



CONGRESSIONAL BUDGET OFFICE COST ESTIMATE

July 1, 2005

S. 662

Postal Accountability and Enhancement Act

*As ordered reported by the Senate Committee on Homeland Security
and Governmental Affairs on June 22, 2005*

SUMMARY

S. 662 would change the laws that govern the operation of the United States Postal Service (USPS), particularly those regarding the cost of pensions and health care benefits of retired workers and the requirement to hold certain funds in escrow. CBO estimates that enacting this legislation would result in on-budget savings of \$37.7 billion and off-budget costs of \$41.6 billion over the 2006-2015 period. (The net expenditures of the USPS are classified as “off-budget.”) Thus, CBO estimates the net cost to the unified budget would be \$3.9 billion over the 2006-2015 period. All of those effects reflect changes in direct spending. In addition, we estimate that implementing S. 662 would have discretionary costs of about \$1.6 billion over the 2006-2015 period, assuming appropriation of the necessary amounts. (Enacting the bill would not affect federal revenues.)

Enacting S. 662 would not affect how much the federal government spends on pension or health care benefits for USPS retirees. By increasing how much the Postal Service pays to finance those benefits and by eliminating the current-law escrow account requirements, however, the bill would increase future budget deficits—as measured by the unified federal budget—for 2008 through 2015, and for several years after 2015. (We estimate a small decrease in the deficit for 2006, and a near-zero impact for 2007.)

Eliminating the escrow account requirement for the USPS would allow that agency to increase spending for capital improvements or other projects, pay down its outstanding debt, postpone or diminish future rate increases, or some combination of these options. Enacting the bill also would reduce direct spending mostly by making the costs of the Postal Rate Commission (PRC) and the USPS Office of the Inspector General subject to appropriation.

Pursuant to section 407 of H. Con. Res. 95 (the Concurrent Resolution on the Budget, Fiscal Year 2006), CBO estimates that enacting S. 662 would cause an increase in direct spending to the unified budget of greater than \$5 billion in the 10-year period beginning in 2016. The

bill would not increase on-budget direct spending by more than \$5 billion during any of the four 10-year periods from 2016 through 2055.

S. 662 contains no intergovernmental or private-sector mandates as defined in the Unfunded Mandates Reform Act (UMRA) and would impose no costs on state, local, or tribal governments.

Major provisions of S. 662 would:

- Eliminate a requirement in Public Law 108-18, the Postal Civil Service Retirement Funding Reform Act of 2003, that the Postal Service place savings from reduced pension contributions in escrow.
- Transfer from the Postal Service to the Department of the Treasury responsibility for paying pension costs associated with military service credits.
- Replace direct payments the Postal Service is making for retiree health care costs with payments designed to prefund some of the health care costs of current employees when they retire.
- Revise the procedure for raising postal rates.
- Modify the USPS Board of Governors and the Postal Rate Commission, which would be redesignated the Postal Regulatory Commission (PRC).
- Make other changes designed to increase the Postal Service's competitiveness with private industry.

ESTIMATED COST TO THE FEDERAL GOVERNMENT

The estimated budgetary impact of S. 662 is summarized in Table 1. The costs of this legislation fall within budget functions 370 (commerce and housing credit), 550 (health), 600 (income security), 900 (net interest), 950 (undistributed offsetting receipts).

TABLE 1. ESTIMATED BUDGETARY EFFECTS OF S. 662

	By Fiscal Year, in Billions of Dollars									
	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015
CHANGES IN DIRECT SPENDING										
On-Budget Effects										
Estimated Budget Authority	-3.1	-3.2	-3.3	-3.5	-3.6	-3.8	-4.0	-4.2	-4.4	-4.6
Estimated Outlays	-3.1	-3.2	-3.3	-3.5	-3.6	-3.8	-4.0	-4.2	-4.4	-4.6
Off-Budget Effects										
Estimated Budget Authority	2.9	3.2	3.5	3.6	3.9	4.3	4.5	4.9	5.3	5.6
Estimated Outlays	2.9	3.2	3.5	3.6	3.9	4.3	4.5	4.9	5.3	5.6
Total Unified Budget Effects										
Estimated Budget Authority	-0.1	0.0	0.1	0.2	0.3	0.5	0.5	0.7	0.9	0.9
Estimated Outlays	-0.1	0.0	0.1	0.2	0.3	0.5	0.5	0.7	0.9	0.9
CHANGES IN SPENDING SUBJECT TO APPROPRIATION										
Estimated Authorization Level	0.1	0.1	0.2	0.2	0.2	0.2	0.2	0.2	0.2	0.2
Estimated Outlays	0.1	0.1	0.2	0.2	0.2	0.2	0.2	0.2	0.2	0.2

