318	600	0.125
Total current portion of debt	**10,100**		**10,100**	
Noncurrent portion of debt - fixed rate notes:				
November 15, 2018	500	3.048	500	3.048
February 15, 2019	700	3.296	700	3.296
May 15, 2019	1,000	3.704	1,000	3.704
May 15, 2019	500	3.513	500	3.513
August 16, 2021	1,000	2.066	1,000	2.066
May 17, 2038	200	3.770	200	3.770
February 15, 2039	1,000	3.790	1,000	3.790
Total noncurrent portion of debt	**4,900**		**4,900**	
Total debt	**$ 15,000**		**$ 15,000**	

At September 30, 2016, scheduled repayments of debt principal are listed below:

(in millions)		Principal Amount
2017	$	10,100
2018		—
2019		2,700
2020		—
2021		1,000
Thereafter		1,200
Total debt maturities	**$**	**15,000**

NOTE 8 - COMMITMENTS AND CONTINGENCIES

Leases

The Postal Service leases premises and equipment under operating and capital leases generally having terms from 1 to 20 years with options to renew. Certain non-cancellable real estate leases have purchase options at prices specified in the leases. The following table provides details for total rental expense for the years ended September 30, 2016, 2015 and 2014:

(in millions)		2016		2015		2014
Non-cancellable real estate leases[1]	$	908	$	915	$	918
GSA facilities leases[2]		31		33		35
Equipment and other short-term rentals		155		155		139
Total rental expense	**$**	**1,094**	**$**	**1,103**	**$**	**1,092**

[1] Sublease income was not material to the financial statements for the years ended September 30, 2016, 2015 and 2014.

[2] General Services Administration leases subject to 120-day cancellation notice.

Future minimum payments for all non-cancellable leases with original lease terms greater than one year are set forth below:

(in millions)		Operating		Capital
2017	$	781	$	82
2018		761		68
2019		711		53
2020		658		39
2021		608		25
Thereafter		3,910		59
Total lease obligations	**$**	**7,429**	**$**	**326**
Less: Interest				70
Total capital lease obligations			**$**	**256**
Less: Current portion of capital lease obligations				63
Noncurrent portion of capital lease obligations			**$**	**193**

Capital leases, recorded at historical cost within *Property and equipment, net* in the accompanying balance sheets, were $766 million and $812 million as of September 30, 2016, and 2015, respectively. Total accumulated amortization related to capital leases was $587 million and $593 million at September 30, 2016, and 2015, respectively. Amortization expense for capital leases was approximately $42 million, $44 million and $44 million for the years ended September 30, 2016, 2015 and 2014, respectively and are included within *Other operating expense* in the accompanying Statements of Operations.

Capital Commitments

Capital commitments consist primarily of commitments to invest in equipment and building construction and improvements. The following table provides details for approved capital projects in progress at September 30, 2016, and 2015:

(in millions)	2016	2015
Mail processing equipment	$ 264	$ 333
Building improvements, construction and building purchase	396	309
Postal support equipment	120	85
Vehicles and other	359	561
Total capital commitments	**$ 1,139**	**$ 1,288**

Contingent Liabilities

The Postal Service's contingent liabilities consist primarily of claims resulting from labor, employment, environmental matters, property damage and injuries on Postal Service properties, and issues arising from Postal Service contracts, personal claims and traffic accidents. Each quarter, the Postal Service evaluates each new claim to determine if it is probable of an unfavorable outcome and if the amount of the potential resolution is reasonably estimable. If so, a liability for the amount is recorded. Preexisting claims are also reviewed and adjusted quarterly for resolutions or revisions to prior estimates.

Provision for Losses

The Postal Service has made adequate provision for probable losses arising from all claims. The following table presents contingent liabilities by current and noncurrent portions and by category, as of September 30, 2016, and 2015:

(in millions)	2016	2015
Current/noncurrent portions of contingent liabilities:		
Current portion[1]	$ 166	$ 132
Noncurrent portion[2]	498	594
Total contingent liabilities	**$ 664**	**$ 726**
Contingent liabilities by category:		
Labor and employment matters	$ 565	$ 637
Asset retirement obligations	47	47
Tort matters	48	38
Contractual matters	4	4
Total contingent liabilities	**$ 664**	**$ 726**

[1] Included within *Payables and accrued expenses* in the accompanying Balance Sheets.
[2] Included within *Other noncurrent liabilities* in the accompanying Balance Sheets.

In addition to the amounts accrued in the financial statements, the Postal Service is subject to other claims and lawsuits which it deems reasonably possible of an unfavorable outcome, which ranged from $225 million to $950 million and from $185 million to $686 million at September 30, 2016, and 2015, respectively. The Postal Service has not recorded accruals for these reasonably possible losses in its financial statements. The Postal Service is from time to time involved in other litigation incidental to the conduct of its business, none of which is expected to be material to its business, financial condition or operations.

Class Action Litigation

As previously reported, on January 14, 2010, the Equal Employment Opportunity Commission's Office of Federal Operations certified the case *McConnell v. Brennan* (first instituted in 2006 as *McConnell v. Potter*) as a class action against the Postal Service, with the class consisting of all permanent-rehabilitation and limited-duty Postal Service employees who were assessed under the Postal Service's National Reassessment Process ("NRP") between the dates of May 5, 2006, and July 1, 2011. The

NRP was a program the Postal Service utilized to ensure that its records regarding employees injured on the job were correct and that employees receiving workers' compensation benefits were placed in jobs consistent with their abilities.

The case alleges violations of the *Rehabilitation Act of 1973* resulting from the NRP's failure to provide a reasonable accommodation, the NRP's wrongful disclosure of medical information, the creation by the NRP of a hostile work environment, and the NRP's adverse impact on disabled employees. The class is seeking injunctive relief and damages of an uncertain amount. If the plaintiffs were able to prove their allegations in this matter and to establish the damages they assert, an adverse ruling could have a material impact on the Postal Service. The Postal Service continues to dispute the claims asserted in the case and is vigorously contesting the matter.

Collective Bargaining Agreements

In April 2016, the Postal Service reached a new three-year collective bargaining agreement with the NRLCA which was ratified by its membership. The new contract includes general wage increases totaling 3.8% over three years (1.2% of which was retroactive to November 2015) with a COLA base month of July 2014 (no retroactive COLA payments), a reduction in the employer share of health insurance premiums, beginning in the 2017 plan year, and the creation of a new non-career employee category to provide weekend and holiday parcel deliveries. The contract will expire on May 20, 2018.

In July 2016, an interest arbitration decision was issued and an arbitrated contract was awarded that established a collective bargaining agreement between the Postal Service and the APWU. The contract, which will expire on September 20, 2018, was the result of a legally-mandated binding arbitration process that was required when the parties reached impasse in negotiating a new collective bargaining agreement after the prior agreement expired in May 2015. The new contract includes general wage increases totaling 3.8% over three years (1.2% of which was retroactive to November 2015) with a COLA base month of July 2014 (no retroactive COLA payments), a reduction in the employer share of health insurance premiums, beginning in the 2017 plan year, and annual increases in uniform and work clothing allowances. The award also converted approximately 5,000 non-career positions to career positions.

In May 2016, the Postal Service agreed to extend contract negotiations on new collective bargaining agreements with both the NALC and the NPMHU. The contracts with NALC and NPMHU each expired on May 20, 2016, and the respective parties mutually agreed to extend negotiations beyond the deadline, and these negotiations were continuing as of September 30, 2016.

NOTE 9 - RETIREMENT PLANS

The majority of career employees participate in one of two U.S. government pension programs, the Civil Service Retirement System ("CSRS") and the Federal Employees Retirement System ("FERS"), which are administered by OPM. These plans provide for retirement, death and termination benefits for eligible employees based on specific eligibility and participation requirements, vesting periods and benefit formulas. Each employee's participation in either plan is based on the starting date of employment with the Postal Service or other U.S. government entity.

As government-sponsored benefit plans, CSRS and FERS are not subject to the provisions of the *Employee Retirement Income Security Act of 1974*, as amended. Likewise, because the Postal Service cannot direct the costs, benefits or funding requirements of these plans, it accounts for program expenses under multiemployer plan accounting rules. As such, the Postal Service records contributions to the plans as an expense in the period in which each contribution is due. Additionally, annual funding requirements can fluctuate significantly from year to year due to changes in federal law or determination by OPM.

CSRS provides a basic annuity plan benefit to employees hired before January 1, 1984. Dual CSRS provides Social Security benefits in addition to its basic annuity plan for employees hired between January 1, 1984 and January 1, 1987. CSRS and Dual CSRS employees may participate in the Thrift Savings Plan ("TSP"), a defined contribution savings and investment plan administered by the Federal Retirement Thrift Investment Board, although participants do not receive matching contributions from the Postal Service.

