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, 2008**

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 No. 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:

Title of Each Class	Name of Each Exchange on Which Registered
N/A	N/A

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 if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K 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. ☐ Not Applicable ☑

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of "accelerated filer and large accelerated filer" in Rule 12b-2 of the Exchange Act.

Large accelerated filer ☐ Accelerated filer ☐

Non-accelerated filer ☐ (Do not check if a smaller reporting company) Smaller reporting company ☐

Not Applicable ☑

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes ☐ No ☑

The aggregate market value of shares of common stock held by non-affiliates at March 31, 2008, was N/A
Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date.

Common Stock	Outstanding Shares at November 14, 2008
No Common Stock	N/A

United States Postal Service

Table of Contents

Part I

Item 1 – Business

Overview

The United States Postal Service (we) commenced operations on July 1, 1971, as an "independent establishment of the executive branch of the Government of the United States." We are governed by an eleven-member Board of Governors. The Board is composed of nine Governors appointed by the President of the United States with the advice and consent of the Senate, plus the Postmaster General and the Deputy Postmaster General. Under the Postal Reorganization Act, and its successor, the Postal Accountability and Enhancement Act, Public Law 109-435 (P.L. 109-435), we have a legal mandate to offer a "fundamental service" to the American people, "at fair and reasonable rates." We fulfill this legal mandate to provide universal service at a fair price by offering a variety of classes of mail services without undue discrimination among our many customers. This means that within each class of mail our price does not unreasonably vary by customer for the levels of service provided.

We serve individual and commercial customers throughout the nation, competing for business in the communications, distribution, delivery, advertising, and retail markets.

Our Mailing and Shipping Services are sold through almost 37,000 Post Offices, stations, branches, contract postal units, our website *www.usps.com,* and a large network of consignees. We deliver mail to more than 149 million city, rural, Post Office box, and highway delivery points. We conduct our operations primarily in the domestic market, with international operations representing approximately 3% of total revenue.

All references to years, 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 within 2008.

We are not a reporting company under the Securities Exchange Act of 1934, as amended, and are not subject to regulation by the Securities and Exchange Commission (SEC). However, effective for reporting periods ending after September 30, 2007, we are required under P.L.109-435 to file with the Postal Regulatory Commission (PRC) certain financial reports containing information prescribed by the SEC under section 13 of the Securities Exchange Act of 1934. These reports are further described on the following page.

Additional disclosures on our organization and finances, including our *Cost and Revenue Analysis* reports, *Revenue, Pieces, and Weight* reports, *Vision 2013* strategic plan and the *Comprehensive Statement on Postal Operations* may be found on our website at *www.usps.com.* Information on our website is not incorporated by reference in this document.

Postal Accountability and Enhancement Act, Public Law 109-435 (P.L.109-435)

This law was signed by President Bush on December 20, 2006. It revises a number of provisions of the Postal Service's governing statute, codified in title 39, United States Code.

The law divides our services into two broad categories: market-dominant and competitive. Market-dominant services include, but are not limited to, First-Class Mail, Standard Mail, Periodicals, and Package Services. Price increases for these services are subject to a price cap based on the Consumer Price Index – All Urban Consumers (CPI-U). Competitive services, such as Priority Mail, Express Mail, Bulk Parcel Post, and Bulk International Mail have greater pricing flexibility. Throughout this document and in the day-to-day operation of the organization, we refer to market-dominant services as "Mailing Services" and competitive services as "Shipping Services".

For retail customers, the law anticipates that universal service can be preserved at affordable prices. For commercial mailers, the law is intended to provide price predictability. For employees, customers, and taxpayers, the law is designed to provide assurance that the employer portion of the Postal Service's health and retirement benefits becomes fully funded in the future.

P.L.109-435 also directs the U.S. Treasury to resume financial responsibility for the portion of the Civil Service Retirement System (CSRS) pensions of postal employees attributable to military service. This takes the financial burden added by P.L.108-18, estimated in 2003 at approximately $27 billion by the Office of Personnel Management (OPM), away from the Postal Service. P.L.109-435 also abolished a federally mandated escrow requirement and directed that the money previously held in escrow be placed into a new Postal Service Retiree Health Benefits Fund (PSRHBF). Through 2017, we are required to make payments into the PSRHBF that average $5.6 billion per year.

P.L.109-435 reconstituted the former Postal Rate Commission into a regulatory body, renamed the Postal

Regulatory Commission (PRC). The regulations for the price-setting process released by the PRC on October 29, 2007, consist of three parts: (1) regulations related to price adjustments for market dominant products, including the formula for the calculation of the price cap; (2) regulations related to competitive products; and (3) establishment of a Mail Classification Schedule, which categorizes our products as either market dominant or competitive. These price-setting regulations are contained in 39 C.F.R. Parts 3001, 3010, 3015, and 3020.

The Mail Classification Schedule divides mail into Mailing Services or Shipping Services, establishes which types of mail constitute separate products, and presents a brief description of each product. The regulations allow us to make certain classification changes much more easily than under the previous system. This enhances overall pricing flexibility.

The regulations for Mailing Services, constituting almost 90% of all postal revenue, allow price changes every year with limited prior review, as long as the average increase for each class of mail is no greater than the rate of inflation as measured by CPI-U. The regulations permit price increases above the price cap in the event of extraordinary or exceptional circumstances.

The regulations for Shipping Services place no upper limit on price changes. The Governors of the Postal Service can adjust prices as necessary, as long as each product covers 100% of its attributable costs. No product may be cross-subsidized by Mailing Services. In addition, Shipping Services are required to cover 5.5% of the Postal Service's total institutional costs.

On September 11, 2008, the PRC issued Order No. 106 proposing rules on accounting practices and taxes on competitive products income. Comments from interested parties were due to the PRC on October 20, 2008; reply comments were due November 3. A final rule must be issued by December 19, 2008, unless otherwise agreed by the PRC and the Postal Service.

The PRC now has its own Office of Inspector General (OIG). The Postal Service will continue to be required to provide the funding for our Office of Inspector General, the PRC, and the PRC's OIG. Although the funding for these organizations is provided by the Postal Service, the amount of funding is determined by Congress. We are directed via the appropriations process, to provide funds to these organizations in specified amounts.

Additionally, P.L.109-435 requires us to file with the PRC a number of financial reports. These include quarterly reports containing information required by the SEC to be filed on Form 10-Q within 40 days after the end of each fiscal quarter, an annual report containing information required by the SEC on Form 10-K within 60 days after the end of each fiscal year, and current reports containing information required by the SEC on Form 8-K within the prescribed time frame. Our first filings were completed in 2008. Further, P.L.109-435 requires the Postal Service to comply with the rules prescribed by the SEC implementing Section 404 of the Sarbanes-Oxley Act of 2002, which pertain to reporting on the effectiveness of our financial internal controls. The requirement to comply with Section 404 is effective beginning with the 2010 annual report.

Since the law's enactment, we have been meeting its requirements by the applicable deadlines. We have successfully worked with the mailing community, the PRC, and our unions and management associations to make the transition as smooth as possible for all stakeholders.

Strategy

The Government Performance and Results Act (GPRA) requires federal agencies to develop and publish a five-year strategic plan. The Postal Service updates its plan annually to accommodate ongoing business environment changes. This annual planning process incorporates an assessment of recent performance, refinement of strategies, and prioritization of objectives, programs, and budgets to optimize results.

In October 2008, we published *Vision 2013*, our five-year strategic plan, covering the period 2009–2013. *Vision 2013 was* designed to build upon the successes of the Postal Service's *Strategic Transformation Plan*, which helped guide multiple improvements in service, efficiency, and workplace conditions. With *Vision 2013*, the Postal Service commits to continuing this progress. It acknowledges that postal customers and the entire mailing industry are hard-pressed by current economic conditions, and notes that continued service improvements and cost reductions are crucial. The Postal Service will continue to strengthen its core operations and services, balancing an immediate and urgent need to reduce costs with a continued commitment to strategies such as Intelligent Mail®, that are essential to our future. However, in the long term, the Postal Service cannot survive on cost cutting alone; and service improvements will not, by themselves, halt revenue diversion or attract new customers. Growth is crucial to the future of affordable universal mail service.

Vision 2013 also offers a broad perspective of what it will take to continue to provide affordable, universal service and sustain a strong, viable Postal Service for future generations. It describes strategies to grow the business by adapting to changing customer needs; to create new customer value by the Postal Service leveraging its strengths; and to embrace change — incorporating new technology and new approaches to respond more quickly to a rapidly evolving business environment.

Vision 2013 is available online at www.usps.com/strategicplanning/vision2013.htm.

Segments

We operate in one segment throughout the United States, its possessions, territories, and internationally.

Services

The Postal Service is the centerpiece of the U.S. mailing industry, providing a wide variety of services to meet almost any mailing need. Services include the Mailing Services and Shipping Services described below.

Mailing Services

FIRST-CLASS MAIL - Includes domestic and international postcards, letters, or any other advertisement or merchandise up to 13 ounces. This service (or Express Mail or Priority Mail) is required for personal correspondence, handwritten or typewritten letters, and bills or statements of account.

STANDARD MAIL - Is offered for any item, including advertisements and merchandise weighing less than 16 ounces, that is not required to be sent using First-Class Mail. Standard Mail is typically used for bulk advertising to multiple delivery addresses. Content restrictions apply for authorized nonprofit mailers.

PERIODICALS – Are offered for newspaper, magazine, and newsletter distribution and require prior authorization by the Postal Service.

PACKAGE SERVICES - Are offered for any merchandise or printed matter weighing up to 70 pounds. These services include Single Piece Parcel Post, Bound Printed Matter, Library Mail, and Media Mail.

SPECIAL SERVICES - Offer a variety of enhancements that add value to mail services. Many provide added security, proof of delivery, or loss recovery. Examples of these services include: Certified Mail, Registered Mail, Delivery Confirmation, Signature Confirmation, and insurance up to $1,000.

MONEY ORDERS - Are a special service that offer a safe, convenient, and economical alternative to sending cash through the mail. They can be purchased at any Post Office or from any rural route carrier. Postal money orders are available for any amount up to $1,000. Money orders can be cashed at any Post Office or can be deposited or negotiated at financial institutions. Money orders are replaced if damaged, lost, or stolen.

Shipping Services

PRIORITY MAIL – Priority Mail is offered in both the United States and abroad. The domestic offering is a 1–3 day nonguaranteed delivery service and is typically used to send documents, gifts, and merchandise. Priority Mail International provides customers with a reliable and economical means of sending correspondence and merchandise up to 70 pounds to over 190 countries and territories worldwide.

EXPRESS MAIL – Includes Express Mail and Express Mail International. Express Mail is the domestic offering. This overnight, money-back guaranteed service includes tracking, proof of delivery, and insurance up to $100. Delivery is offered to most destinations and is available 365 days a year. A surcharge is added to the price for Sunday and holiday delivery. Commercial prices and volume rebates are available to customers meeting certain volume thresholds. Express Mail International offers fast delivery service to over 190 countries with service guaranteed to select destinations.

PARCELS – Parcel Select and Parcel Return Service are two programs designed to provide economical means of shipping packages. By taking advantage of the "first mile and last mile" aspect of the Postal Service, Parcel Select saves customers money by sorting packages closer to their ultimate destination while Parcel Return Service is a workshare discount program where our customers go to selected sites to retrieve packages sent back to them from their customers. Parcel Select and Parcel Return Service allow us to partner with other companies to serve our respective customers' needs.

Details on our revenue by mailing, shipping, and other categories are found on the Operating Statistics Section, on page 63 of this report.

Pricing and Classification Activity

P.L. 109-435 gave the Postal Service new flexibility in setting price and classification changes. Prices are set by the Governors and are approved by the PRC to be in compliance with the new regulations enacted as part of the law. We plan to adjust prices for our Mailing Services annually in May, with increases no higher than

that of the rate of inflation. We plan to provide at least 90 days' notice of the new prices for Mailing Services.
On February 11, 2008, we announced a May 12, 2008 price adjustment for Mailing Services — First-Class Mail, Standard Mail, Periodicals, Package Services, and Special Services. The average increase by class of mail was at or below the 2.9% rate of inflation, calculated using the CPI-U for the past twelve months using an averaging method approved by the PRC. The First-Class Mail stamp price was increased from 41 cents to 42 cents. For the first time, customers could use the Forever Stamps they purchased before the price change, after the price change without adding additional postage.

Prices for Shipping Services must cover each product's attributable costs, as well as an appropriate share of the institutional costs of the Postal Service. For 2008, the institutional cost coverage percentage, determined by the PRC, was 5.5%. The new pricing flexibility provided by the law allows us for the first time to utilize contract prices, rebates, online price reductions, and other incentives to encourage growth. Prices must be announced at least 30 days prior to the implementation date. We provided 60 days notice prior to the May 12, 2008, price adjustment for Shipping Services.

Highlights of the Shipping Services price adjustments are described below. Express Mail was changed to a zone-based pricing system, with customers paying less for nearby destinations. Customers also receive a 3% price reduction for purchasing Express Mail online or through corporate accounts. Additional price reductions became available for those who ship quarterly minimum volumes. Priority Mail offers a 3.5% savings for customers who use electronic postage or meet other requirements. Parcel Select — our "last mile" delivery to every door — features pricing and volume incentives for large and medium shippers. Parcel Return Service moved entirely to a weight-based pricing system, resulting in significant price reductions for many lighter packages.

The PRC reviewed the new pricing for both Mailing Services and Shipping Services and verified, with a small exception which was resolved, that our prices were consistent with P.L. 109-435.

In March 2008, we introduced the Priority Mail Large Flat-Rate Box, with pricing that included a military discount for the first time. The discount is intended to enhance goodwill and reflect the unique economics of military care packages. We transferred Premium Forwarding Service to the Shipping Services grouping to facilitate future product and service enhancements. Repositionable Notes became a permanent offering.

Information about the PRC and their activities can be found on the PRC website at *www.prc.gov*.

Intellectual Property

We own intellectual property that includes trademarks, service marks, patents, copyrights, trade secrets, and other proprietary information. We routinely generate intellectual property in the course of developing and improving our systems, services, and operations.

Seasonal Operations

Our operations are seasonal. Mail volume and revenue tend to be greatest in our first fiscal quarter, which includes the fall holiday mailing season, and lowest during the summer, our fourth quarter.

Customers

We have a very diverse customer base and are not dependent upon a single customer or small group of customers. No single customer represents more than 3% of our operating revenue. The financial services sector, which includes real estate, represents approximately 15% of our operating revenues.

Government Contracts

No material portion of our business is subject to renegotiation of profits or termination of contracts or subcontracts at the election of the U.S. government.

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.

Environmental Matters

We are not aware of any federal, state, or local environmental laws or regulations that will materially affect our financial results or competitive position, or result in material capital expenditures. However, we cannot predict the effect of possible future environmental legislation or regulations on our operations.

Employees

At September 30, 2008, we had 663,238 career employees, substantially all of whom reside in the United States. We also had 101,850 non-career employees.

Our labor force is primarily represented by the American Postal Workers Union (APWU), National Association of Letter Carriers (NALC), National Postal Mail Handlers Union (NPMHU), and National Rural Letter Carriers Association (NRLCA). More than 85% of our career employees are covered by collective bargaining agreements. By law, we consult with management organizations representing most of the employees not covered by collective bargaining agreements. These consultations provide nonbargaining unit employees in the field an opportunity to participate directly in the planning, development, and implementation of programs and policies that affect them. Our management organizations include the National Association of Postal Supervisors, the National League of Postmasters, and the National Association of Postmasters of the United States. We participate in federal employee benefit programs as required by statute, for retirement, health, and workers' compensation benefits.

Available Information

Financial and other information is available on *www.usps.com:* click on *About USPS and News*. Information on our website is not incorporated by reference in this document.

We make available on our website, free of charge, copies of our annual report and quarterly reports, as soon as reasonably practicable after they are filed with or provided to the PRC. Requests for copies 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

Our operations and financial results are subject to various risks and uncertainties, including those described below, that could adversely affect our business, financial condition, results of operations, and cash flows. The remainder of this report, including sections entitled "Business" and "Management's discussion and analysis of financial condition and results of operations," will provide the reader with a more complete understanding of the risks and uncertainties we confront.

Adverse changes in the economy directly impact our business, adversely affecting our results of operations.

The demand for postal services is heavily influenced by changes in the economy. A continuation of the slowdown in the economy is expected to impact nearly every class of mail negatively. The continual decline in employment, lasting since January 2008, has been indicative of this economic malaise. In recent months, turmoil in the financial markets has resulted in a worldwide credit crisis, which raises economic risk significantly. Moreover, a long run-up in commodities prices – including, most notably, energy prices – was followed by a rapid decline beginning in mid-summer 2008. Volatile market conditions such as these are expected to have an adverse impact on retail sales, investment, consumer spending, and consumer confidence. Adverse trends in retail sales, investment spending, and employment are all likely to depress the demand for postal services.

Expanding use of electronic communications methods and other commercial services compete with some of our principal services. If we do not compete effectively with these services, our business and results of operations will be adversely affected.

The Internet continues to change the communications market. Within the next decade, further innovations in mobile commerce, broadband, interactive TV, data mining software, and new printing technologies will continue to affect the way businesses and consumers interact. Of greatest impact on the Postal Service are electronic alternatives to correspondence and transactions, particularly for First-Class Mail and Standard Mail items such as business correspondence, bills, statements and customer payments and, increasingly, advertising. First-Class Mail volume has already been affected by the Internet, automatic deductions, direct deposit, telephone, fax machines, and other electronic communications.

In addition, major corporations now dominate the parcel and express markets, and the competitive landscape for postal services is becoming more global. Foreign postal operators are moving outside their geographic borders and expanding beyond their traditional postal services into express delivery, logistics, financial, and electronic services. Foreign posts have established significant nationwide sales forces and operations around the country. Currently, eight foreign operators maintain facilities in major metropolitan areas. In addition, many are partnering with international mail service providers to authorize use of their postal indicia for export from the United States. This has contributed to an increase in the outbound market share of our foreign competitors.

While the majority of our prices are now linked directly to general inflation, our costs are not. Accordingly, we may not be able to increase prices sufficiently to offset increased costs, which would adversely affect our results of operations.

P.L.109-435 is intended to benefit both residential and business customers by providing predictable price increases tied to the rate of inflation for Mailing Services (primarily First-Class Mail, Standard Mail, certain Package Services, and Periodicals). These services represent about 90% of total revenues and about 87% of our attributable costs.

While the majority of our prices are now linked directly to general inflation, our costs are not. Postal costs are heavily concentrated in wages, employee and retiree benefits, and transportation. They are significantly impacted by wage inflation, health benefit premium increases, and by the continuous expansion of our delivery network. We believe that both volume and revenue growth, along with increasing productivity improvements, will be required to address the challenge presented by the regulatory price cap.

The contracts with our four largest unions currently include provisions granting cost of living allowances (COLAs). These contracts expire in 2010 and 2011. Under current contract provisions, COLAs are linked to the Consumer Price Index – Urban Wage Earners and Clerical Workers (CPI-W) and are granted semiannually. In 2008 CPI-W was 5.4%. Employee compensation represents a significant portion of our annual expenses; therefore, an increase in the CPI-W greater than had been incorporated into our financial plans could adversely affect financial results. We estimate that an increase in the CPI-W of 0.5% would cause an annualized increase in our COLAs of about $124 million.

Adverse events may call into question our reputation for quality and reliability, which could diminish the value of the Postal Service brand and potentially adversely affect our business and results of operations.

We serve almost every American household and business nearly every day. For the fourth year in a row, the Ponemon Institute named the Postal Service the most trusted government agency and among the ten most trusted of all organizations. The Postal Service brand represents quality and reliable service and therefore is a valuable asset. We use our brand extensively in sales and marketing initiatives, and take care to defend and protect it. Any event that calls into question this quality and reliability could diminish the value of our brand and potentially adversely affect our business and reputation.

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

Fuel prices are a significant part of our expenses. We are exposed to changes in commodity prices primarily for diesel fuel, unleaded gasoline, and aircraft fuel for transportation of the mail, and natural gas for heating facilities. A 1.0% increase in fuel and natural gas costs would result in a $29 million increase in expense. We did not use derivative commodity instruments to manage the risk of changes in energy prices during the periods covered by this report.

We are subject to Congressional oversight, regulation by other government agencies, and also oversight by various other organizations and the public. If we cannot successfully address their various, and sometimes competing, concerns, we may be subject to greater regulation, which could increase our costs or otherwise place additional burdens on our operations.

We are subject to a variety of forms of oversight and scrutiny by Congress, the PRC, mailer organizations, the media, and the general public. This is an outgrowth of our unique status as a provider of a fundamental service to the American people. We attempt to balance the interests of all groups with the need for operational efficiency. Our efforts to be responsive to these various stakeholders sometimes adversely impact the speed with which we are able to respond to changes in mail volumes, or other operational needs. Any limitations on our ability to take management action could adversely affect our operating and financial results.

We are potentially subject to various state legislative proposals which could reduce our revenues, increase our costs, or otherwise place additional burdens on our operations.

States continued to introduce Do Not Mail legislation in 2008, with approximately 16 Do Not Mail bills being considered in 13 state legislatures nationwide. (This includes nine bills that were carried over from 2007.) These bills, modeled after the Do Not Call registry, are designed to limit or stop advertising mail from being mailed to households. Currently, none of the state bills have passed; however, a few of the state legislatures may still be in session.

The Postal Service opposes legislation that would limit mailing, or that would interfere with the availability of an affordable, universal postal system. The Postal Service will continue to communicate the value of the mail by building upon its strong environmental record and its work with mailers on offering consumers choice on how to manage their mail. By working aggressively with mailers, marketers, and advertisers, the Postal Service can continue to improve the quality and relevancy of advertising mail.

Should a state pass Do Not Mail legislation, it would result in lost revenue for the Postal Service. A financial analysis conducted by the Postal Service determined that a national implementation of Do Not Mail legislation would place approximately $6 billion of postal revenue at risk annually.

We rely extensively on technology to operate our systems. A significant failure in a material system could impair our reputation for reliable service and adversely affect our results of operations.

We rely extensively on technology to operate our systems for processing and delivering mail. Our intranet is one of the largest maintained by any organization in the world. Any significant failure of these systems could cause delays in the processing and delivering of mail, which could damage our reputation, result in loss of business, and increase costs of operation.

A failure on our part to protect the privacy of information we obtain from our customers could damage our reputation and result in a loss of business.

We receive a variety of private information from our customers, such as address change data. We have implemented a number of safeguards intended to protect the confidentiality of data that we obtain. Any significant violation of the privacy of this data could damage our reputation and result in loss of business.

We are subject to the risk of biohazards and other threats being placed in the mail.

Although we have implemented extensive emergency preparedness measures to keep the mail, postal employees, and postal customers safe from harm due to biohazards that could be introduced into the mail stream, there continues to be a risk of possible biohazard threats. If new biohazards were to arise and our measures were not sufficient to contain or mitigate the threat, our services could be disrupted. This could adversely affect our revenues, require substantial expenditures to address the threat and could adversely affect our operations and financial condition.

In addition, the U.S. Transportation Security Administration ("TSA") has adopted new rules enhancing many of the security requirements for air cargo, and has proposed additional requirements. Until the requirements of these programs and their application to us are finalized, we cannot determine the effect that these new rules may have on our costs or our results of operations. These rules or other future security requirements for air cargo could impose material new costs on us.

We are also subject to risks and uncertainties that affect many other businesses, including:

- Market acceptance of our new service and growth initiatives;

- Adverse weather conditions or natural disasters, such hurricanes, which can damage our property and disrupt our operations;

- International conflicts or terrorist activities and the effects these events may have on our business or our results of operations; and

- Changes in interest rates and foreign currency exchange rates.

Item 2 – Properties

Real Estate

Our facilities range in size from 60 square feet to 34 acres under one roof, and support retail, delivery, mail processing, maintenance, administrative, and support activities.

Real Estate Inventory	2008	2007
(Actual numbers)		
Leased Facilities	25,272	25,450
Owned Facilities	8,546	8,487
GSA / Other Government Facilities	357	381
Total Real Estate Inventory	**34,175**	**34,318**
Annual Rent Paid to Lessors (Dollars in millions)	**$ 1,011**	**$ 973**

The majority of our small- and medium-sized facilities support the retail and delivery operations located in virtually every community across this country. Our retail and delivery operations are supported by 32,741 leased or owned facilities. We also provide retail services through 3,982 Contract Postal Units and community Post Offices where the facility is owned and maintained by the contractor.

Retail and Delivery Facilities	2008	2007
(Actual numbers)		
Post Offices	27,232	27,276
Classified Branches	1,493	1,508
Classified Stations	3,358	3,379
Carrier Annexes	658	532
Contract Postal Units	3,148	3,131
Community Post Offices	834	895
Total Retail and Delivery Facilities	**36,723**	**36,721**

Our larger facilities typically support mail processing operations, which process millions of pieces of mail on a daily basis, and prepare it for transportation across the country.

Processing Facilities	2008	2007
(Actual numbers)		
Processing and Distribution Centers	269	269
Customer Service Facilities	195	195
Bulk Mail Centers	21	21
Logistics and Distribution Centers	14	14
Annexes	64	66
Surface Transfer Centers	20	14
Airmail Processing Centers	20	29
Remote Encoding Centers	6	10
International Service Centers	5	5
Total Processing Facilities	**614**	**623**

We also have approximately 1,000 other facilities. These facilities include administrative, vehicle maintenance, and miscellaneous support facilities.

Vehicles

We have one of the largest vehicle fleets in the United States, including an extensive fleet of alternative fuel vehicles.

Vehicle Inventory	2008	2007
(Actual numbers)		
Delivery and Collection Vehicles (1/2 - 2 1/2 ton)	197,898	195,211
Mail Transport Vehicles (Tractors and Trailers)	6,455	6,824
Administrative Vehicles and Other Vehicles	5,906	6,169
Service Vehicles (Maintenance)	5,272	5,539
Inspection Service and Law Enforcement Vehicles	3,288	3,482
Mail Transport Vehicles (3 - 9 ton)	2,228	2,297
Total Vehicles	**221,047**	**219,522**

Item 3 – Legal proceedings

We are subject to various claims and liabilities that arise in the normal course of postal operations. These claims generally relate to labor, tort, and contract disputes and are regularly reviewed by management, and where significant, by the Audit and Finance Committee of the Board of Governors, and/or the full Board of Governors. In our evaluation, no single claim is material to our financial statements taken as a whole.

Item 4 – Submission of matters to a vote of security holders

Not applicable to the United States Postal Service. As an “independent establishment of the executive branch of the Government of the United States,” we do not issue stock or other voting securities.

Part II

Item 5 – Market for registrant's common equity, related stockholder matters and issuer purchases of equity securities

Not applicable to the United States Postal Service. As an "independent establishment of the executive branch of the Government of the United States," we do not issue stock or other securities.