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

BASIS OF ESTIMATE

For this estimate, CBO assumes that S. 662 will be enacted near the start of fiscal year 2006. For direct spending, CBO estimates that enacting the bill would result in on-budget savings of \$37.7 billion and off-budget costs of \$41.6 billion over the 2006-2015 period, for a net cost to the unified budget of \$3.9 billion over the 10-year period. In addition, we estimate that implementing S. 662 would cost about \$1.6 billion over the 2006-2015 period, assuming appropriation of the necessary amounts, mostly to fund the USPS Office of the Inspector General and the Postal Regulatory Commission.

Background

The following paragraphs present background information relating to the major provisions of S. 662, mostly for postal finances affected by the bill.

Budgetary Treatment of USPS. Although the Postal Service is a federal agency, its financial operations are classified as off-budget. Despite this treatment, federal budget documents present the net income (gross income minus expenses) of the agency in the unified budgetary totals for the federal government. The Postal Service is required by law to set postage rates to cover its full costs, although from year to year its net income may be positive or negative. In fiscal year 2004, the Postal Service generated \$69.6 billion in collections, mostly from postage and user fees, and had \$65.5 billion in expenses, for a net cash surplus of \$4.1 billion in that year. CBO projects that the USPS will end 2005 with a cash surplus of \$3.8 billion.

USPS and Federal Retirement Plans. Postal Service employees participate in the federal government's two main defined benefit pension programs. Those workers initially hired prior to 1984 are covered by the Civil Service Retirement System (CSRS) while those initially hired after 1983, as well as former CSRS workers who elected to change federal retirement plans in 1987 or 1998, participate in the Federal Employees' Retirement System (FERS). In 2004, about 25 percent of the USPS workforce was covered by CSRS, and the rest were under FERS.

The Postal Service and its employees each make payroll contributions toward the civilian retirement system (CSRS and FERS). Unlike other agencies, the agency contribution rate for most CSRS employees is 17.4 percent of basic pay (most other agencies contribute 7 percent), while the employee contribution rate is 7 percent.¹ For FERS employees, the agency contribution rate for most employees is 10.7 percent, while the employee rate is 0.8 percent, plus Social Security payroll taxes on both employers and employees. Workers in CSRS receive generally higher benefits than those in FERS, but unlike FERS, those in CSRS do not participate in Social Security and do not receive agency contributions toward the Thrift Savings Plan. In addition to its payroll contributions, the Postal Service also makes annual amortization payments toward an unfunded liability within CSRS. In 2004, that payment was about \$250 million.

USPS and Federal Health Benefits. The Postal Service also pays a portion of health care premiums for retired USPS employees who participate in the Federal Employees Health Benefits (FEHB) program. Over 400,000 Postal Service retirees participate in the FEHB program. On average, the Postal Service currently pays about 45 percent of the health care premiums for its retirees. Retirees pay about 30 percent of their FEHB premiums with

1. Public Law 108-18 increased the contribution rate the Postal Service pays for its CSRS employees from 7 percent to 17.4 percent. That legislation also eliminated a series of amortization payments the Postal Service was required to make for unfunded CSRS liabilities. For more details, see CBO's cost estimates of the Postal Civil Service Retirement System Funding Reform Act of 2003 (S. 380 and H.R. 735 from the 108th Congress). These estimates are posted on www.cbo.gov.

general revenues accounting for the remaining amount, roughly 25 percent. In 2004, the Postal Service paid \$1.3 billion to FEHB for premiums for current retirees.

USPS Escrow Fund. Starting in fiscal year 2006, the Postal Service will be required under current law to begin holding funds in an escrow account equal to the difference between what the Postal Service currently pays toward CSRS and what it would have paid for CSRS benefits prior to the enactment of Public Law 108-18. Under current law, CBO estimates the Postal Service will need to hold in escrow about \$3 billion in 2006 and \$43 billion over the 2006-2015 period. S. 662 would eliminate the requirement that USPS deposit such funds in escrow.

