September 24, 2007

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EXECUTIVE VICE PRESIDENT AND
CHIEF HUMAN RESOURCES OFFICER

SUBJECT: Audit Report - Postal Service's Employee Benefit Programs
(Report Number HM-AR-07-003)

This report presents the results of the U.S. Postal Service Office of Inspector General's (OIG) self-initiated audit of the Postal Service's Federal Employees Group Life Insurance (FEGLI) and Federal Employees Health Benefits (FEHB) programs (Project Number 07YG008HM000). The purpose of this review is to provide the Postal Service with information regarding its current employee benefit costs compared to most other federal and quasi-federal agencies participating in the same benefit programs.[1] Our overall objective was to determine if the Postal Service programs are comparable to selected federal and quasi-federal government agencies; and if differences exist between the Postal Service's employee benefit contributions and those provided by the selected agencies. We also determined if changes could be made to the Postal Service's contributions and the potential costs associated with such changes.

We concluded the Postal Service's FEGLI and FEHB programs for bargaining[2] and non-bargaining[3] employees are comparable to the six federal and five quasi-federal agencies against which we benchmarked. However, the Postal Service's contribution rates[4] for both programs were significantly higher compared to most agencies.

For example, the Postal Service pays the full cost of the premiums for almost all employees' FEGLI basic life insurance and for executives' Option-A life insurance and FEHB benefits. Most other agencies pay 33 percent of the FEGLI premiums and 72 percent of the FEHB premiums for their employees. We also found the Postal Service made great progress in reducing future FEHB costs when it successfully negotiated with two of its major unions — the American Postal Workers Union (APWU) and the National Postal Mail Handlers Union (NPMHU) — for a reduction in the

[1] A quasi-federal agency is a colloquial term used in this report to describe non-traditional federal executive branch entities like government corporations, government-controlled corporations, independent establishments, and independent trusts.
[2] Bargaining employees are represented by labor unions that negotiate with the Postal Service for wages, hours, and other terms and conditions of employment. These employees include city and rural letter carriers, clerks, mail handlers, special delivery messengers, maintenance employees, and motor vehicle operators.
[3] Non-bargaining employees are career and non-career employees in supervisory professional, technical, clerical, administrative, and managerial positions in the Executive and Administrative Schedule (EAS) who are not subject to collective bargaining agreements.
[4] The contribution rate is the percentage of the life insurance or health benefit premiums the agency or employer pays on behalf of the recipient.

agency's FEHB contribution rate of 1 percent for each year of the new collective bargaining agreements. This will result in a $713 million savings for the Postal Service over a 10-year period.

We also determined the Postal Service can change existing FEGLI and FEHB contribution rates through negotiations with its unions (for bargaining employees) and consultations with management associations (for non-bargaining employees). These changes could result in significant savings for the Postal Service. Specifically, we estimate the present value of the Postal Service's potential savings resulting from further reductions in benefit program contributions to be $1.073 billion over 10 years.[5] This represents $1.073 billion in funds put to better use and will be reported as such in our *Semiannual Report to Congress*. (See Appendices B and C for a summary of the monetary impact and cost avoidance methodology, respectively.)

This report contains four recommendations that would allow the Postal Service to continue providing employees with benefits that are on a par with those provided other federal employees, while significantly reducing the agency's cost obligations.

Management's comments are responsive and the actions taken should correct the issues identified. Management's comments and our evaluation of these comments are included in the report.

Background

The U.S. Postal Service's *Strategic Transformation Plan 2006–2010* (*Transformation Plan*) states the Postal Service will use comprehensive studies of bargaining and non-bargaining positions to establish and maintain wages and benefits comparable to the private sector's and, at a minimum, the same as those of other federal employees. This is in keeping with its statutory mandate.[6] The *Transformation Plan* also states the Postal Service will explore alternatives to current health benefits programs for future employees.

The Postal Service offers both life and health insurance benefits to all career employees by participating in the FEGLI and FEHB programs. The federal government established the FEGLI Program in 1954 and the Metropolitan Life Insurance Company administers it under a contract with the Office of Personnel Management (OPM). It is the largest group life insurance program in the world, covering over 4 million federal employees and retirees and many of their family members. In calendar year (CY) 2006, the Postal Service paid approximately $200 million for life insurance for its employees. Of this amount, $172 million was for bargaining employees and $28 million was for

[5] We made a similar recommendation for achieving a 10-year savings in our report entitled *Postal Service's Grievance-Arbitration Service Centers* (Report Number HM-AR-06-006, dated August 29, 2006). In that report we acknowledged the Postal Service could only achieve savings with the cooperation and agreement of the four major unions.
[6] Postal Reorganization Act (PRA), Title 39, U.S. Code 39, § 1003 (a) and §1005(f), August 12, 1970.

non-bargaining employees.[7] This represents a $4 million increase from the approximately $196 million paid for life insurance benefits in CY 2005. The Postal Service paid more in life insurance premiums even though the number of employees participating in FEGLI decreased 1.8 percent from CY 2005 to CY 2006.[8]

The federal government established the FEHB Program in 1960 and the OPM's Office of Insurance Programs administers it. It is the largest employer-sponsored group health insurance program in the world, covering over 9 million federal employees, retirees, former employees, family members, and former spouses. In CY 2006, the Postal Service paid approximately $4.7 billion in health insurance premiums for approximately 696,000 career employees. This is an increase of $200 million from CY 2005 and represents 6.5 percent of the Postal Service's total operating expenditures of $71.9 billion. The Postal Service paid more in health insurance premiums even though the number of employees participating in FEHB decreased 1.3 percent from CY 2005 to CY 2006. This occurred, according to the OPM, because the average cost of premiums increased by 6.6 percent in 2006.

