



CONGRESSIONAL BUDGET OFFICE COST ESTIMATE

REVISED March 19, 2003

S. 380 **Postal Civil Service Retirement System Funding Reform Act of 2003**

*As ordered reported by the Senate Committee on Governmental Affairs
on March 5, 2003*

SUMMARY

Enacting S. 380 would permanently reduce payments by the United States Postal Service (USPS) to the Civil Service Retirement and Disability Fund (CSRDF) starting in 2003. CBO estimates that enacting the bill would result in net outlays of \$17 billion over the 2003-2008 period, and about \$40 billion over the 2003-2013 period. That estimate is the total budgetary impact of the proposal, combining both on-budget and off-budget effects. (USPS cash flows are considered off-budget.)

Under the bill, the Postal Service would see its required payments to the CSRDF reduced by \$3 billion to \$5 billion a year. The legislation specifies that the Postal Service and the Department of the Treasury should determine how to apply the savings. CBO expects the Postal Service would use those savings to repay debt, delay future rate increases, and invest in capital projects or other activities to increase productivity.

By reducing USPS payments to the retirement fund, CBO estimates the bill would lower the agency's costs (off-budget) by about \$2 billion over the 2003-2008 period. We also estimate that enacting S. 380 would increase on-budget costs by about \$19 billion over the same period. Thus the net effect of this legislation on the unified federal budget would be a cost of about \$17 billion over the 2003-2008 period largely because on-budget offsetting receipts—representing payments from the Postal Service to the CSRDF—would be reduced. Over the 2003-2013 period, enacting S. 380 would combine off-budget savings of about \$2 billion with on-budget costs of around \$42 billion to produce a net cost of about \$40 billion.

S. 380 contains no intergovernmental or private-sector mandates as defined in the Unfunded Mandates Reform Act (UMRA) and would impose no costs on state, local, or tribal governments.

ESTIMATED COST TO THE FEDERAL GOVERNMENT

The estimated budgetary impact of S. 380 is shown in the following table. The costs of this legislation fall within budget functions 370 (commerce and housing credit), 900 (net interest), and 950 (undistributed offsetting receipts).

	By Fiscal Year, in Billions of Dollars										
	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013
CHANGES IN DIRECT SPENDING											
On-Budget Effects—CSRDF											
Estimated Budget Authority	3.5	2.7	3.0	3.0	3.2	3.6	3.8	4.2	4.6	4.8	5.2
Estimated Outlays	3.5	2.7	3.0	3.0	3.2	3.6	3.8	4.2	4.6	4.8	5.2
Off-Budget Effects—Postal Service											
Estimated Budget Authority	-2.5	-0.6	0.8	0.3	0	0	0	0	0	0	0
Estimated Outlays	-2.5	-0.6	0.8	0.3	0	0	0	0	0	0	0
Total Budget Effects											
Estimated Budget Authority	1.0	2.1	3.8	3.3	3.2	3.6	3.8	4.2	4.6	4.8	5.2
Estimated Outlays	1.0	2.1	3.8	3.3	3.2	3.6	3.8	4.2	4.6	4.8	5.2

NOTES: Components may not add to totals because of rounding.

BASIS OF ESTIMATE

For this estimate, CBO assumes that S. 380 will be enacted in the spring of 2003. CBO estimates that reducing the Postal Service's payments to the retirement fund would reduce the agency's off-budget costs by about \$2 billion over the 2003-2008 period, but enacting S. 380 would increase on-budget costs by about \$19 billion over the same period. The net effect of this legislation on the unified federal budget would be a cost of about \$17 billion over those six years. Over the 2003-2013 period, enacting S. 380 would combine off-budget savings of about \$2 billion with on-budget costs of around \$42 billion to produce a net cost of \$40 billion.