Item 6 – Selected financial data

See the *Financial History Summary* and *Selected Quarterly Financial Data* sections of this report.

Item 7 – Management's discussion and analysis of financial condition and results of operations

Cautionary Statements

Forward-looking statements contained in this report represent our best estimates of trends we know about, trends we anticipate, and trends we believe are relevant to our future operations. However, actual results may be different from our estimates. Certain forward-looking statements are included in this report and use such words as "may," "will," "could," "expect," "believe," "plan," or other similar terminology. These statements reflect our current expectations regarding future events and operating performance as of the date of this report. These forward-looking statements involve a number of risks and uncertainties.

The following are some of the factors that could cause actual results to differ materially from those expressed in, or underlying, our forward-looking statements: effectiveness of operating initiatives; success in advertising and promotional efforts; changes in national and local business and economic conditions, including their impact on consumer and business confidence; fluctuations in currency exchange and interest rates; labor and other operating costs; oil, fuel, and other transportation costs; the effects of war and terrorist activities; competition, including pricing and marketing initiatives and new service offerings by our competitors; consumer preferences or perceptions concerning our service offerings; spending patterns and demographic trends; availability of qualified personnel; severe weather conditions; effects of legal claims; cost and deployment of capital; changes in laws and regulations; costs and delays associated with new regulations imposed by the PRC; and changes in applicable accounting policies and practices. The foregoing list of important factors is not all-inclusive. We have no obligation to publicly update or revise any forward-looking statements, whether as a result of new information, future events, or otherwise.

Critical Accounting Policies

The preparation of financial statements in accordance with accounting principles generally accepted in the United States requires management to make significant judgments and estimates to develop certain amounts reflected and disclosed in the financial statements. In many cases, there are alternative policies or estimation techniques that could be used. We maintain a thorough process to review the application of our accounting policies and to evaluate the appropriateness of the many estimates that are required to prepare the financial statements of a large organization. However, even under optimal circumstances, estimates routinely require adjustment based on changing circumstances and new or better information.

The three critical accounting policies that we believe are either the most judgmental or involve the selection or application of alternative accounting policies, and are material to our financial statements, are those relating to workers' compensation costs, deferred revenue for prepaid postage, and contingent liabilities. Workers' compensation costs are highly sensitive to the estimates of inflation and the length of time recipients stay on the compensation rolls. Deferred revenue for prepaid postage is challenging to estimate because of the difficulty in estimating stamp postage that has been purchased but has not yet been used. Contingent liabilities require significant judgment in estimating potential losses for legal claims. In addition, retirement and health benefits costs for our employees and retirees represent a significant portion of our expenses. Any changes in laws or regulations affecting the amounts, timing, or administration of these benefits could have a material effect on our financial position and results of operations. For additional information, see Note 2, *Summary of significant accounting policies,* in the Notes to the Financial Statements.

We recognize revenue when services are rendered. Because we collect payment in advance of services being performed, we defer the revenue as an estimated liability. This liability is classified as *deferred revenue–prepaid postage* on our balance sheets. In Quarter III of the current year, we improved the model used to estimate the deferred revenue for prepaid postage for stamps. This change was made necessary because the introduction of the Forever Stamp in April 2007, combined with the May 2008 price increase, resulted in a change in consumer behavior regarding the purchase and usage of stamps that was not measurable using our prior estimation techniques. This more accurately captures trends in stamp usage. The change to a new estimation model is considered a change in accounting estimate under Generally Accepted Accounting Principles (GAAP).

As required by GAAP, the impact of the change was recorded in Quarter III, 2008. For the year-ended 2008, we increased the stamp portion of the deferred revenue–prepaid postage liability by $477 million, $230 million of which is considered a cumulative change in estimate and $247 million of which is attributable to changes in consumer behavior during the last two quarters of the year. For further information, see Note 2 to the financial statements.

Results of Operations

In 2008, we had an operating loss of $2,806 million, as compared to a $5,327 million loss in 2007. Operating revenues of $74,932 million for 2008 were 0.2%, or $154 million greater than the $74,778 million earned in 2007. Despite the May 2007 and May 2008 price increases, revenues were negatively impacted by a decline in volume of 9.5 billion pieces. The volume drop was mainly due to the deteriorating economy, which adversely impacted almost every category of mail.

Operating Statistics (Dollars in millions)	2008	2007	2006
Operating Revenue	$ 74,932	$ 74,778	$ 72,650
Operating (Loss) / Income	$ (2,806)	$ (5,327)	$ 969
Net (Loss) / Income	$ (2,806)	$ (5,142)	$ 900
Operating Margin	-3.7%	-7.1%	1.3%
Avg Volume per Day (millions of pieces)	667	705	703

Our 2008 expenses were impacted by high energy prices, COLAs, and the large percentage of our costs, which are fixed. Operating expenses of $77,738 million were $2,367 million less than the $80,105 million incurred in 2007. As discussed later in this section, operating expenses included a decrease in retiree health benefits of $2,677 million and a decrease in compensation and benefits expense of $601 million, which were partially offset by increases in transportation expenses of $459 million and other expenses of $452 million.

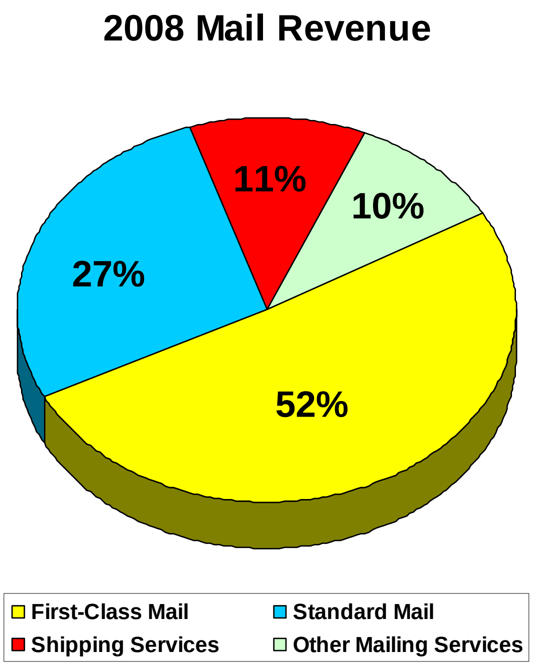
The operating loss for 2007 was $5,327 million, as compared to operating income of $969 million in 2006, a decrease of $6,296 million. This change was largely due to the additional retiree health benefit expenses incurred upon the enactment of P.L.109-435. On April 6, 2007, we transferred $2,958 million, representing the entire amount of funds held in escrow, as required by P.L.108-18, to the Postal Service Retiree Health Benefits Fund (PSRHBF). Since we no longer held these funds, there was a 22% decrease in interest income for the second half of 2007 and this continued into 2008, where interest income declined 82% compared to 2007.

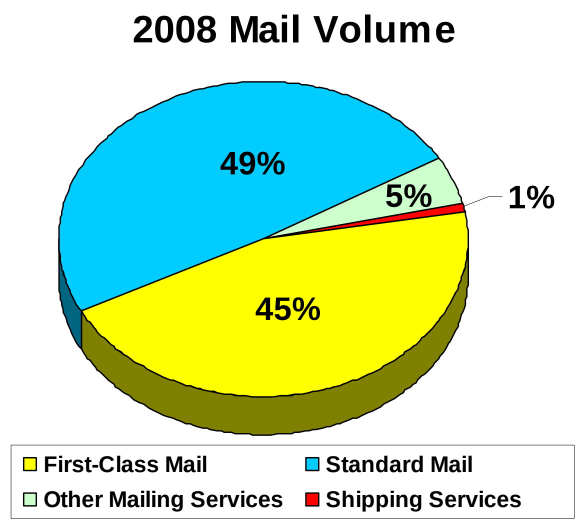
Revenue and Volume

On December 20, 2006, the President signed P.L.109-435. In accordance with that law, the categorization of our products has been updated to reflect the new Mailing Services and Shipping Services groupings. For example, First-Class Mail now also includes First-Class Mail International and is part of Mailing Services. Shipping Services include Express Mail and Priority Mail as well as certain services formerly included with international mail and package services. We have identified changes in categories in the discussion that follows.

2008 was an extremely difficult year for both the U.S. economy and the Postal Service. Declining mail volume is a symptom of the ailing economy. The hard-hit financial sector of the U.S. economy led decliners not just in the stock market, but in the mailing arena as well. Operating revenue for 2008 was $74,932 million, an increase of $154 million from last year, while volume of 202.7 billion pieces declined by 9.5 billion pieces, or 4.5%. The volume decline accelerated as we progressed through 2008, reaching a peak decline of 3.2 billion pieces in the fourth quarter.

Revenue for the first seven and a half months of 2008 was affected by the May 2007 price increase of 5.4%. The remainder of the year was affected by the May 2008 price increase of 2.9%. Although the volume decrease in 2008 was significant, the price increase held revenue flat compared to 2007.





Mailing Services

While Standard Mail volume exceeds First-Class Mail volume, First-Class Mail remains, by far, the largest revenue generator, as illustrated by the two previous revenue charts.

Operating Revenue	2008	2007	2006
(Dollars in millions)			
First-Class Mail	$ 38,179	$ 38,405	$ 37,605
Standard Mail	20,586	20,779	19,876
Periodicals	2,295	2,188	2,215
Package Services	1,845	1,812	1,751
Other Mailing Services*	3,645	3,720	3,715
Total Mailing Services	**66,550**	**66,904**	**65,162**
Total Shipping Services	**8,382**	**7,874**	**7,488**
Total Operating Revenue	**$ 74,932**	**$ 74,778**	**$ 72,650**

** Special services revenue and other income included in "Other" category.*

Mail Volume By Type	2008	2007	2006
(Pieces in millions)			
First-Class Mail	91,697	96,297	98,016
Standard Mail	99,084	103,516	102,460
Periodicals	8,605	8,796	9,023
Package Services	846	914	919
Other Mailing Services*	896	1,081	1,084
Total Mailing Services	**201,128**	**210,604**	**211,502**
Total Shipping Services	**1,575**	**1,630**	**1,636**
Total Mail Volume by Type	**202,703**	**212,234**	**213,138**

** Free mail for the blind included in the "Other" category.*

The current recession has had an adverse effect on advertising mail, particularly with regard to credit card, mortgage, and home equity solicitations. While the trouble in the financial services sector is routinely making headlines, we have also experienced noteworthy declines from mail order catalogue retailers, printing and publishing businesses, and the services sector.

The First-Class Mail category now includes First-Class Mail International. First-Class Mail revenue decreased $226 million, or 0.6%, while volume decreased by 4.6 billion pieces, or 4.8%, in 2008. The revenue decrease occurred in spite of two price increases. Only non-automation presort and First-Class International letters experienced increases in volume. The most significant decline was in single-piece First-Class letters, with a decrease of over 3 billion pieces of mail. The long-term continued decline in single-piece volume reflects the impact of electronic diversion as businesses, nonprofit organizations, governments, and households continue to move their correspondence and transactions to electronic alternatives, such as Internet bill payment, automatic deduction, and direct deposit. The rate of decline accelerated significantly in 2008 as the economy weakened. Presorted First-Class Mail also decreased. This is a reflection of the general curtailment of advertising spending. This curtailment of advertising has significantly impacted both First-Class Mail and Standard Mail.

In 2007, First-Class Mail revenue increased $800 million, or 2.1%, as volume decreased by 1.7 billion pieces, or 1.8%. First-Class Mail represented 51% of total operating revenues and 45% of total volume in 2007.

First-Class Mail Changes from Prior Year

2008	Quarter 1	Quarter 2	Quarter 3	Quarter 4	Total
(Dollars & Pieces in Millions)					
Revenue Change	$ 193	$ 264	$ (180)	$ (503)	$ (226)
Percentage	1.9%	2.8%	-1.9%	-5.4%	-0.6%
Volume Change	(993)	(760)	(1,282)	(1,565)	(4,600)
Percentage	-3.9%	-3.1%	-5.4%	-6.9%	-4.8%

Standard Mail Changes from Prior Year

2008	Quarter 1	Quarter 2	Quarter 3	Quarter 4	Total
(Dollars & Pieces in Millions)					
Revenue Change	$ 201	$ 101	$ (161)	$ (334)	$ (193)
Percentage	3.6%	2.0%	-3.2%	-6.3%	-0.9%
Volume Change	(776)	(760)	(1,368)	(1,528)	(4,432)
Percentage	-2.7%	-3.0%	-5.6%	-6.1%	-4.3%

Standard Mail revenue decreased almost $200 million, or 0.9%, in 2008, while volume decreased 4.4 billion pieces or 4.3%. Standard Mail items are primarily advertising materials and are particularly sensitive to economic contractions. The drop in Standard Mail volume is a direct reflection of the poor state of the economy, as we experienced accelerated declines in volume as the year progressed. The decline of 1.5 billion pieces in Quarter IV was only topped in severity by the 2.2 billion-piece decline in Standard Mail in Quarter I of 2002 following the anthrax attacks and the terrorism of September 11, 2001. The decline is primarily due to the curtailment of advertising, which is expected to continue through 2009, before rebounding beginning in 2010.

In 2007, Standard Mail revenue increased $903 million, or 4.5%, compared with 2006 on 1.0% volume growth. The first quarter was favorably impacted by the carryover effect of the January 2006 price increase. A portion of the third quarter and all of the fourth quarter benefited from the May 2007 rate increase. Standard Mail represented 28% of total operating revenues and 49% of total volume in 2007.

Periodicals volume decreased 191 million pieces, or 2.2%, in 2008. Price increases resulted in a revenue increase of $107 million, or 4.9%. Total periodicals volume has fallen by 16.6% over the last ten years. This long-term, steady decline is the result of the ongoing trend in reading preferences rather than the current economic downturn.

Periodicals volume decreased 227 million pieces, or 2.5% in 2007, driven by the same long-term trend noted above. This resulted in a revenue decrease of $27 million, or 1.2%, in spite of the price increase.

Package Services under the new law now includes single-piece Parcel Post, International Inbound Surface Parcel Post, Bound Printed Matter, Media Mail, and Library Mail. Parcel Select and Parcel Return Service are now part of the Shipping Services group. Price increases resulted in a revenue increase of $33 million, or 1.8%, compared to 2007. Package Services volume decreased 68 million pieces, or 7.4%, in 2008. Revenue increased despite volume decreases, due to the May 2007 and May 2008 price increases.

In 2007, Package Services revenues of $1,812 million increased $61 million or 3.5% on a volume decline of 5 million pieces or 0.5%.

Shipping Services

Under the new law, Shipping Services includes Priority Mail, Express Mail, destination entry Parcel Post, Parcel Select Return Service and International Mail, excluding single-piece First-Class International Mail. Collectively these products earned $8,382 million in revenue, a $508 million increase, or 6.5%, while volume declined 55 million pieces, or 3.4%. The pricing structure of this service group does not have the CPI price cap restrictions of Mailing Services as outlined in P.L. 109-435.

Shipping Services revenue in 2007 of $7,874 million was $386 million, or 5.2% greater than 2006 revenues of $7,488 million, despite a volume decline of 6 million pieces, or 0.4%.

Operating Expenses

Operating expenses are comprised of Compensation and Benefits, Retiree Health Benefits, Transportation, and Other Expenses.

In 2008, total operating expenses of $77,738 million were $2,367 million, or 3.0%, less than 2007, mainly due to the decrease of $2,677 million in retiree health benefits. Retiree health benefits were $7,407 million in 2008, compared to $10,084 million in 2007. The decrease is primarily due to a 2007 one-time charge in addition to the annual amounts required by P.L. 109-435. See Note 4, *Postal Accountability and Enhancement Act, Public Law 109-435 (P.L. 109-435)*, in the Notes to the Financial Statements for more information. Despite the decrease, compensation and benefits, along with retiree health benefits were $60,992 million, or 78.5%, of our operating expenses compared to $64,270 million or 80.2% in 2007. Transportation expense increased $459 million, or 7.1%, while other expense increased $452 million, or 4.8%.

In 2007, total operating expenses of $80,105 million were $8,424 million, or 11.8%, more than 2006. Retiree health benefits increased $8,447 million in 2007, driven by requirements of P.L. 109-435. The law also suspended our retirement payments to the CSRS fund, which, along with a reduction in the estimate of our workers' compensation liability, led to a $479 million, or 0.9%, decrease in total compensation and benefit expenses compared to 2006. A $457 million, or 7.6%, increase in transportation expenses also contributed to the increase in expenses.

Operating Expenses (Dollars in millions)	**2008**	**2007**	**2006**
Compensation and Benefits	$ 53,585	$ 54,186	$ 54,665
Retiree Health Benefits	7,407	10,084	1,637
Transportation	6,961	6,502	6,045
Other Expenses	9,785	9,333	9,334
Total Operating Expenses	**$ 77,738**	**$ 80,105**	**$ 71,681**

Compensation and Benefits

Personnel compensation and benefits were $601 million, or 1.1%, less than 2007, mainly due to reductions in workhours. The average annual COLA increase per employee in 2008 was $469 in March and $1,487 in September. The total impact of COLAs in 2008 was $562 million.

Despite these large COLAs, which increased the 2008 average hourly labor cost 2.5%, we were able to decrease compensation costs by $1,062 million, or 2.5%, by reducing workhours. However, this was partially offset by increases of $162 million, or 2.8%, in retirement expenses and $347 million, or 39.4%, in worker's compensation expense. Decreases in health benefits and other expenses accounted for the remainder of the decrease. Additional information on workhours, retirement, health benefits, and workers' compensation expenses are provided on the following pages.

Compensation and Benefits Expenses (Dollars in millions)	**2008**	**2007**	**2006**
Compensation	$ 40,633	$ 41,695	$ 40,577
Retirement	5,899	5,737	7,006
Health Benefits	5,376	5,401	5,345
Workers' Compensation	1,227	880	1,279
Other	450	473	458
Total	**$ 53,585**	**$ 54,186**	**$ 54,665**

In 2007, personnel compensation and benefits costs of $54,186 million were $479 million, or 0.9%, less than 2006. The decrease was due to elimination of the employer's share of the CSRS contribution resulting from the enactment of the new law and reductions in workhours, complement, and workers' compensation costs.

Although total compensation and benefits were lower in 2007, our labor costs increased by $1,118 million, or 2.8%. COLA increases in 2007 added $871 million to our compensation expenses. These increases were offset somewhat by a decrease of 36 million labor hours. Our 2007 average hourly labor cost increased by 1.6%, compared to an increase of 4.5% in 2006. In 2007, workers' compensation decreased by $399 million. See Workers' Compensation later in this section and Note 11, *Workers' compensation,* in Notes to the Financial Statements for additional information.

Workhours

In addition to labor and benefits rates, workhours are a major driver of our compensation and benefits expense. In 2008, mail processing, customer service, and city delivery and other, workhours decreased by 50 million compared to 2007 offsetting the higher labor rates. The reduction in workhours was in part an outcome of lower mail volumes, which reduced workload. As mail volume fell throughout the year, management initiated a number of efforts to reduce workhours, especially overtime.

Rural delivery increased 0.2 million workhours in 2008. The rural delivery workhour growth was driven by the addition of almost 710,000 new rural delivery points.

Workhours by Function	**2008**	**2007**	**2006**
(Workhours in thousands)			
City Delivery	452,288	462,040	468,918
Mail Processing	293,108	315,825	332,269
Customer Services & Retail	217,236	233,791	246,538
Rural Delivery	189,950	189,709	186,164
Other, including Plant, Operational Support, and Administrative	220,772	221,636	224,840
Total Workhours	**1,373,354**	**1,423,001**	**1,458,729**

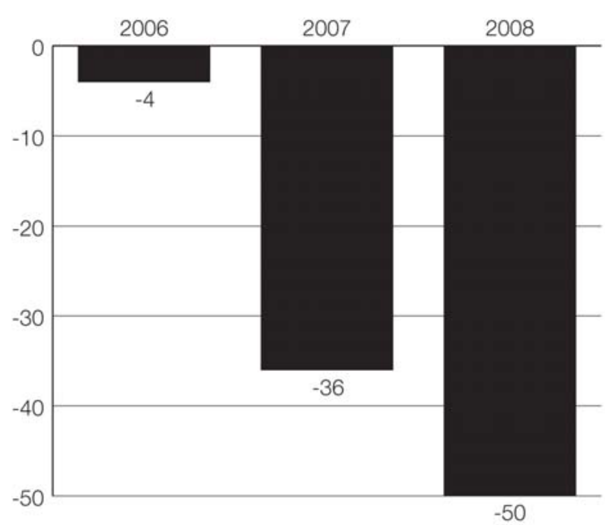
In 2007, total workhours decreased by 36 million hours compared to 2006, partially offsetting the higher labor rates. Mail processing, customer service, and city delivery workhours decreased 36 million hours.

Rural delivery increased 3.5 million workhours in 2007. The rural delivery workhour growth was driven by the addition of more than one million new rural delivery points. Other workhours decreased by three million compared to 2006.

Workhours have been reduced in eight of the last nine years with only 2005 showing a slight increase. Since 2002, workhour reductions have been the single biggest contributor to the ongoing achievement of our savings targets.

Workhour Reductions

(Hours in millions)



In 2007, we entered into new agreements with our four largest labor unions. The APWU and the NRLCA agreed to new four-year contracts, while the NPMHU and NALC entered into five-year agreements. COLA-based changes were included in the agreements.

Our non-bargaining employees receive pay increases through a pay-for-performance program that makes meaningful distinctions in performance. These employees do not receive automatic salary increases, nor do they receive COLAs or locality pay.

Retirement Expense

Our employees participate in one of three retirement programs of the U.S. government, based on the starting date of their employment with the federal government. These programs are the Civil Service Retirement System (CSRS), the Dual CSRS/Social Security System (Dual CSRS), and the Federal Employees Retirement System (FERS). The programs are administered by the OPM. See Note 10, *Retirement programs,* in the Notes to the Financial Statements for additional information.

The expenses of all of our retirement programs, except for retiree health benefits, are included in compensation and benefits expense. These expenses represented 7.6% of our total operating expenses in 2008, 7.2% in 2007, and 9.8% in 2006. Retirement expense for current employees of $5,899 million was $162 million, or 2.8%, greater than in 2007. The 2008 increase is largely attributable to the higher employer contributions resulting from higher average wage rates in 2008, largely due to COLAs. The decrease in 2007, as compared to 2006, is mainly due to the enactment of P.L. 109-435, which suspended our CSRS retirement contribution as of October 14, 2006, but increased our contributions into the PSRHBF.

As described in Note 2, *Summary of significant accounting policies,* in the Notes to the Financial Statements, we account for our participation in the retirement programs of the U.S. government under multiemployer plan accounting rules, in accordance with Financial Accounting Standard Board Statement 87, *Employers' Accounting for Pensions*. Although the Civil Service Retirement and Disability Fund (CSRDF) is a single fund and does not maintain separate accounts for individual agencies, P.L. 109-435 requires us to make certain disclosures regarding the obligations and changes in net assets as if the funds were separate. All of the following information is provided from OPM and represents the most recent data available (i.e. actual data as of September 30, 2007) with projections to September 30, 2008.

Funding Status

The following table provides OPM's estimation of the funding status of the CSRS and FERS programs for Postal Service participants as of September 30, 2007, and 2006, and the projected obligation as of September 30, 2008.

In June 2007, the $17.1 billion surplus attributed to the CSRS plan on September 30, 2006, was transferred to the newly created PSRHBF.

Present Value Analysis of Retirement Programs
as calculated by OPM (9/30/07 latest data available)

(Dollars in billions)

CSRS	**Projected 2008**	**2007**	**2006**
Actuarial Accrued Liability 9/30	$ 200.0	$ 196.9	$ 190.5
Current Fund Balance	196.7	193.8	207.6
(Unfunded) / Surplus	**$ (3.3)**	**$ (3.1)**	**$ 17.1**

FERS	**Projected 2008**	**2007**	**2006**
Actuarial Accrued Liability 9/30	$ 61.1	$ 55.1	$ 49.3
Current Fund Balance	69.9	63.5	58.0
Surplus	**$ 8.8**	**$ 8.4**	**$ 8.7**

TOTAL CSRS and FERS	**Projected 2008**	**2007**	**2006**
Actuarial Accrued Liability 9/30	$ 261.1	$ 252.0	$ 239.8
Current Fund Balance	266.6	257.3	265.6
Surplus	**$ 5.5**	**$ 5.3**	**$ 25.8**

Net Periodic Costs

Information about the net periodic costs for the CSRS and FERS pension plans, which is prepared by OPM, is as follows:

Components of Net Periodic Costs
as calculated by OPM (9/30/07 latest actual data available)

(Dollars in billions)	CSRS Projected 2008	CSRS 2007	FERS Projected 2008	FERS 2007
Actuarial Liability as of October 1	$ 196.9	$ 193.7	$ 55.1	$ 49.3
+Expected Contributions*	0.5	0.5	3.2	3.0
-Expected Benefit Disbursements	(9.4)	(8.9)	(0.8)	(0.7)
+Interest Expense	12.0	11.8	3.6	3.2
-Actuarial Gain due to Actual Experience during FY	-	(4.4)	-	(0.6)
+Actuarial Loss Due to Change in Assumptions	-	4.2	-	0.9
Actuarial Liability as of September 30	**$ 200.0**	**$ 196.9**	**$ 61.1**	**$ 55.1**

** Expected contribution for CSRS consists of employee contributions only.*
Expected contribution for FERS includes both employee and employer amounts

Cost Methods and Assumptions

OPM made the following assumptions in completing its analysis:

- The actuarial cost method is Entry Age Normal
- Long-term economic assumptions are as follows:
  - Rate of inflation – 3.5%
  - FERS COLA – 2.8%
  - Annual general salary increases – 4.25%
  - Interest rate – 6.25%
  - The Postal Service is not required to make any agency contributions to CSRS
  - Postal Service contributions to FERS will not change; contributions will continue at the current rate of 11.2% of pay (the employee contribution is 0.8% of pay)

The OPM Board of Actuaries decided to incorporate an assumption of future mortality improvement into the actuarial valuation as of September 30, 2007. This caused the dynamic normal cost of CSRS to increase from 25.2% of pay to 25.8% and the FERS normal cost to increase from 12.0% to 12.3%.

Components of Net Change in Plan Assets

The following table prepared by OPM shows the components of the net change in plan assets for the CSRS and FERS programs.

