

Postal Reform: An Overview of Budget and Policy Considerations

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Douglas Holtz-Eakin, President*
American Action Forum

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Chairman Carper, Ranking Member Coburn, and Members of the Committee thank you for the opportunity to testify today on the topic of postal reform. In this testimony I describe the financial situation facing the United States Postal Service (USPS) and criteria for evaluating comprehensive reform. This testimony seeks to make three key points:

- The financial situation of the USPS is clearly unsustainable;
- Despite a recent slowdown, there is a large risk that health care spending growth will return to previous rates making the USPS funding of their employee and retiree health benefits a sustained burden; and
- Proposals to reform the postal services should be evaluated by (i) the extent to which they alter the fundamentals of future revenue and costs, (ii) the degree to which costs are shifted from USPS to the federal government as a whole, (iii) the degree to which costs are simply shifted across time, and (iv) the degree to which costs are shifted to employees.

Financial Status of the USPS

The USPS is currently in a dire financial situation. Major financial problems include low cash flow, negative profit margins, monies owed to the Retiree Health Benefits Fund, and a statutorily mandated debt limit of \$15 billion that USPS reached in 2012. These financial woes are exacerbated by the mandate to prefund the Retiree Health Benefits Fund, which was established by the 2006 Postal Accountability and Enhancement Act. This requirement set a specific amount each year to be deposited into the fund and, as a result, drastically increased operating expenses. The USPS has not been profitable since pre-funding the Retiree Health Benefits Fund was required in 2007.¹ However, as the Congressional Research Service notes, the USPS would have run small deficits in the years 2009-2012 even without the cost of prefunding the Retiree Health Benefits Fund.²

As of current estimates, the USPS has \$2.7 billion in cash reserves, and while it holds \$46.1 billion in the Retiree Health Benefits Fund, it cannot use that money to pay down its debt or withdraw it to use as operating revenue; beginning in 2017 USPS will be able to use the money for retiree health care costs. Currently, the USPS has funded only 50 percent of the future retiree health benefits obligation (\$47 billion of the \$93.6 billion future obligation).³

¹ <http://www.fas.org/sgp/crs/misc/R43162.pdf>

² *Ibid.*

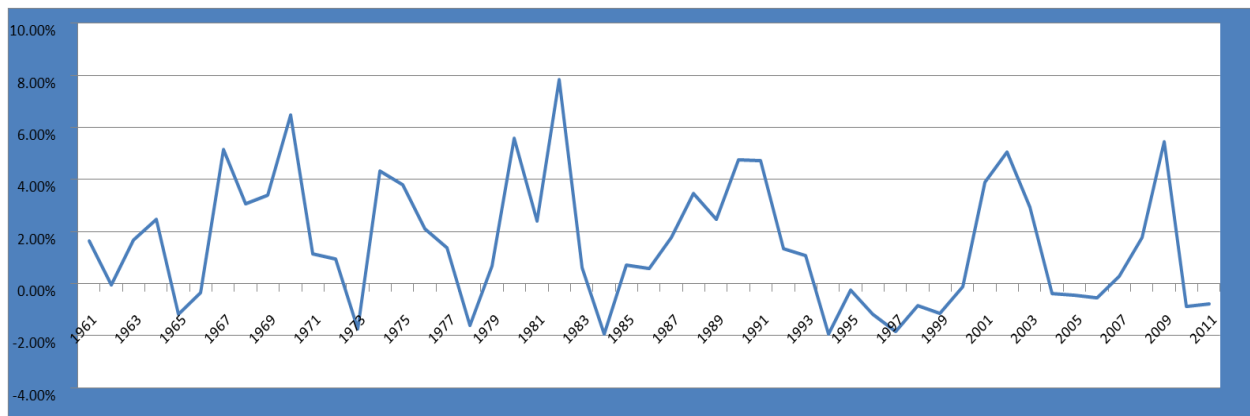
³ *Ibid.*

Personnel costs are crowding out investment in other areas, such as replacing mail delivery trucks. While the number of employees has been reduced and the USPS has made some strides in efficiency, it remains a labor-intensive business model, with 80 percent of costs composed of compensation and benefits. The recession, the growth of e-mail communication and online bill-pay options, and the prevalence of competitive shipping options such as UPS and FedEx, have led to declining mail and decreased revenue. Clearly the *status quo* is not sustainable.

