



July 2013

U.S. POSTAL SERVICE

Proposed Health Plan
Could Improve
Financial Condition,
but Impact on
Medicare and Other
Issues Should Be
Weighed before
Approval

GAO Highlights

Highlights of [GAO-13-658](#), a report to congressional requesters

Why GAO Did This Study

USPS has asked Congress to help restore its financial viability in part by enacting its proposal to create a USPS health care plan outside of FEHBP. This would result in the withdrawal of all postal employees and retirees (about 1 million people) from FEHBP. Under its proposal, USPS's and postal employees' and retirees' share of premiums would first be established by USPS and then, for union-covered employees, in collective bargaining. USPS employee groups oppose or have concerns about USPS's proposal.

GAO was asked to review USPS's proposed health care plan. This report discusses how the plan could affect 1) USPS's financial condition, 2) postal employees' and retirees' benefits and costs, and 3) FEHBP and non-postal enrollees. GAO analyzed USPS and FEHBP data and interviewed officials from USPS, Office of Personnel Management (OPM), OMB, Treasury, CMS, employee groups, and FEHBP plans. See the following page for more discussion of the scope and methodology.

What GAO Recommends

As Congress considers USPS's health care plan, it should weigh the plan's impact on Medicare and other issues, including establishing safeguards for USPS health plan assets and ensuring FEHBP-comparable protections for USPS health plan participants. In a letter commenting on this report, USPS took no position on GAO's recommendations. OPM and Treasury had no formal comments. USPS and Treasury provided technical comments that were incorporated where appropriate.

View [GAO-13-658](#). For more information, contact John E. Dicken at (202) 512-7114 or dickenj@gao.gov, Lorelei St. James at (202) 512-2834 or stjamesl@gao.gov, and Frank Todisco at todiscof@gao.gov.

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Proposed Health Plan Could Improve Financial Condition, but Impact on Medicare and Other Issues Should Be Weighed before Approval

What GAO Found

The U.S. Postal Service (USPS) would likely realize large financial gains from its proposed health care plan, primarily by increasing retirees' use of Medicare. Specifically, USPS estimates that its plan would reduce its retiree health benefit liability by \$54.6 billion, thereby eliminating its unfunded retiree health benefit liability. The plan would also reduce USPS's required total annual health care payments by an estimated \$7.8 billion in the first year of implementation and by \$33.2 billion over the first 5 years of implementation. USPS also projects that relative to the total annual health care payments it would expect to make (reflecting its stated inability to make prefunding payments to fund retiree health benefits), its new plan would reduce its payments by \$2.1 billion in the first year of implementation and \$12.4 billion over 5 years. USPS also projects that its plan would increase the more than \$550 billion that the federal government spends annually for Medicare by \$1.0 billion in the first year and an average of about \$1.3 billion annually in the first 5 years of its health plan—about 0.2 percent of Medicare's annual costs. GAO has previously reported that Medicare is on a fiscally unsustainable path over the long term. Additional costs resulting from USPS's proposed plan would also have to be weighed alongside the fiscal pressure already faced by Medicare, but these costs have not been evaluated by the Office of Management and Budget (OMB) or the Centers for Medicare and Medicaid Services (CMS).

Some elements of USPS's proposal would add uncertainties that could reduce funds available for its employees' and retirees' future health care.

- **Investment of Health Plan Assets:** One of USPS's proposed options for investing health plan assets would increase the risk exposure of these assets by allowing investments in assets other than Treasury securities, such as stocks, as well as commodities, foreign currency, and other investments. If fund assets were invested in non-Treasury securities (including \$46 billion that would be transferred under this option from the current Postal Service Retiree Health Benefits Fund), the fund may experience losses in a market downturn and would thus have reduced assets available for health care. The presence of non-Treasury securities in the portfolio would also raise issues as to the appropriate discount rate for determining prefunding targets for retiree health benefits.
- **Transfer of Surplus Funds:** USPS's proposed option to transfer health fund assets to use for purposes other than health benefits, when assets supporting the USPS health plan exceed liabilities, is not fiscally prudent. If USPS were to consistently exercise this option to help maintain its financial solvency, it could result in an unfunded liability for retiree health benefits.
- **Selection of Assumptions:** Liability measurements are very sensitive to assumptions, and there can be professional disagreements over assumptions. USPS's proposal could potentially allow for the use of overly optimistic assumptions, which could lead to inadequate funding for the health plan over time. This potential could be reduced by having assumptions selected by an independent third party.

Scope and Methodology

To describe the potential financial effects of USPS's proposed plan, GAO reviewed USPS documents detailing key elements of the plan and estimated cost savings. GAO obtained documentation regarding USPS's assumptions, methodology, calculations, underlying data, and projections and reviewed these for internal consistency and consistency with GAO's prior work and for overall reasonableness, and discussed them with officials of USPS and representatives of the Hay Group, which USPS hired to prepare its projections. GAO used its actuarial, economic, and health care expertise and judgment to determine the assumptions and projections were sufficiently reliable for purposes of this review but did not independently validate them. GAO also met with officials from OMB and CMS to discuss the effect of USPS's proposal on Medicare.

To determine the effect that USPS's proposal could have on postal employees' and retirees' benefits, GAO compared the package of services that USPS proposed to cover in the first year of implementation with the services covered in 2013 by seven selected FEHBP plans that had more than 75 percent of the total postal enrollment in FEHBP. To determine the extent to which employees and retirees would have the same legal protections related to employees' and retirees' benefits and costs under USPS's proposed plan as they have within FEHBP, GAO reviewed draft legislation proposed by USPS and federal laws, regulations, and OPM guidance that apply to FEHBP plans.

To describe the effects of a USPS withdrawal on FEHBP and on nonpostal FEHBP enrollees, GAO used OPM data on postal and nonpostal enrollment in FEHBP in 2011 to estimate the change in total program enrollment. GAO also used the data to estimate the effect on enrollment in each of the more than 140 FEHBP plans.

GAO met with officials from USPS management and employee groups and others to obtain their perspectives on USPS's proposed health care plan.

What GAO Found (continued)

Under USPS's health care plan as designed for year one, USPS employees and retirees would have coverage for a similar set of inpatient, outpatient, and prescription drug services as under selected Federal Employees Health Benefits Program (FEHBP) plans, which account for over 75 percent of postal enrollment in FEHBP. USPS's proposed plan would also offer similar levels of coverage for many services, with some exceptions (e.g., services received outside of USPS's approved network). GAO estimated that at least 63 percent of postal enrollees in the selected FEHBP plans would pay similar or lower premiums under the USPS plan, but some employees and retirees could have higher total costs—premiums and out-of-pocket costs for the use of care—due in part to differences in deductibles and maximum spending limits. Also, employees and retirees may need to change providers and would have many but not all the same protections around benefits and costs under the USPS plan as in FEHBP. For example, postal retirees would no longer have the assurance that USPS's contribution to the cost of health benefits would be fixed by law as it is within FEHBP.

A USPS withdrawal from FEHBP would reduce the program's enrollment by an estimated 25 percent. Despite the significant change in enrollment, most nonpostal enrollees would likely not be affected by a USPS withdrawal beyond what selected FEHBP plan representatives expect to be small increases or decreases in premiums. However, USPS's withdrawal could lead the small number of FEHBP plans with primarily postal enrollment to withdraw from the program, which would result in an estimated 29,000 (of over 3 million) nonpostal enrollees having to select a new health plan.

Key Policy Issues

The primary policy decision for Congress to make with respect to USPS's proposed health care plan is whether to increase postal retirees' use of Medicare, which is already facing funding challenges. This is because USPS's proposal would essentially decrease USPS costs but increase Medicare costs. If Congress does not act on USPS's proposal for a new USPS health care plan, GAO continues to believe that Congress and USPS need to reach agreement on a comprehensive package of actions to improve USPS's financial viability. In previous reports, GAO has provided strategies and options that Congress could consider to address constraints and legal restrictions that limit USPS's ability to reduce costs and improve efficiency. GAO also continues to believe that Congress would need to modify the current statutory schedule for prefunding USPS's retiree health benefits payments in a fiscally responsible manner. In this regard, USPS should continue to prefund any unfunded retiree health benefits liabilities to the maximum extent that its finances permit.

If Congress decides to move forward with USPS's proposed health plan as part of a broader reform package, other important policy issues remain to be addressed. Specifically, Congress should consider:

- safeguards for all USPS health plan fund assets by placing appropriate constraints on their asset allocations; such as limiting all investments to Treasury securities, including inflation-indexed Treasury securities;
- standards for the disposition of any surplus health plan assets that reduce the risk of a new unfunded liability emerging in the future; such as standards for amortizing any surplus to mirror the amortization of any unfunded liability;
- designation of an independent entity responsible for selecting actuarial assumptions used to determine the health plan's funded status; and
- protections for postal employees and retirees that are comparable to those under FEHBP, including a formula for retirees' contribution to health costs.

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Abbreviations

CMS	Centers for Medicare & Medicaid Services
EGWP	Employer Group Waiver Plan
ERISA	Employee Retirement Income Security Act of 1974
FEHBP	Federal Employees Health Benefits Program
HBF	Health Benefits Fund
HMO	health maintenance organization
OMB	Office of Management and Budget
OPM	Office of Personnel Management
PAEA	Postal Accountability and Enhancement Act
PHSA	Public Health Service Act
PSRHBFB	Postal Service Retiree Health Benefits Fund
TIPS	Treasury Inflation-Protected Securities
USPS	U.S. Postal Service
USPS OIG	U.S. Postal Service Office of the Inspector General

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July 18, 2013

The Honorable Thomas R. Carper
Chairman
The Honorable Tom Coburn, M.D.
Ranking Member
Committee on Homeland Security and Governmental Affairs
United States Senate

The Honorable Susan M. Collins
United States Senate

The U.S. Postal Service (USPS) has insufficient revenues to cover its expenses, has reached its statutory borrowing limit of \$15 billion, lacks liquidity to maintain its financial solvency, and has projected unsustainable losses. We and the Postmaster General have called on Congress to enact legislation for comprehensive postal reform to address these issues.¹ We have recently testified that USPS needs to reduce its expenses while continuing to fund its retirement obligations.² Compensation and benefits continue to comprise roughly 80 percent of postal costs, with benefit costs comprising close to half of this. Employee and retiree health care benefits are USPS's single most costly benefit. In fiscal year 2012, USPS reported that health benefit payments were \$7.8 billion for current postal employees and retirees,³ not including \$11.1 billion in statutorily required payments—that USPS did not make—to

¹GAO, *U.S. Postal Service: Strategies and Options to Facilitate Progress toward Financial Viability*, [GAO-10-455](#) (Washington, D.C.: Apr. 12, 2010); Patrick R. Donahoe, Postmaster General and Chief Executive Officer, USPS, *Solutions to the Crisis Facing the Postal Service*, testimony before a hearing of the Committee on Homeland Security and Governmental Affairs, United States Senate, 113th Cong., 1st Sess., Feb. 13, 2013.

²GAO, *U.S. Postal Service: Urgent Action Needed to Achieve Financial Sustainability*, [GAO-13-562T](#) (Washington, D.C.: Apr. 17, 2013); *U.S. Postal Service: Urgent Action Needed to Achieve Financial Sustainability*, [GAO-13-347T](#) (Washington, D.C.: Feb. 13, 2013).

³In this report, we use the term “retirees” to refer to postal annuitants or any survivors of postal retirees who receive health benefits.

prefund retiree health benefits.⁴ USPS's reported unfunded liabilities for retiree health benefits combined with its other liabilities totaled \$96 billion at the end of fiscal year 2012.

To improve its finances, USPS has proposed establishing its own health care plan that would provide coverage for the approximately 1 million postal employees and retirees who are currently enrolled in the Federal Employees Health Benefits Program (FEHBP). USPS's plan is designed to increase postal retirees' enrollment in Medicare and take advantage of Medicare subsidies for employer-based prescription drug plans.⁵ To help finance its plan, USPS has proposed as one option a new fund that would inherit all assets (reported at approximately \$46 billion at the end of fiscal year 2012) of the Postal Service Retiree Health Benefits Fund (PSRHBF). The postal unions and management associations and an organization representing federal employees and retirees have raised concerns about

⁴The Postal Accountability and Enhancement Act (PAEA) established the Postal Service Retiree Health Benefits Fund (PSRHBF) and required USPS to begin prefunding the health benefits for its current and future postal retirees. Under the prefunding mechanism established by PAEA, as implemented by the Office of Personnel Management (OPM), USPS payments to OPM would be projected to fund the liability over a period in excess of 50 years, from fiscal years 2007 through 2056 and beyond (with rolling 15-year amortization periods after 2041). PAEA established "fixed" prepayment amounts—meaning that the amounts were set by statute and did not vary with actuarial measurements of the cost of the benefits—in the first 10 years, from fiscal years 2007 through 2016, with actuarially determined payments thereafter. However, the payments required by PAEA were significantly "frontloaded," with the fixed payment amounts in the first 10 years exceeding what actuarially determined amounts would have been using a 50-year amortization schedule. USPS has made a total of \$17.9 billion in prefunding payments, and a total of \$33.9 billion in required prefunding payments remain from the 10 years of fixed payments. Originally due at the end of fiscal year 2011, USPS's \$5.5 billion retiree health benefit payment requirement was delayed until August 1, 2012. Pub. L. No. 112-74, § 632, 125 Stat. 786, 928 (Dec. 23, 2011). USPS missed that payment, as well as the \$5.6 billion that was due by September 30, 2012.

⁵Medicare is the federally financed health insurance program for persons age 65 or over, certain individuals with disabilities, and individuals with end-stage renal disease. Medicare Parts A and B are known as Medicare fee-for-service. Medicare Part A covers hospital and other inpatient stays. Medicare Part B covers hospital outpatient, physician, and other services. Medicare beneficiaries have the option of obtaining coverage for Medicare services from private health plans that participate in Medicare Advantage—Medicare's managed care program—also known as Part C. All Medicare beneficiaries may purchase coverage for outpatient prescription drugs under Part D, either as a stand-alone benefit or as part of a Medicare Advantage plan.

or are opposed to USPS's proposed health care plan.⁶ Some of these groups have suggested that USPS should explore options for reducing costs within FEHBP. However, USPS has stated that it cannot sustain the current approach to providing health benefits and, unless its proposed health plan is implemented, will be unable to pay FEHBP premiums for current postal employees and retirees in future years.

With these issues in mind, you asked us to examine USPS's proposed health care plan. This report addresses (1) the potential effects of the proposed plan on USPS's financial condition; (2) the potential effects of the proposed plan on postal employees' and retirees' benefits and costs; and (3) the potential effects of a USPS withdrawal on FEHBP and on nonpostal FEHBP enrollees.

To describe the potential financial effects of USPS's proposed plan, we reviewed USPS documents detailing key elements of the plan and estimated cost savings. We obtained USPS's projections of its cash expenses, liability, and unfunded liability for health benefits, both under current law and its proposed health plan, as well as USPS's projections of the effect of its proposal on Medicare's total cash expenses. We obtained documentation regarding USPS's assumptions, methodology, calculations, underlying data, and projections. This documentation included reports and memorandums authored by the Hay Group (the actuarial contractor that USPS hired to prepare its projections), as well as responses to our questions on data reliability, including the systems used to compile the data, audits of those systems, and system controls to ensure data accuracy. According to USPS, the Hay Group's updated projections were prepared using valuation software that has been audited by other actuarial firms, and there were no material findings from such audits. USPS also stated that input data and actuarial assumptions used by the Hay Group came from the Office of Personnel Management's (OPM) Office of the Actuary. In addition, the USPS Office of Inspector General (USPS OIG) reported last year that previous USPS projections of the effect of its proposed health plan on its liability for retiree health care

⁶Joseph A. Beaudoin, President, National Active and Retired Federal Employees Association, *Solutions to the Crisis Facing the U.S. Postal Service*, a hearing of the Committee on Homeland Security and Governmental Affairs, United States Senate, 113th Cong., 1st Sess., Feb. 13, 2013.

were reasonable.⁷ As part of this review, the USPS OIG hired the Nyhart Company to review USPS's actuarial assumptions and projections; this company also performed independent actuarial valuations to compare to the Hay Group results. The Nyhart Company also concluded that the Hay Group's estimate of reduction in USPS's liability from USPS's proposed health plan was reasonable. While we did not independently validate the cost estimates, we reviewed these sources for internal consistency and consistency with our prior work and for overall reasonableness, and discussed them with officials of USPS and the Hay Group. Based on these procedures, and using our actuarial, economic, and health care expertise and judgment, we determined that the assumptions and projections were sufficiently reliable for purposes of our review. In addition, we reviewed relevant statutes, proposed legislation, and sections of the President's budget request for fiscal year 2014 pertaining to USPS's health care costs and the requirement for USPS to prefund its retiree health benefits. We interviewed officials from USPS, USPS OIG, the U.S. Treasury Department, OPM, postal unions, postal management associations, and an organization representing federal employees and retirees about USPS's proposal. We also interviewed the Centers for Medicare & Medicaid Services (CMS), and the Office of Management and Budget (OMB) to discuss the effect of USPS's proposal on Medicare, among other topics.

To determine the effect that USPS's proposal could have on postal employees' and retirees' benefits, we compared the package of services that USPS proposed to cover in the first year of implementation with the services covered in 2013 by seven selected FEHBP plans that collectively had more than 75 percent of the total postal enrollment in FEHBP.⁸ We also compared the coverage levels—the proportion of the cost for the

⁷USPS OIG, *U.S. Postal Service Alternative Health Care Plan Proposal: Management Advisory Report*, FI-MA-12-014 (Arlington, VA: Aug. 22, 2012).