Effects on the Unified Budget

S. 662 would not affect how much the federal government spends on pension or health benefits for USPS retirees. However, by increasing how much the Postal Service pays to finance those benefits and by eliminating the current-law escrow requirements, the bill would increase future budget deficits—as measured by the unified federal budget—for 2008 through 2015, and for several years after 2015. Enacting the bill would lead to a small net decrease in the unified budget deficit for 2006, and a near-zero net impact for 2007.

Off-budget payments made by the Postal Service for CSRS and FEHB are transfers to on-budget federal accounts, and are counted as offsetting receipts (a credit against direct spending). Eliminating the USPS transfer to CSRS would reduce on-budget offsetting receipts by \$11.7 billion over the 2006-2015 period. Under the bill, that reduction would be more than offset by a \$49.4 billion increase in on-budget offsetting receipts paid by the Postal Service for the new health benefits fund. Thus, the bill would increase on-budget offsetting receipts by \$37.7 billion over the 2006-2015 period.

The collection of funds to be held in escrow by the Postal Service is recorded as an off-budget offsetting receipt (i.e., simply reflecting the payment by the USPS into escrow). Eliminating the requirement to fund the escrow account would allow the USPS to pay down debt, increase spending for capital improvements or other projects, postpone or diminish future rate increases, or some combination of these activities. CBO estimates that this provision would increase off-budget spending by \$43.2 billion over the 2006-2015 period. Making the costs of the PRC and the USPS Office of the Inspector General subject to appropriation would reduce direct spending by the Postal Service by \$1.6 billion over the next 10 years.

TABLE 2. ESTIMATED CHANGES IN DIRECT SPENDING FOR S. 662

	By Fiscal Year, Outlays in Billions of Dollars									
	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015
CHANGES IN DIRECT SPENDING										
On-Budget Effects										
Civil Service Retirement System	1.8	1.7	1.6	1.4	1.3	1.1	1.0	0.8	0.6	0.4
Postal Service Retiree Health Benefits Fund Net of Retiree Premium Payments to FEHB ^a	<u>-4.9</u>	<u>-4.9</u>	<u>-4.9</u>	<u>-4.9</u>	<u>-4.9</u>	<u>-4.9</u>	<u>-4.9</u>	<u>-5.0</u>	<u>-5.0</u>	<u>-5.0</u>
Total On-Budget Effects	-3.1	-3.2	-3.3	-3.5	-3.6	-3.8	-4.0	-4.2	-4.4	-4.6
Off-Budget Effects										
Eliminate Escrow Account	3.1	3.3	3.6	3.8	4.1	4.4	4.6	5.0	5.4	5.7
Funding for PRC and USPS Inspector General Office Costs Subject to Appropriation ^b	<u>-0.1</u>	<u>-0.1</u>	<u>-0.2</u>							
Total Off-Budget Effects	2.9	3.2	3.5	3.6	3.9	4.3	4.5	4.9	5.3	5.6
Total Unified Budget Effects	-0.1	0.0	0.1	0.2	0.3	0.5	0.5	0.7	0.9	0.9
MEMORANDUM										
Payments from the Postal Service Received by PSRHBF	-5.4	-6.9	-7.2	-7.5	-7.8	-8.1	-8.4	-8.8	-9.2	-9.6
FEHB Premiums Paid from PSRHBF	<u>0.4</u>	<u>2.0</u>	<u>2.3</u>	<u>2.6</u>	<u>2.9</u>	<u>3.2</u>	<u>3.5</u>	<u>3.8</u>	<u>4.2</u>	<u>4.6</u>
Net Outlays of PSRHBF	-4.9	-4.9	-4.9	-4.9	-4.9	-4.9	-4.9	-5.0	-5.0	-5.0

NOTES: FEHB = Federal Employees Health Benefits program; PSRHBF = Postal Service Retiree Health Benefits Fund; PRC = Postal Regulatory Commission; USPS = United States Postal Service.

Components may not add to totals because of rounding.

Amounts in the table represent net changes in offsetting receipts, which are recorded in the budget as changes in direct spending. A positive sign indicates lower offsetting receipts, thus an increase in outlays; negative numbers represent increased offsetting receipts, or a reduction in net outlays.