We benchmarked the Postal Service's FEGLI and FEHB benefit programs against the following six federal and five quasi-federal agencies:

Federal Agencies

- Department of Homeland Security (DHS)
- Department of Defense (DOD)
- Department of Transportation (DOT)
- Department of the Treasury (Treasury)
- Department of Agriculture (USDA)
- Department of Veterans Affairs (VA)

Quasi-federal Agencies:

- Federal Deposit Insurance Corporation (FDIC)
- Federal Reserve Board (FRB)
- National Credit Union Administration (NCUA)
- Office of Thrift Supervision (OTS)
- Tennessee Valley Authority (TVA)

See Appendix D for a profile of the Postal Service and the benchmarked agencies.

Objectives, Scope, and Methodology

We discuss our objectives, scope, and methodology in Appendix E.

[7] The FEGLI Program does not require federal and quasi-federal agencies (including the Postal Service) to contribute to life insurance premium costs for retirees.
[8] Life insurance costs are sensitive to increases in basic pay resulting from promotions, cost-of-living allowances, and pay-for-performance.

Prior Audit Coverage

We did not identify any prior audits related to the objectives of this audit.

Audit Results

Postal Service FEGLI Benefits Are Comparable to Federal and Quasi-Federal Benchmarked Agencies

The Postal Service's FEGLI benefits for bargaining and non-bargaining employees are comparable to the federal and quasi-federal agencies we benchmarked against, in that coverage is basically the same. In fact, we found the Postal Service FEGLI benefits were comparable with most federal and quasi-federal agencies. However, we did note that four of the quasi-federal agencies have alternative life insurance plans (in addition to the FEGLI plan) and the Postal Service has no alternative plans.

The FEGLI benefits consist of basic life insurance coverage and three optional forms of insurance that provide additional coverage. The basic insurance is equal to the greater of (a) the employee's annual basic salary rounded up to the next even $1,000, plus $2,000, or (b) $10,000. The resulting amount is then multiplied by an Age Multiplication Factor.[9] For example, the basic life insurance coverage for a 40-year-old career employee whose annual basic pay is $24,898 is computed as follows:

1. Basic annual pay (rounded up to the next $1,000)	$25,000
2. Add $2,000	2,000
3. Add the amounts in line 1 and 2	27,000
4. Enter the amount in line 3, or $10,000, whichever is greater	27,000
5. Enter the Age Multiplication Factor	1.5
6. Multiply the amount in line 4 by the amount in line 5. This is the total amount of basic life insurance the employee has at his present age.	**$40,500**

The FEGLI optional insurance coverage consists of the following:

- Option A – Standard: $10,000
- Option B – Additional: The amount equal to an employee's annual rate of basic pay (after rounding up to the next even $1,000) times a multiple of one through five (elected by the employee).
- Option C – Family: $5,000 for a spouse and $2,500 for each eligible dependent child, times a multiple of one through five (elected by the employee).

The four benchmarked quasi-federal agencies that offer employee alternative life insurance plans were the FDIC, FRB, OTS, and TVA. For example, the FRB alternative plan generally has the same coverage as the FEGLI program except employees enrolled in the alternative plan after January 1, 2005, cannot continue participation into

[9] The Age Multiplication Factor is based on an employee's age and consists of the basic insurance amount multiplied by an appropriate numerical factor set forth in Title 5, CFR, 870.

retirement.[10] The FDIC's alternative plan also provides the same general coverage as FEGLI, including coverage into retirement. (See Appendix F for a comparison of the benchmarked federal and quasi-federal agencies' alternative life insurance plans.)

The Postal Service is governed by Title 39,[11] which requires the agency to maintain compensation and benefits for all bargaining and non-bargaining employees comparable to the same levels of work in the private sector. Title 39 further provides that, at a minimum, changes to fringe benefits should not, on the whole, be less favorable than the benefits in effect when the PRA was enacted in 1970.[12] We found that, on that date, the Postal Service participated in the FEGLI and was subject to all of its provisions like the rest of the federal government. The result of the Postal Service participating in the FEGLI is that bargaining and non-bargaining employees are receiving benefits in accordance with the law.

The Postal Service determined as far back as 1984 that it could offer life insurance benefits equal to or greater than those provided under the FEGLI program, and at potentially less cost to the agency and some of its employees.[13] However, the agency decided the political ramifications of withdrawing from the FEGLI Program would diminish any financial gains achieved. In addition, there would be little incentive for employees to switch to an alternative plan that might cost them money when the Postal Service paid the full cost of the FEGLI basic life insurance. As a result, the Postal Service did not pursue an alternative life insurance plan.

<u>Significant Differences in FEGLI Contribution Rates</u>

While the Postal Service's FEGLI benefits are the same as the benchmarked agencies, the Postal Service's contribution rates for most employees[14] are significantly higher. Specifically, the Postal Service's contribution rate for FEGLI basic life insurance is 100 percent, while all but one of the benchmarked agencies' FEGLI rates are 33 percent of the premium. The employees pay the remaining 67 percent of the premiums, including Senior Executive Service (SES) employees.

The Postal Service's FEGLI contribution rate for Postal Career Executive Service (PCES), OIG directors, and SES employees[15] is also 100 percent for Option A insurance. The rate paid for Postal Service officers is 100 percent for Option A, and up to three multiples of Option B. (See Appendix F for a comparison of the Postal Service's and the benchmarked federal and quasi-federal agencies' contribution rates.)

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[10] Employees can continue to participate into retirement under the FEGLI Program.
[11] U.S. Code 39 § 1003(a).
[12] U.S. Code 39 § 1005(f).
[13] *Results of Group Life Insurance Feasibility Study*, U.S. Postal Service, 1984; *Final Report Group Life Insurance Feasibility Study*, U.S. Postal Service, November 1986; and *Restructuring the FEGLI Program and the Introduction of Premium Conversion*, U.S. Postal Service, April 1990.
[14] This includes bargaining and non-bargaining employees, PCES executives, Postal Service officers (Postmaster General, Deputy Postmaster General, and vice presidents), OIG directors, and SES employees. Postal Service officers appoint PCES executives, including district managers, area vice presidents, and headquarters vice presidents and executive officers.
[15] The Postal Service's contribution rate for Postal Service OIG employees (EAS 24 and below) and Postal Inspection Service inspectors and forensic personnel are the same as the rest of the federal government (33 percent). The number of employees in these positions as of December 31, 2006, was 2,478.

