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REPORT BY THE

Comptroller General

OF THE UNITED STATES

Need For Overall Policy And Coordinated Management Of Federal Retirement Systems Volume I

Federal retirement systems have developed on an independent, piecemeal basis, resulting in a patchwork of systems providing different benefits to various groups of employees. The Government has neither an overall retirement policy nor an established standard or method to assess the adequacy of retirement benefits. In addition, no uniform practices or principles exist for financing the retirement systems. Moreover, legislative oversight is diffused, in that different committees of the Congress have legislative jurisdiction over the various systems.

GAO believes that an overall Federal retirement policy and a centralized management focus on retirement matters would help assure that the systems develop on a consistent and financially sound basis.

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COMPTROLLER GENERAL'S REPORT TO THE HOUSE COMMITTEES ON ARMED SERVICES AND BANKING, CURRENCY, AND HOUSING; AND THE SUBCOMMITTEE ON COMPENSATION AND EMPLOYEE BENEFITS, HOUSE COMMITTEE ON POST OFFICE AND CIVIL SERVICE

NEED FOR OVERALL POLICY AND COORDINATED MANAGEMENT OF FEDERAL RETIREMENT SYSTEMS

D I G E S T

At the request of three House committee/subcommittee chairmen, GAO studied the desirability of establishing a mechanism to provide coordinated management of all retirement systems for Federal personnel in the executive, legislative, and judicial branches.

GAO reviewed the development of 38 retirement systems established or maintained by the Government and its instrumentalities. The systems cover over 5 million employees, pay over $15 billion annually to approximately 2.5 million retirees and survivors, and report unfunded liabilities in excess of $273 billion.

Based on this review, GAO believes that a centralized focus on retirement matters would help assure that the systems develop on a consistent and financially sound basis.

GAO also believes that the future development of the Government's retirement systems should be guided by principles and objectives embodied in an overall, coherent, coordinated Federal retirement policy. In the absence of such a policy, the systems have developed on an independent and piecemeal basis, resulting in a patchwork of systems providing different benefits to various groups of employees. (See ch. 8.)

Concern over the development of pension plans nationally is evidenced by the July 12, 1978, establishment of the President's Commission on Pension Policy. The Commission is charged with developing policies that can be used as a guide by the public and private sectors to ensure that the Nation has effective and equitable retirement, survivor, and disability programs.

Fragmented congressional committee jurisdictions and responsibilities have probably contributed to the piecemeal evolution of the Federal retirement systems. For example, up to 11 committees in the House and 10 committees in the Senate could have legislative responsibilities for 12 of the systems. Furthermore, the administration of these 12 systems is fragmented among 16 different organizations. (See p. 9.)

The system's provisions vary substantially in regard to

--employee contribution rates,

--benefit formulas,

--retirement eligibility requirements,

--creditable service,

--disability retirements,

--survivor benefits,

--reemployed annuitants, and

--funding methods. (See vol. 2, apps. XXI to XXIV.)

Different retirement benefits for personnel in the separate branches of the Government or for certain positions within a branch may be justified, particularly when such benefits are recognized as part of the total compensation paid to attract and retain needed personnel. GAO has long maintained that both Federal pay and benefits, including retirement, should be established and adjusted within the context of total compensation comparability with the non-Federal sector. However, under the pay comparability processes now in effect, benefit programs are excluded.

GAO reviewed the historical development of each of the systems and their benefit provisions and found it difficult, in most cases, to clearly identify any current management or compensation policies that are now being served by the systems as they are designed.

The 38 retirement systems reviewed were categorized by GAO as follows:

--Twelve Federal personnel retirement systems.

--Seven nonappropriated fund instrumentality retirement systems.

--Fifteen quasi-Federal employee retirement systems.

--One privately administered system.

--Three closed systems.

Federal personnel retirement systems

The uniformed services and civil service retirement systems are the largest of the 12 systems and cover the majority of all Federal personnel.

The uniformed services retirement system differs considerably from most retirement systems for Federal civilian employees. (See pp. 19 to 34.) Major differences include:

--Retirement eligibility after 20 years' service, at any age.

--No vested benefits until 20 years' service is completed.

--Benefits based on final pay.

--No member contributions.

--Disability benefits based on percentage of disbility.

--Survivor benefits not available until member is eligible for retirement.

Uniformed services personnel are also covered by social security and can be eligible for certain retirement-related benefits from the Veterans Administration.

The civil service retirement system was established in 1920 for employees in the competitive civil service. Since then, many changes to the system's provisions have been made, and the present provisions bear little resemblance to those in the original legislation. The system now consists of several different sets of provisions. While most employees are covered by the system's general provisions, certain special provisions apply to Members of Congress, congressional staff, law enforcement and firefighter personnel, and air traffic controllers. (See pp. 34 to 61.)

Separate Federal retirement systems have been established to provide special benefits to certain individuals and groups of employees who were at one time covered by the civil service retirement system. These include:

--Certain employees of the Central Intelligence Agency. (See pp. 89 to 92.)

--Directors of the Administrative Office of the U.S. Courts. (See pp. 87 to 89.)

--Directors of the Federal Judicial Center. (See pp. 87 to 89.)

--Comptrollers General. (See pp. 85 to 87.)

--Presidents. (See pp. 92 to 94.)

In 1942, civil service retirement coverage was expanded to include all Federal civilian personnel, except those subject to another Federal or District of Columbia retirement system. Among those excluded were personnel covered by the Foreign Service, Federal Reserve Board, and the Tennessee Valley Authority retirement systems. Had those systems not existed at the time, these employees would have been covered by the civil service retirement system.

Federal justices and judges were first granted retirement benefits in 1869. Judges who retire from the bench retain their office and, in most cases, continue to perform substantial judicial duties on a voluntary basis. During retirement, such judges receive the current salary of the office. Judges who resign from office perform no further judicial duties and receive the salary of the office at time time of resignation for the remainder of their lives. Nearly all judges retire rather than resign. (See pp. 76 to 82.)

The Tax Court judges retirement system also provides the current salary of the office to retired judges. Retired Tax Court judges are subject to recall and must serve when requested or forfeit all rights to retirement benefits for a 1-year period. (See pp. 82 to 85.)

Nonappropriated fund instrumentality retirement systems

Seven retirement systems have been established for personnel of nonappropriated fund instrumentalities of the Departments of Defense and Transportation. These personnel meet the general criteria used to define Federal employees but are excluded by law from civil service retirement coverage.