PAEA suspended the Postal Service's employer contributions to CSRS that would otherwise have been required under Title *5, Section 8334(a)(1)* of the U.S. Code until 2017, although CSRS employees continue to contribute to the plan. In 2017, OPM will determine whether additional funding is required by the Postal Service for the benefit of its CSRS participants. As a result of the suspension, the Postal Service's employer contribution rate for CSRS was zero for 2008 through 2016.

Effective January 1, 1987, FERS covers employees hired since December 31, 1983, and includes Social Security and TSP benefits in addition to its basic annuity plan. For most current FERS employees, the Postal Service's contribution rates of participating employees' base salaries were 13.7%, 13.2% and 11.9% for the years ended September 30, 2016, 2015 and 2014, respectively.

During 2016, 2015 and 2014, the Postal Service received separate notices from OPM requiring the Postal Service to make additional payments of $248 million, $241 million and $7 million, respectively, to the FERS benefit plan for the benefit of active employees, as well as retirees. In accordance with *Section 8423(b)* of Title 5 of the U.S. Code, the additional payment obligations are based on actuarial valuations and assumptions to supplement the FERS plan which are to be made in equal installments over the next 30 years. The annual increase in payment obligation was $7 million and $234 million for the years ended September 30, 2016, and 2015 respectively. The Postal Service recorded an expense for each year, however the payments were not made and a corresponding liability was accrued each year. The total outstanding amount of $496 million as of September 30, 2016, is included within *Compensation and benefits* in the accompanying Balance Sheets.

FERS 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 is required to contribute to the TSP for FERS employees by contributing an automatic 1% of basic pay and matching a percentage of voluntary employee contributions for up to an additional 4% of basic pay. During the years ended September 30, 2016, 2015 and 2014, the Postal Service recorded TSP expenses of $1.1 billion, $1.0 billion and $1.0 billion, respectively.

The following table provides details for the number of active employees enrolled in CSRS and FERS for the years ended September 30, 2016, 2015 and 2014:

	2016	2015	2014
CSRS and Dual CSRS	33,224	39,791	46,764
FERS	474,326	452,051	441,546
Total enrollment	**507,550**	**491,842**	**488,310**

Employee contributions for the past three years, as a percentage of employee basic pay, were 7.0% for CSRS and either 0.8%, 3.1% or 4.4% for FERS for those employees hired before, during, or after 2013, respectively.

The Postal Service's employer cash contributions to the FERS plan were $4.6 billion, $4.3 billion and $3.9 billion in 2016, 2015 and 2014, respectively. These cash contributions exclude both employee social security contributions and year-end unpaid employer amounts due. For each of 2016, 2015 and 2014, the Postal Service provided more than 5% of the total plan contributions for FERS from all employers (as disclosed in OPM's *Civil Service Retirement and Disability Fund Annual Report*).

The latest available actual data for the government-wide CSRS and FERS plans is September 30, 2014. As of that date, the CSRS plan for the U.S. government, taken as a whole, was less than 35% funded. Total plan assets and accumulated benefit obligations for the CSRS plan were approximately $340 billion and approximately $1.1 trillion, respectively. Total plan assets and accumulated benefit obligations for the Postal Service's portion of the CSRS plan were $182.1 billion and $201.5 billion, respectively. The FERS plan for the U.S. government, taken as a whole, was greater than 90% funded. Total plan assets and accumulated benefit obligations for the FERS plan were approximately $520 billion and approximately $570 billion, respectively. Total plan assets and accumulated benefit obligations for the Postal Service's portion of the FERS plan were $100.9 billion and $104.5 billion, respectively.

NOTE 10 - HEALTH BENEFITS PLANS

The Federal Employees Health Benefits ("FEHB") Program covers nearly all career employees and also covers non-career employees and retirees who meet certain eligibility requirements. OPM administers FEHB and allocates the cost of funding the program to participating U.S. government employers. The Postal Service cannot direct the costs, benefits or funding requirements of FEHB plans, and therefore accounts for program expenses using multiemployer plan accounting rules by recording contributions to the plans as an expense in the period in which the contributions are due. Although OPM determines the actual health benefits premium costs, the allocation of these costs between the Postal Service and most of its employees is determined through agreements with Postal Service labor unions.

In 2014, the Postal Service began to offer its own separate healthcare plan to certain non-career employees who are ineligible for FEHB. For the year ended September 30, 2016, 2015 and 2014, the Postal Service incurred expenses of $33 million, $18 million and $3 million, respectively, for this plan.

Active Employees

The Postal Service paid approximately 74%, 75% and 76% of FEHB premium costs for active employees during the years ended September 30, 2016, 2015 and 2014, respectively. Its employer share of employee healthcare expenses was $5.0 billion, $4.8 billion, and $4.8 billion for the years ended September 30, 2016, 2015 and 2014, respectively, and these amounts are included within *Compensation and benefits* under *Operating Expenses* in the accompanying Statements of Operations.

Retirees

Postal Service retirees who participated in FEHB for the five years immediately preceding their retirement may continue to participate in the plan during retirement. Qualifying survivors of retirees are also eligible to receive benefits. The Postal Service pays its employer portion of FEHB insurance premiums for participating retirees and their qualifying survivors, based on each retiree's length of federal civilian service occurring on or after July 1, 1971. For employees who began their federal civilian service before that date but retired after it, a prorated contribution is determined by OPM.

The PAEA required the Postal Service to prefund retiree health benefits during years 2007 through 2016 by paying annual amounts ranging from $1.4 billion to $5.8 billion, totaling $54.8 billion, into the PSRHBF. Most federal entities and private sector businesses are not subject to this type of prefunding requirement. Because the amounts to be paid into the PSRHBF are set by PAEA, retiree health benefits expense may represent more or less than the full cost of the benefits earned by Postal Service employees during any specific period.

The following table details retiree health benefits expense for the years ended September 30, 2016, 2015 and 2014:

(in millions)	2016	2015	2014
Retiree health benefits premiums	$ 3,305	$ 3,111	$ 2,985
PAEA prefunding expenses to PSRHBF	5,800	5,700	5,700
Total retiree health benefits	**$ 9,105**	**$ 8,811**	**$ 8,685**

Premium Expense

The Postal Service records premium expenses for retirees within *Retiree Health Benefits* under *Operating Expenses* in the accompanying Statements of Operations. The Postal Service's share of premium costs for retirees and qualifying survivors is set by law and is not subject to negotiation with its labor unions, and may therefore fluctuate significantly due to the passage of new federal law, or in some circumstances, as determined by OPM in its capacity as administrator.

PAEA requires that beginning in 2017, the Postal Service's employer portion of these premiums is to be paid from PSRHBF rather than directly by the Postal Service. Also beginning in 2017, the Postal Service will be required to pay the normal costs of retiree health benefits.

PSRHBF Prefunding

The Postal Service recorded PSRHBF prefunding expenses of $5.8 billion, $5.7 billion and $5.7 billion for the years ended September 30, 2016, 2015 and 2014, respectively, and these expenses are included within *Retiree health benefits* under *Operating Expenses* in the accompanying Statements of Operations. In accordance with GAAP, the Postal Service records an expense for its prefunding payments due regardless of whether the obligations are paid.

The Postal Service defaulted on its prefunding payments each year from 2012 through 2016 because it did not have the cash to make the payments and concurrently fulfill its other statutory obligations. Prior to each default, the Postal Service notified key stakeholders including the Administration and Congress of the imminent default. PAEA contains no provisions addressing a payment default, and as of the date of this report, the Postal Service has not been assessed any penalties.

The cumulative amounts of defaulted PSRHBF prefunding payments were $33.9 billion and $28.1 billion as of September 30, 2016, and 2015, respectively, and are recorded as *Retiree health benefits* under *Current Liabilities* in the accompanying Balance Sheets.

The PSRHBF fund balance as of September 30, 2016, as provided by OPM, was $51.9 billion, which is approximately 50% of the total accumulated retiree health benefit obligation of $104.0 billion, calculated by OPM in accordance with governmental accounting standards, as of the same date.

PAEA requires that OPM perform an actuarial valuation no later than June 30, 2017, to determine if additional payments into the PSRHBF are required. If this is the case, OPM must design an amortization schedule under which the Postal Service will be required to fund the actuarially-determined normal costs of retiree health benefits. We are also obligated to begin paying any required amortization of the unfunded liability in 2017. The amount of the future funding requirement could change at any time with the enactment of a new law or the amendment of existing law.

NOTE 11 - WORKERS' COMPENSATION

Postal Service employees injured on the job are covered by FECA, and the Postal Service reimburses DOL for workers' compensation benefits paid to or on behalf of Postal Service employees, plus an administrative fee.

Workers' Compensation Liability

The Postal Service records a liability for its workers' compensation obligations for employees who have been injured on the job and are eligible for benefits, or their qualified survivors. To determine the actuarial valuation of new and existing cases, the Postal Service uses an estimation model that combines four generally-accepted actuarial valuation techniques based upon past claim-payment experience and exposure to claims as measured by total employee hours worked.

