

STATEMENT

of

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before the

THE COMMITTEE ON OVERSIGHT AND GOVERNMENT REFORM
UNITED STATES HOUSE OF REPRESENTATIVES

on

CONTINUING TO DELIVER: AN EXAMINATION OF THE POSTAL SERVICE'S
CURRENT FINANCIAL CRISIS AND ITS FUTURE VIABILITY

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Chairman Towns, Ranking Member Issa, Chairman Lynch, Ranking Member Chaffetz, and Members of the Committee, I am pleased to be here today on behalf of Director John Berry of the Office of Personnel Management (OPM) to discuss "Continuing to Deliver: An Examination of the Postal Service's Current Financial Crisis and Its Future Viability".

OPM commends Chairman Towns and the Committee's efforts to review retirement obligations and other associated matters relating to the financial viability of the United States Postal Service (Postal Service). In particular, OPM appreciates the opportunity to explain the basis for its position in relation to the recent report by the Postal Service's Inspector General.

I would first emphasize that nothing discussed today will affect OPM's ability to deliver annuity payments under the Civil Service Retirement System (CSRS) and retiree health benefits coverage to individuals who have retired from the Postal Service. Postal retirees should have full confidence that they will continue to receive the retirement and health benefits they have earned based upon the valuable services they have performed for our nation.

Before delving into specific details, I would like to note that the issue before us involves questions of public and accounting policy that comes down to the proper allocation of certain pension costs between the Federal Government and the Postal Service, as discussed in more detail below. Notwithstanding the highly technical discussion that we will have today, there is no single "correct answer" in this area. There is more than one reasonable approach that could be used to address this situation. The methodology that OPM has been using since 1974 has been approved by Congress, with the advice of the Government Accountability Office (GAO), conforms with generally accepted actuarial

practices and principles, as required by title 5, United States Code, and is a common actuarial practice used in the private sector. OPM also believes that it produces a fair and equitable allocation of the responsibilities regarding the payment of pensions to certain Postal employees.

The core issue is a single question: How do we determine the Federal Government's fair share of the costs under CSRS for service performed for the Post Office Department (POD) prior to the 1971 establishment of the Postal Service? Congress first spoke to this issue in 1974, when it established the policy whereby increases in the retirement value of pre-1971 Postal employment due to increases in Postal salaries (essentially the sole basis for the increases in value) should be paid for by the Postal Service. This is the policy that OPM has followed ever since in making its calculations.

The Postal Service supported enactment of this policy in 1974 and made no objection to it for almost 30 years until 2003, when it sought a new approach that would reduce its obligations. At that time, the Postal Service proposed that the obligations for pre-1971 service be calculated on the basis of a simple years-of-service approach. Other than one technical flaw¹, this is not an inconceivable approach. While it may be worthy of future consideration by the Congress, OPM believes that it is not possible based upon current legislation.

Background

In 1971, the former POD was converted to the Postal Service, an independent entity. Not long thereafter, Congress carefully considered the issue of who should be responsible for the increases in retirement obligations for pre-1971 POD service and attributable to increases in Postal pay, culminating in the enactment of Public Law 93-349 (1974).

The legislative history of P.L. 93-349 explained the public policy adopted by the Congress. The report of the Senate Committee on Post Office and Civil Service discussed both the policy and specifics of the bill:

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"This legislation will resolve the question of who is to be responsible for increases in the unfunded liability of the Civil Service Retirement and Disability Fund which are attributable to new retirement benefits or pay increases granted to Postal employees.