Employees and retirees are treated quite differently depending upon the retirement plan applicable to their employment. There are no apparent reasons for this other than the plans developed independently of each other. In many cases, benefits provided by the nonappropriated fund plans and social security combined are more generous than benefits received by other Federal civilian employees. (See pp. 94 to 109.)

Quasi-Federal employee retirement systems

Employees of certain Federal instrumentalities, namely the Federal Reserve Banks and the Federal home loan and farm credit banks, have both public and private characteristics. Fifteen of the systems GAO reviewed covered these types of employees. In some cases, the employees were at one time covered by the civil service retirement system and have retained their civil service coverage. In creating these banks, the Congress specified how they were to be established and managed. The banks are exempt from Federal and State taxation, and, in some cases, Federal funding is available if needed to help meet emergency credit needs.

Because of the Government's control over these instrumentalities, valid arguments can be made for considering their employees as Federal for retirement purposes. In fact, some quasi-Federal employees do participate in the civil service retirement system. However, should it be decided that these employees are not Federal, GAO believes that any retirement system covering them should be subject to the laws governing private retirement plans. (See pp. 109 to 123.)

Privately administered retirement plans

Certain employees of the Smithsonian Institution, the United States Department of Agriculture Graduate School, and the

Uniformed Services University of the Health Sciences are covered by retirement plans administered by the Teachers Insurance and Annuity Association-College Retirement Equities Fund which are private nonprofit organizations.

Various reasons were given why these employees are covered by private retirement plans. The primary reasons were either that they were not Federal personnel or that participation in a private plan was necessary to maintain comparability with similar employers in the Washington, D.C., area. GAO found that the Civil Service Commission has, in fact, determined that some of these employees should be considered non-Federal personnel. However, groups of employees in similar circumstances in other organizations are covered by the civil service system. (See pp. 123 to 134.)

Closed systems

Three Federal retirement systems--Panama Canal construction service annuity, Federal lighthouse retirement system, and Panama Canal Zone cash relief program--are "closed systems," that is, no new employees may participate, and when all existing retirees and surviving beneficiaries are deceased, the systems will terminate. These systems are small and rapidly diminishing. (See pp. 134 to 137.)

Federal employees covered by District of Columbia police and firemen retirement system

About 1,500 law enforcement personnel of the Park Police and Secret Service participate in a retirement system designed for municipal police and firemen of the District of Columbia. The system is administered by the District and, in general, provides much better retirement benefits than those received by other protective services personnel covered by the civil service retirement system. (See pp. 138 to 142.)

Financing practices of Federal retirement systems

No uniform method is used in determining the liabilities associated with Federal retirement systems, and costing and funding practices differ considerably. Some systems are financed on a contributory basis; some on a noncontributory basis; some provide for fully funding benefits as they accrue; some provide for partial funding; and others are completely unfunded. The costing and funding procedures used by many of the systems understate the full cost of providing retirement benefits.

In 1976, three major retirement systems--uniformed services, civil service, and Foreign Service--reported unfunded liabilities in excess of $273 billion, an increase of 75 percent since 1970. Conservatively, these liabilities are expected to increase to $349 billion by the end of fiscal year 1986. The inconsistent and inadequate costing and funding methods used for these programs should be corrected. (See ch. 5.)

Social security for Federal employees

The principle that the workers of the Nation should be assured a basic level of family income when earnings are impaired by disability, old age, or death is deeply imbedded in public policy. The social security program provides such basic protection to approximately 90 percent of the Nation's work force.

One of the major inconsistencies of Federal retirement systems is that social security coverage is provided to some personnel but denied to others. Employees covered by 25 of the 38 retirement systems GAO reviewed were also covered by social security.

Social security was designed to be supported on a universal basis, and GAO found no persuasive reasons to exclude many Federal workers from the program. Two of the consequences of this exclusion are that a large number of Federal personnel do not receive the basic protection afforded by social security and do not share in the responsibility of meeting the basic needs of the Nation's elderly and disabled persons. Without universal social security coverage, it will be very difficult, if not impossible, for the Government to provide comparable and equitable retirement benefits to all employees. (See ch. 6.)

Retirement program practices in the non-Federal sector

Many private companies cover substantially all of their employees under one plan. There is a trend toward the consolidating or merging of small State and local government retirement plans into larger State administered ones or into a single consolidated plan. The most important reasons given for these consolidations were to achieve conformity and equality of benefits within the work force. (See ch. 7.)

Recommendations for congressional action

Congressional action is needed if the Government's retirement systems are to develop, collectively, on a consistent and financially sound basis. An overall policy and a coordinated management mechanism over the systems should be established. Inconsistent provisions should be changed and the systems should be better integrated to achieve more equitable treatment of all personnel. Moreover, the inconsistent and inadequate costing and funding methods should be corrected regardless of whether the benefit provisions are revised.

GAO recommends that the appropriate committees of the Congress hold hearings to evaluate in depth the issues raised in this report and to set in motion actions necessary to establish an overall policy and a mechanism for coordinating the management of Federal retirement systems. The following should be considered.

--Establishment of a Federal retirement policy which outlines the principles, objectives, and standards to be followed in providing retirement benefits to military and civilian personnel. The policy should cover such matters as benefit levels, social security coverage, costing and funding, vesting, and administration. It should serve both management and employee needs. While recognizing that special provisions may be justified for particular groups, the guiding principle should be that all Federal personnel are to receive consistent benefits.

--Review of existing systems to determine the extent to which they need changes to conform to the established policy including consolidation of systems wherever practicable.

--Adoption of actuarial valuation methods and funding provisions that reflect the full cost of accruing retirement benefits and charge to agency operations all costs not covered by employee contributions.

--Development of eligibility criteria for participation in a Federal retirement system. Those systems covering employees who do not meet the criteria should be made subject to the laws governing private pension plans.

--Centralization of committee jurisdiction over retirement matters to better assure consistent application of the retirement policy. In the absence of such centralization, the Congress should establish a temporary joint committee to review all Federal retirement systems and recommend needed changes in policies to achieve the above objectives.

--Establishment of a permanent, independent board with authority and responsibility for monitoring the development, improvement, and administration of Federal retirement systems. The membership of the board should include representatives from the private sector and the legislative, executive, and judicial branches, each appointed to a fixed term.