As shown in Table 1, the Postal Service's FEGLI costs for CYs 2004 through 2006 totaled $594 million.

Table 1: Postal Service's Total FEGLI Costs for CYs 2004 Through 2006

Redacted

Source: Postal Service Payroll System
Note: Numbers were rounded.

Table 2 shows the Postal Service's FEGLI costs for Options A and B insurance for CYs 2004 through 2006 totaled $583,982.

Table 2: Postal Service's Total FEGLI Options A and B Costs for CYs 2004 Through 2006

Redacted

Source: Postal Service Payroll System
Note: Numbers were rounded.

Title 39 states the Postal Service will determine the FEGLI contribution rate for bargaining employees through a collective-bargaining process with its employee unions. Article 21 of the current union national agreements requires the Postal Service to maintain the current life insurance program, including the requirement for the Postal Service to pay 100 percent of the contribution rate. In addition, Title 39 states that no variation, addition, or substitution shall be made to fringe benefits except by agreement between the unions and the Postal Service.[16] There is no statutory requirement for the contribution rate for non-bargaining employees; however, the Postal Service has

[16] For most federal agencies, the 33/67 percent agency/employee contribution rates paid are determined by U.S. Code 5, § 8708, Government contributions. The FDIC and the OTS are governed by the Federal Institutions Reform, Recovery, and Enforcement Act (FIRREA) of 1989. Other quasi-federal agencies are governed under other federal statutes, which, like Title 39, specify which portions (if any) of Title 5 may apply to them.

historically paid the same rate as that of the bargaining employees. Further, Title 39 requires the Postal Service to consult with non-bargaining employee management associations[17] regarding any changes.

The Postal Service's FEGLI contribution rate is higher for most employees than the rate other federal and quasi-federal government agencies pay because Title 39 sets no limits on the contribution rates negotiated by the Postal Service and its unions. As a result, the Postal Service and its unions have negotiated increases in the Postal Service's contribution rate from 33 percent in 1971 to its current rate of 100 percent.

We estimated the Postal Service could have saved approximately $396 million in FEGLI contributions in CYs 2004 through 2006 if its contribution rate had been the same as most other federal and quasi-federal agencies. (See Appendix G for the estimated cost-savings analysis.)

<u>Quasi-Federal Contribution Rates for Alternative Programs</u>

As previously mentioned, four of the benchmarked quasi-federal agencies offered their employees alternative life insurance plans (in addition to FEGLI), with varied contribution rates paid by the agencies. For example, the FRB contribution rate was 33 percent, like the FEGLI plan. However, the premium rates were lower than FEGLI, thus costing the employee and the agency less for each employee, for the same level of insurance.[18] As of September 30, 2006, 900 of FRB's 1,850 employees (49 percent) were enrolled in this plan.

The FDIC and OTS contribution rates for their alternative life insurance plans are 100 percent, the same as that paid by the Postal Service (for FEGLI). However, there are some significant differences. For example, the FDIC rate is 100 percent if the employee is not enrolled in FEGLI. For employees enrolled in both FEGLI and the alternative plan, the FDIC pays 33 percent for the FEGLI basic coverage and the employee pays the full cost of the alternative plan. If an employee waives both the FEGLI and the alternative plan, the employee receives a bi-weekly taxable cash payment calculated at 2.3 cents for every $1,000 of annual adjusted basic pay. As of September 30, 2006, 3,147 of FDIC's 4,567 employees (69 percent) were enrolled in the alternative plan. The FDIC does not track any savings it might achieve by having the alternative plan.

<u>Changes to FEGLI Contribution Rates Can Be Made With Significant Savings to the Postal Service</u>

Unlike most federal agencies (including some of our benchmark partners),[19] the Postal Service, its unions, and management associations can change the Postal Service's FEGLI contribution rates and the life insurance plans for bargaining and non-bargaining

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[17] The management associations are the National Association of Postmasters of the United States, National Association of Postal Supervisors, and the National League of Postmasters.
[18] The total premium rates (agency and employee contributions) for the FRB alternative insurance plan were 6.6 cents per $1,000 in coverage, compared to the FEGLI basic premium rate of 22.5 cents per $1,000 in coverage.
[19] FDIC and OTS officials stated they have the option of changing their FEGLI contribution rates under the FIRREA.

employees. [redacted].) Further, we estimated the present value of the amount the Postal Service will pay over the next 10 years to be $1.068 billion more than what it would pay if contributions were the same rate as those of other federal and quasi-federal agencies. (See Appendix I for our calculation of these savings.)

As previously stated, the Postal Service determined it could offer life insurance benefits equal to, or greater than those provided under the FEGLI Program, at potentially less cost. However, the agency believed the political ramifications of withdrawing from the FEGLI Program would diminish any financial gains achieved. More recently, Postal Service officials told us the agency bases its continued participation in the FEGLI Program on their satisfaction with: (1) the employee program benefits, and (2) the OPM's administration of the program. In addition, officials continue to believe that an alternative life insurance program is not feasible because the Postal Service pays 100 percent of the basic insurance premiums, thus employees would have no incentive to switch to a plan that would require employee contributions.

While Title 39 prevents unilateral changes to the FEGLI contribution rates, the Postal Service can make a change in the rates and program benefits through negotiations with its unions and consultation with management associations.

<u>Recommendations</u>

We recommend the Executive Vice President and Chief Human Resources Officer:

1. [redacted].

2. Explore the use of alternative life insurance plans that offer benefits equal to, or greater than those provided under the Federal Employees Group Life Insurance program, but at reduced costs to the Postal Service.