Analysis of Change in Pension Net Assets during FY 2007
as calculated by OPM (9/30/07 latest actual data available)

(Dollars in billions)		CSRS Actual		FERS Actual
Net Assets as of 9/30/2006*	$	207.9		58.0
+Contributions		0.6		3.0
-Benefit Disbursements		(8.9)		(0.7)
-Transfer to Health Benefits Fund		(17.1)		0.0
+Investment Income		11.3		3.2
Net Assets as of 9/30/2007	$	193.8	$	63.5

**OPM restated September 30, 2006 CSRS net assets from $207.6 to $207.9*

As stated previously, CSRDF is a single fund and does not maintain separate accounts for individual agencies. The actual securities of the CSRDF are not allocated separately to CSRS or FERS, or to Postal and non-Postal beneficiaries. The assets of the CSRDF are composed entirely of special issue Treasury securities with maturities ranging up to 15 years. The long-term securities bear interest rates ranging from 4% to 5%, while the short-term securities have an interest rate of 3.75%.

The assumed rates of return on the CSRS fund balance for both 2006 and 2007 was 6.25% while the actual rates of return were 5.42% and 5.51%, respectively. For the FERS fund, the assumed rates of return for both 2007 and 2006 was 6.25%, while the actual rates of return were 5.63% and 5.73%. The projected rate of return on both the CSRS and FERS fund balance for 2008 is 6.25%.

OPM estimates the contributions and benefit payments for the next five years as follows:

Projection of CSRS and FERS Contributions and Benefit Payments*
as calculated by OPM

(Dollars in billions)	CSRS		FERS	
	Total Contributions	Total Benefit Payments	Total Contributions	Total Benefit Payments
2008	$ 0.5	$ 9.4	$ 3.1	$ 0.8
2009	0.4	10.0	3.4	0.9
2010	0.4	10.6	3.7	1.1
2011	0.4	11.2	4.1	1.3
2012	0.3	11.8	4.4	1.5

** Assumes total employee population remains constant*

Health Benefits

Postal employees and retirees may participate in the Federal Employees' Health Benefits Program (FEHBP), which is administered by OPM. We account for our employee and retiree health benefit costs as an expense in the period our contribution is due and payable to FEHBP, using multiemployer plan accounting rules in accordance with Financial Accounting Standards Board Statement 106 (FAS 106), *Employers' Accounting for Postretirement Benefits Other Than Pensions.*

The drivers of our active employee health care costs are the number of employees electing coverage and the premium costs of the plans they select. In 2008, health benefit expenses for active employees were $5,376 million, a decrease of $25 million compared to 2007. This was 6.9% of our total operating expenses. The 2007 expense of $5,401 million was 6.7% of our total operating expenses and increased by $56 million, or 1.0%, over 2006.

Premiums for each plan participating in FEHBP are determined annually by OPM. OPM announced average premium increases effective in January 2008 were 2.0%, 1.8% in January 2007 and 6.6% in January 2006. The low level of premium increases in 2007 and 2008 are the result of lower plan costs and the application of plan reserves to lower premiums. However, in September 2008, OPM announced an average premium increase of 7.0% for January 2009.

Retiree Health Benefits

Eligible postal employees, those with at least five consecutive years participation in the FEHBP immediately preceding retirement, are entitled to continue to participate in FEHBP postretirement. As outlined in FAS 106, the amount we pay into the PSRHBF, plus our portion of the current premium expense, is recognized as an expense when due. See Note 4, *Postal Accountability and Enhancement Act, Public Law 109-435 (P.L. 109-435)* and Note 9, *Health benefit programs,* in Notes to the Financial Statements, for further discussion of this accounting treatment.

P.L. 109-435 made several changes to the way we fund and report our obligations for postretirement health benefits. The law established the PSRHBF and directed OPM to determine any Postal Service surplus in the Civil Service Retirement and Disability Fund as of September 30, 2006, and to deposit the surplus into the PSRHBF by June 30, 2007. OPM attributed to the Postal Service a surplus of $17.1 billion in the CSRS fund as of September 30, 2006, and transferred the funds as required on June 29, 2007. P.L. 109-435 also required that we begin to fund the OPM-determined obligation for retiree health benefits by paying into the PSRHBF the 2006 escrow resulting from P.L. 108-18 ($2.958 billion) and by making additional annual payments averaging $5.6 billion per year through 2016. Beginning in 2017, the PSRHBF will begin to pay our portion of the premium payments. Payment to the PSRHBF was $5.6 billion in 2008 and $5.4 billion in 2007.

Under P.L. 109-435, OPM will continue to charge us for our portion of the premiums for postal retirees currently participating in FEHBP, and we will continue to expense these payments as they become due until 2017. The major drivers of our retiree health benefits premium costs are the number of current participants on the rolls, the mix of plans selected by retirees, the premium costs of those plans, and the apportionment of premium costs to the federal government for retiree service prior to 1971. Retiree health benefit premium expense, exclusive of the expense for the PSRHBF, has increased every year. Retiree health benefits employee premium expense increased 4.7% in 2008 and 5.4% in 2007. The number of Postal Service annuitants and survivors has grown to approximately 452,000 in 2008, compared to 450,000 in 2007 and 448,000 in 2006. The average monthly apportionment, the percentage of retiree premiums charged to the Postal Service, has increased from 66.4% in 2006 to 69.9% in 2008. A summary of the retiree health benefits expense for 2008, 2007, and 2006 is included in the table below.

Retiree Health Benefits Expense	**2008**	**2007**	**2006**
(Dollars in millions)			
Employer Premium Expense	$ 1,807	$ 1,726	$ 1,637
Transfer of 2006 Escrow to PSRHBF	-	2,958	-
P.L. 109-435 Scheduled Payment	5,600	5,400	-
Total	**$ 7,407**	**$ 10,084**	**$ 1,637**

PSRHBF

P.L. 109-435 requires that OPM provide, and that we report, certain information concerning the obligations, costs, and funding status of the PSRHBF. The following table shows the funded status and components of net periodic costs.

Postal Service Retiree Health Benefit Fund Funded Status and Components of Net Periodic Costs as calculated by OPM *	**2008**	**2007**
(Dollars in millions)		
Beginning Actuarial Liability at October 1	$ 80,786	$ 74,815
- Actuarial Gain	(1,136)	-
+ Normal Costs	3,389	3,175
+ Interest @ 6.25%	4,977	4,676
Subtotal Net Periodic Costs	7,230	7,851
- Premium Payments	(1,934)	(1,880)
Actuarial Liability at September 30	86,082	80,786
- Fund Balance at September 30	(32,610)	(25,745)
Unfunded Obligations at September 30	**$ 53,472**	**$ 55,041**

* Medical Inflation Assumption = 7%

The OPM valuation of Post Retirement Health Liabilities and Normal Costs were prepared in accordance with Federal Accounting Standards Advisory Board (FASAB) Statement of Federal Financial Accounting Standards (SFFAS) No. 5. SFFAS 5 requires the use of the aggregate Entry Age Normal actuarial cost method.

Demographic assumptions and an interest rate assumption of 6.25% are consistent with the pension valuation assumptions, and decrements are based upon counts or numbers rather than dollars.

The normal cost, which is on a per-participant basis, is computed to increase annually by a constant medical inflation rate which is assumed to be 7% per annum. Normal costs are derived from the current FEHBP on-roll population with an accrual period from entry into FEHBP to assumed retirement. Entry into the FEHBP is generally later than entry into the retirement systems.

The accrued liability is equal to the total liability less future normal payments. The liabilities and normal costs that appear in the OPM financial statements and are used in agency reporting are based upon annuitant medical costs (including administration costs) less annuitant premium payments. The values used in these valuations are based upon the same methodology and assumptions as for the financial statements except the average government share of premium payments for annuitants is substituted for annuitant medical costs less annuitant premium payments. The government share of premium payments has been adjusted to reflect premium payment levels that correspond to actual costs. This amount is assumed to increase at 7% per annum. For current Postal annuitants, this government share of premium payments is adjusted to reflect the pro-rata share of civilian service to total service for which the Postal Service is responsible. Postal annuitant counts include contracts for which the Postal Service makes no payment. The pro-rata adjustment is made by applying calculated factors based upon actual payments that vary by age and Medicare status of the enrollments. For active Postal employees, the pro-rata share in retirement is assumed to be 93% of the total.

The following table shows the net assets of the PSHRBF.

Net Assets of Retiree Health Benefit Fund (as calculated by OPM)	**2008**	**2007**
(Dollars in millions)		
Beginning Balance at October 1	$ 25,745	$ -
Contributions and Transfers	5,600	25,458
Earnings @ 4.8% and 5.0%, respectively	1,265	287
Net increase	6,865	25,745
Fund Balance at September 30	**$ 32,610**	**$ 25,745**

The assets of the PSRHBF are composed entirely of special issue Treasury securities with maturities ranging up to 15 years. The long-term securities bear interest rates ranging from 4% to 5%, while the short-term securities have an interest rate of 3.75%. The expected rate of return was 6.25% for both 2008 and 2007, while the actual rates of return were 4.8% for 2008 and 5.0% for 2007.

Because there are several areas of judgment involved in calculating this obligation, estimates could vary widely depending on the assumptions used. Utilizing the same underlying data that was used in preparing the estimate in the chart above, the September 30, 2008, obligation could range from $40 billion to $70 billion, solely by varying the inflation rate by plus or minus 1%, while the 2007 unfunded obligation would range from $49 billion to $69 billion using the same assumption.

Projection of PSRHBF Contributions and Benefit Payments

(Dollars in millions)

	Contributions	Payments
2009	$ 5,400	$ -
2010	5,500	-
2011	5,500	-
2012	5,600	-
2013	5,600	-

Workers' Compensation

Our employees are covered by the Federal Employees' Compensation Act, administered by the Department of Labor's Office of Workers' Compensation Programs (OWCP), which makes all decisions regarding injured workers' eligibility for benefits. However, we pay all workers' compensation claims from postal funds.

We record as a liability the present value of all future payments we expect to make for those employees receiving workers' compensation. At the end of 2008, we estimate our total liability for future workers' compensation costs at $7,968 million, an increase of $197 million, or 2.5%, from 2007. In 2007, our liability decreased $92 million, or 1.2%, from 2006. Our workers' compensation expense was $1,227 million for 2008, $880 million for 2007, and $1,279 million for 2006.

As discussed in Note 11, *Workers Compensation*, in the Notes to the Financial Statements, we implemented an improved model for estimating our liability for workers compensation in 2008, with the assistance of an independent actuary. The revised model is similar to that used in the independent actuarial valuation, which formed the basis for the recorded liability in 2007. The revised model combines four generally accepted actuarial valuation techniques to project our future claim payments based upon our currently open claims and our past claim payment experience. In addition, we refined our estimation in 2008 by taking a longer period of claim payment experience into consideration in the projection. The cumulative impact of the changes in estimate reduced our 2007 liability and expense by $685 million and our 2008 liability and expense by $154 million.

In 2008, we experienced a 1.5% increase in the number of medical claims receiving payments and a 3.8% increase in the number of compensation claims receiving payments. The actual claim payments increased $56 million, or 6.2%, over 2007. A factor in this increase were COLAs of 2.4% granted to all compensation claimants in March 2007 and 4.3% granted in March 2008, which raised the payments to all compensation claimants on the rolls. Medical claims payments during the year grew by 8.9%.

In 2007, we experienced a 4.6% decrease in the number of medical claims receiving payments and a 0.2% decrease in the number of compensation claims receiving payments. Although the number of claims receiving payments decreased, the actual cost of claims increased $41 million, or 4.7%, over 2006. A factor in this increase was the 2.4% March 2007 COLA, which raised the payments to all compensation claimants on the rolls.

Transportation Expenses

Transportation expenses for 2008 were $6,961 million, an increase of $459 million, or 7.1%, compared to 2007. Compared to 2006, 2007 transportation expenses increased $457 million, or 7.6%. Transportation costs are largely made up of air and highway transportation.

Transportation Expense	2008	2007	2006
(Dollars in millions)			
Highway Transportation	$ 3,499	$ 3,150	$ 2,977
Air Transportation	3,047	2,990	2,771
Other Transportation	415	362	297
Total Transportation Expense	**$ 6,961**	**$ 6,502**	**$ 6,045**

HIGHWAY TRANSPORTATION

Highway transportation expenses for 2008 were $3,499 million, an increase of $349 million, or 11.1% over 2007. In 2008, the increase was attributed to higher fuel prices, contract labor rates, and contract CPI rates. In addition, some mail that was previously transported via air was moved to surface transportation during the year. In 2008, the average price of gasoline increased approximately 30.4% compared to 2007. Diesel fuel, which makes up 93% of the fuel purchased for highway contracts, was an average of $3.87 per gallon in 2008, compared to $2.70 per gallon in 2007, an increase of 43.3%.

In 2007, our highway transportation expenses were $3,150 million, an increase of $173 million, or 5.8%, over 2006. This was driven by an increase in the number of miles driven, contractual rate increases for the contract drivers, and delivery growth. The increase in fuel prices was somewhat neutralized through leveraging our buying power to obtain favorable pricing by consolidating fueling points and bulk purchasing.

AIR TRANSPORTATION

Air transportation expenses for 2008 were $3,047 million, an increase of $57 million, or 1.9%, compared to the same period last year. Domestic air transportation expenses for 2008 were $2,336 million, a decrease of $57 million, or 2.4%, compared to 2007. International air expenses increased $114 million primarily due to the shift from surface to air delivery, resulting from the elimination of the Global Economy service offering.

Air transportation expenses for 2007 were $2,990 million, an increase of $219 million, or 7.9%, from 2006. In 2007, the increase was driven by growth in mail volume on our cargo carriers and the expansion of peak season operations, which provided improved service to our customers. Additional contributing factors were increases in contract rates for the offshore networks and an increase in fuel expenditures. With the 5% growth in international volume, we also saw a corresponding increase in international air expense compared to 2006.

OTHER TRANSPORTATION

Other transportation expenses for 2008 were $415 million, an increase of $53 million, or 14.6%, mainly driven by an increased number of international terminal dues settlements to foreign postal administrations compared to 2007. Terminal dues settlements are the fees we pay to foreign postal administrations for the outbound international mail that they deliver for us.

In 2007, other transportation expenses were $362 million, an increase of $65 million, or 21.9%, caused by increased international terminal dues settlements to foreign postal administrations and expedited mail delivery transactions as compared to 2006.

Other Expenses

In 2008, other operating expenses of $9,785 million increased $452 million, or 4.8%, from the comparable 2007 amount. The increase was primarily driven by Depreciation and Vehicle Maintenance Services. Vehicle Maintenance Services increased $166 million and includes the fuel used by our carrier fleet. Depreciation and amortization expense increased $167 million, compared to 2007, as a number of equipment projects were completed during the last half of 2007 and the early part of 2008.

Other Operating Expenses	2008	2007	2006
(Dollars in millions)			
Supplies and Services	$ 2,597	$ 2,594	$ 2,643
Depreciation and Amortization	2,319	2,152	2,149
Rent and Utilities	1,779	1,700	1,721
Vehicle Maintenance Service	926	760	709
Information Technology and Communications	658	630	649
Rural Carrier Equipment Maint. Allowance	545	495	485
Other	961	1,002	978
Total	**$ 9,785**	**$ 9,333**	**$ 9,334**

In 2007, other operating expenses decreased $1 million from 2006 comparable amounts, as shown in the table above.

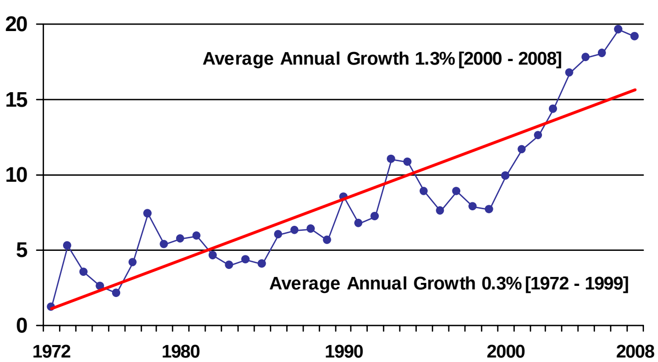
Productivity

We use a single indicator called total factor productivity (TFP) to measure productivity. TFP measures the change in the relationship between outputs (workload processed) and inputs (resource usage). Workload consists of weighted mail volume, miscellaneous output, and our expanding delivery network. Resources consist of labor, materials (including transportation), and deployed capital assets. Workload minus resources used equals TFP.

During FY 2008, TFP declined 0.5%. This marks the first year since 1999 that the Postal Service registered negative annual TFP growth. Despite efforts to manage workforce utilization (reduction of 50 million workhours), utilize material such as supplies and services efficiently, and maximize the return on capital investments (mainly automation), the worsening conditions across most sectors of the U.S. economy during this fiscal year, resulted in a 4.5% decline in mail volume, which we were unable to completely offset.

Aggregate workload for FY 2008 declined 3.0%. This was mainly due to a sharp decline in weighted mail volume, driven by the 8.5% decline in First-Class single-piece mail volume. In response to the workload decrease, we reduced resource usage by 2.4%, compared to last year. Labor usage, in particular, fell 3.6% compared to 2007.

The following graph shows the cumulative TFP trend from 1972 through 2008.



Service and Performance

Management monitors several key statistics to determine performance against our service standards. The major indicators we monitor are the External First-Class (EXFC) on-time mail delivery scores and the Customer Satisfaction Measurement (CSM) scores.

EXFC is an independently administered system that provides an external measure of delivery performance from collection box to mailbox. Although not a system-wide measurement of all First-Class Mail performance, EXFC continuously tests a panel of 463 3-digit ZIP Code areas selected on the basis of geographic area and volume density, thereby providing a measure of service performance from the customer's point-of-view. Results of these measures for the last four quarters are listed below.

EXFC Service Performance Scores	Quarter 1	Quarter 2	Quarter 3	Quarter 4
(Percentage delivered on time)				
Overnight Delivery	96	96	97	97
2-Day Delivery	93	94	95	94
3-Day Delivery	88	92	94	93

As required by P.L. 109-435, we worked with the PRC to create a set of modern service standards for our Mailing Services products. These standards were issued on December 19, 2007, and will be reflected in the service performance measurements published in 2009. The 2008 service scores do not reflect the new service standards.

CSM is an independently administered survey of customer opinions about key areas of service to residential customers. The following table displays the residential satisfaction results for the last four quarters.

Customer Satisfaction Measurement	Quarter 1	Quarter 2	Quarter 3	Quarter 4
(Percentage)				
Service rated excellent, very good or good	92	92	92	93

Capital Resources and Liquidity

CAPITAL INVESTMENTS

At the beginning of 2008, there were 30 Board-approved projects in progress, representing $6.8 billion in approved capital funding. During the year, the Board approved 11 new projects, which totaled $0.9 billion in additional capital funding. A total of 14 projects representing $1.8 billion in approved capital funding were completed. The year ended with 27 open projects that amount to $5.9 billion in approved capital.

While the funding for a project is authorized in one year, the commitment or contract to purchase or build may take place over several years. By year-end, approximately $5.0 billion had been committed to these 27 open projects. Actual capital cash outlays will occur over several years. Through the end of 2008, approximately $3.4 billion has been paid for the 27 projects.

In 2008, capital commitments for all projects were $2.3 billion. See Note 7, *Leases and other commitments*, in the Notes to the Financial Statements for additional information.

Noteworthy projects approved in 2008 include:

The Advance Facer Canceller 200 (AFCS 200) project will deploy 550 AFCS 200 machines. This purchase will address end-of-life issues with existing cancellation equipment initially placed in service over 16 years ago. The new AFCS 200 will include features that improve mail processing operations and enhance service.

The Carrier Route Vehicles project purchased 1,352 vehicles. These vehicles will be used to initiate the next planned phase of providing postal-owned right-hand drive vehicles to rural routes per agreement with the National Rural Letter Carrier's Association.

The purchase of 739 additional Delivery Barcode Sorter Stacker Modules will provide a greater depth-of-sort to existing letter mail processing operations. These units will be installed in 110 postal facilities. The labor savings generated by this program are expected to produce a strong return on investment.

LIQUIDITY

Liquidity is the cash we have with the U.S. Treasury and the amount of money we can borrow on short notice if needed. Our note purchase agreement with the Federal Financing Bank, renewed in 2008 and expiring in 2009, provides for revolving credit lines of $4.0 billion. These credit lines enable us to draw up to $3.4 billion with two days notice, and up to $600 million on the same business day the funds are needed. Under this agreement, we can also use a series of other notes with varying provisions to draw upon with two days notice. This arrangement provides us the flexibility to borrow short-term or long-term, using fixed- or floating-rate debt that is either callable or noncallable. These arrangements with the Federal Financing Bank provide us with adequate tools to effectively fund our cash requirements and manage our interest expense and risk. See Note 5, *Debt and related interest*, in Notes to the Financial Statements for additional information about our debt obligations.

The amount we can borrow is limited by statute. Our total debt outstanding cannot exceed $15 billion, and the net increase in debt at year-end for any fiscal year cannot exceed $3 billion.

Looking forward, our liquidity will be comprised of the approximately $1.4 billion of cash that we have entering 2009, the cash flow that we generate from operations, and the $3 billion that we can borrow if necessary. As was the case in 2008, for 2009 we do not expect cash flow from operations to supply adequate cash to fund our capital investments and the $5.4 billion payment into the PSRHBF required by P.L. 109-435. Consequently, the increase in debt next year could be similar to this year's $3 billion increase.

The majority of our revenue is earned in cash and the majority of our cash outflow is to support our biweekly payroll. Generally, cash flow from operations is at a seasonal peak in our first quarter and seasonal low in our fourth quarter. The first quarter includes the fall mailing and holiday season. In the fourth quarter we make significant cash payments for workers' compensation and retiree health benefits. A large portion of the $7.2 billion in debt we incurred at the end of 2008 was to fund the $6.6 billion in year-end PSRHBF and Workers' Compensation payments It should also be noted that $4.3 billion of the current liabilities on our balance sheet at September 30, 2008, represents items for which we have already collected cash, but have a remaining obligation to perform a future service.
The following table illustrates our scheduled cash flow obligations in future years.

Schedule of Commitments		**Retiree Health Benefits**		**Leases**
(Dollars in millions)				
2009	$	5,400	$	882
2010		5,500		861
2011		5,500		806
2012		5,600		738
2013		5,600		671
After 2013		17,200		5,387
Total	**$**	**44,800**	**$**	**9,345**

Cash Flow

CASH FLOWS FROM OPERATING ACTIVITIES

Net cash used in operating activities was $0.4 billion in 2008 compared to $2.6 billion used by operating activities in 2007. The year-to-year change of $2.2 billion was driven mainly by the reduction in the net loss of $2.3 billion. This, in turn, was largely due to the absence in 2008 of the one-time transfer of $3.0 billion formerly held in escrow to the PSRHBF in 2007. Additional cash was provided in 2008 by an increase of $547 million in prepaid postage. This is due to changes in consumer buying behavior, largely driven by the introduction of the Forever Stamp (See Note 2 to the

Financial Statements – Summary of significant accounting policies – Revenue Recognition/Deferred Revenue – Prepaid Postage). This increase was partially offset by decreases in payables and accrued expenses of $324 million, other noncurrent liabilities of $167 million, money orders outstanding of $127 million, and a decrease in accrued compensation and benefits of $105 million.

Net cash used in operating activities was $2.6 billion in 2007 compared to $3.8 billion provided by operating activities in 2006. The year-to-year decrease of $6.4 billion was driven mainly by the $8.4 billion in payments to the PSRHBF in 2007, as required by P.L. 109-435, partially offset by the $1.6 billion in CSRS payments that we are no longer required to make. This is also reflected in our 2007 net loss of $5.1 billion compared to 2006 net income of $900 million. Additional cash was provided in 2007 by an increase in other noncurrent liabilities of $281 million, primarily contingent liabilities, an increase in compensation and benefits liabilities of $347 million, and increased collections of accounts receivable of $80 million. These cash flow increases were partially offset by decreases in payables and accrued expenses of $93 million, and customer deposit accounts and outstanding money orders of $186 million.

CASH FLOWS FROM INVESTING ACTIVITIES

Net cash used by investing activities was $1.9 billion in 2008 compared to $500 million provided in 2007. Purchases of property and equipment of $2.0 billion decreased $700 million from the $2.7 billion purchased in 2007. Proceeds from building sales and the sale of property and equipment totaled $57 million in 2008 compared to $257 million in 2007. The remainder of the change was due to the absence, in 2008, of the one time 2007 transfer of funds from the escrow restricted cash into operating cash. Excluding this one time item, cash used by investing activities would have decreased $520 million in 2008.

Net cash provided by investing activities was $500 million in 2007 compared to $5.5 billion used in 2006. Nearly all of the year-over-year change can be attributed to the almost $3.0 billion that was placed in escrow as restricted cash in 2006, and then was removed from restricted cash when transferred to the new PSRHBF in 2007. Capital cash outlays of $2.7 billion increased slightly from the $2.6 billion in 2006. Proceeds from the sale of property were $39 million in 2007 compared to $114 million in 2006. In 2007, the sale of the James A. Farley Building and several Philadelphia properties resulted in proceeds from deferred building sales of $218 million. Excluding the escrow, net cash flow used in investing activities would have been virtually unchanged at $2.5 billion for both 2007 and 2006, rather than the $500 million and $5.5 billion reported.

CASH FLOWS FROM FINANCING ACTIVITIES

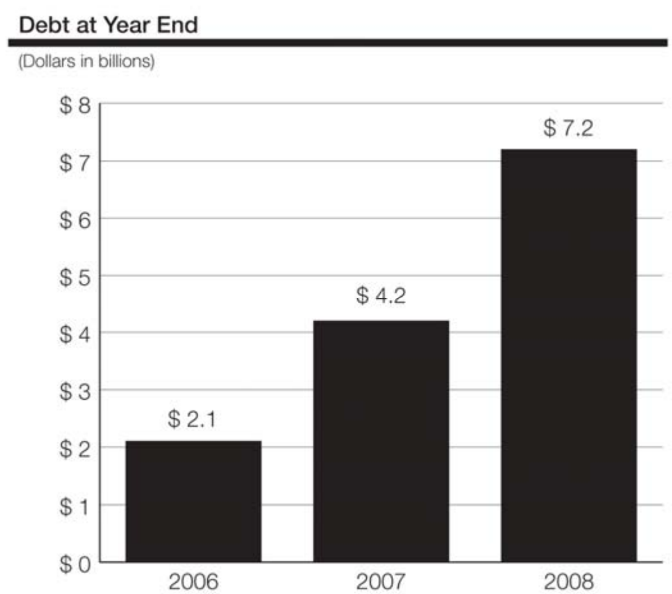
Net cash provided by financing activities was $2.9 billion, $2.0 billion, and $2.0 billion for 2008, 2007, and 2006 respectively. Our borrowing from the Federal Financing Bank increased $3.0 billion, $2.1 billion, and $2.1 billion in 2008, 2007, and 2006 respectively.