Agency comments

In general, the agencies responsible for administering the retirement systems agreed that an overall Federal retirement policy was needed but argued that the separate systems should be continued. They insisted, in some cases, that the special or preferential treatment afforded particular employee groups was justified because their conditions of employment were different from those of other Federal personnel.

Most of the agencies did not comment on GAO's conclusions regarding the advantages of centralizing congressional committee jurisdiction over Federal retirement systems. Similarly, they generally deferred comment on the issue of social security coverage for Federal personnel since the matter is being studied by the Department of Health, Education, and Welfare in conjunction with the Civil Service Commission and Office of Management and Budget.

Those agencies which commented on costing and funding practices generally agreed that all retirement costs should be fully recognized.

Contents

ABBREVIATIONS

AAFES	Army and Air Force Exchange Service
AIME	Average Indexed Monthly Earnings
BLS	Bureau of Labor Statistics
BUPERS	Bureau of Naval Personnel
CIA	Central Intelligence Agency
CPI	Consumer Price Index
DIC	Dependency and Indemnity Compensation
DOD	Department of Defense
ERISA	Employee Retirement Income Security Act of 1974
FCSRS	Federal Civil Service Retirement System

FEHB	Federal Employees Health Benefits
FSLIC	Federal Savings and Loan Insurance Corporation
GAO	General Accounting Office
GSA	General Services Administration
HEW	Department of Health, Education, and Welfare
HI	Hospital Insurance
NAFI	Nonappropriated Fund Instrumentalities
NAVRESO	Navy Resale System Office
NOAA	National Oceanic and Atmospheric Administration
OASDI	Old-Age Survivors and Disability Insurance
OMB	Office of Management and Budget
PIA	Primary Insurance Amount
RMC	Regular Military Compensation
RSFPP	Retired Serviceman's Family Protection Plan
SBP	Survivor Benefit Plan
SMI	Supplementary Medical Insurance
SNF	Skilled-Nursing Facility
TIAA/CREF	Teachers Insurance Annuity Association/College Retirement Equities Fund
TVA	Tennessee Valley Authority
VA	Veterans Administration
VIP	Government Employees Voluntary Investment Plan

CHAPTER 1

INTRODUCTION

The Federal Government is the Nation's largest employer. Its civilian and military personnel are found in virtually every occupation imaginable. To be a "good" employer, the Government's personnel practices, including compensation programs, must be fair and equitable to assure the employment of competent personnel and the prudent expenditure of taxpayers' dollars.

Retirement programs are among the more significant and costly methods the Government uses to compensate its personnel. The Government maintains several retirement systems, each covering different groups of employees. All of the systems operate on the general premise that the income of employees who perform the Government's work should continue, usually at a lower rate, when their working years have ended. Thus, a retirement system is basically a program for providing a pension to retired employees for life. Most of the Government's retirement systems also provide benefits in the event of death, disability, or termination of covered employees.

Since 1974 we have issued a series of reports covering issues related to basic policies, financing, administration, and benefits of the various retirement systems. The reports concluded that better management of the systems is needed, especially that an overall policy is needed to provide objectives and principles to guide future development and improvement of the systems. In the latest report "Federal Retirement Systems: Unrecognized Costs, Inadequate Funding, Inconsistent Benefits" (FPCD-77-48, Aug. 3, 1977), we discussed the need for recognition and funding of the full cost of retirement benefits for the Federal work force and pointed out that many different and inconsistent provisions exist in the various systems without apparent explanation.

This report concerns the issue of whether it is desirable to establish a mechanism to coordinate management of all retirement systems for Federal personnel. The report was prepared at the request of the chairmen of two House committees and a subcommittee responsible for retirement matters.

Retirement plans established or maintained by agencies and instrumentalities of the Federal, State, and local governments are exempt from the Employee Retirement Income Security Act of 1974 (ERISA). ERISA imposed stringent requirements on private sector pension plans in areas such as funding benefit liabilities, fiduciary standards, and employee participation and vesting provisions. The chairmen's request identified 51 retirement programs as being exempted from ERISA on the basis that they were established or maintained by Federal agencies and instrumentalities. These programs are the subject of this report.

CATEGORIZATION OF SYSTEMS

The 51 retirement programs are encompassed in 38 separate retirement systems. (Thirteen of the programs are parts of larger systems.) Of the 38 systems, 3 are no longer being provided to new employees, 12 are clearly designed for Federal personnel and administered by Federal agencies, 1 is administered by a private organization, 7 are applicable to employees of nonappropriated fund activities primarily in the Department of Defense, and 15 are applicable to personnel whose Federal status is subject to debate. The 38 systems, including the 13 separately identified components, are as follows.

Federal personnel retirement systems

1. Uniformed services retirement system

   --Commissioned Corps of the Public Health Service retirement system

   --U.S. Coast Guard retirement system

   --National Oceanic and Atmospheric Administration (NOAA) retirement system

2. Civil service retirement system

3. Foreign Service retirement system

4. Federal Reserve Board retirement system

5. Tennessee Valley Authority (TVA) retirement system

6. Federal judiciary retirement system

   --Supreme Court justices retirement system

   --Widows of Supreme Court justices retirement system

   --Federal judicial survivors annuity system

   --Judiciary of the territories retirement system

7. U.S. Tax Court judges retirement system

8. Comptrollers General retirement system

   --Comptrollers General survivor system

9. Director of Administrative Office of the U.S. Courts retirement system

10. Director of Federal Judicial Center retirement system

11. Central Intelligence Agency (CIA) retirement system

    --CIA employees voluntary investment program

12. U.S. Presidents retirement system

    --Widows of the U.S. Presidents retirement system

<u>Nonappropriated fund instrumentality retirement systems</u>

13. Retirement annuity plan for eligible civilian employees--Army and Air Force Exchange Service

14. Coast Guard exchange employees retirement plan

15. Navy exchange employees retirement plan

16. Bureau of Naval Personnel nonappropriated fund employees retirement plan

17. Group retirement plan for civilian employees of the U.S. Marine Corps exchanges, recreation, funds, clubs, messes, and Exchange Service