"Under the provisions of H.R. 29, the Postal Service will be required to make payments for that portion of any future increase in the unfunded liability of the Civil Service Retirement Fund which results from an employee-management agreement under title 39, United States Code, or any administrative action taken by the Postal Service pursuant to law, which authorizes (1) new or liberalized

¹ As proposed, this new methodology fails to recognize that annuities accrue more slowly during the first ten years of service.

benefits payable from the Fund (other than cost-of-living increases), (2) extension of the coverage of retirement law, or (3) increases in pay upon which benefits are computed." [S.Rep. No. 93-947, at 3-4 (1974)]

The Postal Service supported the concept of the bill. Reprinted in the Committee Report is a March 27, 1973, letter from the Postal Service stating its position:

"This legislation has been proposed on the ground that the Postal Service should operate on a financially self-sufficient basis, meeting its operating costs out of its revenues and not out of hidden subsidies. After careful consideration—and in full awareness of the financial burdens enactment of the bill will impose—the Postal Service has concluded that it is proper, as a matter of principle, for these costs to be imposed on postal ratepayers rather than the taxpayers." [S.Rep. No. 93-947, at 9 (1974)]

Thereafter, Congress enacted a number of laws dealing with other aspects of Postal CSRS funding, including legislation making the Postal Service responsible for funding the cost of cost-of-living-increases (COLAs) applicable to Postal annuities. More than one of these bills included requirements that the Postal Service make payments under schedules set by Congress.

During the period from 1974 through 2002, it was generally assumed that the various Postal payments approximated slightly less than full funding of Postal CSRS obligations. However, this was inaccurate. As noted in the Senate Report on the bill that became P. L. 108-18, *the Postal Civil Service Retirement Systems Funding Reform Act of 2003*:

"On November 1, 2002, the Office of Personnel Management (OPM) had good news for the Postal Service (USPS). A review of USPS payments to the civil service retirement fund for pension obligations to employees on board before 1984 revealed a far more positive picture than had previously been believed. USPS--unlike any other federal agency--is required to pay into the fund an amount that approximates the full cost of its employees' participation in the Civil Service Retirement System (CSRS). Because pension investments have been earning interest at a higher rate than presumed in the statutory funding formula, OPM reported that the Postal Service's deferred liability for pension obligations was only \$5 billion instead of \$32 billion. According to OPM, if USPS continues to make payments based on the latter figure, the liability will eventually be over-funded by \$78 billion. OPM stated that, 'the major reason for the projected over-funding is due to the excess interest earned by the CSRS fund; that is, interest earnings in excess of the 5 percent that was assumed under the statutory funding method.'

"Because of the potential over-funding, and the fact that needed changes in scheduled payments cannot occur without changes to existing laws, OPM sent a legislative proposal to Congress to rectify the situation, while 'protecting

employee interests and the integrity of the [postal] retirement system." [S.Rep No. 108-35, at 2-3 (2003)]

That OPM proposal was enacted, with minor technical changes, as section 2 of the new law. In essence, it converted the funding of Postal benefits under CSRS to the same funding mechanism that is applicable to the Federal Employees' Retirement System. There has been confusion in some quarters as to the intent of Congress with regard to the effect of this change upon the Postal Service's obligations for cost increases due to increases in pay, but that matter is clarified by the Committee Report:

"Because the dynamic normal cost of CSRS includes the effects of future employee pay raises and retiree COLAs, the separate payments that USPS is required to make under current law to fund the future increases in CSRS annuities that result from pay raises and COLAs would no longer be necessary. Consequently, S. 380 would repeal the provisions of law that require the Postal Service to amortize over 15 years the increases in future CSRS annuities that result from annual employee pay raises and retiree COLAs." [S.Rep No. 108-35, at 2-3 (2003)]

Thus, it is clear that the Congress had no intention to absolve the Postal Service for increases in retirement costs due to pay increases, but rather that Congress understood that the inclusion of such costs was an inherent aspect of the funding mechanism it had established.

OPM's methodology for determining USPS CSRS funding obligations was considered by the GAO in Report Number GAO-03-448R, dated January 31, 2003, which included an examination of the OPM legislative proposal enacted months later as P.L. 108-18. In particular, the GAO report "evaluated the reasonableness of OPM's methodologies for allocating estimated benefit payments and other expenses between service rendered before and after July 1, 1971, the effective date of the Postal Reorganization Act," and suggested no changes to the allocation methodology used for Postal Retirement funding.