Financing Activities

DEBT

As an “independent establishment of the executive branch of the Government of the United States,” we receive no tax dollars for ongoing operations. We are self-supporting, 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 Federal Financing Bank.

The amount we borrow is largely determined by the difference between our cash flow from operations, which includes the end-of-year payout of $6.6 billion for retiree health benefits and workers’ compensation, and our capital cash outlays. Our capital cash outlays consist of the funds invested for new facilities, new automation equipment, and new services. On September 30, 2008, we had $7.2 billion in debt outstanding, a $3.0 billion increase from last year.



OTHER INTEREST EXPENSE

In 2008, interest expense was $36 million, an increase of $26 million compared to 2007. The net loss of $2.8 billion in 2008 decreased the number of days we were debt free in 2008 compared to 2007, and resulted in the increase in interest expense. In 2007 and 2006, with less debt to repay, and increased cash on hand, other interest expense was $10 million and $5 million respectively.

INTEREST AND INVESTMENT INCOME

When we determine that our available funds exceed our current needs, we invest those funds with the U.S. Treasury's Bureau of Public Debt in overnight securities issued by the U.S. Treasury. Due to increased levels of debt in 2008, excess cash was mostly used to repay debt, resulting in investment income of $10 million.

In 2007 and 2006, with less debt to repay, and increased cash on hand, we earned investment income of $169 million in 2007 and $140 million in 2006.

We also recognize imputed interest on the funds owed to us under the Revenue Forgone Reform Act of 1993. Under the Act, Congress agreed to reimburse the Postal Service $29 million annually through 2035 for services performed in prior years. See Note 12, *Revenue forgone,* in the Notes to the Financial Statements for additional information.

Interest and Investment Income (Dollars in millions)	2008	2007	2006
Investment Income	$ 10	$ 169	$ 140
Imputed interest on accounts receivable from the U.S. government	25	25	25
Other Interest	1	1	2
Total	**$ 36**	**$ 195**	**$ 167**

Legislative Update

APPROPRIATIONS

Although the Postal Service is self-funded and does not receive any Congressional appropriations to support its operations, some funding is provided to cover the costs of certain statutorily mandated services. In September 2008, the President signed into law P.L. 110-329, to fund the federal government until March 6, 2009. The Postal Service received the October 2008 –March 2009 portion of its $29 million revenue foregone reimbursement. On October 1, 2008, the Postal Service received $88.9 million, to cover cost associated with free mail for the blind and overseas voters mailed in previous years.

INTERNATIONAL AIR TRANSPORTATION BILL

In October 2008, the President signed the *Air Carriage of International Mail Act* (P.L. 110-405), which eliminated the authority of the Department of Transportation (DOT) to set the prices paid by the Postal Service for the air transport of international mail. Under the new provision, the Postal Service is permitted to competitively negotiate the terms of international air mail transportation contracts directly with air carriers, just as we do with our domestic transportation. We will benefit by paying international mail transportation rates set by negotiation, not regulatory procedures.

MEDICARE IMPROVEMENTS FOR PATIENTS AND PROVIDERS ACT

The Medicare Improvements for Patients and Providers Act, Public Law 110-275 was signed into law July 15, 2008. The law reduces the Medicare reimbursement rate for mail order of durable medical equipment but does not make a similar reduction for retail suppliers of such equipment. These changes could have a potential annual negative revenue impact of approximately $40 million.

TOBACCO LEGISLATION

On September 10, 2008, H.R. 4081, *The Prevent All Cigarette Trafficking Act of 2008* (PACT Act), passed the House by a 379 to 12 vote. The bill would make cigarettes and smokeless tobacco non-mailable under the criminal provisions of Title 18 of the U.S. Code. The bill would also place shipping and record-keeping requirements on those selling cigarettes and smokeless tobacco over the phone, through the mail, or via the Internet. Sellers would be required to verify the age and identity of purchasers to reduce sales to minors. In addition, the bill would make failure to comply with state tobacco tax laws a felony. The Postal Service estimates that shipping tobacco constitutes approximately $35–$40 million of revenue annually. A companion bill has been awaiting Senate floor action for over a year.

Outlook

The U.S. economy had experienced a year of slow growth before experiencing an actual contraction of GDP, which began in Quarter IV. Most economists agree that the contraction in GDP will be more serious during the first half of 2009. Global Insight, an economic forecasting and consulting firm, expects real GDP to decline for three quarters in a row beginning with Quarter IV of 2008.

The U.S. economy had slumped long before the current credit crisis began. The housing market, sub-prime mortgage issues, and energy price fluctuations resulted in a year of slow economic growth, causing a major downturn in both First-Class and Standard Mail advertising.

A financially healthy Postal Service is dependent upon a healthy U.S. economy. Retail sales, employment, and investment spending are all significant indicators of mail demand. All three of these indicators are projected to significantly decrease in 2009. Outright declines in consumer spending are anticipated during the final quarter of calendar year 2008 and the first quarter of 2009. These would be the first declines in consumer spending since 1991. Non-farm employment has been in steady decline since February and is expected to continue to decline throughout 2009. Finally, investment spending should see a sharp decrease in 2009.

Revenue Outlook

We project revenue to increase between 1.0% and 2.0% in 2009 on a volume decrease of 3.0% to 4.0%. This expected revenue increase is due primarily to anticipated price increases.

First-Class Mail volume is expected to decline about 2.0% during 2009. Electronic alternatives to mail will continue to decrease First-Class Mail volume. Prior to 2008, this was offset to some degree by growth in First-Class Mail workshare letters and flats.

Standard Mail revenue is expected to decline in 2009.

Periodicals revenue and volume are both projected to decrease in 2009. We expect the modest year-over-year declines in Periodicals volume to continue. While the declines in Periodicals are not dramatic, they are part of a long-term trend.

Both volume and revenue are expected to grow in 2009 for Package Services.

Our Shipping Services products revenues and volumes are expected to grow modestly in 2009. This entire group is influenced by competitor's prices, which may include fuel surcharges. P.L. 109-435 has provided an opportunity for greater competition by the Postal Service in this area of services.

Pricing for shipping services will change in January 2009, with new prices announced in November 2008. The move to a January implementation for shipping services is consistent with industry standards, and provides a clearer picture of the competitive, affordable rates the Postal Service offers. P.L. 109-435 changed the way we operate and conduct business. It provides new flexibility, especially in competitive pricing for shipping services, enabling us to respond to dynamic market conditions and changing customer needs. Prices will change in January for Express Mail, Priority Mail, Parcel Select, Parcel Return Service, and some international shipping products. It will be the first time we will separate price adjustment and implementation dates for our shipping and packaging business from the dates for our mailing services and products.

Expense Outlook

Total expenses for 2009 are estimated to increase between 1.0% and 2.0%. Personnel costs increases in 2009 will be driven primarily by cost-of-living adjustments, contractual pay increases, and increases in health benefits. This will be offset by planned cost reductions. We are offering voluntary early retirement opportunities to almost 25% of our workforce in 2009. The total number of employees who accept the early retirement offer will impact the savings for FY 2009.

Item 7A – Quantitative and qualitative disclosures about market risk

Market Risk Disclosure

In the normal course of business, we are exposed to market risk from changes in commodity prices, certain foreign currency exchange rate fluctuations and interest rates. We currently do not use derivative financial instruments to manage market risks. Additionally, we currently do not purchase or hold derivative financial instruments for speculative purposes.

Fuel Cost Risk

We estimate a 1.0% increase in fuel and natural gas costs would result in a $29 million increase in expense. We did not use derivative commodity instruments to manage the risk of changes in energy prices during the periods covered by this report.

Interest Rate Risk

We have not used derivative financial instruments to manage risk related to interest rate fluctuations for debt instruments.

We estimate that a 1.0% increase in interest rates would have an insignificant impact on our financial statements due to the size and structure of our investment and debt portfolios.

Labor Contracts

As discussed in Item 1A, *Risk Factors*, the contracts with our four largest unions include provisions granting COLAs linked to changes in the CPI-W.

Item 8 – Financial statements and supplementary data

Our audited Statements of Operations, Balance Sheets, Statements of Changes in Net (Deficiency) Capital, and Statements of Cash Flows are included in the Financial Statements section of this report.

Item 9 – Changes in and disagreements with accountants on accounting and financial disclosure

None

Item 9A – Controls and procedures

Management is responsible for the preparation, integrity, and fair presentation of the financial statements of the Postal Service.

Disclosure Controls

We maintain disclosure controls and procedures that are designed to ensure that information required to be disclosed in our quarterly and annual reports is recorded, processed, summarized, and reported within the time frames specified by P.L. 109-435, and that this information is accumulated and communicated to our management, including the Postmaster General and Chief Financial Officer, as appropriate, to allow timely decisions regarding required disclosure. In designing and evaluating the disclosure controls and procedures, we recognize that any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving the desired control objectives, and we were required to apply our judgment in evaluating the cost-benefit relationship of possible controls and procedures.

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, 2008. Based on the foregoing, the Postmaster General and Chief Financial Officer concluded that our disclosure controls and procedures were effective at the reasonable assurance level as of September 30, 2008.

Internal Controls

There have been no changes during the year covered by this report in our internal control over financial reporting or in other factors that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

Item 9B – Other information

None

Part III

Item 10 – Directors, Executive Officers, and Corporate Governance

The Postal Service is governed by an eleven member Board of Governors. The Board is composed of nine Governors appointed by the President of the United States with the advice and consent of the United States Senate, plus the Postmaster General and the Deputy Postmaster General. The nine appointed Governors are:

Name, Age and Term of Office	Positions and Experience
Alan C. Kessler, Chairman of the Board of Governors, Age 58 Governor since November 2000. Term expiring December 2008.	Chairman of the Board of Governors since January 2008. Vice Chairman of the Board of Governors from January 2005 to January 2008. Partner since 1999 at WolfBlock, LLP. Member of the Presidential Transition Team, 1992-93, Former Vice Chair of the Presidential/Congressional Commission on Risk Assessment and Risk Management; Former member of the Electoral College, Pennsylvania. Currently Serves on the Boards of the Greater Philadelphia Chamber of Commerce, the Philadelphia Industrial Development Corporation, and the Central Philadelphia Development Corporation. Former commissioner for Lower Merion Township, Pennsylvania, Member of the Philadelphia City Planning Commission, and member of the Executive Committee of Philadelphia 2000. Chairman, Pennsylvania Supreme Court Continuing Legal Education Board.
Carolyn Lewis Gallagher, Vice Chairman of the Board of Governors, Age 53 Governor since November 2004. Term expiring December 2009.	Vice Chairman of the Board of Governors since January 2008. Chairman, Compensation and Management Resources Committee and Vice Chairman, Audit and Finance Committee. Director of Home Therapy Specialists, Inc. Former President and Chief Executive Officer of Texwood Furniture, Inc. Former Trustee and Board Chair, Texas Employees' Retirement System. Appointed by President Bush in 2003 to serve on the President's Commission on the United States Postal Service.
Mickey D. Barnett, Governor, Age 57 Governor since August 2006. Term expiring December 2013.	Vice Chairman, Government Relations and Regulatory Committee and member, Governance and Strategy Planning Committee. Attorney in Albuquerque, New Mexico. Former member, New Mexico State Senate. Former member, Appellate Nominating Commission for the New Mexico Supreme Court of Appeals. Former Legislative Assistant to Senator Pete Dominici of New Mexico.
James H. Bilbray, Governor, Age 70 Governor since August 2006. Term expiring December 2015.	Vice Chairman of Governance and Strategic Planning Committee, and member, Government Relations and Regulatory Committee. Attorney in Las Vegas, Nevada. Former member, U.S. House of Representatives from Nevada. Former member, Nevada State Senate. Former Deputy District Attorney in Clark County, Nevada.
Louis J. Giuliano, Governor, Age 61 Governor since November 2004. Term expiring December 2014.	Chairman, Ad-Hoc Committee on Operations and member, Compensation and Management Resources Committee and the Governance and Strategic Planning Committee. Former Chairman of Board of Directors, President and Chief Executive Officer of ITT Corp. from 2001 through 2004. Director of the John McNeely Company and Senior Advisor at the Carlyle Group.

Thurgood Marshall, Jr., Governor, Age 52 Governor since December 2006 Term expiring December 2011.	Chairman, Government Relations and Regulatory Committee. Member, Audit and Finance Committee. Partner since 2006 at Bingham McCutchen and principal with Bingham Consulting Group since 2006. Served President Clinton as former Assistant to the President and Cabinet Secretary. Former Director of Legislative Affairs and Deputy Counsel for Vice President Gore.
James C. Miller III, Governor, Age 66 Governor since April 2003. Term expiring December 2010.	Past Chairman of the Board of Governors, 2005 through 2008. Chairman, Governance and Strategic Planning Committee, and member, Audit and Finance Committee. Senior Advisor at the international law firm of Husch and Blackwell Sanders LLP since 2006. Senior Fellow (by courtesy) of the Hoover Institution at Stanford University since 1988. Emeritus Member of the Boards of the Tax Foundation and the Progress and Freedom Foundation since 2003. Member of Boards of Washington Mutual Investors Fund, America Fund Tax-Exempt Series I, the JP Morgan Value Opportunities Fund and Clean Energy Fuels Corp. Former Director, United States Office of Management and Budget from 1985 to 1988. Former Member of National Security Council from 1985 to 1988. Former Chairman of the United States Federal Trade Commission from 1981 to 1985.
Katherine C. Tobin, Governor, Age 57 Governor since August 2006. Term expiring December 2012.	Chairman, Audit and Finance Committee, and member, Compensation and Management Resources Committee. Research and management consultant specializing in high technology industry since 1984. Member, Advisory Board, MentorNet, mentoring network for women in engineering and science. Former head of research teams at Hewlett-Packard Co. and Catalyst, a nonprofit organization for women in business.
Ellen C. Williams, Governor, Age 51 Governor since August 2006. Term expiring December 2014.	Vice Chairman, Compensation and Management Resources Committee and member, Government Relations and Regulatory Committee. Owner and CEO of Ellen C. Williams, LLC, a government affairs and lobbying firm, since its establishment in 2006. Former Vice Chairman of the Kentucky Public Service Commission from 2004 to 2005. Former Commissioner of the Governor's Office for Local Development in Kentucky from 2005 to 2006. Former Chairman of the Republican Party of Kentucky from 1999 to 2004. Staff assistant to former U.S. Representative Larry Hopkins.

The Postal Service Board of Governors has an Audit and Finance Committee.

The Audit and Finance Committee has four Governors, as follows: Governor Tobin, Chairman, Governor Gallagher, Vice Chairman, Governor Marshall, and Governor Miller. The Board of Governors has determined that Governors Miller and Tobin qualify as audit committee financial experts as defined by the rules of the SEC. All Audit and Finance committee members are independent as defined by the rules of the SEC.

The Postal Service currently has nine executive officers. The executive officers are:

Name and Age	Positions and Experience
John (Jack) E. Potter, Age 53	72nd Postmaster General, Chief Executive Officer and member of the Board of Governors since June 2001. Chief Operating Officer and Executive Vice President from October 2000 to June 2001 and Senior Vice President, Operations from February 1999 to October 2000.
Patrick R. Donahoe, Age 52	19th Deputy Postmaster General, Chief Operating Officer and a member of the Board of Governors since April 2005. Chief Operating Officer and Executive Vice President during the years 2001 to 2005. Senior Vice President Operations from February 2001 to September 2001.
Robert F. Bernstock, Age 57	President, Shipping and Mailing Services since June 2008. Chairman and Chief Executive Officer, Securesheet Technologies, a private software company, from September 2006 to June 2008. President and Chief Operating Officer and prior to that Executive Vice President, The Scotts Miracle-Gro Company, a marketer of branded consumer products for lawn and garden care, from 2003 to 2006. Senior Vice President and General Manager, The Dial Corporation, a leading manufacturer of consumer products, from 2002 to 2003. Mr. Bernstock serves as a director on the Boards of the following public companies: Nutri System Inc., The Pantry, Inc., and KBL Acquisition Corp. IV.
Mary Anne Gibbons, Age 58	Senior Vice President and General Counsel since December 2003. Vice President and General Counsel from 1999 to December 2003.
Stephen M. Kearney, Age 52	Senior Vice President, Customer Relations since July 2008. Vice President of Pricing and Classification from September 2001 to July 2008.
Linda A. Kingsley, Age 46	Senior Vice President of Strategy and Transition since January 2007. Vice President of Strategic Planning from August 2003 to January 2007.
Ross Philo, Age 56	Executive Vice President and Chief Information Officer since February 2008. Director of Global Energy Solutions from December 2006 to February 2008 at Cisco Systems. President and Chief Executive Officer from August 2006 to December 2006 of Visean Inc., a global startup company providing remote data communication services for the oil and gas industry. Senior Vice President and Chief Information Officer at Halliburton from December 2003 to April 2006.
Anthony J. Vegliante, Age 57	Chief Human Resources Officer and Executive Vice President since April 2005. Vice President, Labor Relations from February 1999 to April 2005.
Harold Glen Walker, Age 56	Chief Financial Officer and Executive Vice President since August 2006. Vice President of Finance and Chief Financial Officer for Invensys Controls, a company specializing in making parts for heating, cooling and safety products, from September 2001 to October 2002. Vice President of Finance and Chief Financial Officer for Europe, the Middle East and Africa of the appliance manufacturer Whirlpool Corporation from September 1990 to March 2001.

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Code of Ethics

The Standards of Ethical Conduct for Employees of the Executive Branch at 5 Code of Federal Regulations (C.F.R.) §2635 apply to all postal service employees. The Standards were issued in 1993 by the U.S. Office of Government Ethics, and replaced the individual agency standards then applicable to all employees of the executive branch.

The Postal Service has also adopted a Senior Financial Managers Code of Ethics. This Code of Ethics can be found on our website USPS.com under:
http://www.usps.com/financials/_coe/SeniorFinancialManagersCodeofEthics.html.

Our employees are also covered by the Supplemental Standards of Ethical Conduct for Employees of the United States Postal Service at 5 C.F.R. §7001. The Standards and Supplemental Standards are detailed and contain many examples to help employees recognize and resolve ethical issues. We give employees a summary of the standards, and other ethical conduct materials at initial employee orientation training and other times during the year. We also provide annual ethics training for all employees who file a financial disclosure report. To support our employees on ethical issues, we maintain a dedicated phone line and e-mail address for providing ethical advice.

Item 11 – Executive compensation

Compensation Discussion and Analysis

ROLE OF THE BOARD OF GOVERNORS AND STATUTORY COMPENSATION AND BENEFITS REQUIREMENTS AND LIMITATIONS

The Board of Governors of the Postal Service establishes executive officer compensation and benefits, subject to the requirements and limitations of federal law. The Board has delegated to its Compensation and Management Resources Committee ("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 postal management. The Compensation Committee makes recommendations to the full Board for their review and approval.

Federal law governing the Postal Service, set forth in Title 39 of the United States Code, provides that compensation and benefits for all officers in the Postal Service shall be comparable to the compensation and benefits paid for comparable levels of work in the private sector of the economy. The Postal Service is the second largest civilian employer in the nation, with more than 700,000 career and non-career employees as of the end of Fiscal Year 2008. The Postal Service operates more than 200,000 motor vehicles and slightly less than 37,000 post offices. The Postal Service delivers almost half the world's mail and more than 200 billion pieces annually. In Fiscal Year 2008, the Postal Service generated $74.9 billion in revenue. In 2008, the Postal Service ranked 83rd in Fortune Magazine's listing of Fortune Global 500 Companies. By way of comparison, two of our largest competitors ranked 142nd and 214th on this list. If the Postal Service were listed on the Fortune 500 annual ranking of America's largest corporations, it would be ranked 23rd. The same two of our largest competitors are ranked 46th and 68th on that list.

Given the Postal Service's size and scope of operations, the comparability requirement in Title 39 would suggest that the Postal Service's executive officer compensation and benefits should be on par with the compensation and benefits of the very largest private sector companies in the United States. These very large companies typically provide their top executives an annual salary well in excess of $1 million and total compensation and benefits valued at several million dollars through annual and long-term performance incentives that may include a combination of cash payments and stock options and a number of benefits and perquisites.

Although the law governing the Postal Service provides that executives and others should be compensated at a level comparable to the private sector, the Postal Service's status as part of the federal government precludes the ability to achieve a standard of compensation comparable to the private sector. Postal law imposes three different caps on compensation for postal 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 United States Code. 39 U.S.C. § 1003(a). This compensation cap was set at $186,600 for calendar year 2007 and $191,300 for calendar year 2008.

With the approval of the Board, however, the Postal Service may develop a program to award a bonus or other reward in excess of the above compensation cap, as long as this does not cause the officer's total compensation paid to the officer in a year to "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). This total compensation cap was $215,700 for calendar year 2007 and $221,100 for calendar year 2008. In approving any such program, the Board must determine that the bonus or award is based on a performance appraisal system that makes meaningful distinctions based on relative performance.

In addition, the Board may allow up to 12 officers or employees of the Postal Service 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 respective salaries for calendar years 2007 and 2008, this compensation cap was $258,840 for calendar year 2007 and $265,320 for calendar year 2008.

By law, postal employees, including executive officers, are entitled to participate in either the Civil Service Retirement System or Federal Employee Retirement System, depending on when their federal employment began. 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 federal government, postal policy also authorizes certain additional benefits for all officers of the Postal Service, including executive officers. These include participation in the Federal Employees Health Benefits plans, paid life insurance, a periodic physical examination and parking. Other than changes required by law, the Board must authorize any changes to benefits for officers.

Even with the increase in the compensation cap for top postal executives and the benefits available to them, compensation for postal executive officers is still significantly below that of the private sector. As explained later, a consulting firm retained by the Board found that Postal Service executive officers' compensation is only approximately 15% of compensation for comparable executive officers in the comparator marketplace.

Compensation Philosophy and Objectives

The Board recognizes that there is a significant disconnect between the comparability requirement and the compensation caps in the law governing the Postal Service and that the various compensation caps do not enable the Board to provide compensation and benefits for executive officers that are fully comparable to the private sector. 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 the Postal Service, given its status as part of the federal government. These limitations make it difficult for the Postal Service to compete in the marketplace for executive officers and to retain current executive officers. The Postal Accountability and Enhancement Act of 2006 did not allow the Board to overcome these differences or to alleviate internal pay compression. To attempt to achieve some level of comparability within the above confines of the law, the Board has designed a compensation system that balances amounts paid as salary to executives in a given year, with the ability of the executive who meets performance goals and objectives to earn additional compensation, a portion of which may need to be deferred because of the compensation caps.

Within the confines of their legislative authority, the Board's philosophy is that:

- There should be a strong connection between individual executive compensation and the Postal Service's performance on a number of dimensions, including service, net income and productivity.
- Compensation and benefits should be designed to attract and retain top organizational contributors to ensure that the Postal Service has the caliber of executives that will enable it 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 annual 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 the Postal Service's executives.

The Compensation Program

In fiscal year 2007, after enactment of the Postal Act of 2006, the Compensation Committee retained the services of Watson Wyatt, a consulting firm specializing in executive compensation, to assist the Board in implementing the compensation provisions of the Postal Act of 2006 and to review and update the overall program for officer compensation and benefits. Watson Wyatt provided the Compensation Committee with comparative data on market pay and compensation design practices for executive officers in other companies. Because no other organization shares the same mission, scope of operations, and legislative oversight as the Postal Service, the labor market group against which executive officer compensation was benchmarked was generally comprised of organizations that excel in one or more of the Postal Service's core operations of processing technologies, transportation services, retail and delivery and distribution capabilities. Comparator reputation for excellence in their industry also served as a selection criterion.

The data showed that, in addition to base salary, individuals in comparable companies typically receive an annual bonus and an equity interest in the company in the form of stock or stock options and participate in one or more long-term incentive plans.[1] Watson Wyatt found that, due to the statutory compensation caps, compensation for Postal Service executive officers would be only approximately 15% of compensation for comparable executive officers in the comparator marketplace. Finally, it was generally the case that a significant portion of executive officers' total compensation in the comparator companies is at risk and the higher the executive officer's rank, the more total compensation is at risk.

Watson Wyatt developed recommendations based on the Board's objectives to design a compensation program that would optimize the new legislative flexibility, reduce internal pay compression, improve external marketplace competitiveness, honor legislative constraints and existing pay ranges and maximize an objective of the Board for Postmaster General retention. Watson Wyatt recommended that the maximum of the highest salary band (for the Postmaster General) be set at the legislative salary cap. Watson Wyatt recommended that the Deputy Postmaster General's salary should be in the next highest salary band and recommended other executive officers' salary bands based on comparisons with salary relationships in the external market. In all instances the market predicted maximum for executive officers exceeded the maximum available for Postal Service executive officers given the constraints of the legislative pay cap.

After reviewing data provided by the consulting firm and recommendations from the Compensation Committee and the Postmaster General, the Board approved for fiscal year 2007 salary ranges for the Postmaster General, other executive officers and other high-level Postal Service officers commensurate with their scope of responsibility and within the confines of the statutory compensation caps. The Board determined that the Postmaster General's salary should be set at the legislative salary cap, and that the Deputy Postmaster General and the other executive officer salary bands should be based on salary relationships of comparable executive officers in the comparator marketplace. The Board authorized the Postmaster General to establish actual salaries for the other executive officers, within the confines of the salary ranges established by the Board. After experience with the salaries for fiscal year 2007, the Board again reviewed recommendations from the Compensation Committee and the Postmaster General and increased salary ranges by 2.5% for fiscal year 2008.

In 2007 and continuing in 2008, the Postal Service continued 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 the overall performance of the Postal Service. Annual NPA metrics and targets generally take into consideration the Postal Service's performance during the prior year and particular challenges the Postal Service expects to face during the upcoming year. The NPA places emphasis on objective, measurable performance indicators. The Board also sets individual metrics and targets for the Postmaster General and Deputy Postmaster General and authorizes the Postmaster General to establish individual metrics and targets for other officers.

The Board establishes annual pay-for-performance (PFP) incentive opportunities to provide incentives and to reward executives for reaching various levels of performance. Incentive payouts are not made on a particular goal if the Postal Service fails to meet minimum acceptable performance standards. Annual PFP incentives are paid out in cash or deferred for future payment where required due to the compensation caps.

[1] For comparison purposes, Watson Wyatt did not include payments not directly related to performance, such as severance pay and perquisites.

NPA performance goals and rewards fall into several categories. These include areas that an officer may directly influence, such as service, efficiency, employee satisfaction, and productivity, as well as those that are more susceptible to being affected by general economic conditions, such as revenue generation.