18. U.S. Army nonappropriated fund employees retirement plan

19. U.S. Air Force nonappropriated fund retirement plan for civilian employees

<u>Quasi-Federal employee retirement system</u>

20. Savings association retirement fund, Federal Home Loan Bank Board

21. First farm credit district retirement plan

22. Farm credit retirement plan--Columbia district

23. The retirement plan for eligible employees of farm credit institutions in the fourth district

24. Farm credit system retirement plan--New Orleans district

25. Production Credit Association retirement plan for the New Orleans district

26. Sixth farm district group annuity plan

27. Employees retirement plan of the seventh farm credit district

28. Ninth farm credit district pension plan

29. Farm credit banks of Houston pension plan

30. Farm credit banks of Houston thrift plan

31. Berkeley farm credit employees retirement plan

32. Twelfth district farm credit retirement plan

33. Federal land banks of Columbia salary reduction thrift plan for farm credit employees

34. Farm credit district of Baltimore retirement plan

Privately administered system

35. Teachers insurance annuity association/college retirement equities fund (TIAA/CREF)

    --Private role employees of the Smithsonian Institution

    --Graduate school of the U.S. Department of Agriculture

    --Faculty members of the Uniformed Services University of the Health Sciences

Closed systems

36. Federal lighthouse retirement system

37. Panama Canal construction service annuity

38. Panama Canal Zone cash relief program for non-U.S. citizens

Employees covered by many of the systems also participate in the social security program as do temporary and intermittent workers. Further, the District of Columbia's police and firemen's retirement system covers certain employees of the U.S. Secret Service and U.S. Park Police.

The 38 retirement systems cover over 5 million employees and, in the latest year for which information was available on all systems (generally fiscal year 1976), paid about $15.9 billion to approximately 2.5 million retirees and survivors.

SCOPE OF REVIEW

Our review included:

--Analysis of managerial responsibilities for each system, both in the Congress and the administering agencies.

--Review of the historical development of each system and its benefit provisions.

--Evaluation of methods used to calculate and fund the costs of the various systems.

--Examination of the desirability of including all Federal personnel under the social security program.

--Identification of retirement practices and system consolidation trends in the non-Federal sector.

In performing the review, we analyzed retirement legislation and related documents, records and reports, actuarial valuations, statistical reports, and other studies of retirement matters. We interviewed officials at the various agencies responsible for administering the systems, and we also obtained information from 17 non-Federal employers on their retirement programs and related policies and practices.

CHAPTER 2

OVERVIEW

When should employees retire? How much should they receive? What is the purpose of retirement? Who should be covered by a retirement system? Are there any circumstances under which special or preferential benefits should be provided to certain groups? These and many other basic questions need answers before a rational retirement system can be established. However, Federal retirement systems have developed without such overall guidance.

Federal retirement systems differ in many respects, and covered personnel are treated quite differently depending upon the retirement system that applies to them. The differences include widely varying provisions on when employees become eligible to retire, benefit formulas, disability policies, survivorship provisions, contribution rates, reemployed annuitant practices, and others. Because retirement is an integral part of employee compensation, different benefit provisions mean different rates of compensation for employees who may be performing similar or equivalent functions and who are otherwise paid the same. In our opinion, the same provisions should apply to all Federal personnel unless there are compelling reasons to the contrary, and this criterion was used as the basis for our evaluation.

We found that, essentially, Federal retirement systems and their provisions have developed on an independent and often piecemeal basis. In many cases, we could find no explanation or reasons why different provisions were adopted. In others, the circumstances existing at the time of adoption have changed, but the benefits have been allowed to continue.

We believe that establishment of a definitive Federal retirement policy and a mechanism for coordinating the management of retirement systems is highly desirable. If the separate systems remain, their provisions should be made more consistent and the systems should be better integrated to achieve more equitable treatment of all personnel. Moreover, the inconsistent and inadequate costing and funding methods used for Federal retirement systems should be corrected regardless of whether the benefit provisions are revised.

This study did not address the matter of the level of benefits Federal retirement systems should provide. It is evident that certain of the systems are far superior to others, but, in the absence of an overall retirement policy for guidance, we have no basis on which to judge which level of benefits would be most appropriate for Federal personnel.

Different retirement benefits for personnel in the separate branches of the Government or for certain positions within a branch may be justified, particularly when such benefits are recognized as part of the total compensation paid to attract and retain needed personnel. As discussed in a previous report, 1/ we believe that Federal pay and benefits, including retirement, should be viewed as a compensation package and established and adjusted within the context of total compensation comparability with the non-Federal sector. Under the comparability processes now in effect, benefit programs are excluded.

A key issue that must be resolved in establishing a Federal retirement policy is the matter of social security coverage. Personnel covered by some of the systems are also covered by social security, whereas others are precluded by law from participating in social security through their Federal employment. Thus, if all personnel are to receive consistent and equitable benefits, social security should be provided to all or none. Based on our review, we believe social security should form the base for Federal retirement benefits and should cover all personnel.

Another significant issue requiring resolution is the eligibility criteria for coverage under a Federal retirement system. Existing criteria are vague and have been inconsistently applied. Many systems cover organizations and personnel whose relationship to the Government needs clarification. We believe good arguments can be made for considering the covered personnel to be Federal employees for retirement purposes, particularly since other employee groups of similar status are now in Federal systems. The criteria must be clarified, and those systems and employees not meeting the criteria should be made subject to the laws governing private retirement programs.

Implementation of a new retirement policy and the elimination of unjustified inconsistencies would not be easy. In addition to the basic policy issues of what benefits should be provided, who should be covered, who should administer the programs, what congressional committee(s) should have jurisdiction, etc., many practical difficulties inherent

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1/"Need for a Comparability Policy for Both Pay and Benefits of Federal Civilian Employees" (FPCD-75-62, July 1, 1975).

in any major change to ongoing programs are involved. For example, decisions would be required on whether the policy should be effective immediately for all personnel or apply prospectively only. A more important difficulty, perhaps, is the opposition to change that has been voiced by employee groups who now receive special or preferential benefits. Because of tradition, these groups and their employing organizations have generally become convinced that they deserve special treatment. We believe such preferential treatment should be continued only when it is clearly justified on the basis of an established retirement policy.

In essence, we have found that the lack of an overall, coherent Federal retirement policy, along with independent system development and piecemeal changes, has resulted in many inequities. Coordinated management of Federal retirement systems is needed. Development of an overall retirement policy would not necessarily depend on centralization of congressional committee jurisdiction over retirement matters, but it would certainly be facilitated by such action. Similarly, centralized authority and responsibility for monitoring the development and improvement of Federal retirement systems would result in greater consistency and provide a responsible focal point for retirement matters in the Government.