⁸The seven FEHBP plans we selected had the highest numbers of postal enrollees of all FEHBP plans and together represented over 75 percent of postal enrollment in FEHBP in 2011, the most recent year of enrollment data available. All seven of the FEHBP plans that we selected were offered nationally. The selected plans included: the standard and basic options of the Blue Cross and Blue Shield Service Benefit Plan (which count as two plans using OPM's definition of plan), the NALC Health Benefit Plan (sponsored by the National Association of Letter Carriers), the American Postal Workers Union Health Plan, the Government Employees Health Association, Inc. Benefit Plan (which included both the high and standard options), the Mail Handlers Benefit Plan, and the Rural Carrier Benefit Plan.

service that the plan will pay—under the USPS plan and the selected FEHBP plans for 29 services, including a range of inpatient, outpatient, and prescription drug services.⁹ To determine the effect of the proposal on postal employees' and retirees' costs, we performed a number of analyses. First, we compared USPS's projected 2013 premiums for the three options under its proposed plan—the high, middle, and value options—with the 2013 premiums for the selected FEHBP plans and estimated the percentage of enrollees in the selected plans who would pay similar or lower premiums under USPS's proposed plan.¹⁰ Second, we assessed the effect on employees' and retirees' total costs—premiums plus any out-of-pocket costs for the use of care—of moving from FEHBP to the proposed postal plan. To do so, we compared other elements of USPS's proposed plan that could influence out-of-pocket costs, including deductibles and out-of-pocket maximums, with the selected FEHBP plans.¹¹ We also estimated what employees and retirees would pay at different levels of total annual cost, that is, the total cost claimed by providers, under USPS's proposed high and middle options

⁹We selected services for which the USPS plan and all selected FEHBP plans provided some level of coverage. We compared coverage levels for services received in the plans' approved network of providers, i.e., "in-network services," and services received outside of the approved provider network, i.e., "out-of-network services." Our comparison of coverage levels accounted for the interaction of the different plans with Medicare. We excluded one of the selected FEHBP plans from this comparison because the structure of benefits for the plan was not comparable to that under the proposed USPS plan.

¹⁰For 2013 FEHBP premiums, we used publicly available data from OPM. We defined "similar" premiums as those within 10 percent of the premium the employee or retiree would have paid in 2013 for their FEHBP plan and "lower" premiums as those more than 10 percent less than the FEHBP premium. Our analysis accounted for the Medicare Part B premiums for those Medicare-eligible retirees who were in selected FEHBP plans who were not enrolled in Medicare Part B, since all Medicare-eligible retirees would be assumed to enroll in Medicare Part B under the proposed USPS plan.

¹¹We excluded one of the selected FEHBP plans from this comparison because the structure of the deductibles and out-of-pocket maximums was not comparable to those under the proposed USPS plan.

and under the FEHBP plan with the largest number of postal enrollees.¹² To determine the extent to which employees and retirees would have the same legal protections related to employees' and retirees' benefits and costs under USPS's proposed plan as they have within FEHBP, we reviewed draft legislation proposed by USPS, federal laws, regulations, and OPM guidance that apply to FEHBP plans. We supplemented our review by interviewing officials from USPS and OPM, as well as representatives from postal unions and management associations about the potential effects of the USPS proposal on employees and retirees.

To describe the effects of a USPS withdrawal on FEHBP and on nonpostal FEHBP enrollees, we used OPM data on postal and nonpostal enrollment in FEHBP in 2011 to estimate the change in total program enrollment and the age distribution of enrollees. We also used the data to estimate the effect on enrollment in each of the more than 140 FEHBP plans. Using OPM data on the plans offered in each state and the premiums charged for those plans in 2013, we determined choices that nonpostal enrollees would have in the event that a USPS withdrawal led a health plan to leave FEHBP. To supplement this analysis, we interviewed OPM officials and representatives from 10 selected FEHBP plans to discuss how a USPS withdrawal would affect nonpostal enrollees, plan participation in FEHBP, and premium rates.¹³ We took a number of steps to assess the reliability of the OPM data including interviewing OPM officials on the limitations of the data and checking the data for inconsistencies and anomalies. We determined the data to be sufficiently reliable for the purposes of estimating changes in enrollment and

¹²We estimated enrollee costs if total annual costs of health care were \$2,500, \$10,000, \$17,000, and \$50,000. For each cost scenario, we assumed a distribution of costs across inpatient and outpatient services and prescription drugs. For example, at \$2,500 in total annual costs, we assumed that about 47 percent of costs were for outpatient services and the rest of costs were for prescription drugs; and, at \$50,000 in total annual costs, we assumed 67 percent was for inpatient care, 32 percent for outpatient care, and 1 percent for prescription drugs. We based our assumptions on those used by USPS's contracted actuaries in estimates that they performed, because we did not have data on the distribution of costs in FEHBP across these categories; and we conducted a sensitivity analysis to ensure that our results were not overly sensitive to the assumptions. We applied the cost-sharing requirements of each plan to the costs in each service category and then added premium costs to estimate total enrollee costs.

¹³The selected plans together comprised over 70 percent of FEHBP enrollment and ranged in the percentage of enrollment that postal employees and retirees represented from over 90 percent to less than 10 percent. Several of the selected plans were offered by the same carrier. In total, we spoke to officials from six carriers.

illustrating the choice in plans that nonpostal enrollees would have if their plan withdrew from FEHBP; where relevant we stated the limitations of the data in the findings.

We conducted this performance audit from September 2012 to July 2013 in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

Background

Current USPS Health Benefits Provided Through FEHBP

USPS currently participates in FEHBP, a program administered by OPM that offers a choice of health plan options to all postal and nonpostal federal employees and retirees.¹⁴ More than 140 health plans participate in FEHBP; these include fee-for-service plans and health maintenance organizations (HMO). The specific options available to enrollees depend on where one lives since fee-for-service plans are generally offered nationally while HMOs offer coverage in selected areas.¹⁵ FEHBP plans generally cover a comprehensive array of medical services, including inpatient and outpatient services and prescription drugs. However, plans offer different levels of benefits, with many plans offering a choice between a more expensive option, which offers a higher level of coverage and a less expensive option, which offers a lower level of coverage. Premium prices also vary across plans and within plans and depend on whether one is enrolled in self-only coverage or family coverage. FEHBP enrollees can change health care plans during an annual open enrollment period or when they experience a qualifying life event, such as a change

¹⁴Additionally, OPM oversees FEHBP, including contracting with participating plans, reviewing proposed benefits and premiums, issuing guidance, and responding to enrollees' appeals of benefit denials. FEHBP is unique in that OPM plays the role of employer sponsor as well as having responsibility for oversight.

¹⁵In 2011, the most recent year of data available, 80 percent of FEHBP participants were enrolled in fee-for-service plans and 20 percent in HMOs, and the distribution among postal enrollees was about the same.

in family status. According to OPM officials, an average of 5 percent of enrollees changed plans annually from 2003 through 2010.

Postal employees also pay Medicare taxes and therefore may become eligible for Medicare coverage generally at age 65. For retirees enrolled in Medicare and FEHBP, including postal retirees, Medicare is the primary insurer, and the FEHBP plans generally cover any expenses that Medicare does not cover. Eligible retirees are not required to enroll in Medicare. According to FEHBP data, in 2011, about 22 percent of eligible postal retirees in FEHBP were not enrolled in Medicare coverage of outpatient services, known as Part B, and 8 percent were not enrolled in Medicare coverage for hospital services (Part A).¹⁶ According to an OPM actuary, most eligible FEHBP retirees do not enroll in prescription drug coverage under Medicare (Part D). FEHBP plans provide prescription drug coverage that is as good or better than Medicare.¹⁷ There is no penalty for choosing not to enroll in Medicare; however, retirees who later decide to enroll in Part B must pay a penalty.¹⁸ For retirees in FEHBP who choose not to enroll in Medicare, their FEHBP plan remains the primary payer and they would continue to receive the same level of coverage through that plan as they did prior to becoming eligible for Medicare.

USPS and its employees and retirees share the cost of health care benefit premiums.¹⁹ For fiscal year 2012, USPS reported paying \$5.2

¹⁶For most people, Medicare Part A is premium-free unless the beneficiary or spouse has worked fewer than 40 quarters in his or her lifetime, but the beneficiary is responsible for required deductibles, coinsurance, and copayment amounts. Beneficiaries must pay a premium for Part B coverage, which generally was \$99.90 per month in 2012. Beneficiaries are also responsible for Part B deductibles, coinsurance, and copayments.

¹⁷When private coverage for prescription drugs is at least as good as the coverage under Part D, then retirees do not need to enroll in Part D. If retirees later chose to cancel their private health insurance, Medicare would permit them to enroll in Part D without penalty, subject to some restrictions. For example, there are limitations on how much time can elapse between canceling private insurance coverage and enrolling in Part D.

¹⁸Medicare beneficiaries generally would be billed an extra 10 percent of their monthly premium for each full 12-month period that they were eligible for Part B coverage but did not sign up for it.

¹⁹The federal government also absorbs some costs for those employees whom also had service with the United States Post Office Department (predecessor to USPS) which is prorated to reflect the number of years of such service by postal retirees. 5 U.S.C. § 8906(g).

billion toward employee premiums, an amount that represented 78 percent of the premium cost (see table 1). USPS's share of the premium cost for employees is established through collective bargaining with its four major postal unions and in consultation with its three management associations. If USPS and its unions cannot agree on the share of premium costs, the share is determined in binding arbitration. The law requires USPS's employee benefits to be at least as favorable as those in effect when the Postal Reorganization Act of 1970 was enacted.²⁰ USPS's contribution rates for employees have historically been higher compared to the rates paid by other federal agencies for federal employees,²¹ but USPS's contribution rates will be decreasing in the coming years under current agreements with its unions and management associations.²² USPS's share of premium costs for postal retirees is set according to a statutory formula and is not subject to negotiation with its unions. In fiscal year 2012, USPS reported it paid \$2.6 billion toward the costs of current retirees' health benefit premiums. In addition to paying a portion of retiree premiums, USPS has been required since 2007 to make annual payments to prefund retiree health benefits.²³ However, USPS failed to make those payments in fiscal years 2011 and 2012.²⁴ USPS's failure to make its prefunding payments notwithstanding, health care expenses represent a significant portion of total USPS expenses.

²⁰39 U.S.C. § 1005(f).

²¹As set by statute, for current nonpostal employees as well as both postal and nonpostal retirees and survivors, the government pays 72 percent of the average premium across all FEHBP plans but no more than 75 percent of any particular plan's premium. 5 U.S.C. § 8906(b).

²²More than 85 percent of USPS career employees are covered by collective bargaining. Under the current collective bargaining agreements and arbitration awards, USPS's contribution for health care premiums for these employees will decrease to approximately 76 percent in 2016. Managers are not covered by collective bargaining agreements and are compensated under a pay-for-performance program. Under the current pay packages, USPS's contributions for these employees will decrease to approximately 72 percent in 2015.

²³5 U.S.C. § 8909a(d)(3)(A).

²⁴Originally due at the end of fiscal year 2011, USPS's \$5.5 billion retiree health benefit payment was delayed until August 1, 2012. Pub. L. No. 112-74, § 632. USPS missed that payment as well as the \$5.6 billion payment that was due by September 30, 2012, resulting in \$11.1 billion of missed payments in 2012.

Table 1: USPS Health Benefits Payments, Fiscal Years 2007 through 2012

Dollars in billions

Fiscal year	Premium payments for employee health benefits	Premium payments for retiree health benefits	Prefunding payments made for retiree health benefits	Total USPS payments for health benefits
2007	\$5.4	\$1.7	\$5.4	\$12.5
2008	5.4	1.8	5.6	12.8
2009	5.3	2.0	1.4	8.7
2010	5.1	2.2	5.5	12.9
2011	5.2	2.4	0.0	7.7
2012	5.2	2.6	0.0	7.8

Source: USPS.

Note: Numbers may not add to total due to rounding. Health benefit premium payments were made by USPS to the OPM-managed Employee Health Benefits Fund that finances the FEHBP. Retiree premium payments were for postal retirees and survivors participating in FEHBP. Prefunding payments were statutorily required payments from USPS to the OPM-managed PSRHB. 5 U.S.C. § 8909a. A looming USPS cash shortfall necessitated last-minute congressional action to defer costs by reducing the 2009 prefunding payment from \$5.4 billion to \$1.4 billion. Pub. L. No. 111-68, div. B, § 164(a), 123 Stat. 2023 (Oct. 1, 2009). Due to subsequent cash shortfalls, USPS did not make its \$5.5 billion and \$5.6 billion retiree health benefit prefunding payments that were due in fiscal year 2012 (\$5.5 billion of which had been statutorily delayed from fiscal year 2011 to fiscal year 2012). Under accounting standards, these required prefunding contributions are included in USPS's expenses for financial reporting purposes, regardless of whether the payments are actually made; missed payments are reported as a liability on USPS's balance sheet. Thus, USPS's expenses exceeded its payments for health benefits in fiscal year 2012 by the \$11.1 billion required prefunding contributions that were due but not paid—so that USPS's reported expenses for health care in fiscal year 2012 were \$18.9 billion, whereas its actual health care payments were only \$7.8 billion.

In December 2012, we reported that USPS's deteriorating financial outlook will make it difficult to continue the current schedule for prefunding postal retiree health benefits in the short term, and possibly to fully fund the remaining \$48 billion unfunded liability over the remaining decades of the statutorily required actuarial funding schedule.²⁵ However, we also reported that deferring funding could increase costs for future ratepayers and increase the possibility that USPS may not be able to pay for some or all of its liability. Our 2012 report discussed various funding approaches, the related short- and long-term effects, and key factors for Congress to consider in restructuring USPS's current retiree health benefit prefunding requirements. We continue to believe that it is

²⁵GAO, *U.S. Postal Service: Status, Financial Outlook, and Alternative Approaches to Fund Retiree Health Benefits*, [GAO-13-112](#) (Washington, D.C.: Dec. 4, 2012).

important for USPS to prefund these benefits to the maximum extent that its finances permit, recognizing that multiple options exist to prefund benefits and amortize unfunded liability.

USPS's Proposed Health Care Plan Elements and Legislative Changes

USPS's health care proposal to withdraw from FEHBP and administer its own health plan includes a number of key elements that are designed to reduce USPS's cost of providing health care benefits (see table 2). The USPS plan would be available to about 498,000 current employees and about 477,000 retirees and would have benefits of comparable aggregate "actuarial value" to the largest FEHBP plan in the first year of implementation.²⁶ After the first year, benefits for current retirees must continue to meet that standard, and while the standard will no longer apply for employees, any changes to employee benefits would be subject to collective bargaining.²⁷

The USPS plan would include high, middle, and value options that would range in price. USPS would self-insure the benefits—that is, USPS would set aside funds to pay for benefits rather than purchasing insurance from an insurance company. USPS plans to hire a health insurance company to administer its proposed plan, a plan that would include processing claims, negotiating payment rates with health care providers, and providing wellness and disease management programs.²⁸ (See appendix I for more information on the USPS proposed health plan.)

²⁶The USPS legislative proposal specifically indicates that the type and the average level and value of a plan's benefits will be benchmarked against the type and level of benefits provided under FEHBP and that the "aggregate actuarial value of benefits shall be at least equivalent to that of the FEHBP plan with the highest enrollment." For those eligible for Medicare, the aggregate actuarial value will include the value of Medicare benefits. The actuarial value of the benchmarked coverage would be documented in an actuarial opinion that meets actuarial standards of practice. Note that "actuarial value," as used in this context, is a limited concept that measures the estimated value of benefit coverage, but does not take into account premium costs, and so does not capture estimated total out-of-pocket costs for a typical participant. Two different health insurance plans could have the same actuarial value but very different participant premiums.

²⁷Under USPS's plan, benefits for employees who retire after the USPS plan is implemented, i.e., "future retirees," do not have to meet the comparability standard described in the preceding footnote.

²⁸USPS officials also anticipate contracting to administer pharmacy benefits. In addition, USPS officials said they also may contract with HMO plans in certain geographic locations.

Under one financing option (which USPS refers to as “Scenario 2”), USPS would pay for health benefits out of a newly created Postal Service Health Benefits Fund (HBF), which would include some portion of reserve funds currently set aside for FEHBP and all funds from the PSRHBF, which would be abolished upon its transfer to the HBF. Under Scenario 2, USPS proposes that it be allowed to invest the HBF in non-Treasury securities, such as investments in stocks and private sector bonds, under the oversight of a USPS-appointed committee. According to USPS, assets of this fund would not be federally guaranteed, except for those invested in federally guaranteed securities. USPS has also proposed another option for financing its health plan (which USPS refers to as “Scenario 1”) under which the Congress could leave the funds in the PSRHBF, so that retiree health benefits under the proposed USPS plan would continue to be financed out of the PSRHBF. See appendix II for more detail on these aspects of the USPS proposal, which are discussed further in the next section of this report.

Table 2: Key Elements of the Proposed USPS Health Care Plan

Element	Description
100% participation of eligible retirees in Medicare Parts A and B	USPS’s plan is designed so that all Medicare-eligible retirees would enroll in Medicare Parts A and B. Those who do not enroll would have their benefits reduced by the amount Medicare would have paid had the individual enrolled. As is the case under FEHBP, Medicare would serve as the primary payer of health care costs, and for existing retirees, the USPS plan would cover 100 percent of any costs above the amounts covered by Medicare Parts A and B.
Prescription drug benefits that qualify the plan for federal subsidies and drug discounts	USPS would design the prescription drug benefits under its plan to qualify as an Employer Group Waiver Plan (EGWP) under Medicare Part D. This would qualify USPS to receive—for those eligible for Medicare—a federal subsidy from the Medicare program for drug costs, a discount from pharmaceutical companies for brand name drugs, and federal coverage for drug costs above a catastrophic limit.
Introduction of two new tiers of coverage	The proposed plan would include four coverage tiers: self only, self and spouse, self and children, and self and family. Premiums for each tier would be set according to the claims experience of the group. USPS’s proposed addition of two tiers (self and spouse and self and children) to the options available under FEHBP would be to reflect the various stages of family status that participants may experience over the course of their career and retirement.
Purchasing plan administration services from a single vendor through a competitive bidding process	USPS would contract with a single vendor to administer its plan; that vendor would negotiate with providers for payment rates, process claims, and provide wellness and disease management programs.
Requirement that future retirees be subject to plan deductibles and cost-sharing upon enrolling in Medicare	For employees retiring a year or more after the USPS plan becomes effective (i.e., “future retirees”), Medicare would be the primary insurer once the enrollee becomes eligible, and the USPS plan would cover costs above what Medicare pays. However, future retirees would be required to meet the USPS plan deductible and pay coinsurance.