The Board believes that this mix of goals has helped the Postal Service to continue delivering record-breaking service even in the face of an unsettled economy. Indeed, in Fiscal Year 2008, the Postal Service exceeded every one of its service goals, goals that were set at very aggressive levels at the start of the fiscal year. Particularly in a troubled economy, in order to remain viable, the Postal Service must serve its customers with the highest levels of efficiency and productivity. Rewarding executive officers for achieving these aggressive goals is one way that the Postal Service sustains these very high levels of performance. This is particularly true in light of the significant limits on officer compensation imposed by law.

For each goal, the Postmaster General establishes indicators identifying the type of performance that will enable the Postal Service to achieve or surpass the goal. These performance 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 pay-for-performance goals will be tied to overall corporate performance. The executive officers' goals are aligned with national performance goals and linked to the overall success of the Postal Service.

Once the goals and indicators are established, executive officers are advised as to what the Postal Service expects of them in terms of performance during the year, how their performance will impact the entire Postal Service, and the potential level of performance-based incentives they can expect depending on the Postal Service's and their individual performance. Under this program, an individual executive officer can receive a rating of Non-Contributor, Contributor, High Contributor or Exceptional Contributor, with a numerical rating within each category, depending on how the Postal Service performs on the national indicators and the individual's performance, as determined by the Postmaster General. As shown in the chart below, a rating of Non-Contributor would result from an overall numerical rating of between 0 and 3. A rating of Contributor would result from a numerical score of between 4 and 9. A rating of High Contributor would result from a score between 10 and 12 and a rating of Exceptional Contributor would result from a score between 13 and 15.

Overall Performance Rating	
Adjective Rating	**Number Rating**
Exceptional Contributor (EC)	13, 14, 15
High Contributor (HC)	10, 11, 12
Contributor (C)	4 to 9
Non Contributor (NC)	1, 2, 3

Based on the individual executive officer's performance rating, the executive officer would be eligible for an increase to base salary as well as a performance-based lump sum payment. Due to limitations placed by the statutory cap, increases to the maximum of the salary range for executive officers generally follow the percentage increase to the Executive Schedule 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 are based on the executive officer's performance rating given by the Postmaster General and multiplied by a range of 1.33% to 2.50% based on the degree to which the individual has achieved previously set individual goals and metrics. The Postmaster General's discretion on Pay-for-Performance incentives for executive officers in a given year is limited by the Postal Service's overall performance on NPA goals and metrics. All executive officer performance scores must average to the Postal Service's overall NPA performance score for the fiscal year.

Determinations on salary increases are made after the end of the fiscal year and new salaries become effective for the following calendar year. For calendar year 2008, based on fiscal year 2007 performance, the Postmaster General increased the other named executive officers' salaries by an average of 2.25%.

Despite the many accomplishments of the named officers in fiscal year 2008, the Postmaster General decided to freeze all postal executives' salaries for calendar year 2009 due to the significant financial challenges facing the Postal Service in fiscal year 2009. The Postmaster General's salary, which is determined pursuant to his contract, will also be frozen for calendar year 2009.

Subject to the Compensation Committee's review, the Postmaster General determined the fiscal year 2008 performance bonuses for the other named executive officers, based on his judgment of the named executive officers' performance on a number of factors. In addition to the Postal Service's overall performance, the Postmaster General considered the individual named executive officer's contributions to the overall performance of the Postal Service in terms of improving service, reducing costs, and/or increasing employee satisfaction, the named executive officer's performance on individual goals, and particular challenges faced by the named executive officer in his or her area of responsibility. The Postmaster General also considered the named executive officer's contributions, if applicable, to implementing the Postal Act of 2006. Compensation awarded in excess of the statutory limit was deferred.

The Board recognizes that, particularly for the Postmaster General, the restraints in governing law make it difficult to provide an overall level of compensation and benefits that comes even close to a level of comparability with similarly-situated individuals in the private sector. Based on a desire to retain the Postmaster General in his current role as well as to attempt to provide him with compensation and benefits that provide comparability to the extent legally possible, the Board entered into an employment agreement with the Postmaster General. The agreement provides that the Postmaster General's salary is set at the maximum of the compensation cap. In addition, the agreement provides for certain additional items of compensation and benefits beyond that offered to other executive officers. Among other items, the Postmaster General's agreement provides for performance-based incentive payments each year upon achievement of performance objectives set by the Board, in addition to any pay-for-performance award to which the Postmaster General may be entitled under the Postal Service's pay-for-performance program.

Based on the Postal Service's achievement on pay-for-performance goals and metrics for 2008, the Governors awarded Mr. Potter $18,300 for fiscal year 2008. Pursuant to his contract, the Governors awarded Mr. Potter a performance incentive of $116,741 for fiscal year 2008. In doing so the Governors considered Mr. Potter's effective leadership during the difficult economic challenges of 2008, his implementation of a number of process improvements that led to record service levels at a lower cost, the steps he took that strategically positioned the Postal Service to maintain its viability for the future, and his achievement of personal goals set by the Governors for the fiscal year.

Other items of additional compensation and benefits for the Postmaster General are identified in the tables that follow. To the extent the statutory compensation cap precludes payment of any amounts earned by the Postmaster General in a particular year, these amounts are deferred for payment at a later date.

Components of the executive officer compensation and benefits program are further outlined as follows.

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, base salaries are 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, to reflect factors such as 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 return to the Postal Service. As discussed above, the Postal Service uses a national performance assessment program to set annual corporate performance goals and metrics. Executive officers' individual performance ratings are determined by the Postmaster General based on the degree to which the individual has achieved previously set individual goals and metrics.

Other Compensation Incentives

Executive officers are also eligible for performance awards for specific activities that reflect a high degree of leadership. Only a few of these individual awards are given out each year. In addition, executive officers are eligible for retention and recruitment incentives designed to attract and retain highly talented and marketable individuals in key postal positions.

Retirement Annuities

Officers are covered either by the Civil Service Retirement System (CSRS) or the Federal Employees Retirement System (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 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 5 years to 10 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 5 years of service, with a requirement of completing at least 5 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 1 percent of high-3 salary per year of service, or 1.1 percent for retirement at age 62 with at least 20 years of service. Optional retirement thresholds are the Minimum Retirement Age (MRA is 55 to 57 depending on year of birth) with 30 years of service, age 60 with 20 years of service, age 62 with 5 years of service, or MRA with 10 years of service (at a reduced benefit), with a requirement of completing at least 5 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 percent or less, at 2 percent when the CPI increase is between 2 and 3 percent, and at CPI - 1 when the CPI is at least 3 percent. Disability, early retirement, deferred and survivor benefits are available.

Defined Contribution: The Thrift Savings Plan (TSP) is similar to 401(k) plans. CSRS and FERS employees may contribute up to the indexed IRS maximum ($15,500 in 2008). There is no Postal Service contribution for CSRS employees. For FERS employees, after an initial waiting period of 6 months to a year, the Postal Service makes an automatic contribution of 1 percent of basic pay and a matching contribution of up to 4 percent of basic pay, for a total employer contribution of up to 5 percent 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 ($5,000 in 2008). TSP investment options are a government securities fund; index funds that track the Lehman Brothers U.S. Aggregate Bond Index, the S&P 500, the Wilshire 4500, and the Morgan Stanley Capital International EAFE (Europe, Australasia, Far East) stock index; and lifecycle funds.

Supplemental Non-Qualified Deferred Compensation

Where appropriate and on a highly selective basis (and currently only to the Postmaster General), the Postal Service offers supplemental non-qualified deferred compensation as a recruitment or retention tool. As noted above, the Postmaster General's employment agreement provides for incentive compensation payments each year upon achievement of performance objectives as set by the Board, in addition to any pay-for-performance award to which the Postmaster General may be entitled under the Postal Service's pay-for-performance program.

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 salary. All premiums for Option A, Option B, and basic coverage are paid by the USPS. At their own expense, officers may elect additional Option B coverage in an amount equal to two times their salary. Also at their own expense, officers may elect Option C, family optional insurance coverage, of up to 5 multiples of $5,000 for their spouse and $2,500 for each eligible dependent child. Officers continuously covered under FEGLI for the 5 years immediately preceding retirement, or since the first opportunity, may continue coverage during retirement (if entitled to an immediate annuity). USPS pays former officers an actuarially determined lump sum to cover the cost of Option A premiums during retirement to retiring officers.

Health Benefits

The Postal Service participates in the Federal Employees Health Benefits ("FEHB") program, which allows all career employees to be enrolled in one of a number of individual or family health benefit plans offered as part of this program. The Postal Service pays the full cost of the premium for its officers and executives. For employees who have participated in an FEHB plan for the five years preceding their retirement, the Postal Service is required by law to continue paying up to 75% of their FEHB plan premium.

Other Benefits

To remain competitive with the comparator marketplace, the Postal Service also offers the following additional benefits to its executive officers: periodic physical examinations, parking, financial counseling services, employer-paid life insurance premiums, and membership in up to two airline clubs per year.

Fiscal Year 2008 Executive Officer Compensation

Summary Compensation Table

Name and principal position	Year	Salary ($)	Bonus ($)	Non-equity incentive plan compensation ($)	Change in pension value and Nonqualified deferred compensation earnings ($)	All other compensation ($)	Total ($)
(a)	(b)	(c)	(d)	(g)	(h)	(i)	(j)
John E. Potter	FY08	$263,575	$0	135,041	$381,496	$77,347	857,459
Postmaster General, CEO							
H. Glen Walker	FY08	$218,654	$0	$11,700	$30,352	$18,988	$279,694
CFO & Executive VP							
Patrick R. Donahoe	FY08	$238,654	$0	$36,000	$316,805	$8,567	$600,026
Deputy Postmaster General & COO							
Anthony J. Vegliante	FY08	$228,654	$0	$32,200	$209,273	$12,693	$482,820
Chief Human Resources Officer & Executive VP							
Mary Anne Gibbons	FY08	$218,654	$0	$26,400	$82,875	$10,388	$338,317
Sr. VP, General Counsel							

Note: Column (g) The amount listed for Mr. Potter in this column reflects the pay-for-performance amount the Governors awarded to Mr. Potter based on the Postal Service's overall national NPA performance ($18,300) plus the amount of incentive compensation the Governors awarded to Mr. Potter pursuant to his employment agreement ($116,741). Mr. Potter's non-equity incentive plan compensation is deferred due to the compensation cap and will be paid in ten annual installments after he leaves postal employment. The amounts listed for the other named executive officers are the amount Mr. Potter awarded to these individuals based on the NPA score and individual performance.

Column (h) Mr. Potter, Mr. Donahoe, and Mr. Vegliante all participate in the Civil Service Retirement System, which is a defined benefit plan. Mr. Walker and Ms. Gibbons participate in the Federal Employees Retirement system, a portion of which is a defined benefit plan. The calculation of retirement annuities under CSRS and FERS is explained on pages 36 and 37 in the Retirement Annuities section of this Compensation Discussion and Analysis. The amounts shown in column (h) for each of these individuals are the amounts by which the value of their annuities has increased since the end of fiscal year 2007. "Nonqualified 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 fiscal year 2008.

Column (i) For all executive officers listed, the 'All Other Compensation' category includes: financial planning services, Thrift Savings Plan employer matching contribution for FERS employees, non-cash awards, parking, physical examinations, life insurance premiums paid for by the Postal Service, airline clubs, spousal travel. Security costs valued at $ 69,253 are also included for the Postmaster General.

Grants of Plan-Based Awards

The following table presents information regarding non-equity incentive grants to the named executive officers for fiscal year 2009. Whether executive officers receive an award and, if so, the amount for an award for fiscal year 2009 will depend on the Postal Service's and the individual's performance.

Name	**Grant date**	**Estimated future payouts under non-equity incentive plan awards**		
		Threshold ($)	**Target ($)**	**Maximum ($)**
(a)	(b)	(c)	(d)	(e)
John E. Potter	October 2008	$14,115	$31,838	$99,495
H. Glen Walker	October 2008	$11,704	$26,400	$82,500
Patrick R. Donahoe	October 2008	$12,768	$28,800	$90,000
Anthony J. Vegliante	October 2008	$12,236	$27,600	$86,250
Mary Anne Gibbons	October 2008	$11,704	$26,400	$82,500

Note: Columns (c)-(e). The USPS Pay-for-Performance (PFP) program relies on a 15-point scale with clearly defined and transparent corporate goals. The minimum threshold for any payment is set at a rating of 4 and the maximum threshold for payment is set at a rating of 15. The PFP plan target in any given year is set at a rating of 6. Incentives are not paid for any rating of less than 4. Individual ratings vary but the corporate score is used as the regulator.

Pension Benefits

The table below shows the present value of accumulated pension benefits payable to the named executive officer.

Name	**Plan name**	**Number of years credited service (#)**	**Present value of accumulated benefit ($)**
(a)	(b)	(c)	(d)
John E. Potter	USPS Pension Benefit	n/a	$1,350,318
John E. Potter	CSRS Annuity	30 Years	$2,453,057
H. Glen Walker	FERS Annuity	2 Years	$ 60,702
Patrick R. Donahoe	CSRS Annuity	33 Years	$2,522,570
Anthony J. Vegliante	CSRS Annuity	31 Years	$2,171,701
Mary Anne Gibbons	FERS Annuity	23 Years	$ 815,758

Note: Column (d) *Mr. Potter is the only USPS officer who also has a USPS Pension Benefit pursuant to contractual agreement. The amount in the first line in column (d) above for Mr. Potter above is payable to Mr. Potter for his employment as Postmaster General for his attainment of required performance objectives over the six-year period from June 2001 – June 2007 and was not based on his years of service to the Postal Service. Since 2007, the Board has not continued the USPS Pension Benefit and has frozen the amount of that benefit. Instead, since that time, Mr. Potter has been eligible for a performance incentive each year if he meets required performance objectives. The above amount of USPS Pension Benefit will be paid to Mr. Potter in monthly installments during his lifetime after he leaves postal employment, with a survivor annuity equal to 55% of the amount payable to Mr. Potter. All officers, including Mr. Potter, are eligible for Federal CSRS or FERS retirement benefits available to career employees of the Federal Government. These benefits are described in the Retirement Annuities section of this compensation discussion and analysis. The present value of the accumulated Federal CSRS or FERS benefit represents the value of the pension over the actuarial lifetime, as of September 30, 2008. Mr. Walker and Ms. Gibbons participate in FERS and the other named executive officers participate in CSRS. Mr. Potter and Mr. Donahoe are eligible for early retirement, the calculation of which is described in the Retirement Annuities section of the compensation discussion and analysis. The valuations for Mr. Potter and Mr. Donahoe reflect reductions that would apply for early retirement, as neither of these individuals has reached the age required for optional retirement. The valuation for Mr. Walker assumes that he has satisfied vesting requirements for retirement; however, because of his short tenure with the Postal Service, Mr. Walker's retirement annuity has not vested.*

Nonqualified Deferred Compensation

The following table presents information regarding the contributions to and earnings on the named executive officers' deferred compensation balances during the fiscal year ended September 30, 2008, and also shows the total deferred amounts for the named executive officers as of September 30, 2008.

Name	Executive contributions in last FY ($)	Aggregate earnings in last FY ($)	Aggregate balance at September 30, 2008 ($)
(a)	(b)	(c)	(d)
John E. Potter	$135,041	$20,232	$593,649
Patrick R. Donahoe	$ 11,500	$ 591	$ 27,720
Anthony J. Vegliante	$ 0	$ 525	$ 14,397

Notes:
Column (b) The amounts in this column represent amounts deferred due to the compensation cap.
Column (c) The Postal Service calculates Interest on deferred compensation at 5.0% per year.
Column (d) Mr. Potter's balance of $593,649 includes awards and performance incentives he earned in the 1990s before becoming Postmaster General, performance incentives he earned during the period from 2001 to 2007, interest earned on these amounts, and the amount shown in column (b) for Mr. Potter that was deferred in the last fiscal year.. The remaining portion is for interest on the above amounts. This total amount for Mr. Potter is payable in equal installments over a 10-year period after Mr. Potter's postal employment ends.

Director Compensation

Name	Fees earned or paid in cash ($)	All other compensation ($)	Total ($)
Alan C. Kessler	$34,500	$0	$34,500
Carolyn Lewis Gallagher	$36,600	$0	$36,600
Mickey D. Barnett	$36,000	$0	$36,000
James H. Bilbray	$35,400	$0	$35,400
Louis J. Giuliano	$36,600	$0	$36,600
Thurgood Marshall, Jr.	$36,300	$0	$36,300
James C. Miller III	$36,300	$0	$36,300
Katherine C. Tobin	$36,600	$0	$36,600
Ellen C. Williams	$33,600	$0	$33,600

Note: 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.

Potential Payments Upon Termination

As described in the Compensation Discussion and Analysis, the Postmaster General has an employment agreement with the Postal Service that provides for, among other things, pension benefits and deferred compensation payable at certain intervals following his departure from the Postal Service. The Postmaster General is the only named executive officer with an employment agreement. In addition, the Postmaster General is eligible to receive benefits pursuant to the Civil Service Retirement System (CSRS). All of the other named executives are subject to the standard policies governing the CSRS or the Federal Employees Retirement System (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 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, 2008. 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 the Federal Employees Health Benefits Plan for the requisite period of time prior to retiring.

Deferred Compensation

All federal employees, including Postal Service 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 an employee's total annual compensation to exceed the compensation limit, or the year in which an employee leaves federal service, whichever occurs first. Additionally, as described in the note accompanying the Pension Benefits table in the Compensation section of this report, the Postmaster General's employment agreement provides for performance-based incentive payments; these are also deferred. When the Postmaster General concludes his Postal Service employment, all deferred earnings, plus interest, will be paid to him in ten annual installments, beginning in the tax year after the tax year in which he ends his Postal Service employment. Had the Postmaster General terminated his Postal Service employment on September 30, 2008, his first annual payment derived from his deferred compensation, commencing in 2009 would have been $45,861; this annual installment would vary slightly thereafter, due to accumulated interest. In addition to the Postmaster General, named executive officers appearing in the Nonqualified Deferred Compensation table in the Compensation section of this report have deferred compensation in the amounts indicated therein. These amounts would be paid to them in lump sums shortly following their departure, had they ended their Postal Service employment on September 30, 2008.

Supplemental Pension Benefit

As described in the note accompanying the Pension Benefits table in the Compensation section of this report, the Postmaster General's employment agreement provides for a Postal Service pension benefit. The Pension Benefits table reflects the present value of this accumulated benefit. Had the Postmaster General terminated his employment as of October 1, 2008, his annual Postal Service pension benefit would have amounted to $68,730.

Severance Payment

Pursuant to his employment agreement, the Postmaster General is entitled to a monthly severance payment, which when added to his CSRS benefits and Postal Service pension benefit, will equal 1/12th of his annual salary at the date of the termination of his Postal Service employment. This benefit would continue for one year after the Postmaster General leaves his employment with the Postal Service. Had he terminated his employment as of September 30, 2008, the annual value of this benefit would have been $71,732. No other named executive officer may receive severance payments.

Insurance Benefits

The Postmaster General's employment agreement provides that for a period of one year after he leaves the Postal Service, he will be provided continuation of his medical, life and disability insurance coverage, subject to changes made in these programs as they apply to active officers of the Postal Service, and further, subject to the Postmaster General making the contributions required from active officers of the Postal Service. As a federal retiree, Mr. Potter would be entitled to participate in the Federal Employees Health Benefits (FEHB) Program and the Federal Employees' Group Life Insurance (FEGLI) Program in the manner available to all qualifying federal employees. As of September 30, 2008, the one year severance period value of the Postal Service's contributions to cover the extra cost of retiree premiums for this insurance coverage would be $13,982.60. After the expiration of this one-year period, as a federal retiree, Mr. Potter would be entitled to participate in the Federal Employees' Health Benefits (FEHB) Program in the manner available to all qualifying federal employees.

Outplacement Assistance

At the conclusion of his employment, the Postmaster General will be entitled to reasonable outplacement assistance by a provider selected by the Postal Service. This assistance may continue for up to two years from the date of the Postmaster General's separation from service. Had the Postmaster General separated from the Postal Service on September 30, 2008, the cost of this assistance for one year would have been $10,500. In the event a second year's outplacement assistance is necessary, its cost might be slightly higher.

Accrued Annual Leave

All Postal Service employees are entitled to receive and accrue paid days off, known as annual leave. Upon their separation from the Postal Service, all postal 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, 2008.

Name	Value of accrued annual leave ($)
John E. Potter	$248,104
H. Glen Walker	$ 29,615
Patrick R. Donahoe	$125,423
Anthony J. Vegliante	$256,538
Mary Anne Gibbons	$ 19,462

Compensation Committee Report

The Compensation and Management Resources Committee has reviewed and discussed the Compensation Discussion and Analysis with management and, based on such review and discussions, the Compensation and Management Resources Committee recommended to the Board of Governors that the Compensation Discussion and Analysis be included in this Report.

The Compensation and Management Resources Committee
Carolyn Lewis Gallagher, Chairman
Ellen C. Williams, Vice Chairman
Louis J. Giuliano, Member
Katherine C. Tobin, Member

Compensation Committee Interlocks and Insider Participation

The Compensation and Management Resources Committee, composed of Chairman Gallagher, Vice Chairman Williams, Mr. Giuliano and Ms. Tobin, was responsible for making recommendations to the Board of Governors with respect to compensation decisions. There are no Compensation Committee interlocks and no Postal Service employee serves on the Compensation and Management Resources Committee.

Item 12 – Security ownership of certain beneficial owners and management related stockholder matters

Not applicable to the United States Postal Service. 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

We enter into significant transactions with other government agencies, as disclosed throughout these financial statements.

All of the Governors of the Postal Service Board of Governors who are currently serving and have been appointed by the President of the United States with the advice and consent of the Senate are independent based on the New York Stock Exchange definition of independence.

Item 14 – Principal accountant fees and services

In 2002, the Board of Governors selected Ernst & Young LLP as its independent auditor to perform external auditing services. The competitively awarded five-year contract, contained a renewal option of up to 3 years. The five-year contract has ended and we are now in the three-year option period. The option period has an estimated value of $26.5 million covering the financial statement audits for fiscal years 2008 - 2010. As with previous contracts for external audit services, Ernst & Young LLP will not perform consulting work for us for the duration of the contract. Fees for audit services totaled approximately $5.9 million in 2008 and approximately $3.3 million in 2007, including fees associated with the annual audit, including the reviews of the Postal Service's quarterly reports on Form 10-Q.

Financial Review
Part IV

Item 15 – Exhibits and Financial Statement Schedules

(a)(1) and (2) Financial Statements; Financial Statement Schedules

In 2002, the Board of Governors selected Ernst & Young to audit the Postal Service's financial statements, together with the notes thereto. The reports of Ernst & Young LLP dated November 12, 2008 are presented on page 46 of this Form 10-K. The financial statements included are the Statement of Operations, the Balance Sheets, the Statements of Changes in Net Capital (Deficiency), the Statements of Cash Flows and Notes to the Financial Statements.

1. Financial Statements

Report of Independent Registered Public Accounting Firm – page 46
Statements of Operations for the Years Ended September 30, 2008, 2007 and 2006 – page 47
Balance Sheets as of September 30, 2008 and 2007 – pages 48-49
Statements of Changes in Net (Deficiency) Capital for the Years Ended September 30, 2008, 2007 and 2006 – page 50
Statements of Cash Flows for the Years Ended September 30, 2008, 2007 and 2006 – page 51
Notes to Consolidated Financial Statements – pages 52-61

2. Financial Statement Schedules

Operating Statistics from the Years Ended September 30, 2004 to 2008 – pages 62-65
Financial History Summary from the Year Ended September 30, 2004 to 2007 – page 66
Selected Quarterly Financial Data from The beginning of the year 2007 to 2008 – page 67

(a)(3) Exhibits

Exhibit Number	Description of Exhibit
10.1	Employment/Compensation Contract of Postmaster General as of August 8, 2007 as amended November 25, 2008.
10.2	Employment/Compensation Contract with President of Shipping and Mailing Services (filed with the PRC on August 11, 2008, as Exhibit No. 10.1 to the Quarterly Report on Form 10-Q for the quarter ended June 30, 2008.
10.3	Employment/Compensation Contract with Chief Information Officer (filed with the PRC on May 8, 2008, as Exhibit No. 10.1 to the Quarterly Report on Form 10-Q for the quarter ended March 31, 2008.
31.1	Certification of Principal Executive Officer Pursuant to Rules 13a-14(a) and 15d-14(a) under the Securities and Exchange Act of 1934, as Adopted Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31.2	Certification of Principal Financial Officer Pursuant to Rules 13a-14(a) and 15d-14(a) under the Securities and Exchange Act of 1934, as Adopted Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
32.1	Certification of Principal Executive Officer Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
32.2	Certification of Principal Financial Officer Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

Report of Independent Auditors

ERNST & YOUNG

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Report of Independent Registered Public Accounting Firm

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, 2008 and 2007, and the related statements of operations, changes in net capital, and cash flows for each of the three years in the period ended September 30, 2008. 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) 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. We were not engaged to perform an audit of the United States Postal Service's internal control over financial reporting. Our audits included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the United States Postal Service's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and 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, 2008 and 2007, and the results of its operations and its cash flows for each of the three years in the period ended September 30, 2008, in conformity with U.S. generally accepted accounting principles.

In accordance with Government Auditing Standards, we have also issued our report dated November 14, 2008 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, 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.