The need for increased attention to retirement matters in both the public and private sectors has been recognized by President Carter. On July 12, 1978, the President established a Commission on Pension Policy to conduct a comprehensive review of retirement, survivor, and disability programs in the United States. The Commission is responsible for developing national policies that can be used as a guide for development of the programs to assure that they are effective, equitable, and financially sound.

CHAPTER 3

LACK OF CENTRAL FOCUS ON FEDERAL RETIREMENT SYSTEMS

For the 12 systems previously identified as being clearly federally administered and providing benefits to Federal military and civilian retirees and their survivors (see pp. 2 and 3), up to 11 committees in the House of Representatives and 10 committees in the Senate could have legislative responsibilities, and 16 different organizations have legal responsibility for system administration. 1/

CONGRESSIONAL RESPONSIBILITIES FOR RETIREMENT SYSTEMS

The Congress establishes and monitors the basic policies for Federal retirement systems through the enactment of legislation and oversight by congressional committees. Critics inside and outside the Congress have discussed the problem of fragmented committee jurisdiction over Federal programs and how it can perpetuate fragmented program administration. Fragmented responsibilities for retirement matters are probably a primary reason for the absence of an overall policy and the independent evolution of the various Federal retirement systems.

Senate reorganization

The Senate committee reorganization instituted in the 95th Congress reflected a desire to develop integrated legislative programs. In stating the purpose of the reorganization, the Committee on Rules and Administration reported:

> "The jurisdictions of the committees are proposed to be recast so as to avoid fragmentation of overall legislative programs; to concentrate into a single committee all proposed legislation regarding a particular area of the government."

Earlier, the Senate Temporary Select Committee to Study the Committee System discerned strong support for three goals, including one that stated:

> "The Senate should strengthen the committee system's ability to develop integrated legislation, perform comprehensive oversight and reduce present

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1/Our review of congressional and administrative responsibilities was limited to these 12 systems.

wasteful demands on Senators' time, by consolidating subject jurisdictions in fewer committees while preserving acceptable levels of jurisdictional competition."

Examples of consolidation found in the reorganization plan include energy, commerce, and international policy. Budget oversight was consolidated through the 1974 Budget and Impoundment Control Act. Federal retirement system oversight and legislative responsibilities, however, were not affected by the Senate reorganization and remain fragmented in the Senate as well as in the House of Representatives.

Ambiguous and fragmented jurisdictions

An analysis of formally assigned committee jurisdictions clearly demonstrates the fragmented and sometimes ambiguous nature of retirement responsibilities. For instance, it would appear from the descriptions of their duties that the House Committee on Post Office and Civil Service and the Senate Committee on Governmental Affairs are responsible for all Federal employee retirement programs. As described in the Committee Reform Amendments of 1974 for the House of Representatives and in the Committee System Reorganization Amendments of 1977 for the Senate, these two committees are assigned responsibility for "status of officers and employees of the United States, including their compensation, classifications, and retirement." However, the House and Senate Committees on Armed Services are assigned responsibility for pay, promotion, retirement, and other benefits and privileges of members of the Armed Forces, and the Committees on Veterans' Affairs in the House and Senate are responsible for "pensions of all wars of the United States, general and special." No other committee jurisdictional statements mention Federal retirement.

Other committees, however, clearly exercise jurisdiction over retirement systems for agencies included in their responsibilities. The Foreign Service retirement system, for instance, comes under the House Committee on International Relations and the Senate Committee on Foreign Relations. In addition, both the House and Senate Judiciary Committees maintain responsibility for the Federal judiciary retirement system.

Committee jurisdictions cannot always be neatly categorized because retirement matters appear to cut across various committee jurisdictions. Potentially, 10 of 22 standing House committees, 9 of 15 standing Senate committees, and 1 select committee in each the House and Senate could contribute to Federal retirement system oversight and policy formulation. The above committees with retirement responsibility do not include the two Veterans' Affairs Committees.

Examples of specific retirement programs where committee jurisdictions seem unclear include the Public Health Service, Coast Guard, NOAA, Federal Reserve System, and the TVA. Jurisdiction over the Public Health Service, Coast Guard, and NOAA retirement programs is not clear because their benefits are primarily based on Armed Forces retirement provisions. Changes in the Armed Forces retirement package proposed and/or considered by the House and Senate Armed Services Committees could affect these three programs without direct consideration by the committees specifically overseeing these agencies--the House Committees on Interstate and Foreign Commerce and Merchant Marine and Fisheries and the Senate Committees on Human Resources and Commerce, Science, and Transportation.

The Federal Reserve System and TVA, on the other hand, base their retirement system authority on general administrative statements in the law and not on specific retirement legislation. Whether the appropriate committees include - retirement matters in their jurisdiction is not clear; we were unable to find printed hearings or reports on these two systems.

The fragmented congressional responsibilities for Federal retirement systems are demonstrated by the diagram on the following page.

ADMINISTRATION OF FEDERAL RETIREMENT SYSTEMS

Administrative functions for each retirement system are generally performed independently and many organizations are involved. Administration of each of the 12 systems involves two levels--Federal agencies whose employees are covered by the systems and the system managers. Agency functions cover activities up to, but not including, claims processing. Normally, these functions are:

--Maintaining employee contribution records (for a contributory system).

--Maintaining/verifying service records.

--Preretirement counseling, including estimating annuities and completing retirement applications.

--Determining retirement eligibility.

System manager functions include all activities from processing retirement claims to maintaining retirees and survivors on the retirement rolls. These functions can include:

--Processing of claims.

--Annuity computation.

--Annuity roll maintenance.

--Developing systems and preparing studies.

--Policy preparation and determination.

--Budgeting, auditing, and accounting.

--Fund maintenance.

--Investment management.

--Annuity check processing.

In most of the 12 systems, covered personnel are employed by one agency, and, for these systems, agency and system manager functions are performed by the same individual or group of individuals within the agency. For example, the U.S. Tax Court judges retirement system applies only to Tax Court judges, and one person in the Budget and Accounting Office of the U.S. Tax Court spends about 20 percent of his time performing both agency and system manager functions. On a larger scale, the TVA's Retirement Services Branch performs system manager functions for the TVA retirement system and it is also responsible for performing TVA's agency functions in relation to the system.

For the civil service retirement system, which covers employees in many Federal agencies, the Civil Service Commission's Bureau of Retirement, Insurance, and Occupational Health performs the system manager functions, whereas the personnel offices in the individual agencies perform the agency functions.