Element	Description
USPS Health Benefits Fund	<p>Under one option of USPS's proposal (which USPS refers to as "Scenario 2"),^a its health plan would be financed by a newly created fund called the HBF that would include: (1) the entire Postal Service Retiree Health Benefits Fund that would be abolished upon its transfer to the HBF; (2) the balance of the fund that finances FEHBP allocable to contributions by USPS, postal employees and retirees, including any reserve fund amounts; (3) USPS contributions under its health plan; (4) contributions of postal employees and retirees under the USPS health plan; (5) any interest on HBF investments; (6) any other USPS receipts allocable to the USPS health benefits plan; and (7) appropriations based on the service of officers and employees of the former U.S. Post Office Department.</p> <p>Under its proposal, USPS would be authorized to invest HBF assets without the approval of the Secretary of the Treasury in non-Treasury securities, such as stocks and bonds, as well as commodities, foreign currency, and real property. Also, USPS indicates that HBF assets could not be used for (1) loans to USPS, such as to enable it to remain solvent; (2) USPS payments to the federal government, such as for pensions and workers' compensation; or (3) to finance USPS investments or USPS nonpostal initiatives to generate revenue.</p> <p>In any year when the amount of HBF assets exceeds USPS's estimated actuarial liability for retiree health benefits, USPS could authorize the surplus amount to be transferred to the Postal Service Fund that finances most USPS expenses, provided that such authorization is made pursuant to a recommendation by a majority of the Committee overseeing the HBF.</p>
USPS funding of retiree health benefits	USPS would continue to prefund retiree health benefits, but under a purely actuarial approach, without the fixed (non-actuarial) payments required under current law through 2016. Payments to the HBF would be based on the "normal cost" and amortization of any unfunded liability or surplus of its retiree health care liabilities over an amortization period ending at the later of 40 years after implementation or 15 years from the then-current year.

Source: GAO analysis of USPS information.

^aUSPS has also proposed another option for financing its health plan (which USPS refers to as "Scenario 1") under which retiree health benefits would continue to be financed from the PSRHB.

According to USPS officials:²⁹

- USPS cannot implement its proposed health plan without changes to federal law. Although USPS already has limited authority to move current employees from FEHBP into a USPS-run plan, it would need

²⁹GAO did not independently verify USPS's statements regarding its current authority or the need for additional authority as provided herein.

additional statutory authority to allow the USPS Board of Governors to establish initial health benefits and premiums for this plan.³⁰

- Legislation would be needed to move postal retirees out of FEHBP and into a USPS plan. With regard to the portions of its plan that interact with Medicare, if given the authority to move retirees into a USPS plan, USPS already has the authority to design the program in such a way to reach 100 percent participation in Medicare and to allow USPS to participate in an Employer Group Waiver Plan (EGWP).³¹
- USPS would need legislation to create a special enrollment period for those Medicare-eligible retirees who previously chose not to enroll in Parts A and B—similar to the special enrollment periods currently available—and to exempt these enrollees from the financial penalty for late enrollment in Medicare Part B.
- Finally, USPS would need legislation to access assets in the PSRHB, eliminate statutorily fixed prefunding payments for retiree health benefits, and restructure statutory requirements for amortizing any unfunded liabilities for retiree health benefits.

Some elements of USPS's proposed health care plan are being explored on a smaller scale within FEHBP. For example, OPM currently has a pilot under way to try to increase enrollment in Medicare by providing the incentive that the FEHBP plan would pay the Part B premium on behalf of the enrollee. In 2013, the second year of implementation, only one FEHBP plan and 2,400 enrollees were participating in the pilot, and there were no measurable effects on cost. In addition, as of March 2013, OPM officials said that the agency was in discussions with several plans about restructuring plans' drug benefits to receive federal subsidies under Medicare Part D, as USPS is planning to do under its proposal. However, OPM officials said that the agency does not have the authority to introduce some of the measures that USPS is proposing. For example, FEHBP plans cannot achieve 100 percent participation in Medicare using

³⁰According to USPS officials, USPS has the authority under current law to move employees from FEHBP to a USPS plan, subject to reaching a collective bargaining agreement for those employees represented by collective bargaining. However, negotiating for this change through the collective bargaining process also would subject the initial benefit package and contribution rates to collective bargaining. Thus, a statutory change is needed to allow the initial benefit package and premium amounts to be set by the Board of Governors.

³¹According to USPS officials, USPS would contract with a prescription drug plan sponsor to implement the EGWP.

the approach that USPS has proposed. According to officials, the agency also does not have the authority to introduce additional tiers of coverage, such as the self-and-spouse and self-and-children tiers included in the proposed USPS plan. In April 2013 testimony, OPM proposed that it be provided with more flexibility to take additional measures to contain drug costs, increase competition, and introduce a new tier of coverage in FEHBP.³²

USPS Would Likely Realize Large Financial Benefits from Its Health Plan, Mainly by Increasing Retirees' Use of Medicare, but Some Plan Elements Could Decrease Funds Available for Retiree Health Benefits in the Future

USPS would likely realize large financial benefits from its proposed health plan, with USPS estimating that it would: (1) reduce its retiree health benefit liability by \$54.6 billion, thereby eliminating its unfunded retiree health benefit liability; (2) reduce its required payments by \$7.8 billion in the first year of implementation; and (3) reduce its required payments by \$33.2 billion over the first 5 years of implementation. Most of the financial benefits from the proposed plan would result from increasing postal retirees' use of Medicare, thereby increasing Medicare costs. In addition, some elements of USPS's proposal could lead to decreased funds available for retiree health care in the future. First, one proposed option for investing health plan assets could leave plan assets exposed to risk of loss. Second, the ability to transfer surplus funds to use for purposes other than health benefits could result in unfunded liabilities. Third, the process for selecting economic and demographic assumptions could create risks of excessive surplus transfers or inadequately funded retiree benefits. Lastly, the collective bargaining process could result in binding arbitration that is not required to consider USPS's financial condition—which could result in higher costs and thus unfunded liabilities.

³²Jonathan Foley, Director, Planning and Policy Analysis, OPM, *The Federal Employees Health Benefits Program*, testimony before the Subcommittee on Federal Workforce, U.S. Postal Service, and the Census, Committee on Oversight and Government Reform, United States House of Representatives, 113th Cong., 1st Sess. (Apr. 11, 2013).

USPS Projects Large Financial Gains from Its Health Plan and Improved Liquidity, Largely by Increasing Medicare Use

USPS would likely realize large financial gains from reducing its liabilities for retiree health care through implementation of its proposed health plan. USPS projects its health plan assets would slightly exceed its liability for retiree health care. It estimates a liability reduction of \$54.6 billion—resulting in a \$3.7 billion surplus instead of a \$50.9 billion unfunded liability if the plan were implemented on January 1, 2014 (see table 3).³³ USPS projects that its plan would immediately eliminate its existing unfunded liability for retiree health care, which was \$47.8 billion at the end of fiscal year 2012.³⁴ Consistent with this projection, USPS has proposed that Congress eliminate its statutorily fixed prefunding payments. However, it is important to recognize that elimination of an existing unfunded liability does not necessarily eliminate the need for continued prefunding payments. The existing workforce would continue to earn future retirement benefits that must be funded, as USPS proposes to do. In addition, liability measures of this type are subject to significant revision or fluctuation, and are likely to change, as underlying economic and demographic experience and estimates change. USPS's proposal calls for additional payments, on an actuarial basis, as needed, to pay for ongoing benefit accruals for its workforce³⁵ and to amortize any unfunded liability for retiree health benefits.

³³The estimates in this section address the implications of USPS's proposal for prefunding and for USPS's cash flow and liquidity. USPS's proposal would have different implications for its financial reporting (its accounting costs). USPS currently accounts for the costs of its participation in FEHBP using a "multiemployer" plan basis under the accounting standards, under which accounting costs are set to match USPS's required payments. Under USPS's proposed plan, its accounting would switch to a "single employer" plan basis under the accounting standards. On a single employer plan basis, USPS would recognize any unfunded liability (or overfunded asset) for retiree health care benefits on its balance sheet based on the accounting standards (which measure the unfunded liability differently than the measure used for funding purposes discussed in the report), would accrue expense on an actuarial basis rather than a current-required-payments basis, and would use a different basis for setting assumptions for estimating the cost of future retiree benefits.

³⁴USPS has no unfunded liability for health benefits provided to current employees, which are financed by USPS on a pay-as-you-go basis.

³⁵The cost of these future retirement benefits attributable to a year of employees' service is called the "normal cost."

Table 3: USPS-Projected Liabilities and Assets for Retiree Health Care under FEHBP and the USPS Proposed Health Plan, Projected to September 30, 2014

Dollars in billions	
Liability for retiree health care under FEHBP	100.0
Assets for retiree health care under FEHBP ^a	49.1
Unfunded liability under FEHBP	50.9
Change in liability from FEHBP to USPS's health plan	(54.6)
Remaining liability under USPS's health plan	45.4
Assets for retiree health care under USPS health plan	49.1
Unfunded liability (surplus) under USPS health plan	(3.7)

Source: USPS.

Note: For purposes of these projections, USPS's health plan would begin on Jan. 1, 2014.

^aFor purposes of these projections, assets supporting the USPS health plan were assumed to continue to be invested in special-issue Treasury securities. These assets were assumed to initially consist of the assets of the PSRHBF that would be transferred into a newly-created HBF supporting the USPS health plan. The assets of this new fund did not include a portion of the FEHBP reserve fund that USPS is proposing to be transferred into the new fund.

Increased use of Medicare under USPS's proposed plan would account for most of the projected reduction in USPS's liability for retiree health costs (i.e., reduction in future USPS health costs) and increase the federal government's future Medicare net spending. First, USPS's proposal would lead to greater enrollment of eligible postal retirees in Medicare Parts A and B,³⁶ with Medicare acting as the primary insurer for those enrollees and the USPS plan paying costs above what Medicare would cover for current retirees.³⁷ Second, USPS would receive a Medicare subsidy from participating in a Medicare Part D Employer Group Waiver Plan (EGWP), as well as benefits from discounts from drug suppliers on brand-name drugs. According to USPS, these two elements of the plan are responsible for \$48.8 billion, or 89 percent, of the \$54.6

³⁶As of the end of 2011, about 8 percent of Medicare-eligible postal retirees were not enrolled in Medicare Part A and 22 percent were not enrolled in Medicare Part B—slightly lower than the nonpostal FEHBP population, of which 11 percent and 25 percent did not enroll in Parts A and B, respectively.

³⁷Future retirees would not receive 100 percent coverage from the combination of Medicare and the proposed USPS plan, since the USPS plan proposes requiring that future retirees pay all costs up to the plan deductible and a portion of additional costs for care.

billion projected reduction in USPS's liability for retiree health benefits, assuming the plan is implemented on January 1, 2014 (see table 4).

Table 4: USPS-Projected Reduction in Its Liability for Retiree Health Benefits, Projected to September 30, 2014

Dollars in billions	
Aspect of proposed plan	
All eligible postal retirees enroll in Medicare Parts A & B	(23.1)
USPS participates in Medicare Part D EGWP	(25.7)
Subtotal: Medicare-related elements	(48.8)
Other elements of USPS health plan ^a	(1.8)
Use different assumptions to estimate USPS liability ^b	(4.1)
Total	(54.6)

Source: USPS.

Note: Numbers may not add to total due to rounding. For purposes of these projections, USPS's health plan would begin on Jan. 1, 2014.

^aUSPS projected a \$3.6 billion liability reduction from adding cost exposure for future retirees and a \$1.6 billion liability reduction that USPS projects it would achieve from contracting with a single vendor to administer its health plan, including processing claims, negotiating payment rates with health care providers, and providing wellness and disease management programs; these projected reductions were partially offset by a \$3.4 billion projected liability increase from the four-tier structure of the proposed USPS health plan.

^bUSPS estimated its liability for retiree health benefits using assumptions consistent with those that OPM uses to determine USPS's funding requirements for federal pension programs. These assumptions are not the same as those used by OPM to estimate USPS's liability for retiree health benefits. Current law requires OPM to determine the value of USPS's retiree health benefit liability based on actuarial assumptions that are consistent with those used by OPM for its financial reporting of liabilities for federal employee benefits.

Turning to the projected impact of USPS's proposed health plan on USPS's liquidity, the implementation of USPS's proposed health plan for current postal employees as well as retirees is projected by USPS to result in lower costs and thus greater liquidity for the Postal Service Fund, which is used to finance most USPS expenses.³⁸ Under current law, USPS projects that its required payments for health care will total \$61.8 billion for the 5-year period of 2014 through 2018. Whereas under its proposed plan, it projects those payments would be reduced by \$33.2

³⁸The Postal Service Fund is a revolving fund established in the U.S. Treasury for the deposit of all revenues, interest, appropriations, proceeds from borrowing, or any other receipts from USPS's operations. The fund is available to USPS to carry out the purposes, functions, and powers of USPS. 39 U.S.C. § 2003.

billion over this period, with the first-year reduction being \$7.8 billion (see table 5).³⁹ About half of this \$33.2 billion difference (\$17.2 billion) would result from eliminating required fixed payments to prefund retiree health benefits from 2014 to 2016.

Table 5: Projected USPS Payments from the Postal Service Fund for Health Benefits under FEHBP and USPS's Proposed Health Plan

Dollars in billions						
	2014	2015	2016	2017	2018	Total
USPS payment requirements from the Postal Service Fund under FEHBP under current law	13.6	13.7	14.0	10.2	10.3	61.8
USPS payments from the Postal Service Fund under proposed USPS health care plan	5.8	5.8	5.7	5.7	5.6	28.6
Difference	7.8	7.9	8.3	4.5	4.7	33.2

Source: USPS.

Note: Years are calendar years.

USPS made a separate calculation of the expected effect of its proposed plan on its short-term liquidity. Under this calculation, USPS assumed that it would continue to not make prefunding payments required by current law, but that it would pay for its share of premium payments for workers and retirees. It compared these expected payments to its expected payments under its proposed new health care plan. Under this calculation, USPS would reduce its payments by \$2.1 billion in 2014 and by \$12.4 billion over the 2014 to 2018 period. Close to half of the estimated first-year savings of \$2.1 billion would result from reducing USPS's premium costs for retirees, largely due to the Medicare-related elements of the USPS health plan. In addition, USPS projects that about

³⁹While USPS projects that its required payments for health care will total \$61.8 billion over 2014 through 2018 under current law, USPS officials also have stated that USPS would not be able to make this level of required payments. The required payments for health care under current law consist of USPS's share of premium payments for its workers, plus retiree health prefunding payments, plus, through fiscal year 2016 only, USPS's share of premium payments for retirees. In addition, USPS's proposal would eliminate the existing \$11.1 billion owed for missed prefunding payments in 2012, plus another \$5.6 billion assuming the 2013 required prefunding payment is missed as well. Adding in the elimination of this \$16.7 billion would increase the 5-year savings from \$33.2 billion to \$49.9 billion.

\$0.5 billion of the \$2.1 billion would result from lower costs for employees.⁴⁰

The estimated liquidity improvement reflects the lower costs expected from moving out of FEHBP, where enrollee premiums reflect a large minority of Medicare-eligible retirees who do not enroll, to a USPS plan where all Medicare-eligible retirees are presumed to enroll. USPS also estimates that some of the liquidity improvement would result from efficiencies gained in contracting with a single vendor to administer its health plan. Some postal employee organizations have objected to having postal employees and retirees withdrawn from FEHBP, with one union official testifying that there is potential for some cost savings for USPS within FEHBP.⁴¹

Neither CMS nor OMB has estimated the potential short- or long-term effects of the USPS proposal on Medicare costs or the net effects on the federal budget. However, as to the short-term effect, USPS projected that its plan would increase the more than \$550 billion spent annually for Medicare by \$1.0 billion in the first year of its proposed health plan and an average of roughly \$1.3 billion annually in the first 5 years of its health plan—about 0.2 percent of Medicare’s annual costs.⁴² We have previously reported that Medicare is on a path that is fiscally

⁴⁰The remaining portion of the reduction in payments under this alternative calculation by USPS would result from making actuarial prepayments instead of pay-as-you-go premium payments for retiree benefits.

⁴¹Fredric V. Rolando, President, National Association of Letter Carriers, *Solutions to the Crisis Facing the U.S. Postal Service*, testimony before a hearing of the Committee on Homeland Security and Governmental Affairs, United States Senate, 113th Cong., 1st Sess. (Feb. 13, 2013).

⁴²These projections factor in additional Medicare spending for Parts A and B and drug subsidies under the EGWP, offsetting Part B contributions from additional postal retirees enrolling in Part B, and offsetting drug discounts under the EGWP. USPS projected that the total cost to the federal government would be less than the \$1 billion increase in Medicare spending in the first year of implementation, because USPS’s plan would reduce health care premiums for postal retirees some of which is financed by the federal government. USPS estimates that the proposal would reduce the federal share of postal retiree premiums by about \$300 million annually. As previously noted, the federal government also absorbs some costs for those employees who also had service with the United States Post Office Department, which is prorated to reflect the number of years of such service by postal retirees. 5 U.S.C. § 8906(g).

unsustainable over the long term.⁴³ Spending for Medicare Part A already exceeds dedicated revenue, and the Part A trust fund is currently expected to be exhausted by 2026. Total Medicare spending is expected to increase as a share of GDP in coming decades, putting greater pressure on the rest of the federal budget. While there are significant uncertainties about the future growth of health care spending, particularly related to the sustainability of cost containment mechanisms over the long term, additional costs from USPS's proposed plan would also have to be weighed alongside the fiscal pressure already faced by Medicare.

**Some Elements of
Proposed Plan Could
Reduce Funds Available
for Retiree Health Care in
the Future**

**Potential Decrease in Future
USPS Health Plan Assets**

Some elements of USPS's proposal could reduce funds available for health care in the future, including one proposed option for managing health plan assets; the disposition of health plan assets deemed "surplus;" and the assumptions used to calculate liabilities.

Under one option of USPS's legislative proposal (which USPS refers to as "Scenario 2"), assets supporting its health plan could be invested in stocks, private sector bonds, and other non-Treasury securities exposed to risk of loss.⁴⁴ Currently, as with the Postal Service Fund that USPS uses to pay most of its expenses, all assets of the PSRHBF are invested solely in special-issue Treasury securities backed by the full faith and credit of the federal government. In contrast, USPS has stated that it would seek increased investment returns on assets of a newly created HBF. Under Scenario 2, the HBF would inherit all of the assets of the existing PSRHBF (reported at \$45.7 billion at the end of fiscal year

⁴³See GAO, *High-Risk Series: An Update*, [GAO-13-283](#) (Washington, D.C.: February, 2013); *Medicare: Program Remains High Risk Because of Continuing Management Challenges*, [GAO-11-430T](#) (Washington, D.C.: Mar. 2, 2011); and *The Federal Government's Long-Term Fiscal Outlook: Spring 2013 Update*, [GAO-13-481SP](#) (Washington, D.C.: Apr. 11, 2013).