- a. Starting in July 2006, CBO assumes that payments of FEHB premiums for Postal Service retirees would be paid out of the Postal Service Retiree Health Benefits Fund instead of being paid directly by the Postal Service as under current law. The bill would have no effect on spending by the FEHB program for health benefits for Postal Service annuitants.
- b. S. 662 would reduce USPS payments for workers' compensation, which would reduce direct spending by about \$50 million over the 2006-2015 period. These effects are also included in these figures.

The combined effect of the \$37.7 billion net increase in on-budget receipts, the \$43.2 billion reduction in off-budget offsetting receipts, and a \$1.6 billion reduction in USPS direct spending would produce \$3.9 billion in direct spending costs for the unified budget over the 2006-2015 period. Those effects are presented in Table 2 and explained in more detail below.

On-Budget Effects (Direct Spending)

CBO estimates the on-budget effect of the pension and health care provisions in S. 662 would be a net increase in offsetting receipts of \$3.1 billion in 2006, \$16.7 billion over the 2006-2010 period, and \$37.7 billion over the 2006-2015 period. That increase in on-budget collections (i.e., reduction in direct spending) would come from increased transfers (off-budget outlays) coming from the USPS. (The off-budget effects are discussed in the following section.)

Civil Service Retirement Contributions. S. 662 would change the way the Postal Service finances retirement benefits for current and retired employees. Starting in October 2005, the bill would transfer financial responsibility for military service credits earned by Postal Service employees and retirees participating in CSRS from the Postal Service to the Department of the Treasury. Military service credits represent time served in the U.S. military that is credited toward benefits under the civilian retirement system. Most federal agencies are not responsible for the cost to the pension system of the military service credits incurred by their CSRS employees, but P.L. 108-18 transferred responsibility for military service credits from the Treasury to the Postal Service beginning in June 2004.

The Office of Personnel Management (OPM) estimates that transferring responsibility for military service credits from the Postal Service back to the Treasury would cause the Postal Service to have overfunded its obligation to CSRS by about \$20.3 billion through September 2005.² Consequently, under S. 662, the Postal Service would no longer be obligated to make either agency contributions or any further annual amortization payments for CSRS. (Employee contributions would continue at 7 percent of basic pay and retirement benefits under CSRS would not change.)

2. This overfunding, which is calculated on a net-present-value basis, represents an estimate of the total amount of money the Postal Service will have contributed toward CSRS from 1971 through September 30, 2005, minus the agency's CSRS liabilities if USPS bears no financial responsibility for the pension costs associated with military service credits. The projected overfunding is due primarily to larger-than-expected returns on assets held in the Civil Service Retirement and Disability Fund.

Spending by the Postal Service—including amounts paid into other federal accounts—is considered off-budget spending. However, the Civil Service Retirement and Disability Fund (CSRDF) is an on-budget account, so the amounts the CSRDF collects from the Postal Service are on-budget offsetting receipts. Reducing payments the Postal Service makes to the CSRDF would result in a reduction in off-budget spending and a reduction in on-budget offsetting receipts. CBO estimates that transferring responsibility for military service credits, and the attendant reduction in CSRS contributions such a change would bring, would reduce on-budget receipts by \$1.8 billion in 2006 and \$11.7 billion over the 2006-2015 period. Although the Treasury Department would then be responsible for the costs associated with those pension liabilities under the bill, the Treasury payment and receipt by CSRDF are both on-budget intragovernmental transactions. That is, the bill would replace one intra-governmental transfer with another. Instead of a transfer from the off-budget Postal Service to the on-budget CSRDF, there would be a transfer from the Treasury to the CSRDF.

Postal Service Retiree Health Benefits Fund. S. 662 also would change the way the Postal Service finances its share of the cost of providing health care to retirees. Instead of directly paying a portion of the health premiums incurred by current retirees each year, the USPS would begin paying for estimated costs of retiree health care as such costs are accrued by current workers. Starting in 2006, S. 662 would require the USPS to make payments equal to the annual increase in retiree health care liabilities accrued by current employees. These payments would be deposited into a new on-budget account, the Postal Service Retiree Health Benefits Fund (PSRHBF), which would earn interest at the same rate as the CSRDF. CBO currently projects that the CSRDF fund will earn about 5.75 percent next year. The Postal Service's share of health care premiums for current retirees would be paid out of the PSRHBF as soon as adequate funds are available in the account to do so.