Changes in the liability are primarily attributable to the combined impacts of routine changes in actuarial assumptions, new compensation and medical cases, the progression of existing cases and changes in discount (interest) and inflation rates, including long-term COLA rates for compensation claims and medical rates for medical claims. These rates are updated as of the Balance Sheet date and factored into the model in accordance with GAAP.

To determine the fair value of the liability each quarter, the Postal Service first estimates the future total cost of workers' compensation claims based on the dates of claim-related injuries, frequency or severity of the injuries, the pattern of historical payments to beneficiaries and the expected trend in future costs. The Postal Service then calculates the amount that would need to be invested at current discount (interest) rates to fully fund the future total cost of claims, and this calculated present value is the fair value of workers' compensation liability.

An independent actuary assists in determining the liability for claims arising more than 15 years ago for years 1972 through 2001. The percentage increase in payments between 15-year old claims and closure of all claims is applied to the latest 15 years' estimates directly calculated within the estimation model for both compensation and medical losses.

The liability calculation is highly sensitive to changes in discount rates. For example, a 1% increase in the discount rate would decrease the September 30, 2016, liability and related expense by approximately $2.2 billion. Similarly, a 1% decrease in the discount rate would increase the September 30, 2016, liability and related expense by approximately $2.7 billion.

The following table details inflation and discount rates used to estimate the liability as of September 30, 2016, 2015 and 2014:

	2016	2015	2014
Compensation claims liability:			
Discount rate	1.9%	2.4%	2.8%
Wage inflation	2.6%	2.7%	2.9%
Medical claims liability:			
Discount rate	1.9%	2.4%	2.7%
Medical inflation	5.5%	5.7%	9.0%

Workers' Compensation Expense

The impacts of changes in discount rates and inflation rates, as well as the actuarial valuation of new cases and revaluation of existing cases, are components of total workers' compensation expense as recorded in the accompanying Statements of

Operations. As described above, the Postal Service pays an administrative fee to the DOL, which is also a component of workers' compensation expense.

Included in the 2016 and 2015 workers' compensation expenses are prescription drug charges of which $173 million and $99 million, respectively, are for pharmacy-compounding costs. The Postal Service disputed these compounding cost charges and initially withheld $69 million from its October 2015 payment to the DOL, which ultimately was paid in accordance with legal requirements, and withheld $151 million from its October 2016 payment to the DOL. These disputed amounts as of September 30, 2016, and 2015, are included as part of the current liability within *Workers' compensation costs* in the accompanying Balance Sheets.

The table below details the components of workers' compensation expense for the years ended September 30, 2016, 2015 and 2014:

(in millions)		2016		2015		2014
Impact of discount rate changes	$	1,026	$	809	$	485
Actuarial revaluation of existing cases		(113)		(886)		45
Costs of new cases		1,697		1,767		1,956
Administrative fee		72		70		68
Total workers' compensation expense	**$**	**2,682**	**$**	**1,760**	**$**	**2,554**

2015 Workers' Compensation Change in Accounting Estimate

The Postal Service revised the calculation used in its valuation model to determine the actuarial revaluation of existing cases beginning in the first quarter of 2015. The impact of the change in estimate decreased the workers' compensation liability and corresponding expense by $353 million in the first quarter of 2015 and for the year ended September 30, 2015. This was considered a change in accounting estimate under GAAP. Management believes this change better reflects current injury trends and provides the best estimate of workers' compensation liability at that date.

NOTE 12 - REVENUE FORGONE

The Postal Service has historically offered below-cost postage prices to certain categories of mailers, including, but not limited to, non-profit organizations, blind individuals, local newspapers, publishers of educational material and oversees mailers of absentee voting ballots. Between 1971, when the Postal Service became independent, and 1991, Congress reimbursed the Postal Service for the revenue it had "forgone" by offering below-cost postage prices to these mailers.

The *Revenue Forgone Reform Act of 1993* (the "RFA") phased in higher postage prices for certain of these mailers, retaining "free and reduced mail" only for the blind and for overseas absentee ballots. The RFA also authorized $1.2 billion to be paid to the Postal Service in 42 annual "installment" payments of $29 million each from 1994 through 2035 as reimbursement for revenue forgone during the RFA's 1991-to-1998 phase-in period.

Installment Payments

The Postal Service has recognized the present value of the installment payments as revenue and recorded a corresponding receivable, which is reduced each year that the installment payment is received. Although the RFA authorized the reimbursement, the Postal Service must submit an appropriation request to Congress each year in order to receive the annual revenue forgone payment.

During both 2016 and 2015, the Congress appropriated and paid $29 million for each of the respective annual installments. However for the years 2011 through 2014, some or all of these installment amounts were not appropriated and therefore not received by the Postal Service. The total unfunded amount was $104 million as of September 30, 2016, and is included within *Receivables, net* in the accompanying Balance Sheets. The Postal Service includes the total past-due installments in each annual appropriations request.

Outstanding receivables associated with the installment payments were $405 million and $413 million as of September 30, 2016, and 2015, respectively. These are not expected to be paid within one year due to the prolonged appropriation process, and are therefore classified as noncurrent within *Other assets* in the accompanying Balance Sheets.

The Postal Service recognized interest income of $22 million for each of the years ended September 30, 2016, 2015 and 2014, respectively, for interest imputed on the outstanding receivable for the installment payments, and this imputed interest is included within *Interest and investment income* in the accompanying Statements of Operations.

Free and Reduced Mail

Congress has historically appropriated funds each year for free and reduced mail, however the annual appropriation may be higher or lower than the amount the Postal Service requests. At the end of each fiscal year, any difference between the actual amount Congress appropriated and actual amounts the Postal Service incurred to provide the subsidy during prior periods is reflected through an adjustment of the following year's funding request. Likewise, the Postal Service recognizes revenue based upon the actual amounts the Postal Service incurred to provide the subsidy during the year.

For free and reduced mail, the Postal Service recognized revenue of $59 million, $63 million and $52 million for the years ended September 30, 2016, 2015 and 2014, respectively, and this is included within *Operating Revenue* in the accompanying Statements of Operations. Outstanding receivables associated with free and reduced mail were $14 million and $57 million as of September 30, 2016, and 2015, respectively. These are expected to be paid within one year, and are therefore classified as current within *Receivables, net* in the accompanying Balance Sheets.

NOTE 13 - FAIR VALUE MEASUREMENT

The Postal Service defines fair value based on the price that would be received upon sale of an asset or the price that would be paid to transfer a liability between unrelated parties.

The carrying amounts of certain current assets and liabilities, including cash, accounts receivable, accounts payable, accrued expenses and the current portion of debt, approximate fair value due to their short-term nature. Assets within *Property and equipment, net* are recorded at cost and measured at fair value on a nonrecurring basis if they are determined to be impaired or classified as assets held for sale.

Noncurrent receivables and noncurrent debt are measured using inputs of the fair value hierarchy. This model prioritizes observable and unobservable inputs used to measure fair value, and consists of three broad levels, 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 observable data, such as 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.

Considerable judgment is involved in using this model to determine estimates of fair value and, accordingly, they may not necessarily be indicative of amounts that would be realized upon disposition of a specific asset or liability.

For the years ended September 30, 2016, and 2015, no significant transfers between *Level 1* and *Level 2* assets or liabilities occurred. The carrying amounts and fair value of these items are presented for disclosure purposes only in the following table:

	2016		2015	
(in millions)	**Carrying Amount**	**Fair Value**	**Carrying Amount**	**Fair Value**
Revenue forgone installment receivable*	$ 405	$ 527	$ 413	$ 511
Noncurrent portion of debt	$ 4,900	$ 5,492	$ 4,900	$ 5,394

* The carrying amount is included within *Other assets* (which includes items in addition to revenue forgone) in the accompanying Balance Sheets.

The revenue forgone installment receivable qualifies as a financial instrument in accordance with authoritative literature. To calculate its fair value, the Postal Service recognizes the imputed interest it is owed as interest income and estimates the value of this receivable using the interest method, which converts future cash flows to a single discounted amount using interest rates for similar assets, which are considered *Level 2* inputs. The Postal Service then calculates the net present value of anticipated annual installment payments to be received, discounted by the 20-year U.S. Treasury Constant Maturity Rate, which was 1.99% and 2.60% as of September 30, 2016, and 2015, respectively.

The noncurrent portion of debt also qualifies as a financial instrument. Because no active market exists for the Postal Service's debt with the FFB, the fair value of the noncurrent portion of this liability has been estimated using expected future payments at risk-adjusted discount rates provided by the FFB, considered *Level 3* inputs.