⁴⁴For example, plan assets could be invested in commodities, foreign currency, and real property. The plan also could acquire a controlling interest in stock of a private company, subject to certain limitations. USPS investment of plan assets would not require approval of the Secretary of the Treasury. See app. II for more detail.

2012).⁴⁵ Other assets of the HBF would include a portion of the current OPM-managed Employee Health Benefits Fund that supports FEHBP⁴⁶ that would be transferred to USPS, as well as ongoing contributions from USPS and from employees and retirees participating in the plan.

Under Scenario 2, USPS's investment policy for the HBF would be managed by a Committee subject to specified provisions of the Employee Retirement Income Security Act of 1974 (ERISA)⁴⁷ pertaining to certain fiduciary duties and responsibilities. ERISA requires that plan assets be managed solely in the interest of plan participants and their beneficiaries for the exclusive purpose of providing benefits and defraying plan expense; with the care, skill, prudence and diligence of a prudent man acting in a like capacity; and to generally diversify the assets so as to minimize the risk of large losses.

Large private sector pension plans typically invest substantial portions of plan assets in asset classes such as stocks, often including some allocation to "alternative" asset classes such as private equity or hedge funds.⁴⁸ While such types of investments can offer the potential for

⁴⁵Under Scenario 2, the PSRHBF would be abolished upon transfer of its assets to the new HBF. Under a separate option (which USPS refers to as "Scenario 1") the PSRHBF would be continued and used to finance retiree health benefits under USPS's health plan. See app. II for more detail.

⁴⁶See app. II for more detail.

⁴⁷ERISA governs most private sector benefit plans. The USPS proposal would provide that Committee members are subject to the provisions applicable to fiduciaries under sections 1104 – 1106, 1108, and 1110 of title 29, U.S. Code, and, to sections 1131 and 1132 of title 29, U.S. Code, only to the extent they concern the performance of fiduciary responsibilities. Since the USPS proposal provides that the plan established by the USPS is a "governmental plan" under ERISA, the provisions of Title I of ERISA generally would not apply to the plan. See 29 U.S.C. § 1003(b)(1). Therefore, oversight and enforcement provisions of Title I of ERISA not specifically made applicable in the proposal would not apply to the plan and the extent of the Department of Labor's role in ensuring compliance remains unclear.

⁴⁸See GAO, *Defined Benefit Pension Plans: Recent Developments Highlight Challenges of Hedge Fund and Private Equity Investing*, [GAO-12-324](#) (Washington, D.C.: Feb. 16, 2012); Randy Diamond, "Volatility plays starring role in allocation shifts," *Pensions & Investments*, vol. 38, no. 3 (2010); Arleen Jacobius, "Funds still carrying torch for alternatives: Private equity, real estate asset classes show double-digit increases in 2011," *Pensions & Investments*, vol. 40 no. 3 (2012); Christine Williamson, "Top pension funds put 20.3% more into hedge fund strategies," *Pensions & Investments*, vol. 41 no. 3 (2013); and S&P Dow Jones Indices LLC, *S&P 500® 2011: Pensions and Other Post-Employment Benefits (OPEB)* (New York, NY: July 2012).

returns significantly in excess of those on Treasury securities, and thus the potential for significantly lower long-term funding costs, they also have a significant risk of loss relative to investments in Treasury securities. Private sector companies and state and local governments that prefund retiree health benefits are permitted to, and do, invest plan assets in non-Treasury securities, typically in a mix that includes significant allocations to stocks and private sector bonds, among other asset classes. The National Association of Letter Carriers, noting the low interest rates on Treasury securities, has suggested that USPS remain in FEHBP, but with the PSRHBF invested in index funds of the federal Thrift Savings Plan. These proposals would allow USPS to seek higher investment returns, but there would be additional risk.

The U.S. Treasury Department's standard position and policy is that federal investment funds should be invested only in Treasury securities to minimize risk of loss.⁴⁹ According to Treasury officials, the position of the U.S. Treasury Department is that no USPS funds—including any funds of a USPS health plan—should be invested outside of the Treasury and should instead remain invested in special-issue Treasury securities to ensure their safety.⁵⁰

If USPS health plan fund assets were invested in non-Treasury securities that have more risk than Treasury securities and a market downturn caused severe losses in asset value, health benefits to postal employees and retirees could potentially decline or be jeopardized, such as through changes in plan provisions in reaction to unfunded liabilities or eventual inability to pay some benefits because of lack of funds. According to USPS, under its proposed health plan, there would be no explicit federal guarantee of USPS health benefits for postal employees, annuitants, or survivors, including any participants in the USPS health plan. If a market downturn caused losses in the value of fund assets, this would reduce funds available for postal health care. The impact of such losses could be magnified because a market downturn that negatively affected the value of plan assets could be associated with a more general economic downturn that negatively affected USPS mail volume and revenues. A

⁴⁹According to Treasury officials, there would be no protection of the value of the assets of the HBF, with the exception of any investments in special-issue Treasury securities.

⁵⁰Treasury officials also cited other advantages of Treasury securities, such as minimizing investment and administrative costs.

simultaneous decline in plan assets and USPS revenue could be a potential threat to USPS's financial viability or to workers' and retirees' benefit security should plan assets be invested in risky non-Treasury securities.

USPS is currently not well positioned to face a potentially significant decline in the value of plan assets, as it continues to incur significant operating losses and experience a continuing decline in mail volume, particularly in First-Class Mail. USPS could have great difficulty earning profits on its postal business to eventually make up investment losses it might incur on its over \$45 billion of health plan assets. Due to its financial difficulties, USPS has missed \$11.1 billion in prefunding payments for retiree health benefits and has recently reported that, given its low levels of liquidity, it will likely be forced to miss future prefunding payments.⁵¹

One other asset class that could be an option as part of a portfolio for prefunding USPS's retiree health care benefits would be inflation-indexed Treasury securities (known as TIPS). Since the amount of future retiree health care expenditures can be expected to vary with levels of future medical inflation, which in turn can be expected to vary somewhat with general inflation, inflation-indexed securities would provide a partial hedge against the risk of future medical inflation and retiree health expenditures. According to the U.S. Treasury Department, both TIPS and nominal (non-inflation-indexed) Treasury securities are safe and secure, backed by the full faith and credit of the United States government.⁵²

In response to concerns that have been expressed about the investment of assets for retiree health care in other than Treasury securities, USPS developed an alternative option for financing its health plan (which it refers to as "Scenario 1"). As previously discussed, under Scenario 1, the

⁵¹USPS, *Quarter II, 2013 Report on Form 10-Q*, p. 16.

⁵²Treasury officials told us that while the U.S. Treasury Department has issued both marketable Treasury securities to the public and special-issue Treasury securities for various federal programs, it has not to date issued any special-issue TIPS. Special-issue Treasury securities are protected by the U.S. Treasury Department against fluctuations in market value. While payments of interest and principal on Treasury securities are backed by the full faith and credit of the United States government, if marketable Treasury securities are sold prior to maturity, the market value could be less than the principal amount, depending upon prevailing interest rates, so such securities could be sold at a loss.

PSRHBF would be continued and used to finance retiree health benefits under USPS's health plan, though without continued OPM management since the plan would be administered by USPS. All future funding of USPS's retiree health benefits liability would be deposited into the PSRHBF. According to USPS, the current and future assets of the PSRHBF would continue to be invested as now, in special-issue Treasury securities or otherwise as might be directed by Congress. USPS would prefer to have some input on the structure of the asset holdings so that the PSRHBF's investments would be matched by duration to the expected benefit payments. According to USPS, this could be accommodated with the use of Treasury securities and is a sounder way of matching assets and liabilities than is currently in place. USPS officials stated that Congress's adoption of either scenario would be acceptable to USPS.

If USPS is permitted to, and does, invest plan assets in non-Treasury securities such as stocks, an important issue that would have to be resolved would be the appropriate method for determining the "discount rate" used in calculating USPS's liability for prefunding purposes. The discount rate is a key assumption in estimating the value of retirement liabilities, and there is significant disagreement among actuaries, economists, and other professionals regarding the appropriate approach to determining it.⁵³ One school of thought calls for basing the discount rate on an expected long-term rate of return based on the allocation of plan assets. This is the model generally used, for example, for determining funding targets for state and local government pension plans.⁵⁴ Since stocks have a higher expected return, on average, than bonds, a greater allocation of plan assets to stocks increases the discount rate, which in turn lowers the estimated liability and the needed amount of prefunding payments. This can also create an incentive to invest a

⁵³The "discount rate" is used to convert projected payments in the future into present values. We have a separate ongoing review examining the discount rate controversies for pension plans. See [GAO-13-112](#) for additional discussion of the discount rate used for USPS's current participation in FEHBP. There are different types of liabilities calculated for different purposes, including liabilities for financial reporting purposes and liabilities for determining prefunding targets and payments. The discount rate for financial reporting purposes is governed by relevant accounting standards. The discussion here is about the discount rate for prefunding purposes.

⁵⁴This model is also used for multiemployer pension plans and for prefunding retiree medical benefits in the private and state and local government sectors, when these are funded.

USPS's Proposal for
Transferring Surplus Assets
Could Create Future Unfunded
Liability

greater proportion of plan assets in investments such as stocks. A different school of thought calls for basing the discount rate on bond yields, which produces a discount rate that is independent of the allocation of plan assets. A variation of this approach is used for private sector single-employer pension plans under the Pension Protection Act of 2006.⁵⁵ There are many possible variations on the bond-yield approach, but these types of approaches generally produce a more conservative discount rate than the expected-return-on-plan-assets approach. Hybrid approaches are also feasible. Factors to consider in establishing the discount rate model that would be used for a USPS-sponsored plan include the fragile state of USPS's finances, the mature age profile of USPS's workforce, and the large number of USPS retirees. These circumstances would point to a more conservative approach to setting USPS's prefunding discount rate.

We are concerned with USPS's proposal to allow the transfer of surplus assets because if surpluses are consistently transferred, then an unfunded liability—the difference between the liability and plan assets—for retiree health benefits could result. Under Scenario 2 of USPS's proposal, in any year that assets supporting the USPS health plan exceeded USPS's liability for retiree health benefits, the Committee appointed by USPS to oversee its health plan could transfer the estimated surplus to the Postal Service Fund that USPS uses to pay most of its expenses, including its general operating expenses. According to USPS, a transfer could not occur unless the Committee concluded, after receiving an actuarial report, that the transfer would not violate the requirement that the assets in the HBF supporting the USPS health plan exceed its estimated actuarial liability. USPS officials told us that their principal concern is that they would prefer to have the question of the potential disposition of excess assets set aside for retirees addressed in legislation, to avoid uncertainties they told us have arisen with respect to this issue in funding the Civil Service Retirement System and the Federal Employees Retirement System. They noted that it is possible to envision some circumstances in which a surplus could be quite large, and as a result, some guidance from Congress as to the potential disposition of a surplus, under whatever strictures Congress would see fit to impose, would be appropriate. They told us that while they made an initial

⁵⁵Pub. L. No. 109-280, § 112(a), 120 Stat. 780, 798 (Aug. 17, 2006), codified at 26 U.S.C. § 430(h)(2).

proposal in their August 2011 legislative language, they are open to any reasonable resolution of this issue.

In our view, except in special circumstances, transferring surpluses creates risk because liability measurements for retirement benefits are inherently uncertain and subject to significant revision and fluctuation as more information becomes available and as economic and demographic conditions change.⁵⁶ In addition, under Scenario 2, the more than \$45 billion saved to prefund retiree health benefits would no longer be restricted to that purpose but could be used to pay for employee health benefit costs and plan administration. OPM officials noted that USPS could face health claims costs that exceed what it is expecting, and as a self-insured plan, USPS would be fully responsible for financing those costs. Given USPS's financial condition, using the funds previously set aside to finance retiree health benefits may be necessary for financing unexpected increases in health plan costs. In this regard, USPS officials told us that at least in Scenario 1 and possibly in either scenario, USPS would expect to segregate and not commingle assets designated for retiree health benefits from those that might be maintained in the management of the health benefits funds required for active employees.

In 2011, we reported on considerations and options regarding the disposition of any surplus assets in USPS's Federal Employees Retirement System subaccount.⁵⁷ Similar considerations are relevant to any surplus assets relative to USPS's liability for retiree health benefits. A transfer of surplus assets would raise the risk of a future unfunded liability—a risk that would increase significantly if there were automatic, recurring transfers. A one-time transfer can sometimes be justified by special circumstances. A significantly safer and more prudent approach is to amortize any surplus over an extended period—for example, to match the amortization period to that required to address any unfunded liability, which has an element of fairness in that it would treat surpluses and unfunded liabilities symmetrically. The amortization amount would be an offset to the normal cost (the annual prefunding cost for the future

⁵⁶In addition, if the plan assets were also subject to significant risk and fluctuation in value, such as through investments in the stock market, it could make the unfunded liability even more unstable, so that transferring surplus for other uses would be even riskier.

⁵⁷GAO, *U.S. Postal Service: Allocation of Responsibility for Pension Benefits between the Postal Service and the Federal Government*, [GAO-12-146](#), Appendix II (Washington, D.C.: Oct. 13, 2011).

Use of Overly Optimistic
Assumptions Could Decrease
Funds

benefits being earned by current workers), reducing USPS's prefunding payment somewhat. Another approach would be to use the surplus to offset the entire normal cost, thereby reducing the prefunding payments to zero (for as many years until the surplus is used up). This approach would be more risky than the amortization approach in that it would essentially return the surplus more quickly, but significantly less risky than transferring the entire surplus all at once. This approach would be similar to that allowed for private sector pension plans.

Under USPS's proposal, there can be some risk of overly optimistic assumptions in valuing the funded status of USPS's health plan—resulting, for example, in actual investment returns that are less than the assumptions, or liabilities that are larger than anticipated by the assumptions—potentially leading to inadequate funding of benefits. Although USPS has proposed some safeguards over the selection of assumptions, an additional safeguard would be to have assumptions selected by an independent third party.

Selecting long-term assumptions for asset returns, medical inflation, and other economic and demographic variables involves judgment, with room for professional disagreement and differing estimates, which can have a very large impact on the estimated size of the retiree health liability and on the amount of prefunding payments. For example, in recent years the USPS OIG has had disagreements over certain assumptions selected by OPM's actuaries.⁵⁸

Under USPS's proposal, the current oversight function provided by OPM, including its staff of actuaries, would no longer apply. USPS has stated that it is important to establish a solid structure for governance and oversight of its proposed plan. USPS has also said it would adopt a best practices approach for governance and oversight based on models in the private sector. Oversight of the plan would include the formation of a Health Benefits Plan Management Committee, which would include members selected by USPS, including members recommended by the unions, management associations, and the U.S. Treasury Department. Specifically, USPS would retain the services of an independent actuary qualified under the U.S. Qualifications Standard and subject to the U.S.

⁵⁸USPS OIG, *Estimates of Postal Service Liability for Retiree Health Care Benefits*, ESS-MA-09-001(R) (Arlington, VA: July 22, 2009).

Code of Professional Conduct and Actuarial Standards of Practice to perform an annual actuarial valuation of the USPS health benefit plan and fund.

While these safeguards are important, they do not provide for selection or oversight of assumptions that would be independent of USPS or its chosen contractors. Given the tens of billions of dollars involved, the sensitivity of results to assumptions, USPS's financial condition, and potential pressures from different constituencies, assumptions could be selected by an independent actuarial body. Potential models could include the Board of Actuaries for the federal civilian pension program and the Boards of Actuaries for the military retirement programs.

Expanded Collective Bargaining over Health Benefits and Premiums Could Increase Costs without Regard to USPS's Financial Condition

USPS health benefit costs and liabilities could increase over time because, under USPS's proposal, the scope of the collective bargaining process would be expanded to cover health benefits and premiums. In this regard, the collective bargaining process, which could result in binding arbitration, does not require the consideration of USPS's financial condition. Although the collective bargaining process could potentially result in appropriate modifications to the USPS health plan over time, it also could result in changes that increase USPS's health benefits costs, such as expanded benefits, an increase in the percentage of claims costs that the USPS health plan covers, or decreases in employee and retiree premiums. It is important to note that even if USPS does not agree to such changes in collective bargaining, the changes could result from binding arbitration. In this regard, arbitrators also are not required to consider USPS's financial condition during binding arbitration. In 2010, when we found USPS's business model was not viable, we recommended Congress consider multiple actions, including changing the statutory framework for collective bargaining to ensure that binding arbitration takes USPS's financial condition into account.⁵⁹ We recently reaffirmed this recommendation in testimony in early 2013 before the Senate and House postal oversight committees.⁶⁰ USPS supports this recommendation, but according to USPS officials, even without such a requirement for arbitrators, any future arbitration would be exceedingly

⁵⁹ [GAO-10-455](#).

⁶⁰ [GAO-13-562T](#) and [GAO-13-347T](#).

unlikely to dramatically escalate the cost of health benefits beyond those contemplated by its health plan.

Compared to FEHBP, Postal Employees and Retirees Would Have Coverage for Similar Services, but Elements of the Proposed Plan’s Design Could Lead to Higher Costs for Some Enrollees

Under the proposed USPS plan, as designed for the first year, postal employees and retirees would have coverage for a similar package of services as those covered by selected FEHBP plans that we reviewed, and the level of coverage would be similar for many services, with some exceptions.⁶¹ We estimate that, had the proposed USPS plan been implemented in 2013, most employees and retirees would have had similar or lower premiums compared to the selected FEHBP plans; but total costs—premiums and costs for the use of care—could be higher for some, due in part to higher deductibles and out-of-pocket maximums under the USPS plan. In addition, employees and retirees would have many but not all of the same protections relating to coverage and costs under the USPS plan that they have in FEHBP.