Under S. 662, any overfunding toward CSRS liabilities (after financial responsibility for military service credits reverts to the Treasury) would be transferred from the CSRDF to the PSRHBF by June 30, 2006. Based on information provided by OPM, CBO anticipates that the transfer to the new fund would total \$21.2 billion and would occur in June 2006. This amount reflects the \$20.3 billion in estimated CSRS overfunding plus interest that would accrue between the end of the valuation period in September 2005 and when CBO assumes the asset transfer would take place in June 2006.

Under the bill, the Postal Service also would make annual amortization payments toward the unfunded liabilities for health care costs of both current and future retirees. The unfunded liability would be the difference between the assets held in the PSRHBF and the net present value of accrued liabilities projected for retiree health care. The bill would direct OPM to compute the required prefunding and amortization payments consistent with assumptions and methodologies for financial reporting used by OPM under current law. That computation

would be subject to review by the PRC at the request of the Postal Service. The bill specifies that payments would be made at the end of each fiscal year.

Based on information provided by OPM and using CBO's current projections of long-term interest rates, CBO anticipates that the net present value of the unfunded liability for the health care costs of retirees under the bill would amount to about \$49 billion at the end of 2006 and fall to about \$45 billion by the end of 2015. CBO estimates that payments by the Postal Service for prefunding health care costs of retirees and amortization payments for the remaining unfunded liability would be \$5.4 billion in 2006 (net of the 2006 premium adjustment described below), \$34.7 billion over the 2006-2010 period, and \$78.8 billion over the 2006-2015 period. Those amounts could change significantly if future interest rates are much different than currently projected by CBO.

For fiscal year 2006, S. 662 would reduce the initial prefunding and amortization payments otherwise due at the end of the year under the bill. The reduction would reflect all contributions directly paid to the FEHB program by the Postal Service in fiscal year 2006 for its share of premiums for current annuitants—about \$1.3 billion in that year. (Such contributions would be made by June 30, 2006, prior to the transfer of assets from the CSRDF into the PSRHBF.) Before applying the offset, CBO estimates that the total payments required under the bill for prefunding retiree health costs and making amortization payments toward the remaining unfunded liability would be \$6.7 billion in 2006. The final payment required under the bill, net of the adjustment for specified 2006 premium contributions, would be \$5.4 billion in 2006 as stated above.

CBO expects that the transfer of \$21.2 billion from the CSRDF to the PSRHBF resulting from the shift in responsibility for military service credits would occur in June 2006. Therefore, the Postal Service would cease making payments under current law for its share of FEHB premiums for annuitants beginning in July 2006, with those premium payments instead being drawn from the PSRHBF. (As mentioned earlier, the bill also would direct the Postal Service to deduct all fiscal year 2006 contributions toward its share of health premiums for current retirees made prior to July 2006 from initial prefunding and amortization payments otherwise due under the bill for fiscal year 2006.) CBO estimates that change in the funding mechanism for retiree health benefits would reduce off-budget payments by the Postal Service for FEHB premiums by \$0.4 billion in 2006 (which reflects premium payments, under current law, for the last three months of fiscal year 2006), \$10.2 billion over the 2006-2010 period, and \$29.4 billion over the 2006-2015 period. On-budget payments for those amounts would then be transferred from the PSRHBF to the FEHB program to pay the Postal Service's share of health care costs for retirees.

Health premiums paid by the Postal Service for FEHB and any payments that would be made into the new PSRHBF would be considered on-budget offsetting receipts. CBO estimates

that the increase in on-budget receipts as a result of changes in how the Postal Service finances its health care obligations would be \$4.9 billion in 2006, \$24.5 billion over the 2006-2010 period, and \$49.4 billion over the 2006-2015 period.

Off-Budget Effects (Direct Spending)

CBO estimates that enacting S. 662 would result in net off-budget costs of \$2.9 billion in fiscal year 2006, \$17.2 billion over the 2006-2010 period, and \$41.6 billion over the 2006-2015 period. Those amounts reflect the effects of allowing the Postal Service to increase other spending, reduce postal rates, or some combination of these actions because the bill would eliminate the requirement for the Postal Service to fund the escrow account. The net costs also reflect off-budget savings from a provision in the bill to make the costs of the PRC and the USPS Office of the Inspector General subject to appropriation, thus reducing direct spending by about \$1.6 billion over the next 10 years. In addition, S. 662 would reduce USPS payments for workers' compensation, which would reduce direct spending by about \$50 million over the next 10 years. The bill contains many other provisions that could affect USPS cash flows in each year, but we estimate that they would not have a significant net effect on the USPS over the long term.

