Statement by Thomas O. S. Rand
To the President's Commission
On the United States Postal Service

Good afternoon. My name is Thomas Rand. I am currently with Aon Consulting. Until 1998, when my partners and I concluded the sale of our business to Aon, I was a principal and cofounder of the actuarial consulting firm, Williams, Thacher & Rand.

While with WTR and subsequently with Aon, I have consulted with the Postal Service on a wide range of benefit issues since 1984. I have supported the Postal Service in labor negotiations, served in an expert witness capacity in numerous arbitrations, and served on the panel in the Valtin arbitration proceedings in 1993. I have also assisted numerous private sector employers with benefit and labor relations issues in a career in the benefits consulting business that began in 1970.

I have also served continuously as a trustee of the UMWA Combined Benefit Fund since that fund's inception in 1993. The Combined Fund was created by the Congress in energy legislation passed in late 1992, and is responsible for overseeing health benefits provided retired coal miners and their dependents.

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I'm here this afternoon to talk with the Commission about the subject of employee benefits, a subject of great importance to the Postal Service.

As the graph on page one of your handout makes clear, employee benefits, including paid leave, represent a very substantial portion of USPS' total compensation paid to employees.

Total compensation paid during FY 2002 was $51.5b. The total cost of benefits was just under 40% of that expenditure, approaching $20b.

There are three major components of that cost. Taken together, paid leave, retirement benefits and health benefits account for more than 85% of benefit costs.

As my testimony will show, these benefits provide USPS employees with a significant benefits premium, compared with their counterparts in the private sector.

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The benefits package USPS provides employees is comprehensive.

USPS employees participate in all of the benefit programs offered to Federal employees, and in other benefits unique to the Postal Service.

No matter how the value of this benefits package is measured, USPS employees realize a significant premium compared with benefits provided workers in the private sector and this benefits premium continues to grow.

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One common way to value the USPS benefit package compared with the private sector is on the basis of cost. In the graph on page 3 of your handout, costs are expressed on a dollars-per-hour worked basis, consistent with the approach used by the Bureau of Labor Statistics (BLS) to report on benefit costs in the private sector.

As you can see here, USPS costs significantly exceed costs among private sector employers, and the difference is particularly striking in USPS' three major cost areas—retirement, health care and paid leave. The comparison here is based on December, 2002 data for the Postal Service and BLS, for full-time employees only.

In the aggregate, the cost of benefits provided USPS employees exceeds the cost of benefits provided full-time employees in the private sector by 61%.

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Another commonly accepted way to look at the comparative value of benefits is to value the benefit features for a hypothetical employee or group of employees.

This type of value calculation neutralizes differences in cost related to other factors, including:

1. Wage differences. Essentially all benefits other than health insurance are related to pay, and since USPS workers have a significant wage premium compared with their private sector counterparts, that premium contributes significantly to USPS costs; and

2. Demographic differences, such as location, age and gender and the prevalence of family coverage for health benefits.

The graph on page 4 of your handout illustrates the results of a recent study prepared by the Hay Group that uses standard actuarial methodologies to measure the value of the Postal Service's benefit package compared with the Hay Group's private sector database. That data base for 2002 included 943 private sector employers who elected to participate in Hay's annual survey. The survey is designed to measure and compare benefit values among large and medium-sized employers.

The numbers presented here represent the value of USPS benefits for an employee with an annual salary of $40,000, in mid-career, who participates in FERS and the Thrift Savings Plan. For this hypothetical employee, the value of USPS' benefits package is 25% greater than that provided by the average employer responding to the Hay Survey.

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Under either analytical method, two key areas that account for most of the benefits premium are the Postal Services' health insurance and retirement benefits.

Using the employer cost comparison, almost 65% of the difference between the cost of benefits to USPS and the cost incurred by employers in the private sector is based on these two benefits.

Taken together, they represent among the most significant fiscal challenges that the Postal Service faces. These are challenges the Postal Service shares with employers across the entire United States economy.

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Let's examine these two areas—retirement and health benefits—separately, because each presents issues that are directly related to USPS' lack of control over benefit features so long as USPS remains tied to the current federal retirement and health benefit programs.

There are two major issues associated with USPS' excessive costs in the retirement plan area compared with private sector employers, and both are embedded in the defined benefit plan (the pension plan) provided employees.