NOTE 14 - QUARTERLY FINANCIAL DATA (UNAUDITED)

The following table sets forth the Postal Service's unaudited *Statements of Operations* for the quarterly periods ending September 30, 2016, and 2015:

	2016			
(in millions)	**Quarter 1**	**Quarter 2**	**Quarter 3***	**Quarter 4**
Total revenue	$ 19,359	$ 17,767	$ 17,718	$ 16,654
Total operating expenses	19,002	19,760	19,237	18,900
Income (loss) from operations	357	(1,993)	(1,519)	(2,246)
Interest income (expense), net	(50)	(47)	(48)	(45)
Net income (loss)	**$ 307**	**$ (2,040)**	**$ (1,567)**	**$ (2,291)**
	2015			
	Quarter 1	**Quarter 2**	**Quarter 3**	**Quarter 4**
Total revenue	$ 18,761	$ 16,970	$ 16,555	$ 16,642
Total operating expenses	19,475	18,399	17,101	18,851
Loss from operations	(714)	(1,429)	(546)	(2,209)
Interest income (expense), net	(40)	(40)	(40)	(42)
Net loss	**$ (754)**	**$ (1,469)**	**$ (586)**	**$ (2,251)**

* Includes a nearly $1.1 billion change in accounting estimate, which was reflected in operating results as an increase to total revenue and a decrease to loss from operations and net loss by the same amount.

ITEM 9. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE

None.

ITEM 9A. CONTROLS AND PROCEDURES

DISCLOSURE CONTROLS AND PROCEDURES

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 PAEA and that this information is accumulated and communicated to 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 September 30, 2016. 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.

CHANGES IN INTERNAL CONTROL OVER FINANCIAL REPORTING

There were no changes in the our internal controls over financial reporting during the quarter ended September 30, 2016, that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

MANAGEMENT'S REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING

Our management is responsible for establishing and maintaining adequate controls over financial reporting. Internal control over financial reporting is a process to provide reasonable assurance regarding the reliability of our financial reporting for external purposes in accordance with GAAP. Internal control over financial reporting includes maintaining records that, in reasonable detail, accurately and fairly reflect our transactions, providing reasonable assurance that transactions are recorded as necessary for the preparation of our financial statements, providing reasonable assurance that receipts and expenditures of assets are made in accordance with management authorization and providing reasonable assurance that unauthorized acquisition, use, or disposition of assets that could have a material effect on our financial statements would be prevented or detected on a timely basis. Because of its inherent limitations, internal control over financial reporting is not intended to provide absolute assurance that a misstatement of our financial statements would be prevented or detected.

Management conducted an evaluation of the effectiveness of our internal control over financial reporting based on the framework in *Internal Control – Integrated Framework (2013)* issued by the Committee of Sponsoring Organizations of the Treadway Commission. Based on this evaluation, management concluded that our internal control over financial reporting was effective as of September 30, 2016.

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

The Temporary Emergency Committee of the Board of Governors of the United States Postal Service

We have audited the United States Postal Service's internal control over financial reporting as of September 30, 2016, based on criteria established in Internal Control - Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (2013 framework) (the COSO criteria). The United States Postal Service's management is responsible for maintaining effective internal control over financial reporting, and for its assessment of the effectiveness of internal control over financial reporting included in the accompanying Management's Report on Internal Control Over Financial Reporting. Our responsibility is to express an opinion on the United States Postal Service's internal control over financial reporting based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States) and in accordance with attestation standards established by the American Institute of Certified Public Accountants. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, testing and evaluating the design and operating effectiveness of internal control based on the assessed risk, and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

A company's internal control over financial reporting is a process designed 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. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of the inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, the United States Postal Service maintained, in all material respects, effective internal control over financial reporting as of September 30, 2016, based on the COSO criteria.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the auditing standards generally accepted in the United States of America, and the standards applicable to financial audits contained in *Government Auditing Standards*, the balance sheets of the United States Postal Service as of September 30, 2016 and 2015, and the related statements of operations, changes in net deficiency, and cash flows for each of the three years in the period ended September 30, 2016 of the United States Postal Service and our report dated November 15, 2016 expressed an unqualified opinion thereon that included an explanatory paragraph regarding the United States Postal Service's ability to generate sufficient cash flow to meet all of its financial obligations throughout their fiscal year ending September 30, 2017.

/s/ Ernst & Young LLP

McLean, Virginia
November 15, 2016

ITEM 9B. OTHER INFORMATION

None.

PART III

ITEM 10. DIRECTORS, EXECUTIVE OFFICERS AND CORPORATE GOVERNANCE

BOARD OF GOVERNORS

We are governed by an eleven-member Board consisting of independent Governors appointed by the President with the advice and consent of the Senate, the Postmaster General and the Deputy Postmaster General. One Governor currently sits on the Board:

Name, Age and Term of Office	Positions and Experience
James H. Bilbray, Chairman of the Board of Governors, Age 78 Governor since August 2006. Term expired December 2015. Holdover Term expiring December 2016.	Chairman of the Board since December 2015. Vice Chairman of the Board of Governors, 2012-2015. Member of the Compensation and Management Resources Committee and the Audit and Finance Committee. Former member, U.S. House of Representatives from Nevada (1987-95). Former member, Nevada State Senate (1981-87). Former Deputy District Attorney in Clark County, Nevada (1965-67). Member of 2005 Defense Base Closure and Realignment Commission.

TEMPORARY EMERGENCY COMMITTEE

As referenced throughout this report, the Board is currently without a statutory quorum due to the failure of the Senate to act on the pending nominations for the Board. Given the loss of a statutory quorum, we filed a Federal Register notice that was published on December 16, 2014, which advised the public of actions taken during the November 2014 Board meeting to ensure that we continue to operate, notwithstanding the loss of a statutory Board quorum. During the November 2014 meeting, the Board adopted a resolution establishing the TEC, composed of the remaining members of the Board, to exercise those powers reserved to the Board that are necessary for continuity of operations.

The Governors also issued a resolution regarding the exercise of the powers vested solely in the Governor(s), as distinguished from the Board. The resolution clarifies that the inability of the Board to constitute a quorum does not inhibit or affect the authority of the Governor(s) then in office to exercise those powers vested solely in the Governor(s), upon the concurrence of an absolute majority of the Governor(s) then in office. For ease of use, references to the “Board” or the “Board of Governors” encompass the TEC as appropriate.

AUDIT AND FINANCE COMMITTEE

The Audit and Finance Committee (“Audit Committee”) is composed of Governor Bilbray, who is Chairman of the Audit Committee. The Board has determined that Governor Bilbray does not qualify as an “audit committee financial expert” as defined by the rules of the SEC. Absent Senate confirmation of the pending nominations for the Board, of which at least one nominee qualifies as an audit committee financial expert, the Board will continue to be left without an audit committee financial expert. Governor Bilbray is independent as defined by the rules of the SEC.

COMPENSATION AND MANAGEMENT RESOURCES COMMITTEE

The Compensation and Management Resources Committee (“Compensation Committee”) is composed solely of Governor Bilbray, who is Chairman of the Compensation Committee. During 2016, Chairman Bilbray was responsible for making recommendations to the Board with respect to compensation decisions.

EXECUTIVE OFFICERS

We had eight executive officers as of September 30, 2016, as per the schedule below:

Name and Age	Positions and Experience
Megan J. Brennan Age 54	74th Postmaster General, Chief Executive Officer and a member of the Board since February 2015; Vice Chairman of the Board since December 2015. Chief Operating Officer and Executive Vice President from December 2010 to February 2015. Previously, Vice President, Eastern Area Operations from December 2006 to December 2010, and Vice President, Northeast Area Operations from April 2005 to December 2006.
Ronald A. Stroman Age 64	20th Deputy Postmaster General and Government Relations Officer and member of the Board since April 2011. Served as Staff Director, Committee on Oversight and Government Relations at the U.S. House of Representatives, from 2009 to April 2011. Prior to this, served as Managing Director, Office of Opportunity and Inclusiveness, U.S. General Accounting Office, from 2001 to 2009.
David E. Williams Age 51	Chief Operating Officer and Executive Vice President since February 2015. Previously, Vice President, Network Operations from December 2006 to December 2010, and Vice President, Engineering from April 2005 to December 2006.
Kristin A. Seaver Age 48	Chief Information Officer and Executive Vice President since April 2016. Previously, Vice President, Capital Metro Area Operations from October 2013 to April 2016. Prior to that, served as Area Manager, Operations Support in the Northeast Area from October 2011 to 2013 and Area Manager, Operations Support in the Eastern Area from June 2007 to September 2011.
Joseph Corbett Age 56	Chief Financial Officer and Executive Vice President since 2009 (except for a brief period from June 20 through September 30, 2012, when he served as Acting Chief Information Officer and Executive Vice President). Founder and Managing Director of FinSol, LLC, a finance and accounting CFO services firm from 2005 to 2009. Consultant, Chief Financial Officer and Executive Vice President of BearingPoint, Inc., a U.S. government contracting, consulting, and systems integration company, from 2004 to 2005. Executive Vice President and Chief Financial Officer of Intelsat, Ltd., from 1998 to 2004 and Intelsat Controller from 1995 to 1998.
James P. Cochrane Age 61	Chief Marketing and Sales Officer and Executive Vice President from January 2016 to October 2016. Acting Chief Marketing and Sales Officer and Executive Vice President from April 2015 to January 2016. Chief Information Officer and Executive Vice President from October 2013 to April 2015. Prior to that, served as Vice President, Product Information from May 2010 to October 2013, and Vice President, Ground Shipping from September 2008 to May 2010.
Thomas J. Marshall Age 54	General Counsel and Executive Vice President since May 2013. Previously, Deputy General Counsel from March 2009 to May 2013. Prior to that, Managing Counsel, Civil Practice, from February 2004 to March 2009.
Jeffrey Williamson Age 41	Chief Human Resources Officer and Executive Vice President since March 2013. Previously, Vice President, Pricing from June 2012 to March 2013. Postal Service MIT Sloan Fellow Representative from May 2011 to June 2012. Manager, Performance and Field Operations from September 2009 to May 2011. Prior to that, Manager, Network Development and Support from October 2006 to September 2009.