Elimination of Escrow Fund. P.L. 108-18 permanently reduced payments by the USPS to the CSRDF. As a result of that act, USPS payments to the CSRDF declined by \$2.5 billion to \$5.5 billion annually beginning in 2003. For fiscal years starting in 2006, P.L. 108-18 requires that savings resulting from reduced payments to the CSRDF be considered an operating expense of the Postal Service and held in escrow, remaining unavailable for obligation unless authorized by subsequent legislation.

S. 662 would amend P.L. 108-18 to eliminate the escrow fund requirement. As a result of this provision, the Postal Service could lower rates and thus reduce its revenues from the levels expected under current law, or maintain rates and increase spending, or some combination of these actions. The net outlays of the Postal Service would increase because collections would not be deposited in escrow. CBO estimates that eliminating the escrow requirement would increase net off-budget spending by about \$3.1 billion in 2006, \$17.9 billion over the 2006-2010 period, and \$43.2 billion over the 2006-2015 period. Much of the spending would go toward making new payments to the on-budget account for health care costs.

Make Costs of PRC and USPS IG Subject to Appropriation. Under current law, the PRC and the Inspector General of the Postal Service are funded from the Postal Service Fund without annual Congressional appropriation. In total, these offices spent about \$140 million in 2004. S. 662 would authorize the appropriation of such sums as may be necessary from

the Postal Service Fund for these offices. Thus, enacting this legislation would reduce direct spending—and therefore, increase spending subject to appropriation—by about \$140 million annually beginning in fiscal year 2006.

Workers' Compensation Costs. The bill would lower workers' compensation payments made by the USPS by reducing an injured postal worker's long-term disability payments when the individual reaches retirement age as defined by the Social Security Act. Based on information provided by the USPS, CBO estimates that these savings would total roughly \$50 million over the 2006-2015 period. In addition, CBO estimates that there would be a negligible net savings to the Department of Labor's workers' compensation account, which is on-budget.

Changes to USPS Rate-Setting Procedures. Under the bill, the Postal Service would be directed to define the cost basis for the different products and services it supplies. These products and services would broadly be categorized as market-dominant products and competitive products. Different rate-setting procedures would apply to these different categories of products and services.

Market-Dominant Products. Under S. 662, market-dominant products would include: first-class mail, special services, periodicals, standard mail, media mail, library mail, bound printed matter, single-piece parcel post, and single-piece international mail.

S. 662 would require the PRC to establish, within one year of enactment, a new system for regulating postage rates for market-dominant products. This new system would include annual limitations on the percentage change in rates based on the Consumer Price Index for All Urban Consumers (CPI-U). Under the legislation, however, these annual limits could be exceeded under extraordinary circumstances.

Since 1970, increases in postage rates have largely tracked the rate of inflation. Over the past 10 years, rates were increased in 1995, 1999, 2001, and 2002 as a result of rate cases, and the Postal Service has begun preparation for a rate increase in 2006. Under the bill, we expect that the Postal Service would increase rates for market-dominant mail services more frequently than under current law but by smaller increments (as defined by the annual limitation relative to the CPI-U). Over the long term, CBO does not expect that enacting S. 662 would significantly change the revenues from market-dominant products that the Postal Service would be expected to receive under current law.

Competitive Products. Under S. 662, competitive products would include the following: priority mail, express mail, mailgrams, bulk international mail, and bulk parcel post. Currently, the competitive products contribute less than 15 percent of total postal revenues.

S. 662 would direct the PRC to prohibit subsidizing competitive products by market-dominant products, ensure that each competitive product covers its attributable costs, and ensure that all competitive products collectively cover their share of the institutional costs of the Postal Service. After these requirements have been implemented, the USPS could change rates for competitive products as long as the cost coverage requirements are met and the PRC has reviewed the proposed changes. In addition, the Postal Service would have to provide public notice and justification of changes in rates.

In addition, S. 662 would require the Postal Service to establish a new off-budget fund, the Competitive Products Fund, solely for revenues and expenditures associated with competitive products. We expect that it could be difficult to differentiate postal expenses related only to competitive products as USPS uses the same employees and facilities to handle both market-dominant and competitive products.