⁶¹Services cannot be compared beyond the first year, because USPS’s benefits could change. Under USPS’s proposal, the requirement that benefits be similar in type and value to that of the most popular FEHBP plan is limited to the first year for employees. For current retirees, the standard extends beyond the first year. For those who retire after the first year, the USPS proposal offers no benchmark for comparability with FEHBP plan benefits.

Under the Proposal, Postal Employees and Retirees Would Have Coverage for Similar Services at Similar Coverage Levels when Compared with FEHBP, with Some Exceptions

Under the USPS plan as designed for the first year of implementation, employees and retirees would generally have a similar set of services covered, including inpatient and outpatient services and prescription drugs, as they have under selected FEHBP plans.⁶² For example, like the selected seven FEHBP plans that we reviewed, the proposed USPS plan would cover inpatient hospital room and board, surgery, visits to primary care and specialist physicians, chemotherapy, laboratory tests, and prescription drugs. The proposed USPS plan also would cover some services that were not covered by all selected FEHBP plans, such as routine hearing tests. However, USPS had not determined as of February 2013 whether the USPS plan would provide coverage for three services—acupuncture, family planning and contraceptive care, and infertility diagnostic services—covered by all selected FEHBP plans.⁶³

When comparing coverage levels—the portion of service costs paid by the insurer for covered services—we found employees and retirees in the selected FEHBP plans that we reviewed would have similar or higher levels of coverage for many services under the USPS plan.⁶⁴ Compared to the selected FEHBP plans we reviewed, the USPS high and middle options would provide employees and current retirees not eligible for Medicare with levels of coverage within or above the range of coverage offered by selected FEHBP plans for more than half the in-network services we reviewed (23 of 29 for the proposed USPS high option and 21 of 29 for the middle option). For example, the proposed USPS middle option would cover 85 percent of in-network surgery costs and the high option would cover 90 percent; the selected FEHBP plans we reviewed

⁶²Our review includes the seven plans with the highest enrollment of postal employees and retirees, which comprised about 78 percent of total FEHBP enrollment from postal employees and retirees. The remaining 22 percent of postal employee and retiree enrollment was spread across 140 other FEHBP plans, which we did not review.

⁶³USPS officials said they would determine coverage when procuring a contract with a vendor to administer the health plan. Family planning/contraceptive care can include coverage for contraceptive counseling and medical goods such as implantable contraceptives. Not all plans cover all of the same procedures or items within a category of goods or services.

⁶⁴We excluded one of the seven selected FEHBP plans that we reviewed from this comparison of coverage levels because the structure of benefits for the plan was not comparable to that under the proposed USPS plan.

would cover from 85 percent to 90 percent (see table 6).⁶⁵ For current USPS retirees who are eligible for Medicare, coverage for inpatient and outpatient services would generally be the same under the proposed USPS plan as under the selected FEHBP plans, with the USPS plan covering 100 percent of the cost beyond what Medicare covers.

Table 6: Examples of Services for Which the USPS Proposed Plan Offers Levels of Coverage for In-Network Care within the Range of Coverage Offered by Selected FEHBP Plans

Service	In-network coverage levels for USPS plan		Range of in-network coverage levels for selected FEHBP plans
	Middle option	High option	
Chemotherapy and radiation therapy	85%	90%	85% to 90%
Outpatient diagnostic laboratory services	85%	90%	85% to 100%
Inpatient hospital admission ^a	85%	90%	85% after \$200 copayment to 100% after \$100 copayment
Routine physical exam (adults and children)	100%	100%	100%
Surgery (outpatient and inpatient)	85%	90%	85% to 90%

Source: GAO analysis of USPS proposal and 2013 FEHBP plan brochures.

Note: The selected FEHBP plans included: the standard option of the Blue Cross and Blue Shield Service Benefit Plan, the NALC Health Benefit Plan (sponsored by the National Association of Letter Carriers), the American Postal Workers Union Health Plan, the Government Employees Health Association, Inc. Benefit Plan (which included both the high and standard options), the Mail Handlers Benefit Plan, and the Rural Carrier Benefit Plan. These plans are all national, fee-for-service plans, as the proposed USPS plan would be, and do not include high-deductible or consumer-driven plans.

^aThis includes room and board and other hospital services and supplies related to inpatient admission.

⁶⁵An example of a service for which coverage under the USPS plan is above the range of the selected FEHBP plans is brand-name prescription drugs listed on a plan formulary and purchased through a retail pharmacy. However, levels of prescription drug coverage are also affected by which specific drugs are included on the plan formulary, and the composition of formularies is at the discretion of individual plans or their pharmacy-benefits vendors.

While the proposed USPS plan would provide similar levels of coverage for many services, we found some exceptions where employees and retirees would have lower levels of coverage or where it was unclear how the level of coverage would compare for a service. For example, employees and non-Medicare-eligible retirees would have lower coverage under USPS's high option for 2 of the 29 in-network services (primary care office visits due to illness and outpatient mental health or substance abuse treatment).⁶⁶ In addition, USPS's middle option would provide lower levels of coverage than the selected FEHBP plans we reviewed for those and 2 other services (visits to specialist physicians and maternity care services).⁶⁷ For several other in-network services, whether the USPS plan would provide higher, comparable, or lower levels of coverage would depend on the cost of the service.⁶⁸ Finally, we could not compare the coverage levels for one service (ambulance ground transport) because USPS had not determined at what level the plan would cover the services.

We found a few other instances where employees and retirees would have lower levels of coverage under the USPS plan. Specifically, levels of coverage would generally be lower for out-of-network services, for those insured under USPS's value option, and for future retirees when they become eligible for Medicare.

- *Services received out-of-network.* Employees and non-Medicare-eligible retirees generally would have lower coverage levels for out-of-network services under the proposed USPS plan than under the selected FEHBP plans we reviewed. For example, for surgical

⁶⁶For visits to in-network primary care doctors due to illness, the proposed USPS high option would cover \$5 to \$15 less per visit than the selected FEHBP plans we reviewed, and the proposed middle option would cover \$15 to \$25 less per visit. For outpatient mental health or substance abuse services from in-network providers, the proposed high option would cover \$20 to \$30 less per visit, and the proposed middle option would cover \$30 to \$40 less per visit.

⁶⁷Under the proposed USPS middle option, coverage for visits to in-network specialists would be between \$10 and \$32 less than selected FEHBP plans. Coverage for maternity care from in-network providers would be between 5 percent and 15 percent less than selected FEHBP plans.

⁶⁸For example, the proposed USPS plan would provide lower coverage than the selected FEHBP plans for generic drugs from a mail-order pharmacy that cost more than \$150. USPS's plan would provide coverage within the range of selected FEHBP plans for drugs costing between \$50 and \$150 and greater coverage for drugs costing less than \$50.

services from out-of-network providers, the selected FEHBP plans would cover from 65 to 75 percent of allowable charges; the proposed USPS high option would cover 60 percent, and the proposed USPS middle option would cover 50 percent.⁶⁹ Representatives from one selected FEHBP plan noted that generally 10 percent to 20 percent of enrollee charges are for services received out of network. USPS officials reported that their discussions with health insurance carriers indicated that out-of-network claims represented 2.5 percent to 10 percent of total claim costs.

- *USPS's value option.* USPS's value option would generally have lower levels of in-network and out-of-network coverage than the selected FEHBP plans we reviewed for employees and non-Medicare-eligible retirees. However, USPS officials expected a smaller proportion of employees and retirees to select this option as compared to the high and middle options.
- *Future retirees when they become eligible for Medicare.* Those who retire after the first year of implementation would be subject to the USPS plan's annual plan deductibles and cost-sharing for covered services even after enrolling in Medicare. The selected FEHBP plans we reviewed waive the annual plan deductible and do not require copayments for inpatient and outpatient services for retirees who enroll in Medicare.

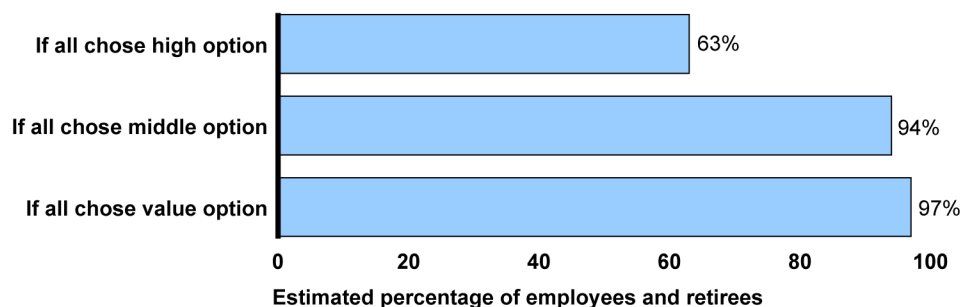
In addition, while covered services and coverage levels may be similar under the USPS plan and the selected FEHBP plans, some postal employees and retirees may have to find new providers in order to avoid paying the higher out-of-network charges. Further, the more than 20 percent of Medicare-eligible postal retirees who are not enrolled in Medicare Part B, but are assumed to do so under the postal plan, will need to select Medicare participating providers in order to receive full coverage of care.

⁶⁹"Allowable charges" are set by each plan and reflect the amount that a plan considers reasonable or customary for a specific service. A plan's allowable charges sometimes can vary based on geographic area. In general, in network providers negotiate with health plans to determine the allowable charge for various services.

At Least 63 Percent of Employees and Retirees in Selected FEHBP Plans Would Pay Similar or Lower Premiums, but Elements of the Proposed USPS Plan Could Lead to Higher Total Costs for Some

Our estimates indicate that under USPS's proposed plan most postal employees and retirees would have had similar or lower premiums than under the seven selected FEHBP plans in 2013. Depending on which USPS option was chosen, we estimated that from 63 percent to 97 percent of employees and retirees would have premiums that are similar (within 10 percent) or lower (more than 10 percent less) than the premiums they would have paid under FEHBP.⁷⁰ For example, if all postal employees and retirees in the selected FEHBP plans chose USPS's middle option, 94 percent of them would pay similar or lower premiums, which for employees with self-only coverage, would mean paying anywhere from about \$100 more to \$1,000 less in premiums annually under the USPS middle option than under their current FEHBP plan (see figure 1).⁷¹

Figure 1: Percentage of Postal Employees and Retirees from Selected FEHBP Plans Who Could Obtain Similar or Lower Premiums under the Proposed USPS Health Plan, 2013



Sources: GAO analysis of USPS estimates of 2013 premiums, 2013 premiums for seven selected FEHBP plans, and OPM data on FEHBP enrollment in 2011.

⁷⁰As previously noted, we defined "similar" premiums as those within 10 percent of the projected premium for the proposed USPS plan and "lower" as those more than 10 percent less. Those that would not pay similar or lower premiums would pay premiums more than 10 percent higher under the USPS proposed plan than under their FEHBP plan.

⁷¹Those with self-only coverage would be more likely than those needing family coverage to have similar or lower premiums under the proposed USPS plan. For example, we estimated that 70 percent of employees and retirees with self-only coverage would have similar or lower premiums under the proposed USPS high option than under their FEHBP plan. By comparison, we estimated that 58 percent of those with self-and-family coverage would have similar or lower premiums under the USPS high option. Medicare-eligible retirees who were not enrolled in Part B in FEHBP but would be enrolling under the USPS plan would be more likely than other enrollees to have higher premium costs under the USPS proposal because of the addition of the Part B premium.

Note: For these estimates, we defined “similar” premiums as those within 10 percent of the premium the employee or retiree would have paid in 2013 for their FEHBP plan and “lower” premiums as those more than 10 percent less than the FEHBP premium. The estimates assume that enrollment in the selected FEHBP plans did not change from 2011 to 2013. Estimates also use USPS’s assumptions of the distribution of those with family coverage under FEHBP across the three levels of family coverage offered under the USPS proposed plan. The estimates account for Medicare Part B premiums that Medicare-eligible retirees are assumed to pay under USPS’s proposed plan.

The selected FEHBP plans included: the standard and basic options of the Blue Cross and Blue Shield Service Benefit Plan, the NALC Health Benefit Plan (sponsored by the National Association of Letter Carriers), the American Postal Workers Union Health Plan, the Government Employees Health Association, Inc. Benefit Plan (which included both the high and standard options), the Mail Handlers Benefit Plan, and the Rural Carrier Benefit Plan. These plans are all national, fee-for-service plans, as the proposed USPS plan would be, and do not include high-deductible or consumer-driven plans.

However, certain elements of the proposed USPS plan in combination with lower levels of coverage for some services could lead to higher total costs—premiums and out-of-pocket costs—for some employees and retirees than under the selected FEHBP plans we reviewed. Specifically, though deductibles and out-of-pocket maximums for in-network care under the USPS proposed high option would be similar to or lower than the selected FEHBP plans we reviewed, total deductibles and maximums for in-network and out-of-network care would generally be higher.⁷² For example, total out-of-pocket maximum amounts for family coverage for in-network and out-of-network services would be at least \$8,000 more under the proposed high option and at least \$14,000 more under the proposed middle option than under any selected FEHBP plan (see table 7). The proposed USPS plan also includes a separate \$1,500 out-of-pocket maximum for prescription drugs, which would provide more cost protection for prescription drug spending than most of the selected plans but less than the FEHBP plan with the greatest number of postal enrollees. The differences in deductibles and out-of-pocket maximums under the USPS plan—on their own, or in combination with lower coverage levels for some services—could lead to higher total costs for some postal employees and non-Medicare-eligible retirees, including those who would have lower premiums under the USPS plan.

⁷²For our analysis of annual plan deductibles and out-of-pocket maximums, we excluded one of the seven selected FEHB plans because the structure of the deductibles and out-of-pocket maximums was not comparable to that under the proposed plan.

Table 7: Comparison of Proposed USPS Annual Plan Deductibles and Out-of-Pocket Maximums to Those of Selected FEHBP Plans

	Range for selected FEHBP plans	USPS plan	
		High option	Middle option
Annual deductible for in-network services			
Self-only	\$275 to \$400	\$250	\$500
Self and family	\$550 to \$800	\$500	\$1,000
Total annual deductible for in-network and out-of-network services ^a			
Self-only	\$300 to \$660	\$750	\$1,500
Self and family	\$600 to \$1,500	\$1,500	\$3,000
Annual out-of-pocket maximum for in-network services			
Self-only	\$4,000 to \$6,000	\$3,000	\$4,000
Self and family	\$4,000 to \$6,000	\$6,000	\$8,000
Total annual out-of-pocket maximum for in-network and out-of-network services ^b			
Self-only	\$4,500 to \$10,000	\$9,000	\$12,000
Self and family	\$5,000 to \$10,000	\$18,000	\$24,000

Source: GAO analysis of USPS proposal and 2013 FEHBP plan brochures.

Note: Separate deductibles and out-of-pocket maximums for prescription drug services are not included. The selected FEHBP plans included: the standard option of the Blue Cross and Blue Shield Service Benefit Plan, the NALC Health Benefit Plan (sponsored by the National Association of Letter Carriers), the American Postal Workers Union Health Plan, the Government Employees Health Association, Inc. Benefit Plan (which included both the high and standard options), the Mail Handlers Benefit Plan, and the Rural Carrier Benefit Plan. These plans are all national, fee-for-service plans, as the proposed USPS plan would be, and do not include high-deductible or consumer-driven plans.

^aUnlike the selected FEHBP plans, the proposed USPS plan would have a separate annual deductible for out-of-network services. The total in-network and out-of-network annual deductible reflects the sum of the separate in-network and out-of-network deductibles.

^bUnlike the selected FEHBP plans, the proposed USPS plan would have a separate out-of-pocket maximum for out-of-network services. The total in-network and out-of-network out-of-pocket maximum reflects the sum of the separate maximum limits for in-network and out-of-network care.

Employees and non-Medicare-eligible retirees could be at greater risk for higher costs due to these plan elements depending on: the amount and the cost of care they use, their use of out-of-network providers, and whether they have family coverage.

- Employees and non-Medicare eligible retirees who use relatively high amounts of care and have family coverage risk having higher

costs under USPS's plan. For example, employees with family coverage who used \$50,000 worth of in-network health care would have spent an estimated \$2,116 more with the proposed USPS high option and about \$3,474 more with the proposed middle option than with the FEHBP plan with the largest number of postal enrollees.⁷³ By comparison, an employee with family coverage who used \$2,500 worth of health care costs from in-network providers would have faced lower out-of-pocket costs under either the proposed USPS high option or middle option than under the FEHBP plan (see table 8). We found that employees and non-Medicare-eligible retirees who choose the new self-and-spouse and self-and-children coverage tiers offered in the USPS proposal could face higher costs than under the FEHBP plan's self-and-family option if their total health care costs are \$50,000.⁷⁴

- Employees and non-Medicare eligible retirees who use out-of-network care also could face higher total costs under the proposed USPS plan. For example, compared to the FEHBP plan with the largest number of postal enrollees, we estimated that employees with self-only and family coverage would have higher out-of-pocket costs under many scenarios. An employee with family coverage using \$50,000 worth of health care with 30 percent of outpatient care received out of network would have spent an estimated \$3,195 more under the proposed USPS high option and about \$5,193 more under the proposed USPS middle option than under the FEHBP plan with the largest number of postal enrollees (see table 8).⁷⁵ When we assumed a lower

⁷³These higher costs would be attributable almost entirely to the plan elements since the 2013 premiums for family coverage under the largest FEHBP plan were higher than USPS's middle option and almost the same as the high option.

⁷⁴For example, at \$50,000 of total health care costs using all network providers, we estimated that employees enrolling in self-and-children coverage would pay about \$900 more under the USPS high option and \$2,700 more under the middle option than under the FEHBP plan. The estimated total cost difference under the \$50,000 scenario for non-Medicare-eligible retirees enrolling in self-and-spouse would be similar.