Postal Service FEHB Benefits Are Comparable to Federal and Quasi-Federal Benchmarked Agencies

The Postal Service FEHB benefits for bargaining and non-bargaining employees are comparable to the six federal and five quasi-federal agencies we benchmarked against, in that the coverage is basically the same. We also found the Postal Service FEHB benefits were comparable to most federal and quasi-federal agencies. However, we did note that two of the quasi-federal agencies have alternative health insurance programs in addition to the FEHB plans, and one does not participate in FEHB.

Currently, the FEHB Program offers more than 350 health insurance plans (health plans),[20] including fee-for-service plans and health maintenance organization plans. Each health plan carrier charges different premium rates that typically change each year, following the annual contract negotiations between OPM and the health plan carriers. New rates resulting from these negotiations begin on the first day of the first pay period in January of the year following the negotiations. (For types of health plans and premium rates go to www.opm.gov/insure/health/07rates/2007non_postal.xls and www.opm.gov/insure/health/07rates/2007Postal.xls.)

In addition to the 350 plans, we found the following four fee-for-service FEHB health plans, which are available only to specific federal employee groups:

- Association Benefit Plan for civilian employees in selected agencies.
- Foreign Service Benefit Plan for members of the American Foreign Service Protective Association.
- Rural Carrier Benefit Plan for National Rural Letter Carriers' Association (NRLCA) members (postal and non-postal employees).
- Panama Canal Area Benefit Plan for members of the Association of Retirees of the Panama Canal Area.

The two benchmarked quasi-federal agencies that offer employees alternative health plans (in addition to the FEHB health plans) were the FDIC and the TVA. Specifically, the FDIC offers dental and vision benefits and contributes to the premium costs. The TVA does not participate in the FEHB Program but offers alternative health benefit programs. (See Appendix F for a comparison of the Postal Service and benchmarked federal/quasi-federal agencies' alternative health insurance plans.)

As stated earlier, Title 39 requires the Postal Service to maintain fringe benefits for its employees that are comparable to the private sector's and, at a minimum, maintain benefits that, on the whole, are not less favorable than those in existence when the PRA was enacted in 1970. We found that, on that date, the Postal Service participated in the FEHB and was subject to all its provisions like the rest of the federal government.

The result of the Postal Service participating in the FEHB plans is that bargaining and non-bargaining employees are receiving benefits in accordance with the law.

Significant Differences in FEHB Contribution Rates

The Postal Service's FEHB contribution rates for most employees,[21] compared to most other federal and quasi-federal government, are significantly higher. Specifically, the

[20] A health plan is a group insurance policy or contract; medical or hospital service agreement; membership or subscription contract; or similar group arrangement provided by a carrier for the purpose of providing, paying for, or reimbursing expenses for health services.
[21] Like FEGLI, this includes bargaining and non-bargaining employees, PCES executives, Postal Service officers, OIG directors, and SES employees.

Postal Service's current rate is 85 percent of the weighted average premium cost of all FEHB plans, but no more than 88.75 percent of the total premium for any individual plan. The FEHB rate for most other federal and quasi-federal agencies is 72 percent of the weighted average premium cost of all FEHB plans, but no more than 75 percent of the total premium for any individual plan.

In addition, the Postal Service's FEHB contribution rate for PCES, OIG directors, and SES employees is 100 percent, while there is no similar benefit provided to employees with comparable grades at the agencies against which we benchmarked.[22] Postal Service officials told us the rate paid for PCES employees improves the recruitment and retention of those employees. (See Appendix F for a comparison of the Postal Service's and benchmarked federal/quasi-federal agencies' contribution rates.)

As shown in Table 3, the Postal Service's FEHB cost for CYs 2004 through 2006 was nearly $13.9 billion.

Table 3: Postal Service's Total FEHB Costs for CYs 2004 Through 2006

Redacted

Source: Postal Service Payroll System
Note: Numbers were rounded.

The Postal Service's contribution rates for APWU and NPMHU bargaining employees will decrease beginning in CY 2008. The new collective bargaining agreements between the Postal Service and these two unions[23] reduced the Postal Service's contribution rate by 1 percent for each year of the agreements. The terms of the new contracts affect FEHB plan years 2008 through 2011 for the APWU and FEHB plan years 2008 through 2012 for the NPMHU. We estimated the present value of the Postal Service's cost savings over 10 years as a result of the negotiated changes with the APWU and the NPMHU is approximately $713 million. (See Appendix J for our calculations of this savings.)

[22] The Postal Service's contribution rate for OIG employees (EAS 24 and below), Postal Inspection Service inspectors, and forensic personnel are the same as the rest of the federal government (72 percent).
[23] The Postal Service was unable to reach agreement with the NRLCA on a new collective bargaining agreement and the parties have moved to the next step in the bargaining process.

The reductions to the Postal Service's contribution rate results in a corresponding increase to the employees' contribution. It should be noted, however, that the APWU agreement requires that, in 2008, the Postal Service's contribution rate for employees' premiums for the APWU Consumer Driven Health Plan will be 95 percent (a 10 percent increase).[24]

[redacted].

The Postal Service's FEHB contribution rate (like FEGLI) is established by Title 39, which requires the rate be determined through the collective bargaining process, as well as any changes to the rates and program. For CY 2007, Article 21 of the national agreements requires a contribution rate of 85 percent, not to exceed 88.75 percent of the total premium. Also, like FEGLI, there is no statutory requirement for the FEHB contribution rate for non-bargaining employees. The Postal Service contributes the same rate for bargaining employees and it must consult with employee management associations for any changes.

The Postal Service's FEHB contribution rate is higher for most employees than the rate most other federal and quasi-federal entities pay because Title 39 sets no limits on the contribution rates the Postal Service and its unions negotiate. As a result, the Postal Service and its unions have negotiated higher contribution rates since the 1970s.

We estimated the Postal Service could have saved approximately $2.13 billion in FEHB contributions in CYs 2004 through 2006 if its contribution rates had been the same as most other federal and quasi-federal agencies.[25] (See Appendix K for our calculations for this savings.) Further, we estimated the present value of the amount the Postal Service will pay over the next 10 years to be $6.2 billion more than what it would pay if contributions were the same rate as other federal and quasi-federal agencies.[26] (See Appendix L for our calculation of these costs.)