Health Care Costs

Health care costs have constituted a growing portion of operating costs for the vast majority of employers; large or small, public or private. Accordingly, considerable fanfare has been given to slower growth of National Health Expenditures in recent years. It is difficult to parse out the individual impacts of slow economic growth, health policy and medical practice trends on the growth in spending. For federal programs, the slowdown may also reflect a disproportionate influx of younger Medicare beneficiaries and the expiration of major drug patents. In spite of this, in evaluating USPS reforms it may be prudent to plan for the risk of higher rates of growth in spending. Table 1 below shows that, while national health expenditure growth has been low relative to GDP growth in the past, it has always come back to exceed GDP growth rates.

Table 1: Growth in National Health Expenditures Per Capita Minus GDP Growth Rate, 1961-2011



Source: Calculated from CMS NHE Historical Data & Bureau of Economic Analysis GDP Data

Currently, postal employees receive health coverage through the Federal Employee Health Benefit (FEHB) plans and are eligible for federal retirement programs. When federal employees reach 65 years old and are eligible for Medicare, they sometimes decline the full Medicare benefits available to them, as their retiree health benefits will cover additional benefits like prescription drugs, dental care and vision services.

Health care costs are a large liability now and an even larger liability for the future. The USPS needs to anticipate these future costs. However, the USPS can only raise mail prices in line with inflation - using the Consumer Price Index for urban consumers (CPI-U). By contrast, health care costs grow faster than inflation. As a result, even if mail volume were to stay constant, growth in revenue would not be able to keep pace with health costs. In 2012, per capita health costs for individuals on commercial insurance plans and Medicare grew by 5.8 percent; the CPI-U for 2012 was 1.7 percent.^{4,5}

Reform Criteria

Evaluating proposals seeking to ameliorate the USPS's financial trouble should focus first and foremost on the impact on business fundamentals: the scale, scope and pricing of products that will underlie revenue growth and the efficiency, productivity, and compensation of capital and labor that underlie the cost structure.

Alternatively, proposals may simply shift costs from the USPS. For example, it has been argued that USPS "overpays" into the Federal Employee Retiree System because contributions are based on all federal employees, not calculated based on the postal service population. Should USPS begin paying less for their employees, other federal employees and the taxpayer will pay more. Similarly, a proposal to create an exclusively USPS health plan has been introduced, but taking away nearly one-quarter of the FEHB enrollees may cause plans in some areas to leave the market, resulting in increased premiums for other FEHB plans. In both cases, reform merely shifts costs to the overall federal budget.

Secondly, policy makers would be wise to consider the present impact and the future impact of reform. Just as costs can shift from the USPS budget to elsewhere in the federal budget, costs can be shifted to the future, ensuring short-term improvement but not long-term sustainability. For example, dropping the prefunding requirement for the Retiree Health Benefits Fund would help the post office's financial situation in the short and medium term, but with longer life expectancies and the unpredictability of health care costs, the USPS could find itself with a large population of retirees to support and even greater costs

Conclusion

⁴ <http://www.healthleadersmedia.com/content/HEP-283505/Healthcare-Cost-Growth-Steamrolls-CPI.html##>

⁵ <ftp://ftp.bls.gov/pub/special.requests/cpi/cpiiai.txt>

The USPS is in crisis and Congress has critical decisions to make about the future of postal services. Performing a critical analysis of the current financial situation, planning for short-term improvements and long-term sustainability, and considering the holistic impact of any reforms will ensure that costs and benefits are weighed appropriately.