Background

Although the Postal Service is a federal agency, its financial operations are classified as being off-budget. Despite this treatment, federal budget documents present the net income

of the agency in the budgetary totals. The Postal Service is required by law to set postage rates to cover its full costs. In fiscal year 2002, the Postal Service generated \$68.1 billion in collections, mostly from postage and user fees, and had \$67.4 billion in expenses. The agency has the authority to borrow up to \$15 billion from the Treasury; at the end of fiscal year 2002, its outstanding debt with the Treasury stood at \$11.9 billion.

Postal employees participate in the federal government's two main defined benefit pension programs. Those workers first hired prior to 1984 are covered by the Civil Service Retirement System (CSRS) while those first hired after 1983, as well as former CSRS workers who elected to change coverage, participate in the Federal Employees' Retirement System (FERS). In 2002, about 30 percent of the USPS workforce was covered by CSRS, and the rest were under FERS.

The Postal Service and its employees each make payroll contributions toward both CSRS and FERS. For CSRS workers, both the standard agency and employee contribution rates are 7 percent. For FERS employees, the agency contribution rate for most employees is 10.7 percent, while the employee rate is 0.8 percent. Although CSRS provides more generous benefits than FERS, unlike FERS, CSRS is not a fully funded pension system, meaning that agency and employee contributions alone are not enough to finance the program's benefits. In an effort to make up the shortfall between contributions and benefits for its current and former employees, the Postal Service makes lump-sum payments to the retirement system each year. In 2002, those payments amounted to about \$3.9 billion.

The Office of Personal Management projects that, under current law, the Postal Service will eventually overfund pension obligations for its workers by as much as \$71 billion. The projected overfunding is due primarily to higher-than-expected returns on assets held in the CSRDF.

On-Budget Effects

S. 380 would change the way the Postal Service finances retirement benefits for many of its current and former employees. The proposal would replace two amortization payments the Postal Service now makes to CSRDF—amounting to a combined \$4 billion in 2003 and is expected to grow to nearly \$6 billion in 2013—with a new annual payment of \$434 million over the next 40 years that would amortize the agency's estimated unfunded liability of about \$5 billion. The net effect of changes in amortization payments is to reduce Postal Service payments to the CSRDF by \$4 billion in 2003, \$19.5 billion over the 2004-2008 period, and \$43.5 billion over the 2004-2013 period.

The legislation also would replace the fixed contribution rate, which the Postal Service currently makes for its approximately 225,000 employees covered by the CSRS, with a rate intended to pay the full normal cost of CSRS benefits (including military service credits). This change would effectively increase the Postal Service's contribution rate for most covered employees from 7 percent to 17.4 percent of payroll. In 2004, the first full year of contributions at the higher rate, CBO estimates that this would increase the agency's retirement contributions by nearly \$1 billion, but that increase would gradually decline as the CSRS covered workers retire. Employee contribution rates for those in CSRS, as well as agency and employee contributions for those in the Federal Employees' Retirement System, would be unaffected by the legislation.

The Postal Service is an off-budget entity and contributions and payments that it makes to the retirement trust fund are considered offsetting receipts. Reducing overall payments the Postal Service makes to the CSRDF would result in a reduction of on-budget receipts to the government. To the extent that the Postal Service uses its savings to reduce its debt to the Federal Financing Bank, on-budget interest receipts would also be lower. Assuming the changes made by S. 380 are effective in April 2003, CBO projects the net on-budget effect of the bill would be a cost of \$3.5 billion in 2003 and approximately \$19 billion over the 2003-2008 period.

Off-Budget Effects

CBO estimates that enactment of S. 380 would reduce net expenditures of the USPS by \$2 billion over the 2003-2008 period.

Estimated Effects on Postal Outlays for Fiscal Years 2003-2006. The Postal Service's response to the change in its pension payments is uncertain, but CBO anticipates that the agency will use the savings from S. 380 to:

- Repay \$2 billion of its outstanding debt in fiscal year 2003,
- Invest \$1 billion in fiscal year 2003 and \$2 billion in 2004 in additional capital projects or other activities aimed at improving productivity, and
- Delay the next postal rate increase—anticipated late in fiscal year 2004, until fiscal year 2007.