As shown in the following table, it cost at least $38 million in fiscal year 1976 to administer the 12 retirement systems. This amount does not include the cost of enlisted personnel retirement in the Army or agency functions costs under the civil service system for which estimates were not available. For other systems in which system

Retirement system	System manager	Fiscal year 1976 administrative costs
		(000 omitted)
Uniformed services:		
Military	Army	$ 8,971.3
	Navy	4,233.6
	Air Force	3,761.5
	Marines	1,675.9
Commissioned Corps of the Public Health Service	Department of Health, Education, and Welfare	171.1
Coast Guard	Department of Transportation	553.0
NOAA	Department of Commerce	9.7
Uniformed services total		$19,376.1
Civilian systems:		
Civil Service	Civil Service Commission	17,021.6
Foreign Service	Department of State	516.6
Federal Judiciary	Administrative Office of the U.S. Courts	21.5 21.5
Director of Administrative Office of the U.S. Courts	Administrative Office of the U.S. Courts	(a)
Director of Federal Judicial Center	Administrative Office of the U.S. Courts	(a)
U.S. Tax Court Judges	U.S. Tax Court	7.2
Board of Governors, Federal Reserve System	Federal Reserve Board	99.9
TVA	TVA	898.9
U.S. Presidents	General Services Administration	0.6
Comptrollers General	General Accounting Office	0.5
CIA	CIA	286.0
Civilian systems total		$18,852.8
Total administrative cost		$38,228.9

a/There were no annuitants receiving benefits from these systems during fiscal year 1976.

manager and agency functions are generally intertwined, it was often impossible to separate costs associated with each of the two functions; therefore, both types of costs are included.

Administration of the uniformed services retirement system

The uniformed services retirement system covers the Army, Navy, Air Force, Marine Corps, Coast Guard, and commissioned officers corps of the Public Health Service and NOAA. Each of the military services administers the system for its members with some policy guidance from the Department of Defense (DOD). The Coast Guard, Public Health Service, and NOAA, which are under the Departments of Transportation; Health, Education, and Welfare; and Commerce, respectively, administer their portions of the system. Certain retirement functions of NOAA are administered by the Navy.

All members of the above organizations must participate in the system, and the benefit provisions are generally the same for each group covered.

The idea of consolidating retirement system administrative functions is not new to the military. A DOD task force studied various degrees of consolidation ranging from centralizing policy guidance to a complete physical consolidation of retired pay functions for the Army, Air Force, Navy, Marine Corps, and Coast Guard.

The task force considered five alternatives to the current system. According to the study, most of the alternatives required large initial, one-time investments to make them operational. The most expensive alternative was to physically consolidate retired pay functions for all of the services. The task force estimated it would cost about $7.4 million to implement and would take more than 7 years before the annual recurring cost savings would pay back the initial investment. Thus, in July 1976 the Assistant Secretary for Defense rejected the alternatives requiring a high initial investment and directed the Air Force to develop a manual on military retired pay entitlements and procedures to be used by all the services as standard DOD guidance.

In addition, a Military Pay Procedures Conference was tasked with standardizing, where feasible, retirement forms, documentation, data descriptions, and operational and automatic data processing procedures at military service finance centers. Cost savings through this effort were estimated at about $1.6 million over 10 years. High fixed costs of the clerical functions for processing documents to establish and change accounts and allotments and answer inquiries appears to be a primary reason for this nominal cost savings.

Administration of civilian retirement systems

Nine organizations are responsible for administering the 11 civilian retirement systems. The systems vary in size, eligibility requirements, and benefit provisions. In addition, administrative responsibilities vary by organization. Some organizations perform both agency and system manager functions; others perform only one function.

About 90 percent of the $19 million spent on civilian system administration in 1976 was Civil Service Commission system manager costs. The remaining 10 percent was incurred by the other eight civilian retirement system managers. The composition of these costs poses some inherent constraints to realizing cost savings through consolidation of administrative responsibilities, including the intertwining of agency and system manager functions, the presence of fixed system manager costs, and lack of data to project organizational efficiency. Only a very small percentage of the costs could be potential savings through consolidation.

The agency and system manager functions are so intertwined for many systems that it is impossible to separate them. This limits the number of functions that potentially can be consolidated. One person in the General Accounting Office, for example, spends a small portion of his time performing both types of functions for the Comptrollers General retirement system. In this case, personnel savings would not be realized by transferring the system manager functions to another organization.

On a larger scale, the State Department performs system manager functions for the Foreign Service retirement system which covers certain employees of the Department of State, United States Information Agency, 1/ and Agency for International Development while concurrently performing agency functions for Foreign Service employees at the State Department.

1/Effective April 1, 1978, the functions previously carried out by the United States Information Agency and the Bureau of Educational and Cultural Affairs of the Department of State were consolidated into the International Communication Agency.

If these system manager functions were transferred, it is doubtful that more than five to six positions could be eliminated at State. Several of the other retirement systems have similar characteristics.

Even where it is possible to clearly delineate system manager functions, some of the costs are necessary and would be incurred by any consolidated organization performing the functions. The actual amount of savings, if any, is difficult to determine since, to a great extent, realizable savings would depend on the efficiency of the consolidated administration.

For example, the Federal Reserve's Division of Personnel paid $84,000 to a separate office to perform most system manager functions for a year. The entire $84,000 would not be a potential savings through consolidation since a portion of the service costs would be required under any administrator. The portion that pertains to computer usage, personnel costs for claim processing, record maintenance, etc., would be necessary with any combined system.

Returning to the State Department example, it may be possible to eliminate five or six staff positions at State by transferring the system manager functions to a larger organization. The larger organization, however, would incur some costs to assume these functions. It would still be necessary, for example, to process claims and maintain payment records and annuity rolls. Any savings resulting from a consolidation would depend on the efficiency of the organization accepting these new responsibilities. Since at present each system has different rules and regulations, any consolidated administrative organization would have to incur additional personnel costs to have a staff capable of processing the diverse applications. This could result in a net overall cost increase rather than in generating savings from the transfer of functions.

Even if all employees were in an identical system, it might or might not be more efficient for a larger organization to perform all system manager functions.

CONCLUSIONS

There is no centralized management focus in the Government on retirement matters. Fragmented congressional committee responsibilities have probably contributed to the piecemeal evolution of Federal retirement systems. Development and implementation of an overall retirement policy would not necessarily depend on centralization of committee jurisdiction, but it would certainly be facilitated by such action. Administrative costs are a relatively minor part of total retirement costs, and many of the costs would still be incurred if one organization was responsible for administering all systems. Thus, as long as the separate systems remain, no particular purpose would be served by combining administrative responsibilities.