[24] The APWU Consumer Driven Health Plan total bi-weekly premiums are lower than the premiums for many other FEHB fee-for-service health plans. For example, the 2007 bi-weekly premium for the APWU plan was $163.58 for self-only compared to the Blue Cross and Blue Shield Service Benefit Plan Standard self-only bi-weekly premium of $199.22. As a result, the higher employer percentage applied to this plan will not necessarily result in higher costs to the Postal Service.

[25] Conversely, paying at the lower rate would result in employees paying an additional cost of $678.96 a year with a self-only health plan and $1,440.52 a year for employees with a self and family plan. A self and family plan covers an employee, his or her spouse, and the employee's unmarried dependent children under age 22. The self-only plan covers only the employee.

[26] This calculation takes into consideration the reduced costs due to the new labor agreements with the APWU and the NPMHU. In other words, the $6.2 billion would be in addition to the savings the Postal Service will realize from the new agreements.

Quasi-Federal Contribution Rates for Alternative Health Insurance Programs

The FEHB or alternative plan contribution rates of other quasi-federal agencies were as follows:

- FDIC's rate was the same as the Postal Service's 2007 rate — 85 percent of the weighted average premium cost of all FEHB plans, but no more than 88.75 percent of the total premium for any individual plan.
- TVA's rate for three alternative health plans was approximately 80 percent.
- OTS contributes $300 (or $11.57) per pay period towards the employee's FEHB plan choice.

Changes to FEHB Contribution Rates Can be Made with Significant Savings to the Postal Service

The Postal Service and its unions can change existing FEHB contribution rates through negotiations with its unions, as stipulated in Title 39 and the national agreements. History shows the Postal Service has taken advantage of this ability when, in 1993, it achieved, through interest arbitration, incremental 1 percent annual reductions from 1994 through 1997; and, more recently (in 2006), when similar incremental 1 percent reductions were agreed to over 4- and 5-year periods with the APWU and the NPMHU, respectively. [redacted]. In addition, statutory requirements allow changes to non-bargaining employee benefits after consulting with management associations.

While the Postal Service has the flexibility to change its FEHB contribution, most federal agencies do not have this option, including the federal and some of the quasi-federal agencies against which we benchmarked. The FDIC and the OTS stated they have the option of changing their FEHB contributions under the FIRREA.

[redacted]

Recommendations

We recommend the Executive Vice President and Chief Human Resources Officer:

[redacted]

[redacted]

Conclusion

We recognize that any attempt to change FEGLI or FEHB contribution rates or life/health insurance benefits must be made with the agreement of the employee unions and in consultation with the management associations. We also understand the potential ramifications of proposed changes to these two benefit programs and that changes to benefit contribution levels are always negotiated in the overall context of the give-and-take of collective bargaining and the appropriate priorities that exist at that time. [redacted].

Management's Comments

[redacted]

[27] The Postal Service appears to be on track to have a $5.2 billion net loss for FY 2007 according to the newly revised Integrated Financial Plan.

Evaluation of Management's Comments

Management's comments are responsive and the planned actions address the issues identified in the findings. [redacted]

The OIG considers recommendations 1 through 4 significant, and therefore requires OIG concurrence before closure. Consequently, the OIG requests written confirmation when the actions are completed. These recommendations should not be closed in the follow-up tracking system until the OIG provides written confirmation that the recommendations can be closed.

We appreciate the cooperation and courtesies provided by your staff during the audit. If you have any questions or need additional information, please contact Chris Nicoloff, Director, Human Capital, or me at (703) 248-2100.

E-Signed by Darrell E. Benjamin,
VERIFY authenticity with ApproveIt

Darrell E. Benjamin, Jr.
Deputy Assistant Inspector General
for Support Operations

Attachments

cc: Doug A. Tulino
Julie S. Moore
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APPENDIX A. ABBREVIATIONS

APWU	American Postal Workers Union
CY	Calendar Year
DHS	U.S. Department of Homeland Security
DOD	U.S. Department of Defense
DOT	U.S. Department of Transportation
Treasury	U.S. Department of the Treasury
EAS	Executive and Administrative Schedule
FDIC	Federal Deposit Insurance Corporation
FEHB	Federal Employee Health Benefits
FEGLI	Federal Employees' Group Life Insurance
FIRREA	Federal Institutions Reform, Recovery, and Enforcement Act
FOIA	Freedom of Information Act
FRB	Federal Reserve Board
NALC	National Association of Letter Carriers
NCUA	National Credit Union Administration
NPMHU	National Postal Mail Handlers Union
NRLCA	National Rural Letter Carriers' Association
OIG	U.S. Postal Service Office of Inspector General
OPM	Office of Personnel Management
OTS	Office of Thrift Supervision
PCES	Postal Career Executive Service
PRA	Postal Reorganization Act
SES	Senior Executive Service
TVA	Tennessee Valley Authority
USDA	U.S. Department of Agriculture
VA	U.S. Department of Veterans Affairs

APPENDIX B. SUMMARY OF MONETARY IMPACT TO THE POSTAL SERVICE

Redacted

Note: We calculated annual escalation factors from the contribution rate payment differences for CYs 2004, 2005, and 2006 for various employee categories (bargaining and non-bargaining).

APPENDIX C. COST AVOIDANCE METHODLOGY

FEHB Premium Payment Savings Methodology Description

Background

The current Postal Service contribution rate for FEHB premium payments for any individual employee is the lower of 85 percent of the OPM-determined FEHB program-wide "weighted average of premiums," or 88.75 percent of the specific plan premium. The program-wide weighted average of premiums is weighted for individual plan participation and the OPM determines a program-wide weighted average of premiums for self-only plans and family plans separately. Because of the mix of plans chosen by employees, the Postal Service ends up paying, generally, 1 to 2 percentage points less than 85 percent of overall premium costs. This can be termed the "85/88.75" formula.