CODE OF ETHICS

All of our employees are required to comply with the Standards of Ethical Conduct for Employees of the Executive Branch ("Standards"). The Standards are published in the Code of Federal Regulations ("CFR") at *5 CFR Part 2635* and cover prohibitions and restrictions on the acceptance of gifts, conflicting financial interests, the obligation of all employees to perform their duties impartially, restrictions on the misuse of government positions, restrictions on certain outside activities and other related ethical obligations.

Our employees are also covered by a set of additional restrictions that apply only to Postal Service employees. These "Supplemental Standards" can be found at *5 CFR Part 7001* and focus on limitations on outside employment and outside business activities that could give rise to a conflict with their official duties.

The Standards and the Supplemental Standards contain many examples to help employees identify and resolve ethical issues. New employees receive ethics training at their orientation and ethics officials provide training throughout the year as required by law and as otherwise deemed appropriate. To ensure that all of our employees can receive timely and accurate ethics advice, we have established a dedicated ethics telephone helpline and an email address that is managed by ethics specialists.

Certain high level employees are also subject to the Senior Financial Managers' Code of Ethics. This Code of Ethics can be found on our website at: http://about.usps.com/who-we-are/financials/senior-financial-managers-code-of-ethics-july-2016.pdf.

ITEM 11. EXECUTIVE COMPENSATION

COMPENSATION DISCUSSION AND ANALYSIS

The Board establishes executive officer compensation and benefits, subject to the requirements and limitations of federal law. The Board has delegated to its Compensation Committee authority for initial review of management proposals related to compensation and benefits for executive officers. The Compensation Committee, which meets several times throughout the year, is composed solely of Presidentially-appointed, Senate-confirmed Governors who are independent of our management. The Compensation Committee makes recommendations to the full Board for its review and approval.

Set forth in Title 39 of the U.S. Code, federal law governing us provides that compensation and benefits for all of our officers shall be comparable to the compensation and benefits paid for comparable levels of work in the private sector of the economy. We are the second largest civilian employer in the nation, with approximately 640,000 career and non-career employees as of the end of 2016. We operate approximately 228,000 motor vehicles and approximately 32,000 retail units. In 2016, we delivered 153.9 billion pieces of mail, almost half of the world's mail, and generated approximately $71.4 billion in revenue. In 2016, we ranked 107th in *Fortune* magazine's listing of *Fortune Global 500* companies. By way of comparison, two of our largest competitors ranked 149th and 192nd on this list. If we were listed on the *Fortune 500* annual ranking of America's largest corporations, we would be ranked 41st. The same two of our largest competitors are ranked 48th and 58th on that list.

Even as the economy continues to be challenged, comparably sized companies typically provide their top executives with annual salaries well in excess of $1 million and total compensation and benefits valued at several million dollars. These compensation packages typically consist of annual and long-term performance incentives, including a combination of cash payments and stock options and a number of benefits and perquisites.

Although our governing law provides that executives and others should be compensated at a level comparable to the private sector, the law does not afford the Governor(s) the tools to achieve this standard of compensation. Compensation for our executive officers remains significantly below that of similarly-ranked senior executives in the private sector.

The law imposes three different caps on compensation for our employees. The first cap provides that no officer or employee may be paid compensation "at a rate in excess of the rate for level I of the Executive Schedule under *Section 5312* of Title 5 of the U.S. Code *39 U.S.C. §1003(a)*. In calendar year 2016, the upper limit on federal salaries rose 1% to $205,700.

With the approval of the Board, we may develop a program to award a bonus or other reward in excess of the compensation cap discussed above, as long as the total compensation paid to the officer in a year does not "exceed the total annual compensation payable to the Vice President [of the United States] under [*3 U.S.C. §104*] as of the end of the calendar year in which the bonus or award is paid." *39 U.S.C. §3686(a)-(b)*. In calendar year 2016, this cap rose 1% to $237,700. The Board may approve a program allowing for bonuses or other rewards if it determines, for the annual appraisal period involved, that the performance appraisal system for impacted employees makes meaningful distinctions based on relative performance.

In addition, the Board may allow up to 12 of our officers or employees in critical senior executive or equivalent positions to be paid total annual compensation up to "120 percent of the total annual compensation payable to the Vice President [of the United States] under [*3 U.S.C. §104*] as of the end of the calendar year in which such payment is received." *39 U.S.C. §3686 (c)*. Based on the Vice President's salary for calendar year 2016, the compensation cap for calendar year 2016 was $285,240.

By law, our employees, including executive officers, are entitled to participate in either CSRS or FERS, depending on when their federal employment began. As applicable to our officers, these retirement systems are described later in this *Compensation Discussion and Analysis*. In addition, in order to remain competitive with comparable employment in private industry and other parts of the U.S. government, our policy also authorizes certain additional benefits for all of our officers, including executive officers. Other than changes required by law, the Board must authorize increases to benefits for officers.

COMPENSATION PHILOSOPHY AND OBJECTIVES

The Board recognizes that a significant disconnect exists between the comparability requirement and the compensation caps in the law governing us and that the various compensation caps do not enable the Board to provide compensation and benefits for our executive officers that are fully comparable to those in the private sector. This is especially true given our current financial challenges. The Board also recognizes that many of the compensation and benefit tools available in the private sector, such as equity ownership, are not available to us, given our status as part of the U.S. government. These limitations make it more difficult for us to competitively recruit in the marketplace for executive officers and to retain current executive officers. We have taken significant steps, described elsewhere in this report, to reduce costs and generate revenue. However, we have sought and continue to need comprehensive legislative change in order to have greater flexibility to reduce costs, generate new revenue and return to financial stability.

In an attempt to achieve some level of comparability within the confines of the law, the Board designed a compensation system intended to balance an executive's annual salary with the ability to earn additional compensation by meeting performance goals and objectives; however, because of the compensation caps discussed above, a portion of this compensation might need to be deferred.

At the start of calendar year 2016, the compensation system operated pursuant to its terms, and eligible non-executive officers received an increase in their basic compensation and a performance lump-sum payment. Increases in basic compensation in calendar year 2016 were dependent upon fiscal year 2015 performance, and averaged 1%. The amount of the performance lump-sum payments issued in calendar year 2016 was also based upon fiscal year 2015 performance, and averaged 3%. However, uncertainty about future payments and the viability of the compensation system continues to negatively impact our ability to retain and recruit talented employees, including executives and executive officers.

The calendar year 2016 increase was preceded by increases in basic compensation that averaged 3% in calendar year 2015 and 1% in calendar year 2014. Prior to 2014, officer compensation was impacted by a freeze in salary and/or a non-payment of performance lump sums for six consecutive years. By comparison, employees of other U.S. government entities only experienced a pay freeze for years 2011 through 2013, and received a 1% annual increase in their basic compensation for calendar years 2014, 2015 and 2016, in addition to step increases and available awards. Furthermore, the U.S. government pay freeze applied only to COLAs and not to longevity (step-increase) raises or performance awards.

Within the confines of its legislative authority and our financial constraints, the Board's compensation philosophy is that:

- There should be a strong connection between individual executive compensation and our performance on a number of dimensions, including service, net income and productivity;
- Compensation and benefits should be designed to attract and retain high-performing executives to ensure that we have the caliber of executives who will enable us to operate at the highest levels of performance and productivity;
- Lump-sum incentives should be set to motivate executives to improve performance continuously on a long-term basis and to perform above the annually-established goals and objectives. If individual performance exceeds the goals and objectives set for the year, the employee should receive additional compensation. Likewise, if overall performance falls below the annual goals and objectives, the individual should be paid less;
- A significant amount of the executive's compensation should be "at risk" and the "at-risk" amount should increase as the executive's level of responsibility increases;
- Innovation, effectiveness as an agent for change, the ability to balance day-to-day priorities and long-term strategies, and organizational value as defined by the achievement of key corporate goals and objectives should be rewarded;
- Executive compensation should be fair and equitable internally, recognizing the width and breadth of the responsibilities of our executives; and
- Executive success is defined by a number of factors, including financial returns, the quality of service we provide, the results achieved by the executive's actions to enhance the organization's efficiency and overcome challenges and whether an executive met established individual goals.

