The GAO Report on the OPM-USPS Dispute on CSRS Pensions: NALC Responds

October 17, 2011

The General Accountability Office issued a report on October 13, 2011, that restates the position it has taken since 2004 that the Office of Personnel Management's allocation of pension costs between the U.S. Postal Service and the Treasury is consistent with current law. The Postal Service and two other agencies, the Postal Regulatory Commission and the USPS Office of Inspector General, armed with independent audits conducted by private sector actuarial experts (The Hay Group and the Segal Company), disagree with this conclusion. Those audits concluded that the OPM's methods transferred $50 billion to $75 billion in costs related to pre-1971 service for the tax-payer funded Post Office Department to the postage ratepayer-funded USPS. [1]

The National Association of Letter Carriers (NALC) and the entire mailing industry, which employs eight million American workers, believe the GAO and the OPM are wrong on this matter. We believe the 2003 CSRS funding reform law and the 2006 Postal Accountability and Enhancement Act, mandates and authorizes the OPM to employ the modern actuarial methods advanced by the independent audits conducted for the USPS OIG and PRC.

Nevertheless, nothing in the GAO's report detracts from the compelling case for enacting H.R. 1351 or similar bills in Congress that provide a reasonable and workable way to address the postal financial crisis caused by the unique and crushing burden placed on the Postal Service in 2006 to pre-fund most of its future retiree health benefit costs in ten years time, just as the economy experience the worst recession in 80 years.

As the GAO report found, "All three methodologies (current, PRC, and USPS OIG) fall within the range of reasonable actuarial methods for allocating the cost to time periods." It goes on to say that "the allocation of costs" is "ultimately a business or policy decision." [2] Although we do not agree that it is reasonable to allow the OPM to value its obligations with static methods (with frozen 1971 wage rates) while requiring the USPS to value its obligations with dynamic methods (with rising wage rates) that impose greater costs on postage rate payers, NALC does agree with the GAO that "Congress can, if it chooses, make another determination about the allocation of current assets and obligations of USPS, of which pension assets are but one component." [3] Indeed, this formulation is precisely the approach taken by H.R. 1351: In order to sensibly address the onerous and unique burden to pre-fund future retiree health benefit costs, Congress should enact legislation along the lines of H.R. 1351 or similar approaches called for by S. 1010 in the Senate. Such action would avert insolvency, obviate the need for reckless downsizing, avoid collateral damage to an important American industry and strengthen the nation's economic recovery.

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[1] *See* USPS-OIG, *The Postal Service's Share of CSRS Pension Responsibility* (Jan. 20, 2010) (USPS-OIG Report) and the HayGroup, *U.S. Postal Service: Evaluation of the USPS Postal CSRS Fund for Employees Enrolled in the Civil Service Retirement System* (Jan. 11, 2010) (HayGroup Report), at 19.

[2] GAO, *U.S. Postal Service: Allocation of Responsibility for Pension Benefits between the Postal Service and the Federal Government* (Oct. 2011) (GAO Report), at 14.

[3] GAO Report, at 16.

NALC therefore calls on the Congress to make the only policy decision that will help stabilize one of the country's greatest institutions and spur a recovery in the national economy by strengthening the $1.3 trillion mailing industry, which employs some eight million American workers. It should implement the findings of the independent, private sector audits and repeal the pre-funding schedule of payments mandated by the PAEA between now and September 2016.

In the absence of this sensible and effective policy change, America's letter carriers call on Congress to suspend the law mandating massive retiree health pre-funding until the national economy recovers, the Postal Service returns to profitability or the stalemate over pension allocations is resolved. The remainder of this memorandum addresses legal and equity issues raised by the GAO report.