In general, most federal and quasi-federal agencies use a different formula for determining their premium liability payouts. They pay the lower of 72 percent of the OPM-determined FEHB program-wide weighted average of premiums, or 75 percent of the specific plan premium, for a given employee. Because of the mix of plans chosen by employees, most federal and quasi-federal agencies end up paying, generally, 1 to 2 percentage points less than 72 percent of overall premium costs. This can be termed the "72/75" formula.

Recently, two of the Postal Service's major unions — the APWU and NPMHU — agreed to 1 percent per year reductions in the Postal Service's FEHB payment formula applicable to their members, over the terms of the new labor contracts, which are for 4 years for the APWU and 5 years for the NPMHU.

Methodology Objectives

(1) Estimate the differences between the actual Postal Service FEHB contribution rates over CYs 2004, 2005, and 2006, and those which theoretically would have been paid if the Postal Service's contribution rate had corresponded to the rate most federal and quasi-federal agencies pay.

(2) Estimate the present value of the differences over 10 years between contribution rates the Postal Service will pay (as its liabilities currently stand) and those which, theoretically, the Postal Service would pay under various scenarios.

Methodology Description

The methodology consisted of several parts:

(1) We created a simulation which provided an equation for translating any premium contribution rate percentage paid under the current Postal Service formula into a theoretical contribution rate percentage paid under the formula used by most federal and quasi-federal agencies.

(2) Using historical FEHB premium information for CYs 2004 through 2006, we calculated the percentage of the total FEHB premium amounts, which the Postal Service paid for all categories of employees. From the calculated percentage of FEHB premiums the Postal Service actually paid and using the equation from part (1), we estimated the percentage of the total premium amounts, which would have been paid under the formula most federal and quasi-federal agencies use. We then calculated the amounts the Postal Service theoretically would have paid under the formula most federal and quasi-federal agencies use and the payment differences for the 3 historical years. We also calculated annual escalation factors from the contribution rate payment differences over the 3-year period for various categories of employees.

(3) Using the results from part (2), we performed a discounted cash flow analysis to estimate the present value of the theoretical premium liability differences over a 10-year period (2008 through 2017) for various categories of employees. To accomplish this, we used health premium cost escalation rates calculated in part (2).

(4) We also performed discounted cash flow calculations to estimate:

(a) [redacted]

(b) [redacted]

(c) [redacted]

(d) The present value over the next 10 years of savings the Postal Service would potentially realize if it reduced the FEHB liability formula for its non-bargaining employees to match the reductions the APWU and NPMHU agreed to in the recently completed contract negotiations for bargaining employees.

Assumptions and Caveats

For the simulations referred to in part (1) under Methodology Description, we created separate simulations for self-only plans and family plans. The difference between the two types of plans is the "weighted average of premiums" amount. We determined from OPM FEHB tables that the bi-weekly weighted average of premiums for self-only plans for CY 2007 is $197.10. For family plans, the bi-weekly weighted average of premiums for CY 2007 is $447.07. In our simulations, these values acted as constraints. The simulations allow varying the mix of individual plan costs and the ratios of plan participants while still meeting the constraints, in a hypothetical, simplified world of three available plans. The results of the simulations are tables relating the Postal Service contribution rate percentages with contribution rate percentages used by most federal and quasi-federal agencies. From the tables, regression equations were determined using Excel's "intercept" and "slope" functions. We concluded the regression equations derived for the self-only and family plan simulations were functionally identical. Therefore, in our determination of the contribution rate differences, we used only the family plan equation throughout.

Percentage increases in the annual premium payments in future years will match the average percentage increase over the CY 2004 through 2006 period.

Future amounts were discounted to the present using a rate of 5.00 percent per year, which is the currently published Postal Service Cost of Borrowing.

FEGLI Premium Payment Savings Methodology Description

Background

The current Postal Service liability for FEGLI premium payments for basic coverage for any individual employee is 100 percent (with some minor exceptions). In general, most federal and quasi-federal agencies pay 33 percent.

The Postal Service also pays some portion of premium payments for Options A and B for certain categories of employees, while most federal and quasi-federal agencies do not pay any portion.

Methodology Objectives

(1) Estimate the differences between actual Postal Service FEGLI contribution rate payments over CYs 2004, 2005, and 2006, and those the Postal Service would theoretically have paid if its contribution rate had corresponded to the rates federal and quasi-federal agencies use.

(2) Estimate the present value of the differences over the next 10 years between contribution rates the Postal Service will pay as its liabilities currently stand, and those the Postal Service would theoretically pay under various scenarios.

Methodology Description

The methodology consisted of several parts:

(1) Using historical FEGLI premium information for CYs 2004 through 2006, we calculated the percentage of the total FEGLI premium amounts the Postal Service paid for all categories of employees. We then calculated the amounts the Postal Service theoretically would have paid under the formula most federal and quasi-federal agencies use and the payment differences for the 3 historical years. We also calculated annual escalation factors from the premium liability payment differences over the 3-year period for various categories of employees.

(2) Using the results from part (1), we performed a discounted cash flow analysis to estimate the present value of the theoretical premium liability differences over a 10-year period (2008 through 2017) between a 100 percent liability scenario and a 33 percent liability scenario for various categories of employees. To accomplish this, we used premium cost escalation rates calculated in part (1).

(3) We also performed discounted cash flow calculations to estimate:

(a) [redacted]

(b) The present value over the next 10 years of the savings the Postal Service would potentially realize if it reduced, in 2011, the FEGLI liability percentage for its non-bargaining employees to match the reductions the major unions agreed to.

Assumptions

Percentage increases in the annual premium payments in future years will match the average percentage increase over the CY 2004 through 2006 period.

Future amounts were discounted to the present using a rate of 5.00 percent per year, which is the currently published Postal Service Cost of Borrowing.