THE COMPENSATION PROGRAM

In 2007, with the assistance of an independent consulting firm specializing in executive compensation, the Compensation Committee recommended and the Board approved a salary band for the Postmaster General to be set at the legislative salary cap. In doing so, the Board's objectives were to design a compensation program that optimized the legislative flexibility granted by the PAEA, improve external marketplace competitiveness and honor legislative constraints and existing pay ranges. For the other executive officers, the Board set pay bands based on salary relationships of comparable executive officers in the external market. In general, the Board has maintained these types of pay band relationships since 2007.

The Board approved Postmaster General Megan J. Brennan's salary at the legislative cap for calendar year 2016. Given our continued significant financial challenges, Postmaster General Brennan asked the Board not to award her any additional compensation beyond salary in calendar year 2016, based on her fiscal year 2015 performance, and the Board agreed. Additionally, the Board supported Postmaster General Brennan's decision not to award our Executive Leadership Team ("ELT") officers any additional compensation in calendar year 2016, based on their fiscal year 2015 performance. As such, the ELT officers did not receive salary increases or performance lump-sum payments for their 2015 performance.

Over the years, the Governor(s) have authorized the Postmaster General to establish salaries for the other executive officers within the confines of the salary ranges established by the Governor(s). As noted above, for calendar year 2016, after reviewing recommendations from the Postmaster General and the Compensation Committee, the Governor(s) approved the application of the PFP system according to its terms and approved an increase in the salary ranges by 1%.

In 2016, we continued to employ a national performance assessment program ("NPA") to set annual performance goals and metrics that vary among executive officers and are weighted to reflect appropriately the degree to which an executive is able to influence our overall performance. The annual NPA metrics and targets generally take into consideration our performance during the prior fiscal year and the particular challenges that we anticipate having to face during the following year. The NPA places emphasis on measurable financial and service performance indicators. The Governor(s) also set individual metrics and targets for the Postmaster General and Deputy Postmaster General and authorize the Postmaster General to establish individual metrics and targets for other officers.

The officer compensation system is intended to operate as follows: the Board establishes annual PFP incentives to provide opportunities for the Postmaster General and the Deputy Postmaster General to earn enhanced compensation, directly tied to the level of their performance. The Postmaster General establishes annual PFP incentives for other officers, to provide them opportunities to earn increased compensation based upon their performance. Incentive payouts are not to be made for a particular goal if we or the individual fails to meet minimum acceptable performance standards. The payment of PFP incentives may sometimes be deferred for future payment where required due to the compensation caps discussed above.

Our economic challenges have continued to persist over the last several years and these challenges have caused uncertainty as to whether officer salary increases or performance bonuses will be awarded on a year-to-year basis. This uncertainty is largely driven by our flawed business model which limits our ability to be financially successful, and which can only be corrected by comprehensive postal legislation.

The Governor(s) believe that this situation must be remedied in the near future, and are concerned that if this situation continues much longer, it will further erode our ability to retain highly-qualified individuals as officers and to recruit the best qualified individuals from the marketplace, if external hiring is deemed to be the best solution to fill critical officer vacancies. Additionally, our financial constraints, which largely are the products of structural defects that only Congress can remedy, have prevented us from fully complying with the statutory mandate that our officers be paid in a manner comparable with their private-sector counterparts.

We continued to use the NPA process to measure performance during 2016. NPA performance goals and rewards fall into several categories that an officer may directly influence, such as service, efficiency, employee satisfaction and productivity, as well as those that are more susceptible to being impacted by general economic conditions, such as revenue generation.

For each goal, the Postmaster General establishes indicators identifying the type of performance that will enable us to achieve or surpass the goal. These indicators are aligned at the corporate, functional and individual levels and are weighted. The higher an individual's position is in the organization, the more his or her PFP goals will be tied to our overall corporate performance. The executive officers' goals are aligned with national performance goals and linked to our overall success.

Once the goals and indicators are established, executive officers are advised as to what is expected of them in terms of performance during the year, how their performance will impact us, and, in years when incentives are authorized, the potential level of performance-based incentives they can expect depending on their individual performance and our performance as a whole. Under this program, an individual executive officer can receive a numerical rating within a range of 1 to 15 depending on how we perform on the national indicators and the individual's performance, as determined by the Postmaster General.

The system is supposed to operate as follows: an individual executive officer's performance rating would make the officer eligible for an increase to base salary, as well as for a performance-based lump-sum payment. Due to statutory cap limitations, increases to the maximum of the salary range for executive officers would generally follow the percentage increase in the applicable statutory cap for any given year. Any salary increases for executive officers are limited by these maximums and are solely performance based, as determined by the Postmaster General. Lump-sum incentive payments would be tied to the Postmaster General's rating of the executive officer's performance, based on the degree to which the individual achieved previously set individual goals and metrics. The Postmaster General's discretion on PFP incentives for executive officers in a given year is limited by our overall performance on NPA goals and metrics. Generally, officer performance scores must average to our overall NPA performance score for the fiscal year.

Salary increases, if any, are determined after the end of the fiscal year, and any new salaries become effective for the following calendar year. In making compensation decisions relating to 2016 performance, the Governor(s) noted that management achieved very significant accomplishments in addressing the many challenges we faced in 2016. Despite a continuing decline in *First-Class Mail* volume over the past several years, management continued to take aggressive actions within its control during 2016 to reduce costs, provide excellent service and secure revenue.

Despite the many significant accomplishments of our management team during 2016, the Governor(s) recognized that we continue to face significant financial challenges. While these challenges resulted in part from our flawed business model and lack of reform, the Governor(s) noted that comprehensive legislative change is needed to enable us to return to financial stability. The absence of legislative change has had, and will continue to have, a significant negative impact on our finances.

COMPONENTS OF OFFICER COMPENSATION AND BENEFITS

Base Salary

Base salaries provide a level of financial security that is appropriate for the executive's position within the Postal Service. Within the confines of law and our difficult financial condition, base salaries are to be scaled within pay ranges designed to be competitive with the market median. As discussed above, maximum payouts in a given year are set by federal law. Executive officer salaries are reviewed at least annually and adjusted, as appropriate and when permitted by financial constraints, to reflect individual performance, range of responsibilities, value and contribution to the organization, and experience.

Annual Incentive

Annual incentives serve as a mechanism for adjusting total compensation levels commensurate with the attainment of planned results, thereby ensuring affordability and appropriate performance that benefits us. As discussed above, we use the NPA to set annual corporate performance goals and metrics. The Governor(s) set the goals and indicators for the Postmaster General and the Deputy Postmaster General, and the Postmaster General establishes goals and indicators for the other executive officers. The Postmaster General's and the Deputy Postmaster General's performance is determined based on the degree to which they have achieved previously set goals and metrics. Likewise, executive officers' individual performance ratings are determined by the Postmaster General based on the degree to which the individual has achieved the previously set goals and metrics.

Other Compensation Incentives

Executive officers are also eligible for recognition awards for specific activities that reflect a high degree of leadership. The Governor(s) authorized the Postmaster General to specify a limited budget for awards to officers in 2016 for exceptional accomplishments during the year. In addition, executive officers are eligible for recruitment, relocation and retention incentives designed to attract and retain highly talented and marketable individuals in key positions. Payments of some of these incentives may be deferred, in whole or in part, due to the compensation limits imposed on our employees as more fully discussed above.

Retirement Annuities

Officers are covered either by CSRS or FERS. Both systems have a defined benefit component and a defined contribution component. CSRS and FERS service is creditable for Medicare coverage. FERS service is creditable for Social Security.

CSRS Defined Benefit
The CSRS Basic Benefit annuity is based on a percentage of the high-3 salary multiplied by years of service. The percentage is 1.5% for the first 5 years of service, plus 1.75% from five years to ten years of service and 2% for all years of service thereafter. Optional retirement thresholds are age 55 with 30 years of service, age 60 with 20 years of service, and age 62 with five years of service, with a requirement of completing at least five years of creditable civilian service. The annuity is fully indexed to the Consumer Price Index ("CPI"). Disability, early retirement, deferred and survivor benefits are available.

FERS Defined Benefit
The FERS Basic Benefit annuity is based on 1.0% of high-3 salary per year of service, or 1.1% for retirement at age 62 with at least 20 years of service. Optional retirement thresholds are the Minimum Retirement Age ("MRA") of 55 to 57 (depending birth year) with 30 years of service, age 60 with 20 years of service, age 62 with five years of service, or MRA with ten years of service (at a reduced benefit), with a requirement of completing at least five years of creditable civilian service. Employees who retire at MRA with 30 years of service, or at age 60 with 20 years of service, receive a retirement supplement approximating the value of Social Security benefits attributable to federal service; this benefit is paid until age 62. Beginning at age 62, the annuity is indexed to CPI, fully when the CPI increase is 2% or less, at 2% when the CPI increase is between 2% and 3%, and at CPI minus 1% when the CPI is at least 3%. Disability, early retirement, deferred and survivor benefits are available.