⁷⁵In this example, out-of-network outpatient care ranged from 8.8 percent of total health care costs under the \$50,000 scenario to 14.2 percent in the \$2,500 scenario. We assumed all costs for inpatient care and prescription drugs came from in-network sources.

proportion of outpatient care from out-of-network providers, we found similar results.⁷⁶

Table 8: Illustrations of Estimated Differences in Employees' Annual Costs under the Proposed USPS Plan and the FEHBP Plan with the Largest Number of Postal Enrollees

	Difference in employees' annual costs compared to the FEHBP plan with the largest number of postal enrollees under different scenarios of total health care costs			
	\$2,500 in total health care costs	\$10,000 in total health care costs	\$17,000 in total health care costs	\$50,000 in total health care costs
All care received from network providers				
Self-and-family coverage				
USPS high option	-\$300	-\$35	\$191	\$2,116
USPS middle option	-\$1,350	-\$704	-\$169	\$3,474
Self-only coverage				
USPS high option	-\$479	-\$215	\$12	\$26
USPS middle option	-\$772	-\$125	\$410	\$724
Combination of care from network and non-network providers^a				
Self-and-family coverage				
USPS high option	-\$51	\$582	\$941	\$3,195
USPS middle option	-\$1,119	-\$130	\$806	\$5,193
Self-only coverage				
USPS high option	-\$231	-\$121	\$462	\$1,284
USPS middle option	-\$541	\$154	\$1,135	\$2,662

Source: GAO.

Notes: Estimates of the difference in employees' annual costs account for both health insurance premiums and out-of-pocket costs for the use of health care services. The estimates assume different distributions of costs across three categories of services—inpatient and outpatient services and prescription drugs—at the four different total health cost amounts. The estimates reflect cost sharing for each category of service and apply the plan's deductibles and out-of-pocket maximums.

⁷⁶For example, when we assumed 10 percent of outpatient care was received from non-network providers, we estimated that employees in self-only or family coverage would face higher total costs under the USPS high and middle options than under the FEHBP plan if their total annual health care costs were \$17,000 or \$50,000. Estimated employee costs under the \$17,000 scenario ranged from \$150 to \$980 higher under the USPS plan and under the \$50,000 scenario from \$650 to \$4,700 higher. (Out-of-network care made up 2.9 percent of total health care costs under the \$17,000 scenario and 3.2 percent of total health care costs under the \$50,000 scenario, since we assumed all inpatient care and prescription drug costs were from in-network providers.)

^aEstimates assume that 30 percent of outpatient care is from out-of-network providers, but all inpatient care and prescription drug purchases are from in-network providers. Out-of-network outpatient care ranged from 8.8 percent of total health care costs under the \$50,000 scenario to 14.2 percent in the \$2,500 scenario. Outpatient care includes such items as diagnostic imaging tests and surgeries for those who have not been admitted to a hospital.

Employees and Retirees Would Have Many but Not All of the Same Protections under the USPS Plan That They Have under FEHBP

USPS included provisions in its legislative proposal to ensure that its proposed plan would be required to meet many of the standards protecting FEHBP enrollees. USPS's legislative proposal requires that the health plan provide continuation of coverage benefits consistent with, and other benefits that comply with, specified standards for employer-sponsored group health plans.⁷⁷ These include limits on excluding coverage for preexisting conditions and standards for benefits for mothers and newborns.⁷⁸ There are other standards that the USPS proposal applies to the USPS plan by incorporating a general reference to the Public Health Service Act (PHSA) in one of the proposal's provisions.⁷⁹ USPS officials stated that inclusion of this provision ensures that the USPS plan would be required to meet the referenced group health plan standards in the PHSA and noted that it is ambiguous whether the PHSA standards would apply to the proposed plan without such a provision.⁸⁰

However, the USPS contribution to the cost of retirees' health benefits would no longer be tied to the statutory formula for federal contribution

⁷⁷According to USPS's legislative proposal, benefits provided by the USPS health plan shall be consistent with provisions of ERISA relating to continuation of coverage requirements (29 U.S.C. §§ 1161-1169) and shall comply with other provisions relating to additional standards (29 U.S.C. §§ 1181-1191c).

⁷⁸See 29 U.S.C. § 1181 (increased portability through limitations on preexisting condition exclusions) and 29 U.S.C. § 1185 (standards relating to benefits for mothers and newborns).

⁷⁹29 U.S.C. § 1185d, which is among the provisions applied to the USPS plan by the proposal, applies the provisions of PHSA, title XXVII, part A (42 U.S.C. §§ 300gg et seq.) to group health plans and health insurance issuers providing health insurance coverage in connection with group health plans. PHSA standards that may be applied through this reference include a prohibition on setting life time limits on the value of coverage and standards for appeals of benefit denials to the health plan and an independent, external reviewer. 42 U.S.C. §§ 300gg-11 (no lifetime or annual limits) and 300gg-19 (appeals process) (PHSA §§ 2711 and 2714, as added by Pub. L. No. 111-148, §§ 1001, 10101, 124 Stat. 130, 884) (Mar. 23, 2010)).

⁸⁰Officials stated that it is ambiguous whether the group health plan provisions of the PHSA would apply by their own force to a self-insured federal governmental plan, which is how the USPS plan would be defined. Officials noted, however, that if USPS offers an HMO option, the HMO would be subject to the PHSA requirements as an insured plan.

pertaining to all federal employees and retirees in FEHBP, which could leave postal retirees more vulnerable to increases in their contribution rates. Though USPS officials have indicated the agency’s intention to keep contribution rates for current retirees consistent with those of retirees within FEHBP, the proposed legislative language does not require USPS to do so. Under FEHBP, postal retiree contribution rates depend on the government contribution rate to premiums for federal employees and retirees, a rate that is established by federal law.⁸¹ Under USPS’s proposal, initial contribution rates for employees and retirees would be set by USPS and there are no standards provided for this initial determination. USPS may also subsequently change contribution rates, and, because the employee unions do not represent retirees, those changes would not be subject to the collective bargaining process. Officials from the association for federal retirees raised concerns about retirees’ lack of representation within the context of the USPS proposal.

A USPS Withdrawal from FEHBP Would Significantly Reduce Program Enrollment but Is Not Expected to Adversely Affect Most Nonpostal Enrollees

If USPS withdraws its employees and retirees from FEHBP, enrollment in FEHBP would decline by an estimated 25 percent, which is about 1 million of the 4 million employees and retirees enrolled in the program. The percentages of enrollees who are employees and retirees would likely remain about the same (see table 9).⁸²

Table 9: Comparison of FEHBP Enrollment in 2011 and under a USPS Withdrawal from FEHBP

	Employees	Retirees	Total
FEHBP enrollment as of 2011	2,236,059 (56%)	1,791,419 (44%)	4,027,478
USPS enrollment	512,216 (51%)	482,587 (49%)	994,803
Estimated FEHBP enrollment if USPS withdraws from FEHBP	1,723,843 (57%)	1,308,832 (43%)	3,032,675

Source: GAO analysis of OPM data.
Note: Numbers represent FEHBP contracts, not the number of covered lives. OPM officials estimated that total covered lives in FEHBP was about 8 million in 2011.

⁸¹5 U.S.C. § 8906(b).
⁸²According to 2013 data from USPS, postal retirees enrolled in FEHBP now outnumber employees enrolled in the program.

In addition, the remaining FEHBP enrollee population would likely be somewhat younger, with increases in the proportion of enrollees who are ages 23 through 44 (see table 10).

Table 10: Comparison of Age Distribution of FEHBP Enrollment in 2011 and Estimated Distribution under a USPS Withdrawal from FEHBP

	Percentage of enrollment in age range					
	Under 23	23-34	35-44	45-54	55-64	65 and older
Enrollment as of 2011	0.2	9.3	11.9	19.6	25.3	33.8
Estimated enrollment if USPS withdraws from FEHBP	0.2	11.3	12.6	18.6	24.3	32.9

Source: GAO analysis of OPM data.

Note: Numbers may not add due to rounding. The age-based 2011 enrollment data represents FEHBP contracts, not the number of covered lives. The data did not break retirees down into postal and nonpostal categories, so our estimates assume that the age distribution of postal and nonpostal retirees was similar. We tested that assumption by reviewing other OPM data on the age distribution of postal and nonpostal retirees.

Despite the significant reduction in FEHBP enrollment, it is unlikely that most nonpostal enrollees would be affected beyond small increases or decreases in premiums. Interviews with OPM officials and representatives from selected FEHBP plans indicated that most nonpostal enrollees' plans would likely continue to participate in FEHBP despite a USPS withdrawal, even if plans lost up to 50 percent of enrollment. For example, representatives from a postal union that offers three plans in FEHBP—all with postal enrollment of less than 25 percent—told us that the association plans to remain in the program regardless of USPS's participation, because the plans would remain profitable. Representatives from the selected plans that had postal enrollment of less than 50 percent expected that a USPS withdrawal would have some small effect on nonpostal enrollees' premiums. For example, representatives from the plan with the largest enrollment expected that a USPS withdrawal might lead to a small increase or decrease in premiums depending on the claims experience of those withdrawing compared with remaining enrollees. Representatives from another large plan estimated a slight decrease (1 to 2 percent) in premiums for the remaining enrolled population. Some plan representatives noted that administrative costs would be spread over a smaller number of people, which could magnify any increases or partially offset any reductions in premiums, as premiums

account for those costs. However, OPM officials noted that plan administrative costs are generally a percentage of total claims costs, about 5 percent, and that the percentage would likely remain the same under a USPS withdrawal.

A USPS withdrawal could result in some nonpostal enrollees needing to select new FEHBP plans. OPM officials told us that the small number of FEHBP plans where enrollment is primarily postal employees and retirees would likely withdraw from the program, because the plans would no longer have enrollees or the plans would not be able to remain competitive with other FEHBP plans without postal enrollees. Of the 147 FEHBP plans offered in 2011, enrollment was primarily composed of postal employees and retirees (70 percent or more) in 4 plans—2 national fee-for-service plans run by postal unions and 2 HMOs with enrollment of around 1,000 (see table 11). If USPS were to withdraw its employees and retirees from FEHBP, one of the 2 affected postal union sponsored plans would lose its entire enrollment, and the other would lose 76 percent of its enrollment.⁸³ If the 4 plans with 70 percent or more postal enrollment discontinue participation in the program under a USPS withdrawal, an estimated 1 percent (about 29,000) of the approximately 3 million nonpostal enrollees in FEHBP would need to select a new health plan. Another roughly 62,000 nonpostal enrollees would be affected if plans with 50 percent to 69 percent postal enrollment decided to leave FEHBP.

Table 11: Number of FEHBP Plans at Various Levels of Postal Enrollment and the Number of Postal and Nonpostal Enrollees in Those Plans as of 2011

Percentage of enrollment that postal enrollees represent	Total number of plans	Postal enrollment	Nonpostal enrollment
70% or more	4	123,383	28,940
50 to 69%	20	108,478	62,266
30 to 49%	40	95,096	167,774
20 to 29%	30	584,738	2,181,778
19% or less	53	83,108	591,917

Source: GAO analysis of OPM data.
Note: The enrollment numbers represent FEHBP contracts, not the number of covered lives. OPM officials estimated that total covered lives in FEHBP was about 8 million in 2011.

⁸³OPM officials noted that under current federal law new employee association sponsored health plans cannot join FEHBP.

Nonpostal enrollees who have to select new plans would have multiple options, but changing plans may have adverse effects for some. Plans leaving FEHBP and enrollees needing to select a new plan are a common occurrence. From 2008 through 2012, more than 100 plans left FEHBP, affecting about 100,000 enrollees.⁸⁴ In all states, nonpostal enrollees in the 4 plans that may choose to depart the program as a result of a USPS withdrawal would have at least 10 fee-for-service plan options from which to choose and may also have one or more HMO options.⁸⁵ Most of the 29,000 enrollees most likely to be affected would also be able to choose a plan with a similar premium to the enrollee's departing plan. However, as was previously discussed, enrollees choosing a new plan with a similar or lower premium could face higher total costs because of differences in coverage levels and cost-sharing requirements. Some nonpostal enrollees who would have to select a new plan may also have to find new providers. Having to identify new providers could cause disruptions in health care for some enrollees, which representatives from one postal union and the association for federal retirees raised as a concern.

OPM officials told us that they do not expect that a USPS withdrawal would have more extensive effects than a small number of plans exiting the program. However, they also noted that any time a large change occurs in the program there can be unintended and unforeseen issues that arise. FEHBP has not experienced a reduction in enrollment of this size in the past. The program's experience with groups of employees leaving includes those that left in the 1980's when six federal agencies introduced their own health plans to provide an alternative to FEHBP for employees.⁸⁶ These agencies had relatively small numbers of employees (from about 150 to 8,500) and, therefore, their employees' leaving FEHBP

⁸⁴The most significant year of plan departures was 2009 when 35 plans withdrew requiring about 70,000 enrollees to select a new plan.

⁸⁵Though HMOs may be offered in all states, they may not be offered in all counties of those states.

⁸⁶The six federal agencies that provided health plans included: the Federal Deposit Insurance Corporation, Office of the Comptroller of the Currency, Farm Credit Administration, Overseas Private Investment Corporation, Federal Reserve Board, and Federal Home Loan Bank Board. Employees selecting the agency plan could return to FEHBP 5 years before retirement to qualify for FEHBP coverage as an annuitant. See GAO, *U.S. Employees Health Benefits: Independent Agencies Offering Their Own Health Plans*, [GAO/HRD-89-49](#) (Washington, D.C.: Mar. 2, 1989).

had a much smaller effect on enrollment than would a USPS withdrawal.⁸⁷ OPM officials stated that these agencies, like USPS, have the legal authority to provide an alternative health care plan to employees. Officials noted that other federal agencies do not have that authority. Other agencies also do not have the direct financial incentive that USPS has to control and manage health care costs, because those agencies are not responsible for retiree health benefit liabilities.

Conclusions

USPS would likely realize large financial gains from reducing its liabilities for retiree health care by implementing its own health plan, thereby significantly reducing the need for future prefunding payments. Most of USPS's financial gains are achieved by increasing the use of Medicare, both by increasing enrollment in Parts A and B and gaining Medicare subsidies for prescription drug coverage under Part D, thereby increasing Medicare spending. Thus, the primary policy decision for Congress to make with respect to USPS's proposed health care plan is whether to increase postal retirees' use of Medicare, thereby decreasing USPS costs and increasing Medicare costs.

If Congress does not act on USPS's proposal for a new USPS health care plan, we continue to believe that Congress and USPS need to reach agreement on a comprehensive package of actions to improve USPS's financial viability. In previous reports, we have provided strategies and options, to both reduce costs and enhance revenues, that Congress could consider to better align USPS costs with revenues and address constraints and legal restrictions that limit USPS's ability to reduce costs and improve efficiency. We also continue to believe that Congress would need to modify the current statutory schedule for prefunding USPS's retiree health benefits payments in a fiscally responsible manner. In this regard, as we have reported, USPS should continue to prefund any unfunded retiree health benefits liabilities to the maximum extent that its finances permit.

⁸⁷According to OPM officials, all agencies returned their employees to FEHBP in the 1990s. According to OPM officials, when the agencies returned to FEHBP, the requirement for 5 years of continuous coverage in FEHBP prior to retirement to be eligible for FEHBP as an annuitant had to be waived for some retirees.

If Congress decides to move forward with USPS's proposed health plan as part of a broader reform package, other important policy issues remain to be addressed to reduce the risks of the proposed plan.

- First, under one alternative USPS's proposal would allow its health plan assets to be invested in stocks, private sector bonds, and other non-Treasury securities exposed to risk of losses. We agree with the U.S. Treasury Department that it is important to ensure the safety of fund assets supporting USPS health benefits for both current postal employees and retirees by restricting these assets to investments in federally guaranteed Treasury securities. However, we would suggest broadening the investment options beyond the special-issue Treasury securities currently used for PSRHB and federal pension funds to include inflation-indexed Treasury securities, to allow for partial protection against future inflation. Also, if Congress were to permit USPS to invest retiree health funds in non-Treasury securities, we would suggest that because of USPS's uncertain financial prospects and mature plan population, USPS not be permitted to use a discount rate, for prefunding purposes, that anticipates average long-term returns on such assets in excess of such long-term returns expected on Treasury securities before such returns have actually been achieved.
- Second, we conclude that the USPS proposal for allowing health fund assets to be transferred to unrelated postal funds in any year that assets supporting the USPS health plan exceeded the liabilities is not fiscally prudent. If USPS were to consistently exercise this option to help maintain its financial solvency, this could result in an unfunded liability for retiree health benefits.
- Third, under USPS's proposal, there can be some risk of overly optimistic assumptions in valuing the funded status of USPS's health plan, potentially leading to inadequate funding of benefits, because USPS's proposal does not provide for independent selection or oversight of assumptions, despite other safeguards USPS has proposed in this area. This risk could be reduced by having assumptions selected by an independent third party, such as an independent board of actuaries.
- Fourth, the USPS proposal ensures that postal employees and retirees in the USPS health plan will receive many but not all of the protections that FEHBP provides. Unlike FEHBP, there would be no statutory formula to establish USPS's share of the costs of retiree health benefits. This lack of a statutory formula means that there would be no limits on the share of costs that retirees may be required to contribute. The USPS proposal would require the plan to comply with other standards that protect enrollees in FEHBP and in nearly all

other private health insurance plans, e.g., standards prohibiting plans from setting lifetime limits on the value of coverage and relating to the review of appeals of benefit denials. However, without an express statutory requirement, it is unclear whether these standards would apply to a USPS plan.

Finally, in previous reports, we have stated—and continue to believe—that Congress should require arbitrators to consider the financial condition of USPS in any binding arbitration of collective bargaining over wages and benefits. Such a requirement would be even more important if USPS establishes its own health plan and its health benefits and contribution levels become subject to collective bargaining.

Matters for Congressional Consideration

A key matter for Congress to consider is whether or not to move forward with a USPS health plan that would result in an increase in retirees' use of Medicare. If Congress decides to approve this proposal, then Congress should also weigh the impact on other issues, including:

1. safeguards for all USPS health plan fund assets by placing appropriate constraints on their asset allocations, such as limiting investments to Treasury securities and inflation-indexed Treasury securities or, if Congress chooses to permit investments in non-Treasury securities, constraints on the discount rate for prefunding purposes so as not to anticipate returns on risk-bearing assets in excess of those on Treasury securities before such returns have actually been achieved;
2. standards for the disposition of any surplus health plan assets that reduce the risk of a new unfunded liability emerging in the future, standards such as amortizing any surplus to mirror the amortization of any unfunded liability, or using any surplus to offset normal cost payments;
3. designation or creation of an independent entity responsible for the selection of actuarial assumptions used to annually determine the funded status of USPS's health plan for purposes of determining prefunding payments; and
4. protections for postal employees and retirees that are comparable to those under FEHBP, including a formula for USPS retirees' contribution to the costs of their health coverage.