CBO expects that the Postal Service would repay about \$2 billion of its outstanding debt to the Treasury in 2003. That action would reduce the agency's interest expenses by about \$60 million annually, beginning in fiscal year 2004. Because the USPS pays an average

interest rate on that debt of only 3 percent, CBO expects the agency would seek to make capital investments with much of the savings that could more effectively contribute to lowering its operating costs and thus contribute to a postponement of its next rate increase. For fiscal years 2005 and 2006, CBO estimates such investments would lead to operational savings of about \$300 million and \$600 million per year, respectively.

In July 2002, the Postal Service raised the price of a first-class stamp from \$0.34 to \$0.37 and raised rates for other classes of mail. Based on information from the Postal Service and on postal revenues to date in 2003, CBO estimates that this rate increase will raise over \$3 billion in additional revenue a year. The CBO baseline assumes a similar rate increase late in fiscal year 2004, including a price of \$0.40 for a first-class stamp.

We estimate that delaying the next rate increase would result in a small loss of revenue in fiscal year 2004 and losses of roughly \$3.5 billion in each of fiscal years 2005 and 2006. A delay in the rate increase also would increase operating expenses because the Postal Service would have to deliver higher volumes of mail than otherwise expected. (When rates go up, mail volume goes down.) Based on information from the Postal Service about the relationship between price increases, mail volumes, and operating costs, we expect that this increase in expenses would be about half a billion dollars annually in 2005 and 2006.

CBO estimates that those changes in postal revenues and expenses would result in lower net outlays of \$2.5 billion in fiscal year 2003 and \$600 million in 2004, with net increases in outlays of \$800 million in 2005 and \$300 million in 2006.

Estimated Effects on Postal Outlays in Fiscal Years after 2006. After 2006, CBO assumes that the Postal Service will use a combination of rate increases and controls on spending to ensure that its income covers the costs of its services, as required by law and as assumed in the CBO baseline. Thus, S. 380 would have no effect on net postal outlays after fiscal year 2006 when we expect the next rate increase would occur.

INTERGOVERNMENTAL AND PRIVATE-SECTOR IMPACT

S. 380 contains no intergovernmental or private-sector mandates as defined in UMRA and would impose no costs on state, local, or tribal governments.

PREVIOUS CBO ESTIMATES

This cost estimate of S. 380 supersedes and replaces the estimate for the same bill that CBO released on March 17, 2003. The previous cost estimate contained an error in the discussion under “Basis of Estimate” of the legislation’s on-budget effects. The earlier estimate said that the on-budget effect of replacing the Postal Service’s current amortization payments to the CSRDF would be to reduce offsetting receipts by \$3.5 billion in 2003, \$15.5 billion over the 2004-2008 period, and \$38 billion during the 2004-2013 period. Those figures were incorrect. CBO estimates the change in amortization payments would reduce receipts by \$4 billion in 2003, \$19.5 billion during the 2004-2008 period, and \$43.5 billion over the 2004-2013 period. This correction does not change CBO’s estimate of either the on-budget or off-budget cost of enacting the legislation. The numbers shown in the table and cited in the “Summary” are unchanged.

On March 14, 2003, CBO transmitted a cost estimate for H.R. 735, the Postal Civil Service Retirement System Funding Reform Act of 2003, as ordered reported by the House Committee on Government Reform on March 6, 2003. CBO estimated that enacting that bill would result in net outlays of \$7.1 billion over the 2003-2008 period and \$7.2 billion over the 2003-2013 period. Estimated outlays for H.R. 735 are lower because, for fiscal years after 2005, that bill would require that savings resulting from reduced payments to the CSRDF be held in escrow and remain unavailable for obligation unless authorized by subsequent legislation. S. 380 does not contain any such requirement.

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