APPENDIX D. PROFILE OF THE POSTAL SERVICE AND THE SIX FEDERAL AND FIVE QUASI-FEDERAL BENCHMARKED AGENCIES AS OF SEPTEMBER 30, 2006

Agency	Federal	Quasi-Federal	Size of Agency (Number of Employees)	Number of Employee Unions	Number of Unionized Employees
Postal Service	X		696,138	7	624,749
DHS	X		168,635	14	48,684
DOD	X		137,887	16	102,505
DOT	X		53,861	22	40,300
Treasury	X		106,623	12	91,091
FDIC		X	4,551	1	4,349
FRB		X	1,850	0	0
NCUA		x	911	1	800
OTS		X	970	1	149
TVA		X	12,600	11	9,626

APPENDIX E. OBJECTIVES, SCOPE, AND METHODOLOGY

The objectives of this audit were to determine whether two of the Postal Service's employee benefit programs were comparable to selected federal and quasi-federal government agencies and to determine if differences existed between the Postal Service's benefit contributions and those provided by the same agencies. We also determined whether changes could be made to the Postal Service's contributions to the benefit programs and the potential costs associated with the changes.

Our scope for the audit was the FEHB and FEGLI benefit programs and the Postal Service's participation in these programs during CYs 2004, 2005, and 2006. We used calendar year instead of fiscal year data for our analysis because changes to the contribution percentages and health plan increases are made on a CY basis and because FEGLI premiums are based on employee annual basic pay in effect at the end of a given pay period.

To accomplish our objectives, we reviewed all applicable laws, regulations, union contracts, policies, and procedures related to the FEGLI and FEHB benefit programs for benchmarked federal and quasi-federal government agencies and Postal Service employees. We also interviewed Postal Service officials regarding the agency's participation in the federal benefit programs and any obstacles to changes in employer FEHB and FEGLI contribution amounts. Additionally, we interviewed the Associate Director, Strategic Human Resource Policy, at the OPM and reviewed and analyzed information obtained from this official relative to the participation of federal and quasi-federal agencies in the FEGLI and FEHB programs. Further, we reviewed available studies and analyses conducted of the FEGLI and FEHB benefit programs regarding the potential effects of changes to these programs.

To determine whether the Postal Service's employee benefit programs were comparable to selected federal and quasi-federal government agencies and if differences existed between them, we conducted benchmarking using a guide published by the American Productivity Quality Center on benchmarking. This was to ensure we were following current business practices with regard to our benchmarking approach.

We identified specific agencies through team brainstorming efforts. The information we considered was:

- Whether the agency was appropriated (federal) or non-appropriated (quasi-federal).
- The size of the agency.
- Whether the agency offered alternative benefit programs.
- The number of employee unions.
- The number of unionized employees.

We researched and identified seven federal and eight quasi-federal government agencies, for a total of 15 agencies as our universe. We then contacted the agencies and requested their assistance with our benchmarking project. In response, 11 agencies (six federal and five quasi-federal) volunteered to participate and return completed questionnaires to us.

The benchmarking questionnaire we developed covered topics including agency involvement in FEGLI and FEHB programs, contribution rates, and the existence of alternative health and life insurance benefits as well as relevant costs.

To determine the legal or regulatory obstacles the Postal Service would face if it sought to reduce its FEGLI and FEHB contribution amounts from the current 100 to 33 percent for basic life, and 85 to 72 percent, respectively, we reviewed relevant laws and requirements, and obtained a legal opinion from the OIG's General Counsel.

To determine what changes the Postal Service can make to its employer and employee FEGLI and FEHB contributions, we reviewed the current union agreements with the four major unions to determine the Postal Service's contractual obligations related to employee benefits. We also reviewed the new national agreements with the APWU and the NPMHU.

To determine the potential costs associated with changes to the Postal Service's contributions to the FEGLI and FEHB benefit programs, we obtained and reviewed the total employer contribution costs in CYs 2004, 2005, and 2006. Because OIG EAS 24 and below employees, Postal Inspection Service inspectors, and forensic staff have their FEGLI and FEHB employer contributions paid at 33 and 72 percent, respectively, we excluded these costs from our total figures for non-bargaining employees. We also excluded from these costs payments made to retirees and deceased benefit payouts. Deceased benefit payouts are captured in the Postal Service's general ledgers but not in the Pay Data and Master Employee files. Additionally, our cost data does not include costs attributed to Medicare tax, cancelled checks, union billings and miscellaneous payroll adjustments, which are posted in general ledgers and are not processed through the Pay Data file.

With the assistance of the OIG economist, we estimated the present value of Postal Service savings over 10 years if it were to reduce its FEGLI and FEHB contributions to match the 33 and 72 percent, respectively, of the federal sector. We also estimated the present value of Postal Service savings over 10 years if it were to reduce its FEGLI and FEHB contributions by 1 percent. (See Appendix C for the cost avoidance methodology used.) In our FEHB calculations, we took into consideration the impact of the new agreements with the APWU and the NPMHU.

We conducted this performance audit from November 2006 through September 2007 in accordance with generally accepted government auditing standards and included such tests of internal controls as we considered necessary under the circumstances. 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. We discussed our observations and conclusions with management officials on August 9, 2007, and included their comments where appropriate.

Data Reliability Testing

To verify the reliability of computer-generated data, we compared our FEHB and FEGLI cost totals obtained from the Postal Service Pay data and Employee Master files to the Postal Service's general ledger entries, which the OIG audits annually. In addition, we consulted with Postal Service Accounting Service Center officials regarding the verification of our cost data.