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1. First, both the defined benefit plans (CSRS and FERS) provide unlimited protection against inflation. CSRS benefits are fully indexed to changes in the CPI. Benefits under FERS are indexed to the CPI minus 1% annually. This feature adds 32% to the cost of the plan, and is rarely provided by private sector employers, except on an ad hoc basis during periods of high inflation.

2. Second, USPS' plans permit career employees to retire as early as age 55 with a full pension. Early retirement benefits in private sector plans are rarely so generous, as the graph shows. This feature adds another 37% to the cost of the FERS plan.

In the graph on page 7 of your handout I show the aggregate effect of these two features, on the value of the FERS plan (and ultimately on its cost). That plan currently covers about 70% of all postal workers and is mandatory for all workers hired after January 1, 1984.

While the basic benefit provided in the FERS plan is about 5% lower than the basic benefit provided by the average employer providing a defined benefit plan in the Hay Group survey sample, when you add in the COLA benefit and the generous early retirement benefit compared with private sector employers, the difference is dramatic.

The FERS plan fully valued is worth one-third more than the average defined benefit plan provided among Hay's survey participants.

It is also important to note that only 51% of the Hay Group survey participants provide a defined benefit plan at all, and that prevalence issue is reflected in the third bar on the graph.

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Now let's turn to the health benefits picture.

USPS provides employees health insurance through the Federal Employee Health Benefit Program (FEHB) which offers a wide variety of health insurance choices.

As with retirement benefits, there are two key drivers of the benefits premium USPS employees enjoy.

1. First, the benefits provided under the array of choices available to federal and Postal employees are more generous than benefits in the average private sector plan.

2. Second, USPS employees contribute relatively little toward the cost of their coverage. On average, private sector workers contribute about 31.5% of the total premium compared with a contribution of 16.5% for postal workers.

The private sector data depicted here is from the annual Mercer/Foster Higgins health benefits survey.

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While the added cost borne by USPS for the active workforce is substantial, the situation is even more burdensome when the cost of retiree health benefits is considered.

Under the rules that apply to participants in FEHB, a particularly important feature for career employees is the availability of continuing coverage in retirement, so long as the employee qualifies for an annuity under the federal retirement system and has been covered continuously under FEHB for at least five years. This retiree coverage is also available for surviving dependents of the participant.

In Fiscal year 2002 the cost for retiree health coverage for the postal service on a cash basis was nearly $1 billion dollars.

In the private sector, by way of contrast, there has been a substantial reduction in the availability of retiree medical coverage and substantial changes in who bears the cost where it is provided.

The Kaiser Family Foundation 2002 survey noted that in 1988 66% of firms with 200 or more employees offered some form of retiree medical coverage. In 2002 only 34% of the same sized firms reported offering retiree medical. And as the survey reported, even when this coverage is made available employer contributions are often limited or not provided at all.

Common approaches to limiting the cost of retiree health care in the private sector include:

1. Attaching age and service requirements to both eligibility and contribution requirements;

2. “Capping” the employer’s contribution toward the cost of the plan at a fixed dollar amount; and

3. In the most extreme cases, eliminating employer contributions toward the cost of retiree coverage altogether.

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As I have noted earlier, USPS incurs the major portion of its benefit costs in programs established and maintained by the Federal Government. In 1971, this approach made sense for a number of reasons, including:

1. Those plans were already in place.

2. Postal reorganization committed USPS to maintaining benefits comparable to the benefits workers had prior to reorganization; and

3. There was a concern that the impact of the removal of the postal service population from the Federal benefit plans would have had a detrimental effect on the remaining participants.

There have been significant changes in private sector benefit practices since 1971 as well as changes in federal benefit programs. Current USPS benefit levels are now significantly above benefits provided in the private sector. The inevitable consequence is that benefit costs have made USPS less competitive.

I believe that there are two ways that the Postal Service could move forward toward greater comparability with the private sector, and greater competitiveness:

1. One would be to stay within the Federal benefit system but obtain legislation to be able to modify benefit provisions and/or employee and retiree contribution requirements in those plans specifically for USPS employees.

2. Without changes to the Federal benefits, USPS could provide separate benefit programs outside of the Federal plans that would include provisions more closely aligned with the private sector. This latter approach, as I understand it, would also require legislation.

In the end, however, major changes to the plans will have to be made, if USPS is to comply more closely with the comparability standard and remain competitive in a global economy.