



October 11, 2011

Ms. Lorelei St. James  
Director, Physical Infrastructure  
U.S. Government Accountability Office  
441 G Street, N.W.  
Washington, D.C. 20548

Dear Ms. St. James:

Thank you for the opportunity to comment on the Government Accountability Office's report titled "Allocation of Responsibility for Pension Benefits Between the Postal Service and the Federal Government."

We disagree with the major conclusions of the report. Your review focuses on the 1974 law (P.L. 93-349), which is not in dispute. All parties agree that the 1974 law made the Postal Service responsible for funding the additional CSRS liabilities resulting from pay increases after 1971.

The issue in question surrounds the CSRS Funding Reform Act of 2003 (P.L. 108-18) as it pertains to the Office of Personnel Management's (OPM) share of CSRS liability. Your report fails to recognize how the 2003 law changed the 1974 law. We do not understand your assertion that the "consequence of the 2003 Act was to leave the 1974 allocation unchanged, notwithstanding the removal of the explicit allocation provision." If, as you state, the allocation provision was removed, it does not seem reasonable to assume the intent of Congress was that the allocation remain unchanged.

In fact, the 2003 law changed the directive to OPM. As the legislative history shows, it was intended to "repeal" the 1974 law (Senate Report No. 108-35, page 6). OPM was required to adopt modern dynamic methods. Dynamic methods dictate that OPM take into account the effect of future salary increases on the total liability. Using these methods, OPM was to capture the size of the postal liability and the respective responsibilities of the Postal Service and OPM to satisfy the liability. Instead, OPM applied dynamic assumptions solely to the Postal Service's share of the liability — not to its own share. It appears that OPM failed to follow the 2003 law and now must agree to do so or be compelled by law for a second time.

Two separate and independent reviews have found that OPM's continued use of the 1974 methodology for its own share is either unfair or not consistent with modern pension standards that use dynamic assumptions and that are required in the 2003 law:

- Our review, conducted with the assistance of the actuarial firm, the Hay Group, argued that the CSRS liability for employees with service prior to 1971 should be split between the Postal Service and the federal government on a years-of-service basis. A years-of-service basis was used to split the liability of retirees' cost-of-living adjustments (COLA) between OPM and the Postal Service prior to the 2003 law. Additionally, we found that the Postal Service's retiree health benefits are also allocated between the Postal Service and OPM on a years-of-service basis, which is instructive regarding the proper structuring of the CSRS benefits. We estimated that the Postal Service had been overcharged \$75 billion from fiscal years 1972 to 2009 for its share of CSRS pension benefits.
- The Postal Regulatory Commission's independent actuary, The Segal Company, advocated a methodology based on private sector accounting standards. Like our methodology, it takes into account the effect of future salary increases on the liability, but it does not split the costs evenly by years of service. Instead, it follows the CSRS pension formula, which provides a higher benefit for later years of service. Under this methodology, Segal estimated the Postal Service overpayment to be \$50 to \$55 billion. The Office of Inspector General believes that this method, though more moderate, represents a second rational approach to implement the 2003 law.

We believe OPM can now, if it chooses, apply dynamic assumptions to the federal share since it has been directed to do so since 2003. Under 5 U.S.C. § 8348, the Postal Service is responsible for the full amount of retirement benefits that are "attributable to civilian employment with the Postal Service." However, it is responsible only for that portion that is attributable to Postal Service employment. The Postal Service is not responsible for the amount attributable to service prior to 1971.

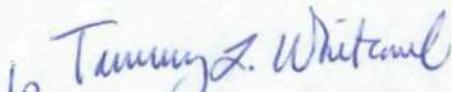
Post Office Department (POD) service prior to 1971 is properly the responsibility of the federal government. The 2003 law established that these amounts should be calculated dynamically as the liability increases with inflation and other factors. As a result, both the Postal Service and federal shares should include the expected salary increases that are part of the final pension benefit. Non-postal federal salaries have also risen since 1971, and OPM accounts for and is responsible for meeting those increased liabilities. OPM's failure to pay the full

CSRS cost of postal service prior to 1971 leaves a hole in the fund. The Postal Service and its employees have been forced to fill the gap. OPM's position, however, is that it needs to be directed more clearly to apply dynamic assumptions to the federal share by a new piece of legislation.

Applying dynamic standards to only part of the liability is not only inconsistent with the law and with modern actuarial standards, but it also results in the extraordinarily unfair assignment of the largest share of the liability to the Postal Service. Under this methodology, the Postal Service could be responsible for 70 percent of the CSRS pension costs for an employee whose service was split evenly (50-50) between the Postal Service and the POD. By using the 1974 static method for the federal share, OPM is leaving a deficit in the CSRS funding by not paying for inflation or pay increases attributable to POD service. To make up the deficit, OPM has overcharged postal ratepayers. Your report argues that no change is necessary since postal ratepayers have already paid these costs, but we believe that these ratepayers have been overcharged long enough. A correction is long overdue.

The current OPM methodology is neither fair nor modern nor does it comply with the 2003 law. We agree with you that action from Congress is necessary to settle this issue once and for all. We believe Congress did just that in 2003. If OPM cannot be convinced of the need to change its methodology, the only alternative is for Congress to compel OPM to act by adding even more explicit reform language to the legislation currently being prepared.

Sincerely,

  
David C. Williams  
Inspector General