Defined Contribution
The TSP has a component that mirrors traditional 401(k) plans; it has a component that mirrors traditional 401(k) plans and an option similar to "Roth" plans. CSRS and FERS employees may contribute up to the indexed IRS maximum ($18,000 in calendar year 2016). We do not make TSP contributions for CSRS employees. For FERS employees, we make an automatic contribution of 1% of basic pay and match a percentage of employee contributions for up to an additional 4% of basic pay, for a total employer contribution of up to 5% of basic pay. Employees who will be at least age 50 in the year of contribution may make a separate catch-up contribution up to the indexed IRS maximum ($6,000 in calendar year 2016). TSP investment options are a government securities fund; index funds that track the Barclays Capital Aggregate Bond Index, the S&P 500, the Dow Jones U.S. Completion TSM Index, and the Morgan Stanley Capital International EAFE (Europe, Australasia and Far East) stock index; and lifecycle funds.

Supplemental Non-Qualified Deferred Compensation
Where appropriate and on a highly selective basis, we have offered supplemental non-qualified deferred compensation as a recruitment or retention tool.

Life Insurance
Officers are entitled to *Basic* group life insurance coverage under the Federal Employees Group Life Insurance ("FEGLI") program in the amount of their annual basic salary, rounded up to the next $1,000, plus $2,000. If *Basic* coverage is held, an officer will also receive an additional $10,000 coverage (*Option A*) and *Option B* coverage up to three times their salary. We pay all premiums for *Option A*, *Option B* and *Basic* coverage.

At their own expense, officers may elect additional *Option B* coverage in an amount equal to two times their salary, or *Option C*, family optional insurance coverage, of up to five multiples of $5,000 for their spouse and $2,500 for each eligible dependent child under age 22. Officers continuously covered under FEGLI for the five years of service immediately preceding retirement, or since the first opportunity to enroll, may continue coverage during retirement (if entitled to an immediate annuity). We pay retired officers an actuarially determined lump sum to cover the cost of *Option A* premiums during retirement.

Health Benefits
We participate in FEHB, which allows all career employees to enroll in one of a number of *Self Only*, *Self-Plus-One* or *Self and Family* health benefit plans offered. We pay a portion of the cost of the premium for our officers and executives. In 2016, our share of the premium was 72% of the federal weighted average premium, limited to not more than 75% of the total premium for any given plan, and enrolled officers and executives paid the balance of the premium for the plan they selected. Employees who retire with immediate entitlement to an annuity are eligible to continue FEHB coverage into retirement, as long as they have participated in FEHB for the five years preceding their retirement or since their first opportunity to enroll.

Other Benefits
To remain competitive in the marketplace, we offer the following additional benefits to our executive officers: periodic physical examinations, parking, financial counseling services and membership in up to two airline clubs per year. In November 2015,

the Governors, in connection with their annual review of the compensation and benefits for the Postmaster General and Deputy Postmaster General, clarified and updated their policies to provide that the Postmaster General and Deputy Postmaster General are entitled to a separation payment in an amount of one year's salary if either is asked to separate from the Postal Service for any reason other than cause and they are otherwise not eligible for immediate retirement (not including early retirement, discontinued service retirement, or retirement at the minimum retirement age with less than 30 years of service). Severance may be paid in a single lump-sum payment or in bi-weekly payments following the date of separation from the Postal Service.

COMPENSATION AND MANAGEMENT RESOURCES COMMITTEE REPORT

The Compensation Committee has reviewed and discussed this *Compensation Discussion and Analysis* with management and, based on such review and discussions, the Compensation Committee recommended to the Board that this *Compensation Discussion and Analysis* be included in this report.

Signature	Title
/s/ James H. Bilbray	
James H. Bilbray	Chairman, Board of Governors

SUMMARY COMPENSATION TABLE

The following presents the compensation of our five most highly compensated executive officers ("named executive officers"):

Name and principal position	Fiscal year	Salary[3]	Bonus[4]	Non-equity incentive plan compensation[5]	Change in pension value and non-qualified deferred compensation earnings[6]	All other compensation	Total
Megan J. Brennan, *Postmaster General & Chief Executive Officer*[1]	2016	$ 286,137	$ —	$ —	$ 590,846	$ 27,801	$ 904,784
	2015	266,981	—	9,500	110,429	28,381	415,291
	2014	236,536	20,000	—	77,271	17,848	351,655
Joseph Corbett, *Chief Financial Officer & Executive VP*	2016	258,195	—	35,000	45,908	21,269	360,372
	2015	246,404	—	44,700	40,634	21,932	353,670
	2014	240,563	—	35,000	36,379	19,432	331,374
James P. Cochrane, *Chief Customer and Marketing Officer & Executive VP*	2016	257,359	10,000	—	254,838	14,019	536,216
	2015	239,702	—	9,400	279,722	10,563	539,387
	2014	230,135	—	—	226,128	9,349	465,612
Thomas J. Marshall, *General Counsel & Executive VP*	2016	251,173	—	—	96,605	19,282	367,060
	2015	238,926	15,000	9,300	99,035	18,821	381,082
	2014	231,504	—	—	69,064	18,568	319,136
David E. Williams Jr., *Chief Operating Officer & Executive VP*[2]	2016	251,173	10,000	—	115,441	19,282	395,896
	2015	223,458	—	7,600	88,153	17,542	336,753
	2014	—	—	—	—	—	—

[1] Ms. Brennan was appointed Postmaster General and Chief Executive Officer as of February 2, 2015; she was Chief Operating Officer prior to that.

[2] Mr. Williams was not a named executive officer in 2014 and, as such, information for 2014 is not reported.

[3] 2016 salary includes one additional pay period of earnings due to a 27th payday which occurred on December 31, 2015.

[4] Ms. Brennan received an award in 2014 for efficiency / cost savings initiatives while in the position of Chief Operating Officer. Mr. Marshall received a Board of Governor's award in 2015. Mr. Cochrane and Mr. Williams received a Postmaster General's award in 2016.

[5] Amounts reflect the performance-based incentive compensation awarded to executive officers for performance in prior fiscal years; as noted above, this incentive compensation was not awarded for 2015. Any amounts that could not be paid to an executive officer, due to the compensation cap or their contract, were deferred for future payment and are also reflected in the non-qualified deferred compensation table below.

[6] Mr. Cochrane participates in CSRS. Ms. Brennan, Mr. Corbett, Mr. Marshall and Mr. Williams participate in FERS. The calculation of retirement annuities under CSRS and FERS is explained in the Pension Benefits table, the associated note and in the *Retirement Annuities* section of *Compensation Discussion and Analysis*. The amounts shown for each of these individuals represent the change in annuity value from the prior year. The increase can also include changes in eligibility conditions that allow members to receive benefits earlier. "Non-qualified deferred compensation earnings" is defined as above-market earnings on deferred income. There were no reportable amounts of non-qualified deferred compensation earnings for the named executive officers in 2016, 2015 or 2014, with the exception of Mr. Corbett, whose above-market earnings on deferred income were $1,647 in 2016, $1,320 in 2015, and $1,008 in 2014.

GRANTS OF PLAN-BASED AWARDS

The following table presents information regarding potential non-equity incentive awards to the named executive officers for 2016. Whether a named executive officer receives an award and, if so, the amount of an award for 2016 will depend on the Postal Service's and the individual's performance during 2016.

	Estimated future payouts under non-equity incentive plan awards			
Name	**Grant date**	**Threshold**	**Target**	**Maximum**
Megan J. Brennan	October 2016	$ 15,175	$ 34,229	$ 106,965
Joseph Corbett	October 2016	13,227	29,836	93,237
James P. Cochrane	October 2016	13,318	30,040	93,876
Thomas J. Marshall	October 2016	12,867	29,024	90,701
David E. Williams Jr.	October 2016	12,867	29,024	90,701

Note: The PFP program relies on a 15-point scale with clearly defined and transparent corporate goals. The PFP target in any given year is set at a rating of 6. The maximum threshold for payment is set at a rating of 15. Individual ratings vary but the corporate score is used as the regulator. Given our financial condition, any individual award is unlikely to exceed the target amount; therefore the maximum amount is entirely unrealistic.

PENSION BENEFITS

The following table shows the present value of accumulated pension benefits payable to the named executive officers as of September 30, 2016:

Name	Plan name	Number of years credited service	Present value of accumulated benefit
Megan J. Brennan	FERS Annuity	30	$ 1,468,463
Joseph Corbett	FERS Annuity	8	239,606
James P. Cochrane	CSRS Annuity	42	3,418,258
Thomas J. Marshall	FERS Annuity	21	659,775
David E. Williams Jr.	FERS Annuity	29	738,294

Note: All named executive officers are eligible for CSRS or FERS. These plans are described in the *Retirement Annuities* section within *Compensation Discussion and Analysis*. The present value of the accumulated CSRS or FERS benefit represents the value of the pension over the individual's actuarial lifetime, as of September 30, 2016. Mr. Cochrane participates in CSRS, and Ms. Brennan, Mr. Corbett, Mr. Marshall and Mr. Williams participate in FERS. Mr. Cochrane is eligible for retirement, the calculation of which is described in the *Retirement Annuities* section within *Compensation Discussion and Analysis*. The valuation for Ms. Brennan, Mr. Corbett, Mr. Marshall and Mr. Williams assumes that they have satisfied vesting requirements for retirement; however, because of their current tenure with the Postal Service, their retirement annuities have not fully vested.