Agency Comments and Our Evaluation

We provided a draft of this report to USPS, the U.S. Treasury Department, and OPM for review and comment. USPS provided comments by letter, which are reprinted in Appendix III; the U.S. Treasury Department and OPM did not provide comments by letter. USPS also provided technical comments, as did the U.S. Treasury Department, which we incorporated as appropriate. USPS commented that it appreciated our thorough and rigorous analysis and took no position on our Matters for Congressional Consideration.

In its comments, USPS emphasized that its proposed restructuring of health care benefits is a key element of USPS business plans that it stated provide a path to solvency and fiscal sustainability for USPS. USPS also emphasized a number of other points related to its proposed health care plan: the potential effects of its proposed plan on Medicare finances; the investments of assets to finance retiree health benefits; and the effects on plan participants, including employees and retirees.

First, USPS noted that with regard to the effect of the proposed plan on Medicare's finances, Congress should consider that USPS and postal employees have been contributing to Medicare for almost 30 years and would be able to fully benefit from those contributions under the proposed plan. USPS stated that the annual savings to USPS and participants from the increased use of Medicare represents less than one day's claims under Medicare, but are a lifeline to USPS and vital to its business plans. As our report stated, USPS projected that its plan would increase the more than \$550 billion spent annually for Medicare by an average of roughly \$1.3 billion a year in the first 5 years of its health plan, which accounts for offsetting increases in Medicare premiums and drug discounts. However, the additional costs from USPS's proposed plan would have to be weighed alongside the fiscal pressures already faced by Medicare.

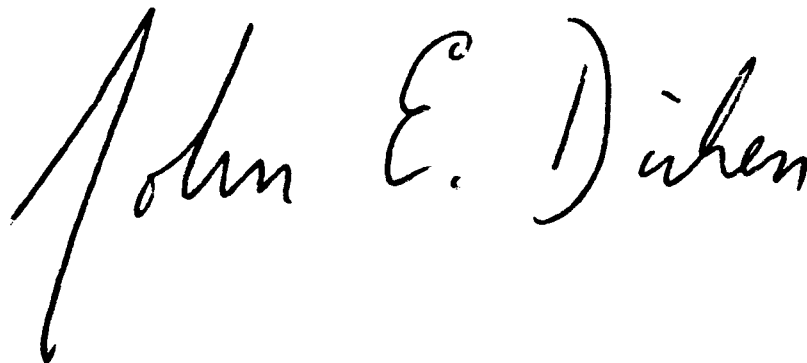
Second, USPS indicated that our report accurately reflected that USPS has proposed two alternative methods of investing USPS health plan assets and that either approach—investing solely in Treasury securities or in a mix that could include other types of assets—would be satisfactory to USPS.

Third, USPS stated that it had reviewed the graphs, tables and text we prepared to illustrate the potential effect on enrollees if the proposed USPS plan is adopted and found the material to be accurate. USPS agreed that our report was accurate in concluding that total costs for some postal employees and retirees could be higher under the proposed

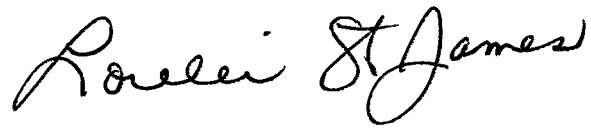
plan, but stated that the majority of enrollees would benefit economically from the proposed plan and provided information elaborating on this point. Our report states that while the majority of enrollees—between 63 and 97 percent—would likely pay similar or lower premiums under the proposed plan; some enrollees could be at risk for higher costs depending on the amount and cost of care they use, their use of out-of-network providers, and whether they have family coverage. USPS also stated in its comments that our report did not discuss the positive effects of USPS's proposed plan on retirees. We disagree with this assessment. The report presents the changes in benefits and costs that retirees would face under the proposed plan, including those that expand coverage and others that could result in higher costs for retirees.

As we agreed with your offices, unless you publicly announce the contents of this report earlier, we plan no further distribution of it until 30 days from the date of this letter. At that time, we will send copies of this report to the appropriate congressional committees, the Postmaster General, OPM, the U.S. Treasury Department, CMS, OMB, and other interested parties. In addition, the report will be available at no charge on GAO's Web site at <http://www.gao.gov>.

If you or your staffs have any questions on this report, please contact John E. Dicken at dickenj@gao.gov or call (206) 512-7114; Lorelei St. James at stjamesl@gao.gov or Frank Todisco at todiscof@gao.gov or call (202) 512-2834. Contact points for our Offices of Congressional Relations and Public Affairs may be found on the last page of this report. Contact information and key contributors to the report are listed in appendix IV.

A handwritten signature in black ink that reads "John E. Dicken". The signature is written in a cursive style with a large, sweeping initial "J".

John E. Dicken
Director
Health Care



Lorelei St. James
Director
Physical Infrastructure Issues



Frank Todisco
Chief Actuary
Applied Research and Methods

The undersigned meets the qualification standards of the American Academy of Actuaries to render the actuarial findings contained in this report regarding the measurement issues, funding issues, and risks associated with retiree health care obligations.

Frank Todisco, FSA, MAAA, EA
Chief Actuary

Appendix I: The Proposed Health Care Plan of the U.S. Postal Service

The U.S. Postal Service's (USPS) health plan would provide coverage for the approximately 1 million postal employees and retirees who are currently enrolled in the Federal Employees Health Benefits Program (FEHBP). It is designed to increase postal retirees' enrollment in Medicare and take advantage of Medicare subsidies for employer-based prescription drug plans. Aspects of the proposed plan would include:

Eligibility: All active employees, including bargaining unit and non-bargaining unit employees, would be eligible to participate in USPS's proposed plan. Further, all current retirees and survivors would be eligible. Employees would be eligible for coverage in retirement under the same circumstances that they are currently eligible for coverage under FEHBP—5 years of continuous coverage in the plan before retirement and eligibility for an immediate annuity. Under the USPS proposal, USPS employees and retirees would no longer be eligible to participate in FEHBP.

Benefits: Under the USPS proposal, for the first year of the health plan, the type and the average level and value of benefits for current retirees (including those who retire within one year of the date of enactment of the proposed legislation) and employees would be comparable to the most highly enrolled FEHBP plan.¹ After the first year, benefits for current retirees must continue to meet that standard. For employees, benefits would no longer have to meet that standard after the first year; however, any changes to benefits for employees would be subject to collective bargaining. Benefits for employees who retire a year or more after the effective date (i.e., future retirees) would also not be subject to the standard of comparable value to the most highly enrolled FEHBP plan.

Plan options: USPS would offer three plan options within a national preferred provider organization plan that would provide varying levels of coverage—referred to as the high, middle, and value options. USPS estimates that the value of benefits under the high option would be slightly higher than the value of benefits of the most highly enrolled FEHBP plan. The value of the benefits of the middle option would be

¹The proposal provides that the "aggregate actuarial value of benefits shall be at least equivalent to that of the FEHB plan with the highest enrollment." For those eligible for Medicare, the aggregate actuarial value will include the value of Medicare benefits. The actuarial value of the benchmarked coverage would be documented in an actuarial opinion that meets actuarial standards of practice.

slightly lower; and the value of the benefits under the value option—designed to provide a more limited benefit—would be significantly lower. USPS would offer an HMO option in geographic areas where large numbers of postal employees are currently enrolled in HMOs—specifically, staff or facility-model HMOs—within FEHBP. As of April 2013, USPS had not determined in which geographic areas HMOs would be offered or what services would be covered and at what levels.

Premiums: Premium rates would vary across the plan options and depending upon which of the four tiers of coverage the employee or retiree needs: self-only, self-and-spouse, self-and-children, or self-and-family. USPS estimates that employee contributions in the first year would equal 26 percent of the cost of the high option, 18 percent of the middle option, and 17 percent of the value option. Retiree contributions are estimated at 32 percent of the cost of the high option and 25 percent of the middle and value options. As with benefits, initial premium contribution rates would be set by the governance board. Any changes to employee contribution rates would be subject to the collective bargaining process.

Plan administration: The USPS plan would be self-insured, which means that USPS would set aside its own funds to pay for benefits rather than purchasing insurance from an insurance company. USPS would administer enrollment, which it currently does for employees participating in FEHBP, but would contract with one or more outside entities to administer benefits. USPS plans to use a competitive bidding process to hire one or more plan administrators, which would be responsible for providing a national provider network, offering care management and patient assistance, processing and reviewing claims, and paying providers.

Appendix II: U.S. Postal Service Proposals for Health Plan Financing

All material in this appendix was summarized from information provided by USPS on the aspects of its proposed health plan financing.¹ GAO did not independently verify the legal accuracy of any of the statements or material contained in the appendix.

Funding the USPS Health Plan, Including Financing of Any Unfunded Liabilities and Repeal of Current Statutory Prefunding and Amortization Payments

The USPS proposal would establish advance funding of its health plan based on payment of a normal cost and amortization of any unfunded liability or surplus of its retiree health care liabilities over an amortization period ending at the later of 40 years after the new plan is implemented, or 15 years from the then-current year, beginning with the fiscal year ending after the implementation date (e.g., September 30, 2014, if the implementation date is January 1, 2014).² The USPS proposal seeks a repeal of all PAEA scheduled and deferred payments to prefund retiree health benefits that have statutorily fixed payments through 2016 and then amortize remaining unfunded retiree health benefit liabilities starting in 2017. In addition, USPS stated that under its proposed health plan, there would be no explicit federal guarantee of USPS health benefits for USPS employees, annuitants, or survivors, including any participants in the USPS health plan.

USPS Has Proposed Two Options to Finance Its Proposed Health Plan for Congress to Consider

Under one option of USPS's legislative proposal (which USPS refers to as "Scenario 2"), the existing Postal Service Retiree Health Benefits Fund (PSRHBF) would be transferred into a newly created Postal Service Health Benefits Fund (HBF). Assets of this new fund could be invested in stocks, private sector bonds, and other non-Treasury securities exposed to risk. According to USPS, in response to concerns that have been expressed about the investment of assets for retiree health care in other than Treasury securities under Scenario 2, it developed a different option for financing its health plan (which it refers to as "Scenario 1"). Under Scenario 1, the PSRHBF would be continued and used to finance retiree health benefits under USPS's health plan. USPS officials have stated that Congress's adoption of either scenario is acceptable to USPS and they are open to any reasonable resolution of issues of asset management by Congress.

¹All references to titles below are to titles of the United States Code.

²This schedule would approximately parallel timeframes currently applicable to the Postal Service Retiree Health Benefits Fund in subsection (d)(2)(B) of section 8909a of title 5.

**Scenario One: PSRHB
Used to Finance Retiree
Health Benefits under
USPS's Health Plan**

Under one option for financing the proposed USPS health plan (which USPS refers to as "Scenario 1") the PSRHB would be continued and used to finance retiree health benefits under USPS's health plan, though without continued OPM management since the health plan would be administered by USPS. All future funding of USPS's retiree health benefits liability would be deposited into the PSRHB. According to USPS, if Scenario 1 summarized above is adopted by the Congress, USPS would expect that all funds set aside for retiree health care benefits would be retained in the PSRHB, and would not be commingled with the funds USPS would use (including any reserve funds such as for incurred but not reported claims and for margin for claims fluctuation) that might be maintained in the financing of the active employee health benefit plan.

Under Scenario 1, USPS stated that the current and future assets of the PSRHB would continue to be invested as now, in special-issue Treasury securities or otherwise as might be directed by the Congress. USPS also stated that it would prefer to have some input on the structure of the asset holdings so that the PSRHB's investments were matched by duration to the expected benefit payments. USPS said that could be accommodated with the use of Treasury securities and is a sounder way of matching assets and liabilities than is currently in place.

**Scenario Two: New HBF to
Finance USPS Health Plan**

Under one option of USPS's legislative proposal (which USPS refers to as "Scenario 2"), the USPS health plan would be financed by the newly created HBF, which would be established by law.³ The HBF would be a revolving fund within the U.S. Treasury, available to USPS without fiscal-year limitation to pay benefits claims and administrative expenses incurred under the USPS health plan. The HBF would contain deposits that include:

- The balance of the PSRHB transferred to the HBF no later than 30 days after enactment with the PSRHB abolished upon such transfer. USPS would make no further contributions to the PSRHB.
- The balance of the OPM-managed Employee Health Benefits Fund (i.e., the fund that finances FEHB) that is allocable to contributions by USPS, its officers and employees, and its annuitants, including any amounts held by OPM in any reserve fund. (USPS would bear no

³All provisions summarized for Scenario 2 would be specified by federal law under USPS's legislative proposal for its health care plan.

further liability for contributions to the Employee Health Benefits Fund.)

- USPS contributions under its health plan.
- Contributions of USPS employees, officers, and annuitants, and the dependents of such persons, under the USPS health plan.
- Interest that may be earned on investments of the HBF.
- Any other receipts of USPS that are allocable to the USPS health benefits plan.
- U.S. Treasury Department payments for service of officers and employees of the former U.S. Post Office Department that are allocable to the Treasury under section 8906(g)(2) of title 5 (i.e., the federal government picks up the portion of costs attributable to pre-1971 service).

After PSRHBF assets are transferred into the HBF, these transferred assets would be comingled with the HBF assets and could be used for any purpose that the HBF could be used. This would permit (but not require) PSRHBF assets to be used after their transfer into the HBF for purposes other than USPS retiree health benefits, such as for USPS health benefits for current employees. However, USPS has stated that if it is able to form its own health care plan outside of FEHBP and thereby reduce its remaining retiree health benefit liability to zero, the funds it has already set aside in the PSRHBF would be dedicated solely to the payment of retiree health benefits. USPS has further asserted that the HBF would be fully insulated from creditors so that, even in the event of USPS insolvency, retiree health benefits would continue to be paid.

In this regard, USPS indicates that federal law would not allow assets of the HBF to be used to (1) loan monies to the Postal Service Fund, such as to enable it to remain solvent; (2) cover other required USPS payments to the federal government, such as for pensions and workers' compensation, if USPS did not have sufficient funds to make such payments; and (3) finance USPS investments in property for post offices or other USPS operations, in delivery vehicles or technology for postal operations, or in nonpostal initiatives to generate revenue.

Investment of Assets of HBF

Under Scenario 2, USPS would be authorized to invest sums in the HBF in instruments or obligations selected by one or more qualified professional asset managers. For purposes of such investments, "qualified professional asset manager" would have the meaning under section 8438(a)(8) of title 5. Through these investments, USPS would seek to increase investment returns on more than \$40 billion in assets of the HBF. Investment decisions for HBF assets would not require the approval of the Secretary of the Treasury, or for the Secretary to be

advised before the purchase or sale of any instrument or obligation of the HBF.

Under Scenario 2, HBF assets could be invested in non-Treasury securities, such as stocks and bonds, as well as commodities, foreign currency, and real property. In this regard, USPS stated that federal law would allow the HBF to acquire a controlling interest in stock of a private company, if such an action was consistent with the Committee's fiduciary responsibilities (including the responsibility to diversify where the assets in the HBF are invested).

USPS-Appointed Committee to
Oversee the HBF

The USPS Governors would be required to appoint a 7-member Committee (the Committee) to oversee the investment and management of the assets of the HBF. Members of the Committee would be required to have substantial experience, training, and expertise in the management of financial investments and health benefit plans.

The Committee would be required to have, at all times, members that include at least 1 person recommended by the Secretary of the Treasury, at least 1 person recommended by the labor organizations recognized under chapter 12 of title 39, and at least 1 person recommended by the supervisors' and postmasters' organizations specified in section 1004(i) of title 39. Each member of the Committee would be appointed for a term of 4 years, subject to a one-time reappointment, except that of the members first appointed, 3 members shall be appointed for terms of 4 years; 2 members shall be appointed for terms of 3 years; and the remaining members shall be appointed for terms of 2 years. In addition, Committee members would be subject to the following provisions applicable to fiduciaries under Employee Retirement Income Security Act (ERISA): sections 1104 through 1106, 1108, and 1110 of title 29, notwithstanding section 1021(e) of title 39 and section 1003(b)(1) of title 29, and with the provisions of sections 1131 and 1132 of title 29 applying only to the extent those provisions concern the performance of fiduciary responsibilities.

Transfer of Any Surplus
Health Plan Assets to
Postal Service Fund

USPS officials told us that their principal concern is that they would prefer to have the question of the potential disposition of excess assets set aside for retirees addressed in the legislation, to avoid the uncertainties they told us have arisen with respect to that question in the funding of the Civil Service Retirement System and the Federal Employees Retirement System. They noted that it is possible to envision some circumstances in which the surplus could be quite large, and as a result, some guidance

from Congress as to the potential disposition of surplus, under whatever strictures Congress would see fit to impose, would be appropriate. They told us that while they made an initial proposal in their August 2011 legislative language, they are open to any reasonable resolution of this issue.

Under Scenario 2, in any year when the amount of assets in the HBF exceeds this fund's estimated actuarial liability, USPS could authorize the surplus amount to be transferred to the Postal Service Fund, provided that such authorization is made pursuant to a recommendation by a majority of the Committee. Before approving such a recommendation, the Committee would be required to obtain an opinion and report by an actuary—who would be required to hold membership in the American Academy of Actuaries and be qualified in the evaluation of healthcare insurance obligations—in accordance with generally accepted actuarial practices and principles, with a certification that a decision to transfer funds would not violate the statutory criteria that the amount of assets in the HBF exceeds this fund's estimated actuarial liability.

Appendix III: Comments from the U.S. Postal Service

JEFFREY C. WILLIAMSON
CHIEF HUMAN RESOURCES OFFICER
AND EXECUTIVE VICE PRESIDENT



Ms. Lorelei St. James
Director, Physical Infrastructure
United States Government Accountability Office
Washington, DC 20548-0001

Dear Ms. St. James:

We appreciate the opportunity to review the Draft Report on the USPS Proposed Health Plan provided us by the GAO. Below are the agency comments. In a separate document are suggested edits where we point out areas where we believe the GAO should make changes to the Report Draft, to correct errors (some of which are quite minor) and to provide a more accurate description of USPS's positions on certain matters, especially on the protections for participants that we have proposed to the Congress.

We want to express our appreciation to the GAO for the thorough and rigorous analysis they have conducted of the legislative proposal USPS has made to the Congress for restructuring health care benefits provided USPS employees, retirees, and their families.