In 2003, the Postal Service first suggested that OPM revise the methodology used to establish the appropriate division of responsibility for pre-1971 Postal employment. The matter was carefully considered by both OPM's Board of Actuaries, and by OPM. The Board of Actuaries stated:

"The Board of Actuaries has reconsidered in detail the methodology used by the U.S. Office of Personnel Management to determine the obligations of the United States Postal Service under the United States Civil Service Retirement System. When private sector plans are transferring participants to a new employer, it is a common practice to allocate liabilities by using a method which reflects the fact that all obligations arising from future salary increases are the responsibility of the new employer. We find this approach to be the most appropriate way to determine the obligations of the Postal Service and further confirm our prior finding that this method clearly follows the intent of Congress in Public Law 93-

349."

The final OPM decision stated:

"The Board of Actuaries has undertaken such analysis [of the methodology], and their conclusions are set forth in the enclosed letter to the undersigned. As you can see from that correspondence, the Board of Actuaries again considered OPM's methodology and approved that methodology, as well as the computation of the resulting Postal supplemental liability. The Board clearly concluded that the methodology OPM used this year is valid and follows the intent of the Act. We believe the Board of Actuaries' conclusion and OPM's concurrence with that conclusion resolves all substantive issues between our different approaches both for fiscal year 2003 as well as for future years."

Congress next revisited Postal Retirement funding with the enactment of P.L.108-435, the *Postal Accountability and Enhancement Act*, in 2006. That law provided for the Treasury to take responsibility for the cost of military service credit in the computation of CSRS annuities, resulting in a \$28 billion dollar savings to the Postal Service, and relieving it from making further CSRS employer contributions based upon a percentage of salary. This change was consistent with the GAO recommendations in the January 2003 report, discussed earlier. OPM did not find any reference in the legislative history of that bill to indicate that Congress took any issue with the methodology by which OPM calculated Postal CSRS obligations. Neither did OPM find any record that the Postal Service raised any concern to Congress about OPM's CSRS allocation method at the time the 2006 legislation was being considered.

Finally, this January, the Postal Inspector General issued the report that led to this hearing.

Discussion

OPM's methodology is based upon long-standing public policy determinations made by prior Congresses. Its actions have been fully consistent with the letter of the law as well as all Congressional expressions of public policy on the subject.

The methodology OPM has applied to determine Postal CSRS funding is generally accepted actuarial practice and is commonly used by pension experts for plan transfers and terminations. Private pension plan transfers are usually made as part of a broader transaction, such as a corporate merger or spin-off, and are part of a negotiation as to the overall allocation of assets and liabilities. Thus the methodology used for allocating pension liabilities for any particular plan must be viewed in the broader scope of the overall asset and liability transaction between the parties. At the time the Postal Service was created in 1971, it assumed certain liabilities, such as those associated with the future retirement benefit accruals for its workforce, but it also received certain considerations, such as the existing assets of the POD.

In sum, OPM believes that the methods currently in use reflect Congressional intent and are consistent with current actuarial practice.

Health Benefits Funding

Funding of Postal Retiree health benefits is an entirely separate matter from the issue of CSRS funding. However, the two subjects are intertwined because the Postal Service wishes to utilize the savings that would result from the Postal IG's recommended approach to CSRS funding in order to satisfy the Postal Service's obligations for retiree health benefits funding.

The Postal Inspector General estimates that adoption of its recommended CSRS methodology would result in approximately \$75 billion of CSRS over-funding. Under current law, any Postal surplus would remain in the Retirement Fund until the end of FY2015, when it would be transferred to the Postal Service Retiree Health Benefits Fund. Even if there were authority to transfer the funds immediately, that would not change the fact that statutory provisions require the Postal Service to make payments for current retirees' employer health benefits contributions, as well as scheduled payments of \$5.5 to \$5.8 billion per year, through FY 2016. Regardless of any decision to change the apportionment of responsibility for pre-1971 service, these other changes sought by the Postal Inspector General would require legislation.

Conclusion

OPM believes that the current methodology is sound public policy, appropriate in the historical context, and consistent with private sector practices. As the Subcommittee examines this situation anew and considers suggestions by the Postal IG for allocating the retirement costs associated with the pre-1971 POD employment of Postal employees, OPM will provide any technical assistance that it can. I appreciate the opportunity to appear before you today and I would be pleased to answer any questions you may have.