NON-QUALIFIED DEFERRED COMPENSATION

The following table presents contributions to, and earnings on, the named executive officers' deferred compensation for 2016:

Name	Executive contributions in 2016[1]	Aggregate earnings in 2016[2]	Aggregate withdrawals / distributions in 2016	Aggregate balance at September 30, 2016
Megan J. Brennan	$ 4,594	$ 662	$ —	$ 15,747
Joseph Corbett	35,000	11,222	—	276,754

[1] This column represents amounts deferred due to the compensation cap or contract agreements. The amount shown for Mr. Corbett reflects the lump-sum performance retention payment required by his employment agreement which has been deferred.

[2] We calculate interest on deferred compensation semi-annually at 5.0% per year for Mr. Corbett per his contract, others are calculated at the Federal Long Term Rate; 4.33% in 2016. Interest is prorated from the relevant pay period of the deferral.

POTENTIAL PAYMENTS UPON TERMINATION

The Postmaster General and all of the other named executives are subject to the standard policies governing CSRS or FERS, as described in the *Compensation Discussion and Analysis*. The present value of these CSRS and FERS benefits are found in the Pension Benefits table in the *Executive Officer Compensation* section of this report. The information below describes and quantifies certain compensation, in addition to that due pursuant to CSRS or FERS, that would become payable under existing plans and arrangements if the named executive officer's employment had terminated on September 30, 2016. Additionally, pursuant to statutes and regulations generally applicable to federal employees, the named executives would be entitled to receive the federal employer's standard contribution toward retiree health benefits, in the event they have qualifying service and participated in FEHB for the requisite period of time prior to retiring.

DEFERRED COMPENSATION

All federal employees, including our employees, are subject to annual compensation limits established pursuant to federal statutes and regulations. When amounts earned by federal employees cannot be paid because of these compensation limits, these payments are deferred until a year in which their payment would not cause total annual compensation paid to exceed the compensation limit, or the year in which an employee leaves federal service, whichever occurs first. Named executive officers appearing in the non-qualified deferred compensation table in the *Executive Officer Compensation* above have deferred compensation in the amounts indicated therein. These amounts would have been paid to them in a lump sum or pursuant to their contract with us following their departure, had they ended their employment with us on September 30, 2016.

Mr. Corbett's employment agreement provides for deferred incentives linked in part to his performance. Mr. Corbett began accruing deferred performance-based compensation at the end of 2010. When Mr. Corbett concludes his employment with us, or on October 22, 2019, if that date is later than Mr. Corbett's departure from the Postal Service, his deferred compensation will be paid to him in three approximately equal annual installments.

SUPPLEMENTAL PENSION BENEFIT

The Governor(s) have not authorized a supplemental pension benefit for any executive officer at this time.

SEVERANCE PAYMENT

Mr. Corbett is entitled to a severance payment of $230,000, in the event that we terminate his employment for any reason other than for cause or breach of contract.

INSURANCE BENEFIT

The Governor(s) have not authorized supplemental insurance benefits for any executive officer at this time. The insurance benefits to which all of our executive officers are entitled are described above.

OUTPLACEMENT ASSISTANCE

The Governor(s) have not authorized any outplacement assistance for any executive officer at this time.

ACCRUED ANNUAL LEAVE

All of our employees are entitled to receive and accrue paid days off, known as annual leave. Upon their separation from the Postal Service, all employees, including the named executive officers, are entitled to be paid, in a lump sum, the value of all accrued annual leave.

The table below shows the accrued value of the annual leave of the named executive officers as of September 30, 2016:

Name	Value of accrued annual leave
Megan J. Brennan	$ 136,449
Joseph Corbett	95,628
James P. Cochrane	46,817
Thomas J. Marshall	49,304
David E. Williams Jr.	—

GOVERNORS COMPENSATION

The following table presents information regarding the compensation of the Governors during 2016:

Name[1]	Fees earned or paid in cash	All other compensation	Total
James H. Bilbray	$ 35,100	$ —	$ 35,100
Louis J. Giuliano[2]	6,867	—	6,867
Ellen C. Williams[2]	6,267	—	6,267

[1] Each Governor receives a basic stipend of $30,000 per year plus $300 per day for not more than 42 days of meetings each year.
[2] The terms of Governors Giuliano and Williams expired on December 8, 2015.

ITEM 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT AND RELATED STOCKHOLDER MATTERS

Not applicable. As an "independent establishment of the executive branch of the Government of the United States," we do not issue equity securities.

ITEM 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS AND DIRECTOR INDEPENDENCE

CERTAIN TRANSACTIONS

We enter into significant transactions with other government agencies, as disclosed throughout this report and the financial statements.

DIRECTOR INDEPENDENCE

Our Governors are appointed by the President with the advice and consent of the Senate, and are independent based on the New York Stock Exchange definition of independence.

ITEM 14. PRINCIPAL ACCOUNTANT FEES AND SERVICES

Annually, the Audit Committee reviews and pre-approves the audit services to be provided by our independent auditors. The Audit Committee must approve other specific services before the independent auditors may perform such services. The Audit Committee also has delegated to the Audit Committee Chairman pre-approval authority with respect to permitted services, provided that any pre-approval decisions must be reported to the Audit Committee at its next scheduled meeting.

Audit fees totaled approximately $10 million and $10 million for the years ended September 30, 2016, and 2015, respectively. Audit fees include fees for professional services associated with the annual financial statement audit, the reviews of our quarterly reports on Form 10-Q and testing of our internal control over financial reporting. We did not incur any other fees from our independent auditors.

PART IV

ITEM 15. EXHIBITS, FINANCIAL STATEMENT SCHEDULES

(a) The following documents are filed as part of this Annual Report:

1. Financial Statements

The following consolidated financial statements of the United States Postal Service for each of the years ended and as of the periods noted are submitted in *Part II. Item 8. Financial Statements and Supplementary Data* of this report.

2. Financial Statement Schedules

None.

All other financial statement schedules have been omitted because they are not applicable or the required information is included in the United States Postal Service's financial statements or the notes thereto.

3. Exhibits

10.1	Employment/Compensation Contract with Joseph Corbett, Chief Financial Officer (filed with the Postal Regulatory Commission on January 29, 2009, as Exhibit No. 10.1 to the Current Report on Form 8-K).
31.1	Certificate of United States Postal Service's Principal Executive Officer Adopted Pursuant to Section 302 of the *Sarbanes-Oxley Act of 2002*.
31.2	Certificate of United States Postal Service's Principal Financial Officer Adopted Pursuant to Section 302 of the *Sarbanes-Oxley Act of 2002*.
32.1	Certificate of United States Postal Service's Principal Executive Officer Adopted Pursuant to Section 906 of the *Sarbanes-Oxley Act of 2002*.
32.2	Certificate of United States Postal Service's Principal Financial Officer 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/Megan J. Brennan
Megan J. Brennan
Postmaster General and Chief Executive Officer

Date: November 15, 2016

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

Date: November 15, 2016

Pursuant to the requirements of the *Postal Accountability and Enhancement Act of 2006*, this Report has been signed below by the following persons on behalf of the United States Postal Service and in the capacities indicated as of November 15, 2016.

Signature	Title
/s/ James H. Bilbray James H. Bilbray	Chairman, Board of Governors
/s/ Megan J. Brennan Megan J. Brennan	Board Member, Postmaster General and Chief Executive Officer
/s/ Ronald A. Stroman Ronald A. Stroman	Board Member and Deputy Postmaster General
/s/ Joseph Corbett Joseph Corbett	Chief Financial Officer and Executive Vice President, (Principal Financial Officer)
/s/ Maura A. McNerney Maura A. McNerney	Vice President, Controller (Principal Accounting Officer)

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, Megan J. Brennan, certify that:

1. I have reviewed this Annual Report on Form 10-K 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 independent registered accounting firm and the Audit and Finance 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 a significant role in the Postal Service's internal control over financial reporting.

Date: November 15, 2016

/s/Megan J. Brennan

Megan J. Brennan

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 Annual Report on Form 10-K 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 independent registered accounting firm and the Audit and Finance 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 a significant role in the Postal Service's internal control over financial reporting.

Date: November 15, 2016

/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 Annual Report of the United States Postal Service ("Postal Service") on Form 10-K for the period ended September 30, 2016, (the "Report"), I, Megan J. Brennan, 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: November 15, 2016

/s/Megan J. Brennan

Megan J. Brennan
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 Annual Report of the United States Postal Service ("Postal Service") on Form 10-K for the period ended September 30, 2016, (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: November 15, 2016

/s/Joseph Corbett

Joseph Corbett
Chief Financial Officer and Executive Vice President