APPENDIX F. COMPARISON OF THE POSTAL SERVICE'S AND BENCHMARKED FEDERAL AND QUASI-FEDERAL AGENCIES' FEGLI AND FEHB CONTRIBUTION RATES AND ALTERNATIVE PLANS AS OF SEPTEMBER 30, 2006

Agency	FEGLI Basic Percent Rate	FEHB Percent Rate	Alternative Life Insurance Plans	Alternative Health Insurance Plans
Postal Service			N/A	N/A
Bargaining	100	85 to 88.75		
Non-Bargaining	100	85 to 88.75		
PCES	100	100		
OIG	33	72 to 75		
OIG GS-15 and SES	100	100		
Inspectors and Forensic	33	72 to 75		
Federal Agencies				
USDA	33	72 to 75	N/A	N/A
DOD	33	72 to 75	N/A	N/A
DHS	33	72 to 75	N/A	N/A
DOT	33	72 to 75	N/A	N/A
Treasury	33	72 to 85	N/A	N/A
VA	33	72 to 75	N/A	N/A
Quasi-Federal Agencies				
FDIC	33 to100	85 to 88.75	▪ Option 1- Employee life insurance coverage is equal to one, two, or three salary multiples, but not more than $600,000. ▪ Option 2A - Spouse life insurance, Option 2A coverage is equal to 50 percent of the employee's FDIC Basic Life Insurance, not to exceed $300,000. ▪ Option 2B – Spouse life insurance, Option 2B is equal to 100 percent of the employee's FDIC Basic Life Insurance, not to exceed $300,000. ▪ Option 3 – Family life insurance provides $10,000 for the employee's spouse and $10,000 for each eligible child.	▪ Dental ▪ Vision (On January 1, 2007, the FDIC's contribution was adjusted from 85 to 80 percent of premium for specific dental and vision options.)
FRB	33	72 to75	• Basic • Option 1 -$10,000 • Option 2- per $1,000 • Option 3- $10,000 for spouse and $5,000 for each child	N/A
NCUA	33	72 to 75	N/A	N/A
OTS[28]	100	72 to 75	• Basic - Employee Life Plan • Option 1 - Optional Employee Life Plan • Option 2 - Spouse Life Plan • Option 3 - Family Plan • Option 4 - Domestic Partner Life Plan • Option 5 - Domestic Partner Family Plan	N/A
TVA	33	N/A	▪ Optional Term Life Insurance and provides employees, at no cost, with $10,000 in life insurance. • Long-term disability benefits equal to 30 percent of employees' high 3-year average salary.	Provides separate health benefit plans for its employees, which offer a choice of three preferred-provider plans with varying levels of coverage. All the options include hospital, physician, and prescription drug benefits, and some include vision coverage.

[28] OTS contributes an additional $300 a year to employees' FEHB.

APPENDIX G. ESTIMATED HISTORICAL COST SAVINGS IF THE POSTAL SERVICE'S FEGLI BASIC CONTRIBUTION RATE WAS 33.33 PERCENT AND OPTION A AND B RATES WERE 0 PERCENT

Redacted

Note: USPS = Postal Service
ROG = Rest of Government
Est. = Estimated
Empl Ded = Employee Deductions

APPENDIX H. PRESENT VALUE OF COST SAVINGS OVER NEXT 10 YEARS IF THE POSTAL SERVICE ACHIEVES 1 PERCENT PER YEAR FEGLI CONTRIBUTION RATE REDUCTIONS FOR BARGAINING AND NON-BARGAINING EMPLOYEES

Redacted

Note: USPS = Postal Service

APPENDIX I. PRESENT VALUE OF COST SAVINGS OVER NEXT 10 YEARS IF THE POSTAL SERVICE BASIC FEGLI CONTRIBUTIONS WERE 33.33 PERCENT INSTEAD OF 100 PERCENT, AND OPTION A AND B CONTRIBUTIONS WERE 0 PERCENT INSTEAD OF 100 PERCENT

Redacted

APPENDIX J. PRESENT VALUE OF COST SAVINGS OVER NEXT 10 YEARS THE POSTAL SERVICE SHOULD ACHIEVE BASED ON THE 1 PERCENT PER YEAR FEHB CONTRIBUTION RATE REDUCTIONS AGREED TO WITH THE APWU AND THE NPMHU

Redacted

APPENDIX K. ESTIMATED HISTORICAL COST SAVINGS THE POSTAL SERVICE WOULD HAVE ACHIEVED BY CHANGING FEHB CONTRIBUTION RATES FROM 85/88.75 to 72/75

Redacted

Note: USPS = Postal Service
ROG = Rest of Government
Est. = Estimated
Empl Ded = Employee Deductions

APPENDIX L. PRESENT VALUE OF COST SAVINGS OVER NEXT 10 YEARS IF THE POSTAL SERVICE ACHIEVES A CHANGE IN THE FEHB CONTRIBUTION RATE FROM 85[29] TO 72 PERCENT

Redacted

Note: Est. = Estimated

[29] This cash flow analysis is based on the contribution rate changing from 85 percent to 72 percent starting in CY 2008 for all four major unions and non-bargaining and PCES employees.

APPENDIX M. THE PRESENT VALUE OF COST SAVINGS OVER NEXT 10 YEARS IF THE POSTAL SERVICE ACHIEVES ADDITIONAL 1 PERCENT PER YEAR FEHB CONTRIBUTION RATE REDUCTIONS IN FUTURE CONTRACTS WITH THE APWU AND THE NPMHU

Redacted

APPENDIX N. THE PRESENT VALUE OF COST SAVINGS OVER NEXT 10 YEARS IF THE POSTAL SERVICE ACHIEVES 1 PERCENT PER YEAR FEHB CONTRIBUTION RATE REDUCTIONS IN FUTURE CONTRACTS WITH THE NALC AND THE NRLCA

Redacted

APPENDIX O. THE PRESENT VALUE OF COST SAVINGS OVER NEXT 10 YEARS IF THE POSTAL SERVICE ACHIEVES 1 PERCENT FEHB CONTRIBUTION RATE REDUCTIONS FOR NONBARGAINING EMPLOYEES (TO MATCH AGREED UPON APWU AND NPMHU REDUCTIONS)

<u>**Redacted**</u>

APPENDIX P. MANAGEMENT'S COMMENTS

<u>**Redacted**</u>

Redacted