Ernst + Young LLP

November 14, 2008

A member firm of Ernst & Young Global Limited

Statements of Operations

(Dollars in millions)	Years Ended September 30, 2008	2007	2006
Operating revenue	$ 74,932	$ 74,778	$ 72,650
Operating expenses:			
Compensation and benefits	53,585	54,186	54,665
Retiree health benefits	7,407	10,084	1,637
Transportation	6,961	6,502	6,045
Other	9,785	9,333	9,334
Total operating expenses	77,738	80,105	71,681
(Loss) Income from operations	**(2,806)**	**(5,327)**	**969**
Interest and investment income	36	195	167
Interest expense on deferred retirement obligations	**-**	**-**	(231)
Other interest expense	(36)	(10)	(5)
Net (Loss) Income	**$ (2,806)**	**$ (5,142)**	**$ 900**

See accompanying notes to the financial statements

Balance Sheets – Assets

	September 30,	
	2008	2007
(Dollars in millions)		
Assets		
Current Assets:		
Cash and cash equivalents	$ 1,432	$ 899
Receivables:		
Foreign countries	450	425
U.S. government	133	155
Other	187	223
Receivables before allowances	770	803
Less allowances	41	44
Total receivables, net	729	759
Supplies, advances and prepayments	193	201
Total Current Assets	**2,354**	**1,859**
Property and Equipment, at Cost:		
Buildings	22,269	21,591
Equipment	21,544	21,060
Land	2,971	2,914
Leasehold improvements	914	842
	47,698	46,407
Less allowances for depreciation and amortization	25,886	24,688
	21,812	21,719
Construction in progress	1,381	1,877
Total Property and Equipment, Net	**23,193**	**23,596**
Other Assets - Principally Revenue Forgone Receivable	**439**	**392**
Total Assets	$ **25,986**	$ **25,847**

See accompanying notes to the financial statements

Balance Sheets – Liabilities and Net (Deficiency) Capital

	September 30,	
	2008	2007
(Dollars in millions)		
Liabilities and Net (Deficiency) Capital		
Current Liabilities:		
Compensation and benefits	$ 3,466	$ 3,571
Payables and accrued expenses:		
Trade payables and accrued expenses	1,246	1,503
Foreign countries	413	452
U.S. government	85	111
Total payables and accrued expenses	1,744	2,066
Customer deposit accounts	1,449	1,499
Deferred revenue-prepaid postage	1,689	1,142
Outstanding postal money orders	720	847
Prepaid box rent and other deferred revenue	461	479
Debt	7,200	4,200
Total Current Liabilities	**16,729**	**13,804**
Noncurrent Liabilities:		
Workers' compensation costs	7,003	6,800
Employees' accumulated leave	2,208	2,129
Deferred appropriation and other revenue	525	591
Long-term portion capital lease obligations	587	618
Deferred gains on sales of property	312	310
Contingent liabilities and other	294	461
Total Noncurrent Liabilities	**10,929**	**10,909**
Total Liabilities	**27,658**	**24,713**
Net Capital		
Capital contributions of the U.S. government	3,034	3,034
Deficit since 1971 reorganization	(4,706)	(1,900)
Total Net (Deficiency) Capital	**(1,672)**	**1,134**
Total Liabilities and Net (Deficiency) Capital	**$ 25,986**	**$ 25,847**

See accompanying notes to the financial statements

Statement of Changes in Net (Deficiency) Capital

(Dollars in millions)

	Capital Contributions of U.S. Government	Retained (Deficit) Earnings Since Reorganization	Total Net (Deficiency) Capital
Balance, September 30, 2005	**$** 3,034	**$** 2,342	**$** 5,376
Net Income	-	900	900
Balance, September 30, 2006	3,034	3,242	6,276
Net (Loss)	-	(5,142)	(5,142)
Balance, September 30, 2007	3,034	(1,900)	1,134
Net (Loss)	-	(2,806)	(2,806)
Balance, September 30, 2008	**$ 3,034**	**$ (4,706)**	**$ (1,672)**

See accompanying notes to the financial statements

Statements of Cash Flows

	Years Ended Sepetember 30, 2008	2007	2006
(Dollars in millions)			
Cash flows from operating activities:			
Net (Loss) Income	$ (2,806)	$ (5,142)	$ 900
Adjustments to reconcile net (loss) income to net cash (used in) provided by operating activities:			
Depreciation and amortization	2,319	2,152	2,149
(Gain) loss on disposals of property and equipment, net	(16)	23	(40)
(Increase) decrease in appropriations receivable revenue forgone	(47)	2	(18)
Increase (decrease) in noncurrent workers' compensation liability	203	(69)	342
Increase in employees' accumulated leave	79	13	100
(Decrease) increase in noncurrent deferred appropriations and other revenue	(5)	(7)	21
(Decrease) increase in other noncurrent liabilities	(167)	281	(67)
Changes in current assets and liabilities:			
Receivables, net	30	80	169
Supplies, advances and prepayments	8	4	(5)
Compensation and benefits	(105)	347	204
Payables and accrued expenses	(324)	(93)	64
Customer deposit accounts	(50)	(148)	(73)
Deferred revenue-prepaid postage	547	(45)	(13)
Outstanding postal money orders	(127)	(38)	55
Prepaid box rent and other deferred revenue	22	37	(20)
Net cash (used in) provided by operating activities	(439)	(2,603)	3,768
Cash flows from investing activities:			
Decrease (increase) in restricted cash	-	2,958	(2,958)
Purchase of property and equipment	(1,995)	(2,715)	(2,630)
Proceeds from deferred building sale	4	218	-
Proceeds from sales of property and equipment	53	39	114
Net cash (used in) provided by investing activities	(1,938)	500	(5,474)
Cash flows from financing activities:			
Issuance of notes payable	4,500	1,000	-
Payments on notes payable	(1,000)	-	-
Net change in revolving credit line	(500)	1,100	2,100
Payments on capital lease obligations, net	(29)	(19)	(37)
U.S. government appropriations - expensed	(61)	(76)	(85)
Net cash provided by financing activities	2,910	2,005	1,978
Net increase (decrease) in cash and cash equivalents	533	(98)	272
Cash and cash equivalents at beginning of year	899	997	725
Cash and cash equivalents at end of year	$ 1,432	$ 899	$ 997

See accompanying notes to the financial statements

Notes to the Financial Statements

Note 1 – Description of business

Nature of Operations

The United States Postal Service (we) provides a variety of classes of mail service to the public, without undue discrimination among our many customers. This means that within each class of mail our price does not unreasonably vary by customer for the levels of service we provide. This fulfills our legal mandate to offer universal service at a fair price. We conduct our operations primarily in the domestic market, with international operations representing approximately 3% of our total revenue.

Our services are divided into two broad categories: mailing and shipping, which account for 89% and 11% of our revenue, respectively. Two lines, First-Class Mail and Standard Mail, account for about 94% of our mail volume, while Priority Mail and Express Mail represent significant services we provide in our shipping category. The principal markets for our services are the communications, distribution, delivery, advertising, and retail markets. Our services are sold and distributed through almost 37,000 Post Offices, stations, branches, contract postal units, and a large network of consignees.

Our labor force is primarily represented by the American Postal Workers Union (APWU), National Association of Letter Carriers (NALC), National Postal Mail Handlers Union (NPMHU), and National Rural Letter Carriers Association (NRLCA). More than 85% of our career employees are covered by collective bargaining agreements.

By law, we also consult with management organizations representing most of the employees not covered by collective bargaining agreements. These consultations provide an opportunity for nonbargaining unit employees in the field to participate directly in the planning, development, and implementation of programs and policies affecting managerial employees in the field.

Postal Reorganization

We commenced operations on July 1, 1971, in accordance with the provisions of the Postal Reorganization Act. We are an "independent establishment of the executive branch of the Government of the United States." Governing decisions are made by a Board of Governors, which consists of nine members who are appointed by the President with the advice and consent of the Senate, plus the Postmaster General and Deputy Postmaster General.

The equity that the U.S. government held in the former Post Office Department became our initial capital. We valued the assets of the former Post Office Department at original cost less accumulated depreciation. The initial transfer of assets, including property, equipment, and cash, totaled $1.7 billion. Subsequent cash contributions and transfers of assets between 1972 and 1982 totaled approximately $1.3 billion, resulting in total government contributions of $3.034 billion. The U.S. government remains responsible for all of the liabilities attributable to operations of the former Post Office Department. However, under the Balanced Budget Act of 1997, the liability for Post Office Department workers' compensation costs was transferred to us.

The Postal Accountability and Enhancement Act (P.L.109-435), enacted December 20, 2006, made significant reforms in the governance of the Postal Service and significantly altered some of our financial responsibilities, particularly with respect to the funding of Civil Service Retirement System (CSRS) benefits and retiree health benefits. See Note 4, *Postal Accountability and Enhancement Act, Public Law 109-435 (P.L. 109-435),* in the Notes to the Financial Statements for additional information.

We enter into significant transactions with other U.S. government agencies, as disclosed throughout these financial statements.

Note 2 – Summary of significant accounting policies

Basis of Accounting and Use of Estimates

We conform to accounting principles generally accepted in the United States (GAAP) and maintain our accounting records and prepare financial statements on the accrual basis of accounting. Following these principles, we make estimates and assumptions that affect the amounts reported in the Financial Statements and Notes. Actual results may differ from estimates.

Segment Information

We operate in one segment throughout the United States, its possessions and territories, and internationally.

Reclassifications

Certain comparative prior year amounts related to deferred gains that we have determined are immaterial to the financial statements and accompanying notes have been reclassified to conform to the current year presentation. These reclassifications had no effect on previously reported operating income and net income.

Cash and Cash Equivalents

We consider securities that mature within 90 days or less from the date that we buy them to be cash equivalents.

Allowance for Doubtful Accounts

We provide an allowance for doubtful accounts on outstanding receivables based on our collection history and an estimate of uncollectible accounts.

Allowance for Doubtful Accounts (Dollars in millions)	2008	2007	2006
Beginning Balance	$ 44	$ 48	$ 50
Provision for Doubtful Accounts	7	12	3
Writeoffs	10	16	5
Ending Balance	**$ 41**	**$ 44**	**$ 48**

Supplies and Repair Parts

Supplies and repair parts consist of repair parts for mail processing equipment. We value these at average cost. Total supplies and repair parts amounted to $112 million at the end of 2008 and $119 million at the end of 2007. A majority of our motor vehicle spare parts are supplied through consignment agreements.

Property and Equipment

We record property and equipment at cost, including interest paid on the money we borrow to pay for the construction of major capital additions. See Note 6, *Property and equipment,* in the Notes to the Financial Statements for additional information.

We depreciate buildings and equipment over their estimated useful lives, which range from 3 to 40 years, except buildings with historic status, which are depreciated over 75 years, using the straight-line method.

Impaired Assets

We record losses on long-lived assets when events and circumstances indicate that the assets might be impaired. In accordance with Financial Accounting Standards Board Statement 144, *Accounting for the Impairment or Disposal of Long-Lived Assets*, we write down impaired assets to the lower of cost or fair value. See Note 6, *Property and equipment,* in the Notes to the Financial Statements for additional information.

Asset Retirement Obligations

We account for asset retirement obligations in accordance with Financial Accounting Standards Board Interpretation 47, *Accounting for Conditional Asset Removal* (FIN 47). Accruals are recorded under "Noncurrent Liabilities, Contingent liabilities and other" on our balance sheets.

Amortization of Leasehold Improvements

We amortize leasehold improvements over the period of the lease or the useful life of the improvement, whichever is shorter.

Leasehold improvements that are placed in service after the start of the lease term are amortized over the shorter of the useful life of the asset or the lease term, including expected renewal options.

Foreign Currency Translation

We have foreign currency risk related to settlements with foreign postal administrations for international mail. The majority of our international accounts are denominated in special drawing rights (SDRs). The SDR exchange rate fluctuates daily based on a basket of currencies comprised of the euro, Japanese yen, pound sterling, and the U.S. dollar. Changes in the relative value of these currencies will increase or decrease the value of our settlement accounts and result in a gain or loss from revaluation reported in the results from operations. The actual currency used to settle accounts varies by country. The impacts on our financial statements from foreign currency fluctuations were insignificant for 2008, 2007, and 2006.

Outstanding Postal Money Orders

We sell money orders to the general public at our retail locations. We charge a fee to the customer at the time of sale. The fee is recognized as revenue at the time of sale. We recognize a liability for money orders we expect to be presented for payment.

Revenue Recognition/Deferred Revenue–Prepaid Postage

We recognize revenue when services are rendered. Because we collect payment in advance of services being performed, we defer the revenue until the services are performed. This is classified as a liability, *deferred revenue-prepaid postage,* on our balance sheets. In Quarter III of the current year, we changed the methodology used to estimate the deferred revenue for prepaid postage for stamps. This update was made necessary because the introduction of the Forever Stamp in April 2007, combined with the May 2008 price increase, resulted in a change in consumer behavior regarding the purchase and usage of stamps that was not measurable using our prior estimation techniques. We developed a new approach that more accurately captures trends in stamp usage. The change to a new estimation technique is considered a change in accounting estimate under GAAP.

As required by FAS 154, the impact of the change was recorded in Quarter III, 2008. For the year ended September 30, 2008, we increased the stamp portion of the deferred revenue–prepaid postage liability by $477 million, $230 million of which is considered a cumulative change in estimate and $247 million of which is attributable to changes in consumer behavior during the last two quarters of the year.

Advertising Expenses

Advertising costs are expensed as incurred and are classified in other operating expenses. Advertising expenses were $106 million in 2008, $121 million in 2007, and $138 million in 2006.

Compensation and Benefits Payable

Compensation and Benefits Payable are the salaries and benefits we owe to current and retired employees, including the amounts employees have earned but have not yet been paid, current workers' compensation, unemployment costs, and health benefits.

Workers' Compensation

We pay for workers' compensation costs under a program administered by the Department of Labor (DOL). These costs include employees' medical expenses, compensation for wages lost, and DOL administrative fees. We record these costs as an operating expense. See Note 11, *Workers' compensation,* in the Notes to the Financial Statements for additional information.

Retiree Benefits

Our employees are eligible to participate in the federal government retirement programs, including pension and retiree health benefits. We are required to provide funding for those plans as determined by the administrator of the plan, the Office of Personnel Management (OPM). We cannot direct the costs, benefits, or funding requirements of these federally-sponsored plans. In accordance with our parent-subsidiary type relationship with the federal government, we account for our participation in these plans using multiemployer plan accounting rules in accordance with Financial Accounting Standards Board Statement (FAS) 87, *Employers Accounting for Pension Costs* and FAS 106 *Employers Accounting for Postretirement Benefits Other than Pensions*. We account for the cost of our employees' participation in these programs as an expense in the period our contribution is due and payable. As more fully described in Note 4, *Postal Accountability and Enhancement Act, Public Law 109-435 (P.L. 109-435),* the law significantly impacted our 2007 costs associated with these programs. See also Note 9, *Health benefit programs*, and Note 10, *Retirement programs*, in the Notes to the Financial Statements for additional information.

Revenue Forgone Appropriation

Revenue Forgone is an appropriation from Congress, which covers our cost of providing free and reduced-rate mailing services to groups designated by Congress. The amount of expense estimated by the Postal Service is submitted to Congress annually. Congress subsequently approves or alters the amount and funds the necessary appropriation. See Note 12, *Revenue forgone,* in the Notes to the Financial Statements for additional information.

Emergency Preparedness Appropriation

Emergency preparedness appropriations are funds we received from the federal government to help pay the costs of keeping the mail, postal employees, and postal customers safe, and are restricted for such use. These funds were accounted for as deferred revenue upon receipt and were largely utilized to procure capital equipment. We recognize revenue for emergency preparedness appropriations at the same time we recognize depreciation expense for capital equipment purchased with these appropriations. The emergency preparedness appropriations revenue recognized during the years ended September 30 was $61 million in 2008, $76 million in 2007, and $85 million in 2006.

Appropriations that have not been recognized as revenue during the years ended September 30 were $550 million in 2008 and $611 million in 2007. The current portion is included in prepaid box rent and other deferred revenue, and the long-term portion is in deferred appropriations and other revenue on our balance sheets.

Note 3 – Recent pronouncements

In September 2006, the Financial Accounting Standards Board (FASB) issued FAS 157, which defines fair value, establishes a framework for measuring fair value, and expands disclosures about fair value measurements. The provisions of FAS 157 are effective as of the beginning of our 2009 fiscal year. FAS 157 does not change any of our measurement or disclosure reporting.

Notes to the Financial Statements

Note 4 – Postal Accountability and Enhancement Act, Public Law 109-435 (P.L. 109-435)

P.L.109-435, enacted December 20, 2006, made significant reforms in the governance of the Postal Service and significantly altered some of our financial responsibilities, particularly in respect to the funding of CSRS benefits and retiree health benefits. The legislation does not change our parent-subsidiary type relationship as an "independent establishment of the executive branch of the Government of the United States." Our employees and retirees continue to participate in all federally sponsored retirement and health benefit plans. Therefore, we continue to account for our participation in U.S. government-sponsored health benefit and retirement plans using multiemployer plan accounting rules in accordance with FAS 106, *Employers' Accounting for Postretirement Benefits Other Than Pensions,* and FAS 87, *Employers' Accounting for Pensions*.

A number of major provisions of P.L.109-435 directly impact our financial statements and are briefly summarized below. For a complete understanding of the law, one must consult the full text, which can be found at www.Thomas.gov.

P.L.109-435 returned to the U.S. Treasury the obligation to fund the portion of the CSRS retirement benefit earned while serving in the military by participants who retire as postal employees. With the return of this funding requirement to the U.S. Treasury, it was estimated by OPM that we had fully funded our CSRS pension obligation as of September 30, 2006. See Note 10, *Retirement programs,* in the Notes to the Financial Statements for more information on our retirement obligations.

Under P.L. 109-435, the Postal Service Retiree Health Benefits Fund (PSRHBF), which is held by the U.S. Treasury and controlled by OPM, was created. The PSRHBF will be used, commencing in 2017, to pay our share of the health insurance premiums for current and future Postal Service retirees. The initial funding of the PSRHBF consisted of $17.1 billion, which was identified by OPM to be the surplus of the Postal Service's portion of the CSRS as of September 30, 2006. Beginning in 2007, P.L.109-435 required us to make annual payments into the PSRHBF. The payment schedule in the law requires us to pay, on average, $5.6 billion per year into the fund for ten years, which began in 2007. This is in addition to our regularly allocated cost of premiums for current retirees, which will continue to be payable through 2016. After these annual payments are complete, OPM will make an actuarial valuation and determine whether any further payments into the PSRHBF are required. We paid $5.6 billion into the PSRHBF in 2008 and $5.4 billion in 2007.

P.L.109-435 repealed the escrow provisions of P.L.108-18, which required us to place into an escrow account by September 2006, any "savings" from the change in the retirement provisions created by P.L.108-18. OPM calculated the savings at $2,958 million as of September 30, 2006. These escrowed funds were shown as restricted cash on our September 30, 2006, balance sheet. P.L.109-435 required that we pay the 2006 escrowed "savings" to the PSRHBF. In 2007, we expensed the entire amount payable to the PSRHBF. On April 6, 2007, these "savings" were transferred to the PSRHBF.

Note 5 – Debt and related interest

Borrowing Limits and Debt

Under the Postal Reorganization Act, as amended by Public Laws 101-227 and 109-435, we can issue and sell debt obligations. However, at year-end we are limited to net annual increases of $3 billion in our debt. Our total debt cannot exceed $15 billion.

Debt Consists of the Following:

Interest Rate %	Terms *	2008	2007
(Dollars in millions)			
NOTES PAYABLE TO THE FEDERAL FINANCING BANK (FFB):			
0.297%**	Short-term revolving credit facility; Payable October 1, 2008 and 2007	$ 2,200	$ 2,900
0.905%	Payable December 11, 2008	2,500	-
0.485%	Payable December 18, 2008	2,000	-
0.155%	Short-term revolving credit facility; Payable December 18, 2008	500	-
3.528%	Overnight revolving credit note; Payable October 1, 2007	-	300
3.101%	Payable November 15, 2007	-	500
3.866%	Payable December 20, 2007	-	500
		$ 7,200	$ 4,200

** All debt is repurchasable at any time at a price determined by the Secretary of the Treasury, based on rates prevailing in the Treasury Security market at the time of repricing.*
*** Prior year rate was 3.366%*

The current value of our debt is what it would cost to pay off the debt if we used the current yield on equivalent U.S. Treasury notes. At year-end, the current estimated value of our debt is $7.2 billion.

Notes to the Financial Statements

Note Purchase Agreements

Our note purchase agreements with the Federal Financing Bank provide for revolving credit lines of $4 billion. These credit lines enable us to draw up to $3.4 billion with two days' notice, and up to $600 million on the same business day the funds are needed. Under these agreements we can also use a series of other notes with varying provisions to draw upon with two days' notice. The notes provide us the flexibility to borrow short-term or long-term, using fixed or floating-rate debt, and can be either callable or non-callable.

Interest Payments on Retirement

There were no cash outlays for interest on the retirement "supplemental liability" in 2008 or 2007 because the enactment of P.L. 109-435 suspended this requirement until 2017. In 2006, the cash outlay was $231 million. See Note 10, *Retirement programs,* in the Notes to the Financial Statements for additional information.

Other Interest Payments

Cash outlays for other interest were $37 million in 2008, $9 million in 2007, and $4 million in 2006.

Note 6 – Property and equipment

Sale of Major Facility

In 2008 and 2006, there were no sales of any major facilities. On March 30, 2007, we sold the James A. Farley building in New York City to the Empire State Development Corporation (ESDC), for $190 million and additional proceeds of up to $55 million, contingent upon the achievement of certain development and leasing criteria by the developer of the property. The Postal Service continues to conduct retail and carrier operations at this facility under the terms of an interim lease with annual rentals of $5.6 million per year. Once the carrier operations are relocated to other facilities, we will continue to conduct retail and some administrative functions in a smaller portion of the building under a 99-year lease, with a rental fee of $1. The Postal Service has an option to require the building owner to change the legal structure of the building ownership into condominium units, with the Postal Service being given the right to purchase the space subject to the 99-year lease.

We accounted for the transaction under the deposit method under the provisions of FAS 66, *Accounting for Sales of Real Estate.* The gain will not be recognized and the asset will not be removed from our accounting records until the lease and other continuing involvement in the building have expired.

In conjunction with this sale, from the funds ESDC paid us, $10 million was set aside for an environmental clean-up fund. Our environmental liability is limited to $10 million and is included on our balance sheet under trade payables and other accrued expenses.

Impaired Assets

The amount of assets that was written down due to impairment in accordance with FAS 144 was immaterial to the balances of fixed assets in 2008 and 2007.

Assets Held For Sale

The balance of those assets held for sale that was classified in accordance with FAS 144 was immaterial to the total fixed asset balance in 2008 and 2007.

Interest Capitalization

No interest was capitalized in 2008, 2007, or 2006.

Repairs and Maintenance

Repairs and maintenance are charged to expense as incurred. This expense amounted to $711 million in 2008, $665 million in 2007, and $641 million in 2006.

Note 7 – Leases and other commitments

Capital

At September 30, 2008, our future minimum lease payments for all noncancelable leases are as follows.

Lease Obligations (Dollars in millions)	Operating	Capital
2009	$ 780	$ 102
2010	763	98
2011	710	96
2012	640	98
2013	579	92
After 2013	4,864	523
Total Lease Obligations	**$ 8,336**	**$ 1,009**
Less: Interest		376
Total Capital Lease Obligations		**633**
Less: Short-term portion of capital lease obligations		46
Long-term portion of capital lease obligations		**$ 587**

Notes to the Financial Statements

Most of these leases contain renewal options for periods ranging from 3 to 20 years. Certain noncancelable real estate leases give us the option to purchase the facilities at prices specified in the leases.

Capital leases included in buildings were $916 million in 2008 and $931 million in 2007. Total accumulated amortization is $419 million in 2008 and $404 million in 2007. Amortization expense for assets recorded under capital leases is classified as depreciation expense, which is included in other operating expenses in the statements of operations.

Our total rental expense for the years ended September 30 is summarized as follows.

Rental Expense	2008	2007	2006
(Dollars in millions)			
Non-cancelable real estate leases including related taxes	$ 967	$ 927	$ 953
Facilities leased from GSA subject to 120-day cancellation	44	46	49
Equipment and other short-term rentals	294	261	192
Total Rental Expense	**$ 1,305**	**$ 1,234**	**$ 1,194**

At September 30, 2008, we estimate our financial commitment for approved capital projects in progress (resources on order) to be $2,830 million, detailed in the following table.

Capital Resources on Order	2008
(Dollars in millions)	
Mail Processing Equipment	$ 1,424
Building Improvements	548
Postal Support Equipment	360
Construction and Building Purchase	459
Vehicles	5
Retail Equipment	34
Total Capital Resources on Order	**$ 2,830**

Expense Commitments

In the normal operating of our business, we enter into commitments for expense contracts. The contracts run for periods from one to ten years. Although these contracts contain clauses for termination by the Postal Service, we normally would have early termination costs.

Expense commitments are classified as miscellaneous, inventory, and research and development. Our miscellaneous expense commitments include contracts for supplies, services, communications, repairs, research, printing and advertising. Our inventory contracts are for vehicle repair parts and mechanized equipment spare parts. These are summarized in the following table.

Expense Resources on Order	2008
(Dollars in millions)	
Miscellaneous Contracts	$ 4,960
Inventory Contracts	50
Research and Development Contracts	39
Total Expense Resources on Order	**$ 5,049**

In addition, P.L. 109-435 mandates annual payments into the PSRHBF. These payments are listed in the following table.

Retiree Health Benefits Commitments	P.L. 109-435 Requirement
(Dollars in millions)	
2009	**$** 5,400
2010	5,500
2011	5,500
2012	5,600
2013	5,600
After 2013	17,200
Total Retiree Health Benefits Commitments	**$ 44,800**

Note 8 – Contingent liabilities

Our contingent liabilities consist mainly of claims and suits resulting from labor, equal employment opportunity and environmental issues, property damage claims, injuries on postal properties, issues arising from postal contracts, personal claims, and traffic accidents.

Each quarter we review significant new claims and litigation for the probability of an adverse outcome. If a claim is deemed "probable" for an unfavorable outcome and the amount of settlement is estimable, we record a liability. Each quarter we also review and adjust any prior contingencies for settlements, or revisions to prior estimates. No individual claim is material to our financial statements when taken as a whole. The following table summarizes contingent liabilities provided for in our financial statements.

Contingent Liabilities	2008	2007
(Dollars in millions)		
Labor	$ 318	$ 526
Equal Employment Opportunity	45	57
Environmental	40	40
Tort	32	39
Contractual	1	14
Total Contingent Liabilities	**$ 436**	**$ 676**

We believe that adequate provision has been made for probable liabilities from claims and suits. The current portion of this liability at September 30, 2008, of $198 million is included on the balance sheets under the heading "Trade payables and accrued expenses". On September 30, 2007, this amount was $248 million. The long-term portion at September 30, 2008, of $238 million is accrued under the heading, "Noncurrent Liabilities, Contingent liabilities and other" in our balance sheet. On September 30, 2007, the long-term liability was $428 million.

We also have other claims and suits that we deem reasonably possible of unfavorable outcomes and for which we cannot yet determine the amounts or a reasonable range of potential losses, if any. No provisions for these are included in our financial statements.

Note 9 – Health benefit programs

Current Employees

Substantially all of our career employees are covered by the Federal Employees' Health Benefits Program (FEHBP). OPM administers the program and allocates the cost of the program to the various participating government agency employers. We cannot direct the costs, benefits, or funding requirements of the federally sponsored plan, and therefore account for these costs using multiemployer plan accounting rules.

Our portion of the cost is based upon the weighted average premium cost of the various employee coverage choices and the specific coverage choices made by our employees. Our employees paid approximately 18% of the premium costs in 2008, and 17% in 2007 and 2006. We paid the remainder of employee health care expense, which was $5,376 million in 2008, $5,401 million in 2007, and $5,345 million in 2006.

Retirees

Employees who participate in the FEHBP for at least the five years immediately before their retirement may participate in the FEHBP during their retirement. The Omnibus Budget Reconciliation Act of 1990 requires us to pay the employer's share of health insurance premiums for all retired postal employees and their survivors who participate in the FEHBP and who retire on or after July 1, 1971. However, we do not include the costs attributable to federal civil service before that date.