As the Postmaster General has testified before the Congress, the proposed restructuring of health care benefits is a key element of USPS business plans that provides a path to solvency and fiscal sustainability for the Postal Service.

We believe that the GAO report will be of great assistance to the Congress as it considers this proposal in the context of more comprehensive postal reform legislation. It is in that spirit that we offer as requested by GAO USPS comments on the GAO Report, so that the Congress will have a complete record before it as it undertakes the important task of crafting the legislation that will be necessary to effect that result.

In summary we believe the following to be the most important points the Congress should consider in reviewing the GAO Report:

- **Integration of the USPS proposed health care plan with Medicare and the effect of the plan on Medicare finances**

USPS and postal employees have been contributing to Medicare for almost thirty years. Our proposal would permit USPS and participants to benefit fully from those contributions after retirement, by assuring that Medicare would be primary and the USPS plan secondary for the purpose of claims payments for expenses covered under Parts A and B of Medicare, and by providing prescription drug benefits under an Employer Group Waiver Plan (EGWP). As the GAO Report points out, the EGWP plan will allow USPS to take advantage of the substantial discounts available for prescription drugs under the provisions of the Patient Protection and Affordable Care Act. Those discounts are available in no other way.

The GAO has reported on the effect on Medicare finances. There are two important points to emphasize, however:

- The savings to USPS and participants are offset significantly by additional participant contributions to Part B of Medicare from new participants, and by the discounts offered by Pharma in the drug pricing arrangements under the PPACA; and

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- The annual savings to USPS and participants represents less than one day's claims under Medicare. Those savings on the other hand are a lifeline to USPS, and vital to our business plans. And these savings do not come at the expense of a single job or require the closing of any post office or postal facility.

- **Investment of assets set aside to fund retiree health benefits**

GAO has correctly noted that USPS has proposed two alternative methods of funding for retiree health benefits:

- Continuation of the Postal Service Retiree Health Benefits Fund, with all assets (current assets plus future contributions) retained in that fund and invested in Treasury instruments; or
- Investing assets in a manner more consistent with the investment of retirement plan assets generally in the U.S. economy, with a mix of investments designed to recognize the lengthy time horizon associated with retirement plan commitments and to seek investment returns that will better the returns likely to be available under the current investment policy for the PSRHB.

Either approach would be satisfactory to USPS. We will abide by the instructions of the Congress with respect to the investment of plan assets.

- **Benefits and costs to participants**

USPS has provided extensive information to the Congress and the Administration on the potential effects of the proposed health care plan on both USPS finances and on participants. We believe that the data we have provided the Congress and the Administration show conclusively that the great majority of participants will have comparable or superior health benefits, at a lower cost to participants. We respectfully provide more extensive comments on these issues for the consideration of the Congress. We would be pleased to provide further information on these subjects as required as the Congress considers action on USPS's proposal.

Comments on the Effects of the USPS Health Care Proposal on Plan Participants

We offer the following comments and observations to provide additional context for the Congress and for USPS stakeholders on the subjects discussed in the GAO Report under the heading "COMPARED TO FEHBP, POSTAL EMPLOYEES AND RETIREES WOULD HAVE COVERAGE FOR SIMILAR SERVICES BUT ELEMENTS OF THE PROPOSED PLAN'S DESIGN COULD LEAD TO HIGHER COSTS FOR SOME ENROLLEES" beginning at page 26 of the GAO Report.

We have reviewed the graphs, tables and text prepared by GAO to illustrate the potential effect on enrollees if the proposed USPS plan is adopted and find the material to be accurate. It is also accurate to state, as GAO does at page 26 of the Report that "total costs—premiums and costs for the use of care—could be higher for some, due in part to higher deductibles and out-of-pocket maximums under the USPS plan." However, the great majority of participants will benefit economically from the proposed plan, and substantially. In that regard some additional context is important.

- A careful review of the data presented in table 7 at page 32 of the GAO Report shows that where health care services are secured in-network, the USPS High Option Plan has deductibles at or below the range shown for the six large FEHB plans with which the data is compared; and the deductible for the USPS Middle Option Plan is only slightly higher than the range presented for the six FEHB plans.
- The same sort of observation can be made with respect to the out-of-pocket maximum exposure under the respective plans illustrated. For the USPS High Option plan, the self-only out-of-pocket

Now on p. 30.

Now on p. 30.

Now on p. 37.

Now on pp. 33-34.

maximum is below the range depicted for the six FEHB plans for in-network services. And for families the out-of-pocket maximum in-network is at the high end of the range depicted in the table for the six FEHB plans, but still within that range.

- In presenting the data in Table 7 for annual deductibles and out-of-pocket maximum exposure for out-of-network services, GAO has not presented data in a way that readily shows the amounts of the out-of-network deductibles and out-of-pocket maximums. Rather, it has summed the in-network and out-of-network deductibles and the in-network and out-of-network maximums assuming that in a given year a participant would be exposed to both. As GAO has pointed out, however, out-of-network care is not only uncommon but is relatively rare (see page 29, Services received out-of-network). And, of course, the percentage of individuals who receive services both in-network and out-of-network in a given year would represent only a subset of that already small population.
- Moreover, officials of the largest FEHB plan by population reported to us that in that plan, out-of-network usage is less than 2% of total claims.
- While GAO has included the seven largest FEHB plans for some purposes, one was excluded from the comparison of the deductibles and out-of-pocket maximum exposure. It is the second largest FEHBP plan by population, and it is an Exclusive Provider Only Plan (EPO). While we would agree that that makes the structure of that plan more like an HMO and that it perhaps should be excluded from the Table 7 for that reason, we should still point out that in such plans there is no benefit at all where services are provided out-of-network. Thus, the out-of-network exposure is unlimited and there are zero out-of-network claims eligible for payment.
- Finally, as we pointed out in our earlier submissions to GAO, USPS established in its market research with major health care vendors that all of the major vendors have robust networks that assure that almost all participants will have ready access to network providers. And where that is not the case, the proposed USPS plans will provide that the vendor must pay benefits subject to the in-network provisions with respect to deductibles, copays, coinsurance and out-of-pocket maximums.

Aggregate Effects on Premiums and Savings to Plan Participants

We believe it will be useful to the Congress and to stakeholders (including employees and retirees) to understand that while there will indeed be instances where a particular participant in a particular year may be exposed to somewhat higher costs, there are many more situations where the costs to participants will be lower, as the GAO Report shows and the graph in Figure 1 at page 31 illustrates to some degree.

Premiums—or premium equivalents, which is the correct term for self-insured plans such as the USPS proposed plan—are projected to be lower by some 16% than premiums under the FEHB plans on average. That reduction is primarily driven by the savings achieved through integrating the plan for retirees with Medicare Parts A and B in the way that is almost universally done in the private sector and in state and local government health care plans that continue to provide health care coverage for retirees; and by introducing the EGWP plan for prescription drug benefits for Medicare eligible retirees, to take advantage of the savings available under Medicare Part D and the provisions of the PPACA which GAO has described in the Report.

That reduction in premiums is achieved while retaining plan designs that are simpler and easier for participants to understand than the multitude of choices available under FEHBP. And the range of plan value—from the most generous High Option Plan to the least generous Value Plan—will be comparable to the range in value available in the FEHB offerings. But there will be some key differences, which we explain briefly below.

Now on pp. 35-36.

This premiums savings will be shared with all plan participants. In the aggregate participants are projected to pay in the first year \$659 million less in premium contributions than they are currently paying for FEHB plans. That will represent a savings of approximately \$700 annually on average for each employee and annuitant who participates in the plan.

Here are some of the other key differences compared with FEHBP:

- GAO has correctly pointed out in the Report that plan costs are not always consistently aligned with plan value. That is especially true in the array of plans within FEHB, where the costs are determined almost entirely by the demographics (and the claims) that have emerged within the plans over time. Some plans with less generous benefits are costly; and some with more generous benefits are inexpensive. There is essentially no correlation between the value of the plans and the cost of the plans in the FEHB system.
- In the simpler array of choices that USPS proposes (which reflects the common approach in employer sponsored plans in the U.S.) there will be a transparent, consistent, and completely understandable relationship between the value of the plan a participant selects and the cost of that plan among the PPO options that are the backbone of the proposed plan structure. The High Option plan will be the most generous and most expensive; the Value plan will be the least generous and least expensive; and the Middle Option plan will be in between.
- This structure will allow participants to make better choices, consistently aligned with their current health care needs and tolerance for risk.
- The reduction in the premiums that the savings makes available also is a factor in USPS's decision to move to a four-tier structure for participant contributions. The four-tier structure is more common in the private sector and in state and local government plans than the two tier approach (self and family choices only) still in use within FEHB. Usually such a change is a zero sum game, requiring that those who need full family coverage pay higher premiums to finance the savings available for those who need to cover only a spouse, or dependent children. The premium savings under USPS's proposal permit the contributions to stay approximately the same as now under FEHBP for those who must cover both a spouse and a child or children (i.e. those who would enroll in the family option under the new USPS plan), for comparable coverage. Those who do not require full family coverage, however, will see a further and significant reduction in their contributions. This could offer savings to virtually all participants over the course of a career with USPS and in their retirement years, as a participant's family status changes over time.

The Effect of the Proposal on Current and Future Retirees

The positive effects of the proposed USPS plan on retirees is not discussed in the GAO Report. To illuminate those effects, it is important to break down the retiree participant population into categories, as follows:

- Current Retirees under Age 65
- Current Retirees Age 65 and over who participate in Medicare
- Current Retirees Age 65 and over who do not participate in Medicare
- Future Retirees

Current Retirees under Age 65

Retirees under age 65 will be in the same position as active employees. Many will benefit by the lower premium structure overall. And all will have the benefit of comprehensive prescription drug coverage,

regardless of whether they select the High, Middle or Value Option Plan. A key feature of the proposed USPS plan design is that the drug benefits will be uniform across all medical plan options. That will encourage all participants to maintain drug regimens, which is important for their health and to assist in avoiding potentially greater medical costs if regimens are not maintained. And the drug benefits under the USPS proposed plans as a general rule are better than those provided under the FEHB plans, especially for those with substantial drug expenses who will exceed the out-of-pocket maximum of \$1,500 annually. Finally, many retirees (whether under age 65 or not) will no longer have dependent children under the plan and will benefit significantly from the USPS plan's four-tier structure, as they will be able to select enrollment options with lower premium contributions than those required for self and family coverage.

Current Retirees Age 65 and over who participate in Medicare

This cohort is the great majority of Medicare eligible retirees, approaching 80% of all retirees over age 65. This group will benefit greatly by the changes USPS has proposed.

As GAO has pointed out in the Report, for medical expenses covered by Parts A and B of Medicare, where Medicare is primary, the combination of Medicare and the supplemental benefits paid by the USPS plan will cover 100% of the expense for virtually all claims.

Moreover, that 100% protection will be available whether the participant elects the High Option Plan or the Middle Option Plan, since either provides sufficiently generous benefits so that, in combination with Medicare as primary, 100% of charges will be paid. Thus, we expect that many current retirees now in more costly FEHB plans will select the Middle Option Plan and benefit from the lower premium cost of that plan compared with their current selection in FEHB, while retaining the same or (when prescription drugs are considered) superior benefits. As we pointed out above, prescription drug benefits are the same regardless of the medical plan option elected, so there is comprehensive drug coverage as well.

USPS intends to communicate these facts aggressively to our retiree population. The opportunity to move to the less expensive Middle Option Plan (or even the Value Plan), coupled with the overall premium savings and the fact that the great majority of those needing dependent's coverage in this cohort will have only a dependent spouse, will provide significant savings to this group of USPS retirees.

Current Retirees Age 65 and over who do not participate in Medicare

As GAO has pointed out in the Report, this cohort of retirees will be required for the first time to pay for Part B of Medicare (currently at the rate of \$104.90 monthly for most Part B participants). However, they will also benefit from all of the savings available to those retirees who do currently participate in Medicare:

- They can select the less costly Middle Option Plan and still retain 100% coverage for those expenses covered under Parts A and B of Medicare;
- They will have excellent drug coverage;
- They will benefit from the lower overall premium structure; and
- Many who now insure self and family will be able to move to self-and-spouse coverage, creating additional savings.

For most such participants, the combination of these savings will compensate or more than compensate for the Part B premiums. Moreover, if they do not have Medicare coverage now, they are currently exposed to the costs associated with the deductibles, copays, and coinsurance features of the FEHB plan in which they participate. Our analysis which we have presented to staff of the key committees in the Congress has shown that particularly those participants in this cohort who have significant medical expenses—with concomitantly high out-of-pocket costs in their FEHB plan—will benefit by many thousands of dollars more than the additional cost of Part B coverage.

Future Retirees

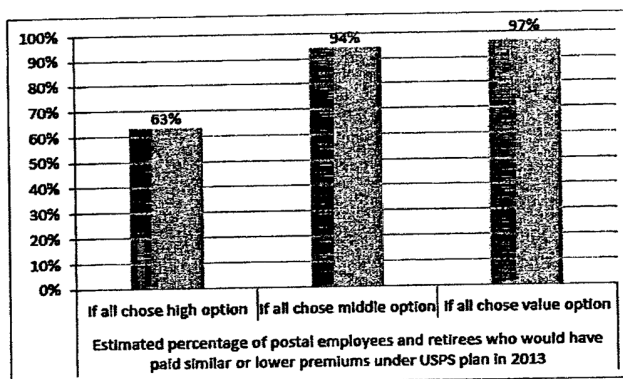
As GAO has pointed out, USPS's proposal does contemplate that for retirees who retire one year or more after the effective date of the new plan, their coverage for Medicare A and B expenses will not be at the 100% level provided retirees now. Their supplemental coverage will be paid on a basis that will leave them with the same deductibles, copays, and out-of-pocket maximums that applied during active employment and during their retirement years before age 65.

As GAO also pointed out in the Report, "[GAO] and other researchers have previously reported that this so-called 'first-dollar coverage' can lead to increased utilization and higher total expenditures in the absence of other cost-control measures." That is one of the principal reasons why the USPS proposal contemplates the elimination of the first-dollar coverage for future retirees. While the same criticism could apply to first dollar coverage for current retirees and for those who elect to retire within the first year after the proposed plan takes effect, USPS would nevertheless continue to provide first dollar coverage to those populations in the interest of avoiding undue disruption to their expected benefits.

This approach is consistent with typical plan design for Medicare eligible retirees in the private sector and in state and local government plans, and it is a necessary element to eliminate the current unfunded liability for retiree health care benefits for USPS.

Comments on Figure 1, Page 31: Percentage of Postal Employees and Retirees from Selected FEHBP Plans Who Could Obtain Similar or Lower Premiums under the Proposed USPS Health Plan, 2013

Figure 1: Percentage of Postal Employees and Retirees from Selected FEHBP Plans Who Could Obtain Similar or Lower Premiums Under the Proposed USPS Health Plan, 2013



Source: GAO analysis of USPS estimates of 2013 premiums, 2013 premiums for seven selected FEHBP plans, and OPM data on FEHBP enrollment in 2011.

Note: For these estimates, we defined "similar" premiums as those within 10 percent of the premium the employee or retiree would have paid in 2013 for their FEHBP plan and "lower" premiums as those more than 10 percent less than the FEHBP premium. The estimates assume that enrollment in the selected FEHBP plans did not change from 2011 to 2013. Estimates also use USPS's assumptions of the distribution of those with family coverage under FEHBP across the three levels of family coverage offered under the USPS proposed plan. The estimates account for Medicare Part B premiums that Medicare-eligible retirees are assumed to pay under USPS's proposed plan.

The graph in Figure 1 at page 31 significantly understates the actual percentage of postal employees and retirees who will benefit from lower premiums under the plan, in the depiction presented in the first bar in the graph on the left.

While the explanatory text below Figure 1 indicates that the distribution of family coverage GAO has assumed across the three tiers reflects the assumptions that USPS has made with respect to that distribution, it is simply not possible that all participants will choose the high option plan, just as participants do not all choose the highest cost plans among the array of plans offered within FEHB.

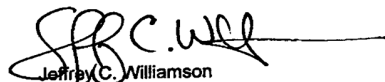
Moreover, the first bar in the graph fails to capture the essential points that we raise immediately above in the discussion of the effect of the new plan offerings on retirees. Especially among the retirees, there will be a substantial migration to the lower cost plans (both the Middle Option and Value Option plans) from high cost FEHB plans, resulting in substantially lower costs for retirees. That reflects the factors cited above:

- A much higher percentage of retirees than active employees will no longer require coverage for dependent children;
- Medicare eligible retirees will benefit from 100% of coverage for those medical expenses covered both by Medicare Parts A and B and by the USPS plans regardless of the plan they select;
- There is no difference in prescription drug benefits regardless of the plan they select;
- The simpler plan structure will help employees and retirees make better plan choices, aligning their choices with their health care needs; and
- The aggressive communications that USPS will undertake to explain the new plan, and the interaction with Medicare benefits to Medicare eligible retirees, will assure that migration.

The result will be that, on an overall basis – that is, when one accounts for various cost-saving factors and the likelihood that enrollees will sort themselves according to what is financially beneficial for them – the percentage of participants who will realize a reduction in their premium contributions will be much higher than the 63% of participants illustrated in the first bar in the graph in Figure 1.

Thank you for this opportunity to provide recommended corrections and comments on this important report to the Congress.

Sincerely,



Jeffrey C. Williamson

Attachment

Appendix IV: GAO Contacts and Staff Acknowledgments

GAO Contacts

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Staff Acknowledgments

In addition to the individuals named above, Robert F. Dacey, Chief Accountant; Beryl H. Davis, Director, Financial Management and Assurance; Gary T. Engel, Director, Financial Management and Assurance; Susan J. Irving, Director for Federal Budget Analysis, Strategic Issues; Thomas J. McCool, Director, Center for Economics, Applied Research and Methods; Susan E. Offutt, Chief Economist; Phyllis Anderson; Teresa Anderson; Susan Barnidge; George Bogart; Russ Burnett; Colin Fallon; Krister Friday; Kenneth John; Gene Kuehneman; Michael Kendix; Hannah Laufe; Kristi Peterson; Steve Robblee; Friendly Vang-Johnson; and Crystal Wesco made key contributions to this report.

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