<u>Background</u>

An employee's Civil Service Retirement System (CSRS) pension is calculated by applying the employee's highest earnings average across *all* the years of the employee's service, including the years worked for the Post Office Department. Basic fairness therefore, as well as actuarial principles, require that USPS and the federal government share the cost of an employee's pension proportionately, based on the number of years the employee worked for each.[4]

OPM's longstanding methodology, however, skews the liability toward USPS, by calculating the federal government's share as though the employee's career ended, and his or her pension liabilities froze, in 1971. An example from the GAO's report provides a stark example of this misallocation of pension liabilities: for a hypothetical employee who spent 40% of her career working for the Post Office Department and 60% for USPS, OPM's methodology would require the federal government to pay just 18% over her pension costs, burdening USPS with the remaining 82%.[5]

<u>OPM's Allocation Methodology Rests on a Law That Was Repealed</u>

In concluding that OPM's skewed approach is "consistent with applicable law," GAO relies on a 1974 statute that it claims transferred to USPS responsibility for increased pension costs that resulted from increases in postal employee pay.[6] Even assuming that GAO's reading of the 1974 statute is correct, its reliance on the statute cannot possibly be, since Congress *repealed* the statutory language in 2003.[7] GAO cannot deny that Congress eliminated the language on which OPM based its allocation methodology. Remarkably, however, GAO

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[4] *See* Horizon Actuarial Services, LLC, *Review of USPS Allocation of Civil Service Retirement System Obligation* (Jan. 25, 2010), at 3 (explaining that under actuarial principles, the cost of future pay increases should be attributed to *each* year of service).

[5] GAO Report, at 13.

[6] GAO Report, at 5.

[7] *See* Public Law 108-18, 117 Stat. 624 (April 23, 2003) (repealing in relevant part Public Law 93-349, 88 Stat. 354 (July 12, 1974)).

concludes that the 2003 repeal made no difference, writing that "the consequence of the 2003 Act was to leave the 1974 allocation unchanged, *notwithstanding the removal of the explicit allocation provision*."[8] GAO's analysis here makes no sense: if Congress deliberately removed the language on which OPM's allocation methodology was based, the only logical conclusion is that Congress intended to change the methodology.

Indeed, Congress left little doubt about its intentions in the 2003 statute, which was enacted after Congress discovered that USPS had been overpaying into the CSRS Fund.[9] The 2003 law requires that USPS's liability be calculated "in accordance with generally accepted actuarial practices and principles."[10] OPM's methodology dates to the 1970's, when there was "little guidance as to the appropriate way to allocate pension costs."[11] OPM's methodology for determining the federal government's share may have been permitted by the now-repealed 1974 statutory language, but it has no basis in modern actuarial practice and principles. Standard actuarial practice employs the concept of "projected pay," which attributes future pay increases to the cost of each year of past service.[12] By attributing pension costs to the period in which they were earned, this actuarial practice avoids unfairly burdening future stakeholders of the enterprise with costs accrued earlier.[13]

The 2003 law also mandates the use of "dynamic assumptions" in determining the retirement system's actuarial costs and liabilities, meaning that it requires anticipating the effects of future pay increases.[14] It thus precludes a static approach to calculating the federal government's share, which freezes the cost of an employee's pre-USPS pension liability as if the employee never received a pay increase after 1971.

Because the legislative record is clear that Congress rejected OPM's approach when it enacted the 2003 statute, GAO errs in its conclusion that the OPM's methodology is nothing more than a "policy choice" that is "consistent with applicable law."

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[8] GAO Report, at 8 (emphasis added).

[9] *See* Sen. Report 108-35, 108th Cong., 1st Sess. (April 8, 2003), at 2-3 (noting that if USPS had continued to contribute to the CSRS Fund at the rate it had been contributing, postal CSRS pensions would have been "over-funded by $78 billion").

[10] 117 Stat. 624, at §2(c). In the 2006 Postal Accountability and Enhancement Act, Congress reiterated its intent that OPM allocate pension costs between the federal government and USPS "in accordance with generally accepted actuarial principles." P.L. 109-435, at §802(c)(1)(B).

[11] Segal, *Report to the Postal Regulatory Commission on: Civil Service Retirement System Cost and Benefit Allocation Principles* (June 29, 2010), at 1.

[12] See June 25, 2010 report from Horizon Actuarial Services, LLC to NALC President F. Rolando, at 1.