As discussed in Note 4, *Postal Accountability and Enhancement Act, Public Law 109-435 (P.L. 109-435)*, resulted in our retiree health benefit expenses increasing dramatically beginning in 2007. Total expenses were $7,407 million in 2008 and $10,084 million in 2007, compared to only $1,637 million in 2006. These costs are reflected as Retiree health benefits in our Statements of Operations.

Note 10 – Retirement programs

Pension Programs

Our employees participate in one of the following pension programs based upon the starting date of their employment with the federal government. Employee and employer contributions are made to the Civil Service Retirement System (CSRS), the Dual Civil Service Retirement System/Social Security (Dual CSRS), or the Federal Employees Retirement System (FERS), all of which are administered by the Office of Personnel Management. Employees may also participate in the Thrift Savings Plan (TSP), which is a defined contribution retirement savings and investment plan. Postal Service employees are authorized to participate in the TSP by the Federal Employees Retirement System Act of 1986. The TSP is administered by the Federal Retirement Thrift Investment Board.

CSRS

Under the Postal Reorganization Act, officers and career employees hired prior to January 1, 1984 are covered by the Civil Service Retirement System, which provides a basic annuity toward which we and the employee contribute at rates prescribed by law. Effective October 14, 2006, P.L.109-435 suspends the obligation of making employer contributions for CSRS employees' retirement. We do not match TSP contributions for employees who participate in CSRS.

DUAL CSRS

Employees with prior U.S. government service who were hired between January 1, 1984, and January 1, 1987, are covered by Dual CSRS, which consists of a basic annuity and Social Security. We and the employee contribute to Social Security and the basic annuity at rates prescribed by law. We do not match TSP contributions for employees who participate in Dual CSRS.

FERS

Effective January 1, 1987, officers and career employees hired since December 31, 1983, are covered by the Federal Employees Retirement System Act of 1986, except for those covered by Dual CSRS. Also included are employees formerly covered by CSRS who elected in 1987, 1988, and 1998 to participate in FERS.

FERS consists of Social Security, a basic annuity plan, and TSP. We and the employee contribute to Social Security and the basic annuity plan at the rate prescribed by law. In addition, we are required to contribute to TSP a minimum of 1% per year of the basic pay of employees covered by this system. We also match a voluntary employee contribution up to 3% of the employee's basic pay, and 50% of a contribution between 3% and 5% of basic pay.

Employee / Employer Contributions

Employer and employee contributions, as a percentage of employee basic pay, are as follows for each of the three plans for 2008, 2007, and 2006.

Retirement Contribution (Percentage)	2008	2007	2006
CSRS Employer	-	-	17.4
CSRS Employee	7.0	7.0	7.0
Dual CSRS Employer	-	-	18.0
Dual CSRS Employee	0.8	0.8	0.8
FERS Employer	11.2	11.2	11.2
FERS Employee	0.8	0.8	0.8

The number of employees enrolled in each of the retirement plans at the end of 2008, 2007, and 2006 is as follows.

Retirement Enrollment by Program (Actual numbers)	2008	2007	2006
CSRS	130,126	144,034	157,945
Dual CSRS	7,128	7,716	8,150
FERS	525,984	533,012	530,043

Expense Components

The following table lists the components of our total retirement expenses that are included in Compensation and benefits expense in the Statements of Operations for 2008, 2007, and 2006.

Retirement Expense (Dollars in millions)	2008	2007	2006
FERS	$ 2,909	$ 2,771	$ 2,652
Social Security	1,932	1,904	1,843
FERS Thrift Savings Plan	1,058	1,007	960
CSRS	0	52	1,450
Dual CSRS	0	3	75
CSRS "Supplemental Liability"	0	0	26
Total Retirement Expense	**$ 5,899**	**$ 5,737**	**$ 7,006**

Employer cash contributions to retirement plans were $3,936 million in 2008, $3,889 million in 2007, and $5,122 million in 2006. These amounts do not include Social Security contributions and interest expense on deferred retirement liabilities.

Beginning in 2004, we had been required by P.L.108-18 to pay an additional annual amount into the CSRS retirement plan, if necessary, each September, as determined by OPM. The "supplemental liability" represented the excess of the actuarial present value of the future benefits liability over the actuarial present value of plan assets, future contributions, earnings, and other actuarial factors related to Postal Service participants in the CSRS plan. In 2006, we paid $257 million including interest towards this liability, of which $231 million was interest and the remaining $26 million a reduction in the principal amount of the liability.

P.L.109-435 relieved the Postal Service of the obligation to pay for the portion of the CSRS pension costs attributable to the military service of its retirees that was previously imposed by P.L.108-18. The cost of these benefits was estimated by OPM to be $27 billion in 2003. The elimination of the military service funding requirement dramatically impacted the funded status of the portion of the CSRS allocated to the Postal Service. OPM determined that, as a result of the changes imposed by P.L. 109-435, the Postal Service portion of the CSRS had a surplus of $17.1 billion as of September 30, 2006. Accordingly, the "supplemental liability" payment previously required by P.L. 108-18 was suspended and no amount was incurred or paid in 2008 or 2007.

The "supplemental liability" payments were suspended until 2017 by P.L. 109-435. At that time, OPM will perform an actuarial valuation and determine whether additional "supplemental liability" payments are necessary.

Note 11 – Workers' compensation

We pay for workers' compensation costs under a program administered by DOL. These costs, recorded as an operating expense, include employees' medical expenses, compensation for wage loss, and DOL administrative fees. The program also provides for payment of benefits to dependents of employees who die from work-related injuries or diseases.

Our liability at September 30, 2008, represents the estimated present value of the total amount we expect to pay in the future for postal workers injured through the end of 2008. The estimated total cost of a claim is based upon the date of injury, pattern of historical payments, frequency and severity of the injuries, and the expected trend in future costs.

We estimated our total liability for future workers' compensation costs to be $7,968 million at the end of 2008 and $7,771 million at the end of 2007. The payout period for this liability will, for some claimants currently on the rolls, be for the rest of their lives.

The liability is sensitive to changes in inflation and discount rates. An increase of 1% in the assumptions would decrease our estimate of the liability by approximately $732 million. A decrease of 1% would increase our estimate of the liability by approximately $871 million.

We implemented a revised actuarial model to calculate our workers' compensation liability at September 30, 2008. The model's methodology is similar to that used in the independent consulting firm actuarial valuation, which formed the basis for the recorded liability in 2007. The revised model explicitly projects the estimated cost to resolve the most recent 10 injury years. We continue to rely on an independent actuarial consulting firm to perform an actuarial valuation on injuries occurring more than 10 years in the past.

Our model estimates the liability for the most recent 10 years using the paid loss development method, two frequency/severity methods, and an expected unpaid method. The paid loss development method estimates the liability based on the historical pattern of payments observed over many years. The frequency/severity methods estimate the liability by considering not only the cost, but the number of claims payments over many years. The frequency/severity methods require that we make explicit assumptions about the future changes in the average payment amounts due to inflation or other cost increases. The expected unpaid method estimates the liability by giving weight to both the expected development from the paid loss development method and the estimated ultimate value from the frequency/severity method. For injuries occurring more than 10 years in the past, an estimate of the ultimate liability is prepared by an independent actuary and incorporated into the new model. All of the methods used in calculating the 2008 and 2007 workers' compensation liability are generally accepted actuarial techniques and are each valid for estimating a liability such as ours.

We also annually review the inflation and discount rates used to determine the present value of estimated future workers' compensation payments. Separate analyses of the appropriate inflation rates for the medical and compensation portions of the liability were performed, utilizing forecasts of medical inflation and inflation in the general economy, and forecasted rates of return on baskets of Treasury securities of varying durations. During 2007, we validated our assumptions and methodology with an independent actuarial firm. Our assumptions used to calculate the liability in 2008 and 2007 are projected returns on investments for compensation claims of 5.6% and wage inflation of 3.0%. For medical claims, we used 5.4% for returns on investments and 5.0% for medical future inflation for both 2008 and 2007.

The workers compensation liability estimation technique used in 2006 and prior years utilized a net discount rate, which was the estimated difference between the expected return on investments in a basket of Treasury securities offset by the estimated inflation rate for medical costs and wages. The net discount rate in 2006 was 3.3% for compensation claims and -0.8% for medical claims. The estimation technique used by the independent actuarial consulting firm in 2007 and by our new model in 2008 uses separate calculations for returns on investment and inflation factors rather than a net discount rate. The combined reduction to our 2007 liability as a result of the changes in actuarial valuation technique, and the underlying assumptions of inflation and discount rates was $685 million. This is shown in the following table.

2007 Workers' Compensation Assumption Changes (Dollars in millions)	Old Assumptions	Current Assumptions	Net Reduction
Compensation Claims	$ 5,565	$ 5,272	$ 293
Medical Claims	2,820	2,428	392
Total Liability	**$ 8,385**	**$ 7,700**	**$ 685**

In 2008, the independent actuary changed their model calculating our liability related to injuries occurring more than 10 years in the past by increasing the length of the period of our past claim payment experience used as a basis to project future claim payments. This change decreased our liability for 2008 by approximately $154 million.

In 2008, we recorded $1,227 million in workers' compensation expense, compared to the $880 million in 2007 and $1,279 million recorded in 2006. The effect of the 2008 and 2007 changes discussed above are accounted for as changes in accounting estimate, as defined by GAAP.

In addition to the cost of workers' compensation claims, DOL charges us an administrative fee for processing claims. In 2008, the administrative fee, which is included in the expense above, was $52 million, compared to $49 million in 2007 and $45 million in 2006.

Note 12 – Revenue forgone

Our operating revenue includes accruals for revenue forgone. Revenue is forgone when Congress mandates that we provide mail services for designated mailers at free or reduced rates. Congress then appropriates money to reimburse us for the revenue that we have forgone in providing these services.

We estimate the amount of services that will be provided during a given year and forward a funding request to Congress. At the end of the year we reconcile this request with the actual usage. Depending upon whether actual usage is higher or lower than our estimate, we will request additional funding or return the excess funding via a reduction to our next revenue forgone funding request.

In 2008, we included $103 million of revenue forgone as operating revenue, $63 million in 2007 and $99 million in 2006. We record requested amounts as government receivables until the appropriations are received.

The Revenue Forgone Reform Act of 1993 authorized Congress to make 42 annual payments of $29 million each, beginning in 1994 and continuing through 2035. These payments are reimbursement for two purposes: services we performed in 1991, 1992, and 1993 for which we have not yet been fully paid; and for shortfalls in the reimbursement for the costs we incurred for processing and delivering certain Nonprofit mail entitled to statutorily reduced costs from 1994 through 1998.

The future payments authorized by the Revenue Forgone Reform Act of 1993 totaled $1,218 million for which we calculated the present value, at 7% interest, to be approximately $390 million. We recognized the $390 million as revenue during fiscal years 1991 through 1998. The discounted present value of the remaining future payments as of the years ended September 30 was $349 million in 2008 and $353 million in 2007.

The total receivable for revenue forgone as of the years ended September 30 was $495 million in 2008 and $476 million in 2007.

Operating Statistics

Category of Service	2008	2007	2006	2005	2004
(In millions of units indicated, unaudited)					
Mailing Services					
First-Class Mail					
Revenue	$ 38,179.3	$ 38,404.5	$ 37,604.9	$ 36,802.7	$ 37,109.8
Pieces, Number	91,696.7	96,297.3	98,016.2	98,567.1	98,433.1
Weight, Pounds	4,165.1	4,401.4	4,418.1	4,448.3	4,467.1
Standard Mail					
Revenue	$ 20,586.3	$ 20,778.6	$ 19,876.5	$ 18,953.5	$ 18,122.5
Pieces, Number	99,084.2	103,516.1	102,459.6	100,943.9	95,565.1
Weight, Pounds	11,017.2	11,820.7	11,771.2	11,656.5	11,148.4
Periodicals					
Revenue	$ 2,294.9	$ 2,187.9	$ 2,215.2	$ 2,160.8	$ 2,191.8
Pieces, Number	8,605.2	8,795.8	9,022.5	9,070.0	9,135.3
Weight, Pounds	3,676.9	3,895.6	4,040.7	4,025.6	4,067.5
Package Services					
Revenue	$ 1,845.5	$ 1,812.3	$ 1,751.1	$ 1,646.5	$ 1,623.3
Pieces, Number	846.2	914.5	918.8	885.0	860.8
Weight, Pounds	2,155.3	2,297.5	2,323.2	2,294.4	2,233.0
U.S. Postal Service					
Pieces, Number	823.7	1,008.4	1,010.1	621.3	529.3
Weight, Pounds	148.9	140.6	128.1	110.7	105.4
Free Matter for the Blind					
Pieces, Number	72.0	72.0	74.2	76.4	71.1
Weight, Pounds	33.3	33.6	35.4	34.4	34.6
Mailgrams					
Revenue	$ -	$ -	$ -	$ 0.8	$ 0.7
Pieces, Number	-	-	-	1.9	1.6
Total Mailing Services Mail					
Revenue	$ 62,906.0	$ 63,183.3	$ 61,447.7	$ 59,563.5	$ 59,047.4
Pieces, Number	201,128.0	210,604.1	211,501.4	210,163.7	204,594.7
Weight, Pounds	21,196.7	22,589.4	22,716.7	22,569.9	22,056.0
Ancillary & Special Services					
Registered Mail					
Revenue	$ 56.9	$ 53.3	$ 72.8	$ 77.2	$ 75.0
Number of articles	3.9	4.3	7.1	7.7	7.4
Certified Mail					
Revenue	$ 717.8	$ 698.2	$ 631.6	$ 600.6	$ 629.5
Number of articles	268.9	280.2	265.7	261.1	273.7
Insurance					
Revenue	$ 144.6	$ 156.7	$ 136.7	$ 132.2	$ 127.8
Number of articles	51.6	57.0	52.8	53.6	53.2
Delivery Receipt Services					
Revenue	$ 704.6	$ 639.7	$ 619.9	$ 577.5	$ 548.4
Number of articles	1,192.2	1,098.3	1,020.3	954.7	841.9
Money Orders					
Revenue	$ 204.8	$ 210.5	$ 191.2	$ 205.9	$ 228.0
Face value of issues (non-add)	$ 25,709.3	$ 27,194.0	$ 28,277.4	$ 28,723.0	$ 28,782.2
Number of articles	149.1	162.9	176.2	180.4	187.2
Box Rent Revenue	$ 896.7	$ 836.9	$ 813.7	$ 791.5	$ 779.9
Stamped Envelope and Card Revenue	$ 24.4	$ 16.9	$ 25.2	$ 21.0	$ 21.9
Other Mailing Services Revenue	$ 894.5	$ 1,108.2	$ 1,224.0	$ 823.6	$ 689.3
Total Ancillary & Special Services Revenue	$ 3,644.3	$ 3,720.4	$ 3,715.1	$ 3,229.5	$ 3,099.8
Total Mailing Services Revenue	$ 66,550.3	$ 66,903.7	$ 65,162.8	$ 62,793.0	$ 62,147.2

Operating Statistics

Category of Service	2008	2007	2006	2005	2004
(In millions of units indicated, unaudited)					
Shipping Services					
Revenue	$ 8,355.0	$ 7,851.6	$ 7,461.1	$ 7,085.2	$ 6,821.3
Pieces, Number	1,574.9	1,629.9	1,636.3	1,579.0	1,510.9
Weight, Pounds	3,040.6	3,053.8	3,215.1	3,271.6	3,224.9
Shipping Services Ancillary & Special Services Revenue	$ 26.7	$ 22.8	$ 26.5	$ 29.2	$ 27.5
Total Shipping Services Revenue	$ 8,381.7	$ 7,874.4	$ 7,487.6	$ 7,114.4	$ 6,848.8
Postal Service Totals					
Revenue	$ 71,261.0	$ 71,034.9	$ 68,908.8	$ 66,648.7	$ 65,868.7
Pieces, Number	202,702.9	212,234.0	213,137.7	211,742.7	206,105.6
Weight, Pounds	24,237.3	25,643.2	25,931.8	25,841.5	25,280.9
Total Ancillary & Special Services Revenue	$ 3,671.0	$ 3,743.2	$ 3,741.6	$ 3,258.7	$ 3,127.3
Total Operating Revenue	$ 74,932.0	$ 74,778.1	$ 72,650.4	$ 69,907.4	$ 68,996.0

Note: The charts have been reformatted to reflect the new Mailing Services and Shipping Services categories. The following summarizes the major reclassification changes.

* The First-Class Mail category includes First-Class Mail International.
* Package Services includes single-piece Parcel Post, International Inbound Surface Parcel Post, Bound Printed Matter, Media Mail, and Library Mail, but now excludes Parcel Select and Parcel Return Service.
* Shipping Services includes Priority Mail, Express Mail, Destination-entry Parcel Post, Parcel Select Return Service, and International Mail, excluding single-piece First-Class International Mail.

Operating Statistics

	2008	2007	2006	2005	2004
(Actual numbers, unaudited)					
Career Employees					
Headquarters and HQ Related Employees					
Headquarters	2,892	2,856	2,761	2,654	2,708
Headquarters - Field Support Units *	4,429	4,527	4,402	4,333	3,396
Inspection Service - Field	2,890	2,991	3,130	3,443	3,648
Inspector General	1,159	1,147	1,071	843	782
Total HQ and HQ Related Employees	11,370	11,521	11,364	11,273	10,534
Field Employees					
Area Offices *	1,316	1,281	1,395	1,420	2,196
Postmasters / Installation Heads	25,250	25,285	25,429	25,322	25,519
Supervisors / Managers	31,787	32,635	33,201	33,234	33,635
Professional Administration and Technical Personnel	8,010	8,058	8,539	8,945	9,168
Clerks	194,773	204,145	213,920	221,644	226,183
Nurses	134	160	166	167	167
Mail Handlers	55,812	57,882	57,158	56,028	54,769
City Delivery Carriers	211,661	222,132	224,400	228,278	228,140
Motor Vehicle Operators	8,558	8,726	8,715	8,689	8,628
Rural Delivery Carriers - Full-Time	68,900	67,584	66,344	64,335	62,762
Building and Equipment Maintenance Personnel	40,248	39,948	39,986	39,893	40,263
Vehicle Maintenance Employees	5,419	5,405	5,521	5,488	5,521
Total Field Employees	651,868	673,241	684,774	693,443	696,951
Total Career Employees	663,238	684,762	696,138	704,716	707,485
Noncareer Employees					
Casuals	12,000	22,078	22,518	19,182	20,529
Nonbargaining Temporary	1,119	1,244	1,135	1,185	1,138
Rural Part-Time: Subs / RCA / RCR / AUX	58,072	60,444	59,087	57,411	56,403
Postmaster Relief and Leave Replacements	12,327	12,169	12,188	12,046	12,157
Transitional Employees	18,332	5,232	5,133	8,460	9,884
Total Noncareer Employees	101,850	101,167	100,061	98,284	100,111
Total Employees	765,088	785,929	796,199	803,000	807,596

* Beginning 2005, employees in the Sales organization were reported as Headquarters-related instead of in the area offices.

Operating Statistics

	2008	2007	2006	2005	2004
(In actual units indicated, unaudited)					
Post Offices, Stations, and Branches					
Post Offices	27,232	27,276	27,318	27,385	27,505
Classified Stations, Branches, and Carrier Annexes	5,509	5,419	5,557	5,622	5,623
Contract Postal Units	3,148	3,131	3,014	3,116	2,889
Community Post Offices	834	895	937	1,019	1,142
Total Offices, Stations, and Branches	36,723	36,721	36,826	37,142	37,159
Residential Delivery Points*					
City Delivery	79,848,415	79,470,894	78,949,153	78,524,242	77,967,046
Rural	37,684,158	37,022,488	36,068,838	34,958,986	33,817,615
PO Box	15,639,031	15,635,480	15,615,744	15,614,801	15,634,610
Highway Contract	2,516,783	2,473,323	2,345,255	2,243,520	2,162,772
Total Residential Delivery	135,688,387	134,602,185	132,978,990	131,341,549	129,582,043
Business Delivery Points*					
City Delivery	7,436,965	7,411,582	7,343,020	7,280,384	7,185,300
Rural	1,407,942	1,360,478	1,297,022	1,230,645	1,172,499
PO Box	4,587,454	4,548,973	4,490,102	4,412,559	4,321,862
Highway Contract	71,538	69,304	65,062	61,228	58,084
Total Business Delivery	13,503,899	13,390,337	13,195,206	12,984,816	12,737,745
Total Delivery Points	149,192,286	147,992,522	146,174,196	144,326,365	142,319,788
Change in Delivery Points	1,199,764	1,818,326	1,847,831	2,006,577	958,512

* The table above shows delivery growth of 958,512 in FY 2004. The absolute growth is 1,782,900 deliveries if FY 2003 were adjusted to reflect the current reporting procedure as implemented in FY 2004.

Financial History Summary

(Dollars in millions)	2008	2007	2006	2005	2004
Statements of Operations					
Total revenue	$ 74,968	$ 74,973	$ 72,817	$ 69,993	$ 69,029
Total expense **	77,774	80,115	71,917	68,548	65,964
Net (loss) income	**$ (2,806)**	**$ (5,142)**	**$ 900**	**$ 1,445**	**$ 3,065**
Operating revenue	$ 74,829	$ 74,715	$ 72,551	$ 69,798	$ 68,960
Revenue foregone	103	63	99	109	36
Total operating revenue	74,932	74,778	72,650	69,907	68,996
Compensation and benefits**	53,585	54,186	54,665	52,449	50,821
Retiree health benefits **	7,407	10,084	1,637	1,495	1,313
Other expenses	16,746	15,835	15,379	14,337	13,717
Total operating expenses **	77,738	80,105	71,681	68,281	65,851
Income from operations	(2,806)	(5,327)	969	1,626	3,145
Interest and investment income	36	195	167	86	33
Interest expense deferred retirement	-	-	(231)	(263)	(103)
Other interest expense	(36)	(10)	(5)	(4)	(10)
Net (loss) income	**$ (2,806)**	**$ (5,142)**	**$ 900**	**$ 1,445**	**$ 3,065**
Balance Sheets					
Current assets *	$ 2,354	$ 1,859	$ 2,041	$ 1,933	$ 1,851
Property, equipment, and other assets	23,632	23,988	26,447	23,065	22,858
Total assets	**$ 25,986**	**$ 25,847**	**$ 28,488**	**$ 24,998**	**$ 24,709**
Current liabilities *	$ 16,729	$ 13,804	$ 11,613	$ 9,160	$ 10,800
Other Liabilities *	10,929	10,909	10,599	10,462	9,978
(Deficit) Equity	(1,672)	1,134	6,276	5,376	3,931
Total liabilities and net capital	**$ 25,986**	**$ 25,847**	**$ 28,488**	**$ 24,998**	**$ 24,709**
Changes in Net Capital					
Capital contributions of the U.S. government	$ 3,034	$ 3,034	$ 3,034	$ 3,034	$ 3,034
(Deficit) Equity since 1971 reorganization	(1,900)	3,242	2,342	897	(2,168)
Total beginning balance	1,134	6,276	5,376	3,931	866
Net (loss) income	(2,806)	(5,142)	900	1,445	3,065
Ending balance	**$ (1,672)**	**$ 1,134**	**$ 6,276**	**$ 5,376**	**$ 3,931**

* Certain reclassifications have been made to previously reported amounts.

** The net impact of P.L.109-435 legislation was $6.8 billion of additional expense in 2007 ($8.4 billion in additional Retiree health benefits less $1.6 billion in CSRS savings).

Selected Quarterly Financial Data

2008		Quarter 1		Quarter 2		Quarter 3		Quarter 4
(Dollars in millions, unaudited)								
Operating revenue	$	20,369		18,916		17,910		17,737
Total operating expenses		19,683		19,622		19,015		19,418
Income (loss) from operations		686		(706)		(1,105)		(1,681)
Interest income (expense) - net		(14)		(1)		7		8
Net Income (loss)	**$**	**672**	**$**	**(707)**	**$**	**(1,098)**	**$**	**(1,673)**

2007		Quarter 1		Quarter 2		Quarter 3		Quarter 4
(Dollars in millions, unaudited)								
Operating revenue	$	19,637	$	18,277	$	18,347	$	18,517
Total operating expenses		22,656		19,577		18,837		19,035
(Loss) from operations		(3,019)		(1,300)		(490)		(518)
Interest income (expense) - net		48		61		37		39
Net (Loss)	**$**	**(2,971)**	**$**	**(1,239)**	**$**	**(453)**	**$**	**(479)**

***2006 quarterly data was not prepared using the same standards and principles of those used in 2007 and 2008. Therefore, it is not comparative to these years and would be misleading to include here.*

Glossary

Accruals. Revenue and expenses that are recorded as they occur, even though they may not have actually been paid.

Amortize. To reduce the value of an asset through regular charges to income over time; or to write off expenses by prorating them over a period of time.

Appropriation. Public funds set aside by Congress for a specific purpose.

Asset. An economic resource that is expected to be of benefit in the future.

Cautionary Statements. Statements contained in Management's Discussion and Analysis that represent our best estimate of the trends we know about, the trends we anticipate, and the trends we think are relevant to our future operations.

Capitalize. To treat an expenditure as an asset; or to compute the present value of a future payment that will be paid over a period of time.

Contribution. The difference between the revenue from a class of mail and that class's volume-variable costs. For example, if a class of mail has revenue of $1.5 billion and volume-variable costs of $1 billion, its contribution is $500 million, which means that this class of mail covers its costs and contributes $500 million to the common costs of all mail services.

Contingent Liability. A potential liability that is contingent on a future event.

Delivery Confirmation. A special service that provides the date of delivery or attempted delivery for Priority Mail and Standard Mail parcels, Bound Printed Matter, and Library Mail.

Depreciate. To periodically reduce the estimated value of an asset over the course of its useful life.

Direct Mail. A form of advertising often employed by businesses to reach targeted groups of potential customers by mail.

Enhanced Carrier Route. A subclass of Standard Mail for mail pieces weighing less than 16 ounces and prepared in carrier route sequence.

Equity. The difference between the value of all assets less all liabilities.

Express Mail. The Postal Service's premium delivery service, providing guaranteed overnight delivery for documents and packages weighing up to 70 pounds. Both domestic and international services are offered.

First-Class Mail. A class of mail including letters, postcards, and all matter sealed or otherwise closed against inspection. This service is required for personal correspondence, handwritten or typewritten letters, and bills or statements of account.

Fiscal Year. As used in the financial section of this report, the Postal Service fiscal year, which is the 12-month period during which the Postal Service keeps accounts, beginning Oct. 1 and closing Sept. 30.

Fixed Asset. Any tangible property such as buildings, machinery and equipment, furniture, and leasehold improvements.