CBO cannot predict the bill's effect on Postal Service revenues from competitive products because the agency could set and change prices with few restrictions, although we would expect that yearly cash flows under the bill would differ from those estimated under current law. CBO also cannot predict how successfully the Postal Service might compete in the open market. However, the highly competitive nature of the mailing industry would tend to keep prices and revenues down, while the labor-intensive cost structure of the USPS would maintain upward pressure on expenses. Thus, over the long term under this legislation, CBO expects the Postal Service to attempt to recover its costs and break even as it did before the enactment of P.L. 108-18.

Spending Subject to Appropriation

S. 662 would authorize the appropriation of such sums as may be necessary, out of the Postal Service Fund, for the PRC and the Inspector General of the Postal Service. (Currently, these offices are funded out of the Postal Service Fund without Congressional action.) Beginning in 2006, this provision would entail about \$140 million a year in spending, subject to appropriation of the necessary amounts. (Spending after 2006 would increase to reflect anticipated inflation.) Enacting the bill would reduce direct spending by the same amounts. Spending on these activities would likely still be considered off-budget since funds would come from the Postal Service Fund.

In addition, S. 662 would require OPM to make actuarial computations related to the CSRS and PSRHSF trust funds and would increase OPM's administrative workload to comply with the requirements under the bill. CBO estimates that such activities would cost less than \$500,000 annually, assuming the availability of appropriated funds.

ESTIMATED LONG-TERM DIRECT SPENDING EFFECTS

Pursuant to section 407 of H. Con. Res. 95 (the Concurrent Resolution on the Budget, Fiscal Year 2006), CBO estimates that enacting S. 662 would cause an increase in direct spending to the unified budget of greater than \$5 billion in the 10-year period beginning in 2016. The bill would not increase on-budget direct spending by more than \$5 billion during any of the four 10-year periods from 2016 through 2055.

Specifically, CBO assumes that, during the decade following 2015, the increases in spending as a result of eliminating the escrow requirement and decreasing contributions toward CSRS would be larger than the decrease in spending due to additional contributions for health care costs. Eliminating that current-law escrow requirement increases the net spending of the Postal Service, which is classified as off-budget. In contrast, the payments from the Postal Service to cover health care costs for retirees generate on-budget savings by increasing on-budget offsetting receipts.

In the three 10-year periods from 2026 through 2055, we estimate the reverse would be true: that increases in health care contributions would be larger than the costs for eliminating the escrow requirement and USPS's contributions to CSRS. In part, this is because CSRS is a closed retirement system, and the effect of eliminating further receipts to the program declines over time, whereas health care contributions continue to increase. Thus, in those later 10-year periods, we estimate both on-budget savings and unified budget savings.

INTERGOVERNMENTAL AND PRIVATE-SECTOR IMPACT

S. 662 contains no intergovernmental or private-sector mandates as defined in UMRA and would impose no costs on state, local, or tribal governments.

PREVIOUS CBO ESTIMATE

On April 25, 2005, CBO transmitted a cost estimate for H.R. 22, the Postal Accountability and Enhancement Act, as ordered reported by the House Committee on Government Reform on April 13, 2005. CBO estimates that enacting that legislation would result in on-budget savings of \$35.7 billion and off-budget costs of \$41.6 billion over the 2005-2014 period, for a net cost to the unified budget of \$5.9 billion over that period.

A key difference between S. 662 and H.R. 22 concerns how the Postal Service would finance the health care costs of retirees. Both of the bills would require payments to prefund the costs associated with the annual retiree health liabilities accrued by current employees.

However, the bills address the unfunded liabilities for the health care costs of current and future retirees in different ways. H.R. 22 would require the Postal Service to pay annual interest costs on the unfunded liability, while S. 662 would require USPS to make amortization payments toward that liability. Also, H.R. 22 would require a minimum level of prefunding by the Postal Service, net of premium disbursement from the PSRHBFF. S. 662 does not include a similar provision.

In addition, H.R. 22 would not reduce USPS costs for workers' compensation, and the cost estimates reflect that difference.

ESTIMATE PREPARED BY:

Federal Costs: Mark Grabowicz for USPS costs, Geoffrey Gerhardt for retirement costs, and Julia Christensen for health care costs

Impact on State, Local, and Tribal Governments: Sarah Puro

Impact on the Private Sector: Paige Piper/Bach

ESTIMATE APPROVED BY:

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