AGENCY COMMENTS

Most of the agencies responsible for administering retirement systems did not comment on our conclusions.

The Department of Transportation stated that centralized congressional committee jurisdiction over retirement matters might have some merit. On the other hand, the Civil Service Commission stated that such centralization was a policy matter for the Congress to decide.

The Departments of State and Transportation stated that, in the absence of reduced administrative costs, they were opposed to any centralization of system administration. The CIA also opposed centralized administration, stating that it needed to continue administering its own system because of the unique security requirements associated with CIA employment.

CHAPTER 4

ARE SEPARATE SYSTEMS AND BENEFITS NEEDED?

Federal retirement systems have evolved without policy guidance. At least 12 separate retirement systems are maintained for various groups of Federal personnel, and Federal agencies and instrumentalities operate up to 23 additional systems for their employees, who, for various and often conflicting reasons, have generally not been considered to be Federal personnel.

In the absence of a Federal retirement policy, the benefit structures of Federal retirement programs have developed and continue to develop on a piecemeal basis. Many inconsistencies and inequities exist among the systems. Even though personnel covered by the systems work for the same employer--the U.S. Government--retirement program provisions differ substantially.

UNIFORMED SERVICES RETIREMENT SYSTEM

The uniformed services retirement system covers members of the Army, Navy, Air Force, Marine Corps, and Coast Guard, and the commissioned officers corps of the Public Health Service and NOAA. In 1976 the system covered about 2.9 million regular and reserve members and paid benefits of approximately $7.3 billion to 1.2 million retirees and survivors. Some aspects of the present system are traceable to laws enacted before the Civil War. However, the current system is based primarily on legislation enacted in the late 1940s. Generally, the laws authorizing retirement for members of the uniformed services are codified in titles 10, 14, 33, and 42 of the United States Code.

Participants are also covered by social security and are eligible for Veterans Administration (VA) benefits. Members contribute to social security but not to the retirement system. VA benefits are offset against benefits payable from the retirement system.

The uniformed services retirement system has several features not generally found in retirement systems for Federal civilian employees. These features include:

--Retirement with immediate benefits at any age after 20 years of service.

--Retirement benefit amounts based on terminal pay rates rather than average pay over a certain number of years.

--No contribution by covered personnel toward the cost of the system.

--No vested rights for members who separate before they are eligible for immediate retirement benefits (20 years).

--Disability benefits based on percentage of disability.

--Availability of survivor benefits only to retirees and active members who are eligible to retire.

<u>20-year retirement</u>

Prior to 1915 military personnel generally were required to serve 30 years before being eligible to retire. The 20-year retirement began in 1915 to aid retention of naval enlisted members and, through enactment of numerous pieces of legislation between 1915 and 1948, has been extended to all members of the military services. Historically, 20-year retirement developed on a piecemeal basis as follows:

1915 - 20-year retirement authorized for enlisted members of the Navy and Marine Corps. Many enlisted members were leaving the service to pursue civilian careers. The Congress established the 20-year retirement provision to induce a greater number of those members to remain in the service, thereby reducing the costs of recruiting, outfitting, and training large numbers of new members.

1938 - 20-year retirement established for naval officers. The 20-year provision was added to give the member a chance to leave the service after 20 years and to eliminate the requirement that naval officers serve 30 years before they could apply for retirement.

1939 - 20-year retirement established for enlisted members of the Coast Guard. The purpose was to improve the efficiency of the Coast Guard by eliminating each year a limited number of enlisted men, who were unable to continue performing arduous work.

1945 - 20-year retirement established for enlisted members of the Army and Air Force to equalize benefits with those of the Navy and to assist in recruiting replacements for World War II veterans returning to civilian life.

1946 - 20-year retirement was extended to Coast Guard officers to make the Coast Guard's retirement laws conform with the Navy's.

1948 - 20-year retirement established for officers of the Army and Air Force. The retirement provision was enacted to place Army and Air Force personnel on a par with Navy and Marine Corps personnel. Before 1948 Army and Air Force officers could apply for retirement after 15 years of service.

The commissioned officers corps of the Public Health Service and NOAA were authorized 20-year retirement in the early 1960s.

The Public Health Service, under the Department of Health, Education, and Welfare (HEW), is an outgrowth of the Marine Hospital Service created in 1798 to provide medical care for American seamen. In 1889 the Marine Hospital Service established the commissioned officers corps and adopted the military personnel system, pay scales, uniforms, and perquisites for commissioned officers. This organization became the U.S. Public Health Service in 1912. The commissioned officers corps also has active and inactive reserve officers for service in times of national emergency.

In 1960 the 20-year retirement was established for reserve and commissioned officers of the Public Health Service to provide an incentive for officers to stay longer in the corps and to make the Service's retirement laws uniform with those of the Armed Forces. Before 1960 the reserve corps was under the civil service retirement system, and the 1960 law was intended to make the reserve corps retirement benefits equitable with the commissioned corps. Active duty members have been part of the uniformed services since 1912. Before 1960 they had to serve 30 years before applying for retirement.

The Public Health Service is organized along military lines. It attempts to meet its physician and dentist needs by recruitment into the commissioned officer corps program. However, the corps has the same entry requirements as the military, and applicants not qualifying for this program may enter the Service as civilian employees with civil service retirement system coverage. Generally, an applicant is disqualified for the commissioned corps because of age (44 or older), physical condition, conscientious objection to military service, or lack of U.S. citizenship. Civilian and commissioned corps physicians and dentists work side by side. In August 1976 we reported that the inequities of the dual personnel and compensation systems in the Service were causing serious morale problems and recommended that a uniform compensation plan be developed for all Federal physicians and dentists. 1/

The forerunner to the current NOAA commissioned officers corps was created in the Coast and Geodetic Survey in 1917. At the time, the major activity of that organization was hydrographic and geodetic (water and land) surveying for which engineers qualified for marine command were needed. Originally this need was met by using Navy and Army officers. However, they were unavailable after the outbreak of the Spanish-American War in 1898. After unsuccessfully trying other methods to obtain needed personnel, the commissioned corps was established in 1917. Subsequently, NOAA was created within the U.S. Department of Commerce in 1970.