Forever Stamp. A stamp that once purchased is good for mailing one-ounce First-Class letters anytime in the future — regardless of price changes. It was introduced in 2007.

Generally Accepted Accounting Principles (GAAP). The rules and procedures of accepted accounting practice as defined by the Financial Accounting Standards Board.

Impaired Asset. When the market value of an economic resource has been permanently lowered below the recorded value of the asset.

Inspector General. The Inspector General is appointed by and reports directly to the Governors of the Postal Service and is independent of postal management. The Office of Inspector General (OIG) primarily investigates and evaluates programs and operations of the Postal Service to ensure the efficiency and integrity of the postal system.

Intelligent Mail. Products and services or a strategy used to describe products and services that use machine readable codes, such as barcodes, to uniquely identify mail. This enables large mailers to follow the progress of their mail through the many stages of processing all the way to delivery.

Leasehold. An asset that gives the Postal Service the right to use property under a lease.

Liability. Any debt or obligation that is owed by the Postal Service at some future period of time.

Mailing Services. Market-dominated products as defined by the PRC. These are products for which the Postal Service has market power to set prices substantially above costs without risk of losing business to others. The Mailing Services products include: First-Class Mail letters and sealed parcels; First-Class Mail cards; Periodicals; Standard Mail; single-piece Parcel Post; Media Mail; Bound Printed Matter; Library Mail; Special Services; and single-piece International Mail.

Operating Expense. Expenses that are incurred in providing our primary business services and products.

Operating Margin. A financial indication calculated by dividing income from operations by operating revenue.

Glossary

Operating Revenue. Revenues that are earned from our primary business services and products.

OPM. Office of Personnel Management. The agency that manages and maintains the government retirement and health benefit plans.

Package Services. Mailing category offered for any merchandise or printed matter weighing up to 70 pounds. These services include Parcel Post, Bound Printed Matter, Library Mail, and Media Mail.

Payable. Money that is owed by the Postal Service.

Periodicals. A class of mail formerly called second-class mail that consists of magazines, newspapers, and other publications.

Postal Inspection Service. The investigative arm of the Postal Service responsible for investigating criminal acts involving the mail and misuse of the postal system.

Postal Regulatory Commission (PRC) (formerly the Postal Rate Commission). An independent federal establishment with oversight responsibility for the Postal Service to review and approve rates, review financial data, and hear and rule on rate and service complaints.

Prepaid. Payments made in advance of service being provided.

Present Value. The value today of a future payment that is discounted at a stated rate of compound interest. For example, the present value of $100 that will be paid to the Postal Service 10 years from now is about $38.55, if we discount that $100 at a rate equal to 10% interest compounded annually.

Priority Mail. Priority mail is a 1-3-day non-guaranteed delivery service.

Receivable. Money that is owed to the Postal Service.

Recognize. To record in Postal Service accounts as income or expense.

Repositionable Notes. Repositionable Notes are specially-designed and applied "Post-It" type notes that let mailers affix a message to the outside of the envelope, calling attention to the mailer's product or service to help the mailer get an extra edge. They are First-Class Mail and Standard Mail products.

Shipping Services. Products that are not Mailing Services and are considered competitive products. The competitive product list includes: Priority Mail; Expedited Mail; Bulk Parcel Post; and Bulk International Mail.

Special Services. A category of services that add value to mail by providing added security, proof of delivery or loss recovery. These services include: Certified Mail, Registered Mail, Delivery Confirmation, Signature Confirmation and insurance up to $1,000.

Standard Mail. Mailing service offered for any item, including advertisements and merchandise weighing less than 16 ounces that are not required to be sent using First-Class Mail. Standard Mail is typically used for bulk advertising to multiple delivery addresses.

U.S. Mail. Any mailable matter that is accepted for mail processing and delivery by the Postal Service.

Universal Service. The Postal Service's mandate and commitment to the nation to provide mail delivery service at uniform and reasonable rates to everyone, everywhere.

Workshare. Tasks performed by mailers that otherwise would be done by the Postal Service, such as, preparing, sorting, barcoding, and transporting mail. Reduced postage rates are offered to these customers.

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/ John E. Potter

John E. Potter
Postmaster General and Chief Executive Officer

Date: November 25th, 2008

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 Postal Service and in the capacities indicated as of November 14, 2008.

Signature	**Title**
/s/ Alan C. Kessler Alan C. Kessler	Chairman of the Board of Governors
/s/ Carolyn Lewis Gallagher Carolyn Lewis Gallagher	Vice Chairman of the Board of Governors
/s/ Mickey D. Barnett Mickey D. Barnett	Governor
/s/ James H. Bilbray James H. Bilbray	Governor
/s/ Louis J. Giuliano Louis J. Giuliano	Governor

/s/ Thurgood Marshall, Jr. Thurgood Marshall, Jr.	Governor
/s/ James C. Miller III James C. Miller III	Governor
/s/ Katherine C. Tobin Katherine C. Tobin	Governor
/s/ Ellen C. Williams Ellen C. Williams	Governor
/s/ John E. Potter John E. Potter	Board Member, Postmaster General and Chief Executive Officer
/s/ Patrick R. Donahoe Patrick R. Donahoe	Board Member, Deputy Postmaster General and Chief Operating Officer
/s/ H. Glen Walker H. Glen Walker	Chief Financial Officer and Executive Vice President

EMPLOYMENT AGREEMENT

EMPLOYMENT AGREEMENT (the "Agreement") by and between the United States Postal Service (the "Postal Service") and John E. Potter ("Mr. Potter").

WHEREAS, Mr. Potter has been appointed Postmaster General by the Governors of the United States Postal Service (the "Governors"), pursuant to their authority under 39 U.S.C. § 202(c); and

WHEREAS, Mr. Potter has been employed by the Postal Service as its Postmaster General prior to the Effective Date, pursuant to employment agreements effective June 1, 2001 and June 1, 2004, including amendments dated January 10, 2006 and May 18, 2006; and

WHEREAS, the Postal Service and Mr. Potter desire to continue Mr. Potter's employment and to enter into this agreement, effective August 8, 2007, (the "Effective Date"), embodying the terms that the Governors have fixed, pursuant to their authority under 39 U.S.C. § 202(c), and in compliance with Internal Revenue Code § 409A, for Mr. Potter's continued employment as Postmaster General;

NOW, THEREFORE, in consideration of the mutual covenants and agreements contained herein, and other good and valuable consideration, the receipt and sufficiency of which is hereby acknowledged, the parties agree as follows:

1. Position. Pursuant to the direction of the Governors and subject to their authority, Mr. Potter shall serve as Postmaster General, as set forth in 39 U.S.C. § 203, with all of the authority, responsibilities, and duties prescribed for that position by statute, regulation, and the Governors.

2. Duties. Mr. Potter agrees to perform the duties and responsibilities of Postmaster General to the best of his ability, in accordance with all statutes, regulations, policies, practices, procedures, and rules applicable to Postal Service employees and officers, including Part 660 of the Employee and Labor Relations Manual ("ELM") governing employee conduct, the Standards of Ethical Conduct for Employees of the Executive Branch, and Chapter 11 of Title 18, U.S. Code, governing conflicts of interest, and including any successors to those statutes, regulations, policies, practices, procedures, and rules. Mr. Potter shall be entitled to a review of his performance at the end of each fiscal year of the Postal Service; however, nothing in this Agreement shall preclude the Governors from reviewing Mr. Potter's performance at other times, in accordance with their authority under 39 U.S.C. § 202(c).

3. Devotion to Postal Service and Confidentiality. During his employment as Postmaster General, Mr. Potter agrees to devote his full time and attention exclusively to the business and affairs of the Postal Service. During his employment as Postmaster General, Mr. Potter further agrees to hold in trust and confidence all information obtained directly and indirectly through his Postal Service employment, and to disclose and use such information only in connection with and to the extent

necessary for accomplishing the work required by this Agreement. Mr. Potter further agrees that he will not take personal advantage of any business opportunities that might benefit the Postal Service which arise during his employment as Postmaster General.

4. Term. The term of Mr. Potter's appointment as Postmaster General shall be indefinite. This Agreement does not constitute a guarantee of continued employment but instead provides for certain rights and benefits for Mr. Potter during his employment, and in the event his employment with the Postal Service terminates.

5. Salary. During his employment as Postmaster General, the Postal Service shall pay Mr. Potter an annual salary equal to 120 percent of the salary payable to the Vice President of the United States of America (the "Vice President") under Section 104 of Title 3, U.S. Code. Based on this computation, Mr. Potter's salary shall be $258,840 as of January 1, 2007. Mr. Potter's salary as determined under this Paragraph 5 shall be adjusted as changes are made to the rate of pay for the Vice President. Mr. Potter's salary shall be payable in equal biweekly installments, subject to appropriate deductions for federal, state, local and other taxes required by law, retirement, life insurance premiums, health insurance, and other usual and ordinary deductions.

6. Leave. As of August 4, 2007, Mr. Potter shall be eligible for all leave and benefits provided to officers of the Postal Service, including any improvements in such leave and benefits that may occur. Any annual leave earned prior to August 4, 2007, shall be unaffected by this agreement.

7. Physical Examination. Mr. Potter shall receive (or be reimbursed by the Postal Service for) an annual physical examination of the type provided to other officers of the Postal Service, provided that during such period of employment, the physical examination shall be performed annually, regardless of the frequency of such examination for other officers.

8. Intellectual Property. All professional publication, documents, and other intellectual property rights evolving from Mr. Potter's work for the Postal Service shall be the sole property of the Postal Service. Mr. Potter agrees to make, execute, and deliver to the Postal Service any and all papers or other instruments on such terms and conditions as may be required for filing of any instrument necessary for preserving an intellectual property right and does hereby assign and transfer to the Postal Service the entire right, title, and interest in and to said intellectual property right.

9. Cause. For purposes of this Agreement, "Cause" shall mean (i) the material breach by Mr. Potter of his duties and responsibilities; (ii) the commission of an act of dishonesty by Mr. Potter relating to Mr. Potter's duties and responsibilities which may or does cause harm to the Postal Service; (iii) the commission by Mr. Potter of an act of moral turpitude which may or does cause harm to the Postal Service; (iv) a material violation by Mr. Potter of the Standards of Ethical Conduct as set forth in 5 CFR Part 2635, 39 CFR Part 447, and Subchapter 660 of the Employee and Labor Relations Manual, or successors thereto; or (v) a personal and material violation by

Mr. Potter of the employment anti-discrimination laws. Nothing in this Agreement shall be construed to limit or waive the Governors' authority to remove the Postmaster General for any reason, including but not limited to removal for Cause. If Mr. Potter's employment with the Postal Service terminates for any reason, the Postal Service shall have no further obligation to employ Mr. Potter in any capacity, and shall have no other obligation to Mr. Potter, other than to provide the compensation and benefits required by this Agreement.

10. Termination. Mr. Potter shall have the right to terminate his employment hereunder thirty (30) days after providing the Governors with written notice of his intent to do so. Mr. Potter will be deemed to have incurred a "separation from service" with the Postal Service for purposes of Internal Revenue Code Section 409A upon his termination of employment with the Postal Service, if the facts and circumstances indicate that Mr. Potter and the Postal Service reasonably believed Mr. Potter would perform no further services for the Postal Service after his termination date, or reasonably believed that the level of services Mr. Potter would perform for the Postal Service after such date (either as an employee or as an independent contractor) would permanently decrease below the default levels set forth in the regulations issued by the Secretary of the Treasury under Internal Revenue Code Section 409A.

   (a) Employee Benefit Plans. Upon Mr. Potter's termination of employment with the Postal Service for any reason, he shall be entitled to the payments or benefits provided pursuant to any employee benefit plans or arrangements of the Postal Service covering Mr. Potter, to the extent that such amounts are otherwise due to him in accordance with the terms of those plans and arrangements. Except as may otherwise be expressly provided to the contrary in this Agreement, nothing in this Agreement shall be construed as requiring Mr. Potter to be treated as employed by the Postal Service for purposes of any employee benefit plan or arrangement following the date of his termination of employment by the Postal Service.

   (b) Outplacement Assistance. If Mr. Potter's employment with the Postal Service is terminated for any reason other than Cause, Mr. Potter will be provided, at Postal Service expense, with reasonable outplacement assistance by a provider selected by the Postal Service. Outplacement assistance will continue for a period not to exceed two years from the date of Mr. Potter's separation from service.

   (c) Supplementary Severance Payment. If Mr. Potter's employment with the Postal Service terminates for reasons other than death or Cause, then, during the Severance Period (as defined below) or, if earlier, until the time of his death, he shall be entitled to a monthly payment (the "Supplementary Severance Payment") in an amount equal to $1/12^{th}$ of the amount which, when added to any monthly CSRS benefits and monthly USPS Pension Benefit otherwise due to Mr. Potter for that month, will equal $1/12^{th}$ of his annual salary rate at the date of his termination of employment with the Postal Service. The term "Severance Period" shall mean the period beginning on the date of Mr. Potter's termination of employment and ending on the one-year anniversary of his date of termination.

(d) Medical, Life, and Disability Insurance. If Mr. Potter's employment with the Postal Service terminates for reasons other than Cause, then, for the Severance Period, he shall be entitled to receive the medical, life, and disability insurance coverage in effect on the date of his termination of employment, subject to such changes made in any such program as they apply to the active officers of the Postal Service, and subject to Mr. Potter making the contributions required from active officers of the Postal Service from time to time for such coverage.

(e) Disability Income Replacement Benefits. If, for any calendar month following Mr. Potter's termination of employment with the Postal Service, he is entitled to disability income replacement benefits under any disability arrangement provided by the Postal Service, payments under such arrangement for any such month shall reduce, on a dollar-for-dollar basis (but not below zero), the amount of the USPS Pension Benefit or the Supplementary Severance Payment, if any, otherwise due to Mr. Potter for that month.

11. USPS Pension Benefit. If Mr. Potter's employment with the Postal Service terminates after January 1, 2007, for any reason other than death or any action that precludes the receipt of an annuity under the Civil Service Retirement System ("CSRS"), he will be entitled to a monthly payment (the "USPS Pension Benefit") commencing for the calendar month following the month in which his termination of employment occurs and continuing thereafter for life. The USPS Pension Benefit shall be set at an amount that produces, as of the first day of the calendar month following the month in which Mr. Potter's employment terminates, a net present value ("NPV") of $1,350,318.00, which equals the NPV of the USPS Pension Benefit to which Mr. Potter would have been entitled under the former Employment Agreements had his employment with the Postal Service terminated on December 31, 2006. The USPS Pension Benefit shall be calculated using the same actuarial assumptions (mortality, discount, and cost-of-living) that were employed by the Office of Personnel Management ("OPM") on December 31, 2006 to determine the present value of benefits paid under CSRS as of that date, without taking into account the value of any survivor annuity that may become payable to Mr. Potter's spouse under paragraph (a) below.

(a) Form of Payment. The USPS Pension Benefit shall be payable in the form of a monthly annuity payable for the life of Mr. Potter, computed as discussed in Paragraph 11, above, with a survivor annuity payable for the life of Mr. Potter's spouse at the time of his death in an amount equal to 55 percent of the amount payable during the life of Mr. Potter. No survivor annuity shall be payable if Mr. Potter is not married at his date of death. If Mr. Potter is married at the beginning of any month after his retirement, then his annuity for that month will be reduced by 10 percent. If Mr. Potter is not married at the beginning of any month after his retirement then his annuity for that month will not be reduced by 10 percent.

(b) Cost-of-Living Adjustment. The monthly annuity payable to Mr. Potter or his surviving spouse under this Paragraph shall be subject to the same cost-of-living adjustment(s) that may apply to Mr. Potter's pension benefits under CSRS, as determined by OPM in accordance with the rules of the CSRS.

12. Pre-Retirement Surviving Spouse Benefit. If Mr. Potter is employed by the Postal Service at the time of his death, then his spouse at the time of his death (his "surviving spouse"), if any, shall be entitled to a Pre-Retirement Surviving Spouse Benefit commencing for the calendar month following the month in which Mr. Potter's death occurs and continuing thereafter for his surviving spouse's life only. The "Pre-Retirement Surviving Spouse Benefit" shall equal the full value of the USPS Pension Benefit Mr. Potter would have received under paragraph 11 of the Employment Agreement.

13. Incentive Compensation Payment.

(a) Generally. On termination of employment for reasons other than Cause, there shall be added to the amount payable pursuant to paragraph 14 of this Agreement (Deferred Compensation) to Mr. Potter (or, in the event of his death, his estate or heirs) an "Incentive Compensation Payment" equal to the sum of the Earned Incentive Amounts set forth below for each fiscal year in which the performance objectives established by the Governors for that year have been achieved. The Governors shall establish such performance objectives in their sole discretion after consultation with Mr. Potter. The "Earned Incentive Amount" for each fiscal year shall be the specified percentage set forth in the table below multiplied by Mr. Potter's annual base salary rate as of the end of the respective fiscal year.

For performance for each of the fiscal years ending in each of the following calendar years:	The percentage earned for that year upon achievement of the performance objectives shall be:
2007	21%
2008	24%
2009	27%
2010	30%

Mr. Potter shall be eligible to receive, in addition to the Earned Incentive Amounts set forth in the table above for the years 2007 through 2010, an additional Earned Incentive Amount that shall be payable only for superior performance, as determined by the Governors in their sole discretion after consultation with Mr. Potter. The additional Earned Incentive Amount for superior performance for each fiscal year shall be the specified percentage set forth in the table below multiplied by Mr. Potter's annual salary rate as of the end of the respective fiscal year.

For superior performance for each of the fiscal years ending in each of the following calendar years:	The additional percentage earned for that year upon achievement of the performance objectives for superior performance shall be:
2007	40%
2008	40%
2009	40%
2010	60%

If Mr. Potter's separation from service or death occurs prior to the end of the Postal Service's fiscal year, the Earned Incentive Amount, if any, which Mr. Potter, his spouse or beneficiaries, as appropriate, may receive for that fiscal year shall be computed as if Mr. Potter had served during the entire fiscal year. All payments due to Mr. Potter, his spouse or beneficiaries, as appropriate, pursuant to paragraph 13(a) of this Agreement shall be made in the manner specified in paragraph 14 of this agreement (Deferred Compensation).

(b) Payment of Additional Bonus. The Incentive Compensation Payment program provided for in paragraph 13(a) shall not limit Mr. Potter's ability to participate in the Pay for Performance program or any other performance award or individual award program available to officers of the Postal Service. Further, if Mr. Potter's separation from service or death occurs prior to the end of the Postal Service's fiscal year, then notwithstanding the terms of the Pay for Performance program to the contrary, Mr. Potter, his spouse or beneficiaries, as appropriate, shall be eligible to receive an additional bonus payment under this Agreement, as determined by the Governors in their sole discretion. Such bonus payment, if any, shall be calculated pursuant to the terms of the Pay for Performance program for such fiscal year, and computed as if Mr. Potter had served during the entire fiscal year. All payments due to Mr. Potter, his spouse or beneficiaries, as appropriate, pursuant to paragraph 13(b) of this Agreement shall be made in the manner specified in paragraph 14 of this agreement (Deferred Compensation).

14. Deferred Compensation. Incentive Compensation Payments and any additional bonus payable pursuant to paragraphs 13(a) and 13(b) above, and cash compensation otherwise payable to Mr. Potter by the Postal Service while he is employed by the Postal Service, including but not limited to, and from performance awards, individual awards, and Economic Value Added amounts (and excluding terminal leave), which is deferred during Mr. Potter's employment with the Postal Service ("Deferred Compensation"),

shall be payable beginning in the tax year following the tax year in which Mr. Potter undergoes a separation from service with the Postal Service. Deferred Compensation shall be subject to the following:

(a) Form of Payment. The Deferred Compensation shall be paid in the form of ten guaranteed equal annual payments, which shall be actuarially equivalent to the cash value of the Deferred Compensation as a lump sum. If Mr. Potter should die before any or all payments are made, the remaining Deferred Compensation payment shall be made to his surviving spouse if she is living, otherwise to his named beneficiary(ies), otherwise in accordance with the order of precedence used by OPM for CSRS lump sum payments. No further payments under this subparagraph (a) shall be made after the ten annual payments have been made to Mr. Potter or his surviving spouse or beneficiary(ies).

(b) Unforeseen Emergency. Notwithstanding subparagraph (a) above, after Mr. Potter's separation from service with the Postal Service within the meaning of Section 409A of the Internal Revenue Code, as amended, and Treasury regulations thereunder ("section 409A"), Mr. Potter shall be permitted to receive a lump sum payment of his Deferred Compensation in the event of an unforeseeable emergency with respect to Mr. Potter, as such term is defined in Section 409A (an "Unforeseeable Emergency"). The Governors shall make all determinations required under Section 409A with respect to an Unforeseeable Emergency. For informational purposes, an Unforeseeable Emergency generally means a severe financial hardship arising from illness, loss or destruction of property, or certain other events, but the definition of Unforeseeable Emergency for purposes of the Agreement shall be as provided in Section 409A.

15. Actuarial Equivalence. For purposes of this Agreement, actuarial equivalence shall be determined using the same actuarial assumptions (mortality, discount, and cost-of-living) that were employed by OPM on December 31, 2006, to determine the present value of benefits paid under CSRS. The discount rate shall be determined using the same rate as used by OPM for determining CSRS funding.

16. Waiver. Any waiver or any breach of this contract shall not be construed to be a continuous waiver or consent to any subsequent breach on the part of either party.

17. Notices. Any notice by Mr. Potter required or permitted hereunder shall be sent by registered or certified mail, addressed to the Chairman of the Board of Governors, 475 L'Enfant Plaza, SW, Room 1813, Washington, DC 20260-1000. Any notice by the Governors required or permitted hereunder shall be sent by registered or certified mail, addressed to Mr. Potter at his home address of record.

18. Assistance with Claims. Mr. Potter agrees that both during and after his employment he shall, at the request of the Postal Service, render all reasonable

assistance and perform all lawful acts that the Postal Service considers necessary or advisable, including but not limited to any litigation or threatened litigation or proceeding involving the Governors, the Postal Service, Mr. Potter, or any officer, employee, or agent of the Postal Service. Mr. Potter shall receive reasonable reimbursement for expenses incurred in performing this assistance.

19. Amendment. This Agreement may be amended or modified upon the written agreement of the parties. No amendment or modification of this Agreement shall be valid or effective unless in writing and executed by the parties to this Agreement.

20. Section 409A Compliance. All references in this Agreement to Mr. Potter's "termination of employment" with the Postal Service, or words of similar meaning, as a condition for the payment of any form of deferred compensation, shall be deemed to be references to Mr. Potter's "separation from service" with the Postal Service within the meaning of Section 409A of the Internal Revenue Code and applying the default rules thereof.

21. Entire Agreement. This Agreement embodies the entire agreement of the parties hereto with respect to its subject matter and merges with and supersedes all prior discussion, agreement, commitments or understanding of every kind and nature relating thereto, whether oral or written, between Mr. Potter and the Governors or between Mr. Potter and the Postal Service. Neither party shall be bound by any term or condition other than as is expressly set forth herein. However, except as otherwise provided in this Agreement, the obligations of the Postal Service and Mr. Potter with respect to compensation and benefits that were paid or distributed prior to the Effective Date shall be governed by the Prior Agreements and Amendments.

22. Representation. Mr. Potter represents and agrees that he has carefully read and fully understands all of the provisions of this Agreement, that he is competent to execute this Agreement, that his decision to execute this Agreement has not been obtained by any duress, that he freely and voluntarily enters into this Agreement, and that he has read this document in its entirety and fully understands the meaning, intent and consequences of this Agreement.

EXECUTED this 8th day of August, 2007.

John E. Potter

JOHN E. POTTER
Postmaster General

JAMES C. MILLER III
Chairman, Board of Governors

AMENDMENT TO THE EMPLOYMENT AGREEMENT
BETWEEN JOHN E. POTTER AND THE UNITED STATES POSTAL SERVICE

WHEREAS, John E. Potter ("Mr. Potter") has been appointed Postmaster General by the Governors of the United States Postal Service (the "Governors"), pursuant to their authority under 39 U.S.C. § 202(c); and

WHEREAS, the United States Postal Service (the "Postal Service") and Mr. Potter have entered into an employment agreement effective August 8, 2007 (the "Employment Agreement"), and

WHEREAS, amendment of the Employment Agreement is necessary as a result of the Postal Service's worsening economic condition, and through no fault on the part of Mr. Potter;

NOW, THEREFORE, in consideration of the agreements contained herein, and in consideration of Mr. Potter's continued employment as the Postmaster General of the United States, the Postal Service and Mr. Potter agree that the Employment Agreement shall be amended, effective January 1, 2009, as set forth herein.

Salary. For the period of January 1, 2009 through December 31, 2009, Mr. Potter's salary during his employment as Postmaster General shall be $265,320, which is his annual salary on the date he signs this agreement. Mr. Potter's salary shall be payable in equal biweekly installments, subject to appropriate deductions for federal, state, local and other taxes required by law, retirement, life insurance premiums, health insurance, and other usual and ordinary deductions.

EXECUTED this 25th day of November, 2008.

John E. Potter
JOHN E. POTTER
Postmaster General

ALAN C. KESSLER
Chairman, Board of Governors

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, John E. Potter, 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-15e and 15d-15e) 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. 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

   c. Disclosed in this report any change in the Postal Service's internal control over financial reporting that occurred during the Postal Service's most recent fiscal quarter (the Postal Service's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the Postal Service's internal control over financial reporting; and

5. The Postal Service's other certifying officer and I have disclosed based on our most recent evaluation of internal control over financial reporting, to the Postal Service's auditors and the audit committee of the Postal Service's Board of Governors (or persons performing the equivalent functions):

   a. All significant deficiencies and material weaknesses in the design or operation of internal controls 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 25th, 2008

/s/ John E. Potter
John E. Potter
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, H. Glen Walker, 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-15e and 15d-15e) 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. 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

   c. Disclosed in this report any change in the Postal Service's internal control over financial reporting that occurred during the Postal Service's most recent fiscal quarter (the Postal Service's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the Postal Service's internal control over financial reporting; and

5. The Postal Service's other certifying officer and I have disclosed based on our most recent evaluation of internal control over financial reporting, to the Postal Service's auditors and the audit committee of the Postal Service's Board of Governors (or persons performing the equivalent functions):

   a. All significant deficiencies and material weaknesses in the design or operation of internal controls 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 25th, 2008

/s/ H. Glen Walker
H. Glen Walker
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, 2008, (the "Report"), I, John E. Potter, 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 25th, 2008

/s/ John E. Potter
John E. Potter
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, 2008 (the "Report"),
I, H. Glen Walker, 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 25th, 2008

/s/ H. Glen Walker
H. Glen Walker
Chief Financial Officer and Executive Vice President