[13] GAO finds no actuarial "error" in OPM's approach, but GAO – unlike USPS-OIG –did not engage an independent actuarial firm to analyze the issue. *See* GAO Report at 3 (describing GAO's methodology as essentially interviewing interested parties and reviewing existing documents).

[14] 117 Stat. 624, at §2(a).

It Is Destructive To Burden USPS With The Pension Costs Related To All Post-1971 Pay Increases

OPM's methodology puts 100% of the pension costs related to post-1971 pay increases on USPS and 0% on the federal government. In defending the purported "fairness" of OPM's approach, GAO notes that USPS is "a self-sustaining entity" and that the federal government has "no control over USPS pay increases."[15]

While the federal government has no control over USPS pay, it is responsible for USPS's pension costs. In the private sector, a successor employer rarely continues the pension plan of its predecessor; the successor usually wants the flexibility to manage its own pension costs. That was not the case when USPS replaced the old Post Office Department. Federal law required that USPS employees participate in the federal retirement plan, a plan created by the federal government and controlled by the federal government. USPS has had no say over the plan and, in particular, does not determine the formula for determining the amount of benefits payable by the plan. Given USPS's lack of control over its pension costs, there is little "fairness" in making USPS bear a disproportionate share of them.

Moreover, while USPS determines pay for its employees, whether by collective bargaining or otherwise, those pay levels are far from excessive. Indeed, USPS pay levels have since 1972 risen at approximately the rate of inflation.[16] Since USPS has not raised pay excessively, it has not caused any disproportionate increase in pension costs, and should not bear a disproportionate share of those costs.

USPS Has Been Subsidizing Other Federal Pension Costs

GAO notes that the change urged by USPS-OIG would result in a transfer of assets to USPS's account in the CSRD Fund from the account for non-postal federal employees, increasing the unfunded liability of the latter account.[17] It may be true that remedying OPM's past wrongful allocation methodology would increase the federal government's unfunded pension liability, but that unfunded liability has been lower over the years than it otherwise would have been *because* USPS was paying more than it should have been into the CSRD Fund, effectively subsidizing the federal government's pension contributions. While USPS should pay its own way, it should not have to subsidize the retirement costs of the rest of the federal workforce. Transferring assets to the postal account will simply right a wrong that has gone on too long.

Correcting OPM's Past Misallocations Could Save USPS from Insolvency

Finally, GAO downplays the impact that correcting OPM's past misallocation would have on USPS's financial fortunes, grudgingly admitting that it "would provide some

[15] GAO Report, at 14.

[16] For example, Bureau of Labor Statistics data show that the Consumer Price Index rose 400.5% from 1972 to 2009, while USPS payroll data show the straight-time pay of postal letter carriers rose 417.4%.

[17] GAO Report, at 16-17.

temporary relief" but asserting that it would not be sufficient to address USPS's long-term financial challenges.[18] But with USPS teetering on insolvency, unable to make its mandated retiree health benefit payments,[19] what it needs now is immediate relief. A transfer of $75 billion, which could be used to satisfy the required retiree health payments,[20] would allow USPS to stay financially afloat. It would give USPS the breathing room it needs to make whatever appropriate changes may be necessary to help assure its long-term financial future.

USPS's long-term financial challenges are not as steep as GAO's report suggests. Indeed, but for the requirement that it pre-fund retiree health benefits, a requirement imposed on no other company or government entity, USPS would have been in the black for the 2007-2009 period, even with the recession depressing mail volume.[21] USPS in recent years has sharply reduced its costs and boosted its productivity. To be able to continue to improve for the long-term, however, it needs the immediate relief that remedying OPM's pension cost misallocation would provide.

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[18] GAO Report, at 18.

[19] GAO Report, at 1.

[20] GAO Report, at 18.

[21] *See* F. Clemente, T. Kiley, *Congressional Mandates Account for Most of Postal Service's Recent Losses*, Economic Policy Briefing Paper #268 (June 2010), at 2 (Table 1).