The NOAA commissioned officers corps is similar to other uniformed services officer programs with the following exceptions:

--NOAA officers are not subject to the Uniform Code of Military Justice except when they are transferred to DOD.

--There are no enlisted or noncommissioned personnel in the NOAA corps.

--NOAA does not have military bases.

In 1961, 20-year retirement was authorized for members of the NOAA corps to encourage more members to stay longer in the service and to bring NOAA's retirement provisions in line with the other uniformed services. Before this legislation, members of the NOAA corps had to serve 30 years before

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1/"Recruiting and Retaining Federal Physicians and Dentists: Problems, Progress, and Actions Needed for the Future," (HRD-76-162, Aug. 30, 1976).

applying for retirement, and 30 years is still considered to be a typical career.

As seen above, there has been no clear, overall legislative objective for 20-year retirement. The purposes range from providing incentives for personnel to leave the uniformed services to providing incentives for personnel to remain. In many cases, 20-year retirement appears to have been authorized for certain groups merely because it was being provided to others.

According to DOD, 20-year retirement serves the following objectives:

--Assists in attracting and retaining qualified members.

--Provides a socially acceptable method of removing some members who must be separated to maintain a young and vigorous force.

--Provides, after many years of faithful service, some degree of financial security.

Since these objectives would seem to be appropriate for any retirement system, we questioned whether 20-year retirement is justified to achieve the objectives for military personnel when similar early retirement benefits are not provided to Federal civilian employees.

Much of the debate centering around early retirement in the military concerns perceptions about the rigors of military life, time spent overseas, and combat readiness. DOD views youth and vigor as a universal requirement for all members regardless of occupational specialty or type of assignment. However, DOD has not been able to explain what it means by a "young and vigorous" force. Also, it does not know how old a service member is when he/she is no longer young and vigorous or what occupations require youth and vigor.

Combat-related jobs may require younger personnel than do other Federal occupations. In noncombat jobs, however, the maturity, experience, and judgment gained through longer service are more valuable than physical stamina and agility. In another study 1/ we examined the career experiences of 800

1/"The 20-year Military Retirement System Needs Reform," FPCD-77-81, Mar. 13, 1978.

military personnel who retired in 1975 to determine where the services were using their career personnel.

Our study disclosed that far more time was devoted by career personnel to support-type activities, such as administration and communication, than to combat-related activities, such as tactical and infantry operations. A full 92 percent of all the enlisted personnel career time and 67 percent of the officers' career months were spent on support-type activities.

Our review indicated that there is no "typical" military career pattern. We found variances in members' overseas experience and in the length of time spent in combat-related occupations. Eighty-one percent of the enlisted sample and 30 percent of the officer sample spent their entire careers in jobs that were noncombat-related. Thus, it would appear that most of the enlisted members' time was spent in duties demanding something less than exceptional youth and vigor. We also noted that during the last one-third of the officers' careers, close to 50 percent of their total months was devoted to administration, supply, and engineering functions. The demand for combat personnel (and exceptional youth and vigor) has traditionally been met by the short-term members or draftees. At the time of our review, 68 percent of the enlisted members with less than 4 years of service were assigned to combat positions. Only about 13 percent of all members entering the armed services remain to retirement.

In keeping with its contention that a "young and vigorous" force is needed in all military occupations, DOD employs a highly competitive and restrictive promotion system that precludes many members from serving full careers in excess of 20 years. Under this "up-or-out" system, DOD retains the right to deny reenlistments to enlisted personnel or to mandatorily retire officers if they twice fail for selection for promotion.

Although 30 years is considered a full career in the military, DOD's objective force profiles and promotions are designed around 20-year retirement for everyone. The up-or-out system is not concerned with an individual's ability to perform effectively, but with the member's relative standing among his peers. DOD's force structure policies do not permit members who are passed over for promotion but are still capable of performing effectively to complete full careers.

Elimination of 20-year retirement for all personnel would either require changes to the up-or-out system or adoption of retirement provisions similar to those found in most civilian retirement systems for the early retirement of personnel involuntarily separated before normal retirement eligibility. It should be noted that, in an April 1976 report, the Defense Manpower Commission described the up-or-out policy as "failure oriented" and questioned the practice of terminating members fully capable of performing their duties simply because of the lack of promotional opportunities. Moreover, as demonstrated above, most career members may spend all or the greatest part of their time in occupations that do not require exceptional youth and vigor. In this regard, on July 25, 1977, the Army changed its promotion policy for medical corps officers. To alleviate a shortage in the medical corps, all fully qualified medical corps officers will be permitted to continue in their current grade while the best qualified officers will be selected for promotion to the next higher grade.

In our opinion, continuation of 20-year retirement for uniformed service personnel is not justified. In 1975 officers retired at an average age of 46 with 24 years of service and enlisted personnel retired at an average age of 41 with 21 years of service. In addition to the unneeded retirements of able personnel that result from the up-or-out policy, other members obviously are retiring voluntarily upon reaching retirement eligibility. The ability to receive retirement benefits at a relatively early age and begin a second career in other employment is, understandably, too powerful an incentive to resist.

Benefit formula

Uniformed services retirement benefits are computed under a formula of 2.5 percent of final basic pay multiplied by years of service. Thus, after 20 years of service, a retiring member will receive 50 percent of final pay. The maximum benefit payable under the system is 75 percent of basic pay attained after 30 years of service. Service longer than 30 years accrues no additional retirement benefit.

We were unable to determine from the legislative history of the system the exact origin or rationale for the benefit formula. The formula was first used in the 1900s to compute retired pay of Navy enlisted personnel. It appears the formula is a modification of a 100-year old law specifying that officers with 30 or more years of service would receive retirement benefits equal to 75 percent of final basic pay. Final basic pay has continued to be used as the computation base.

Similarly, when the current retirement program was adopted, members continued to receive 2.5 percent of basic pay for each year of service. The 2.5 percent multiplier was decided on by extrapolation, i.e., since members used to receive 75 percent of basic pay for 30 years of service (2.5 percent for each year), members should receive 50 percent of basic pay for 20 years of service.

A major difference between military and civilian compensation systems must be recognized in evaluating retirement benefit formulas. Uniformed services personnel receive regular military compensation (RMC), which is often considered the equivalent of a civilian employee's salary or wages. RMC includes:

--Basic pay, which all members receive in taxable cash.

--Quarters, which varies by pay grade and by dependency status. Members are provided either Government quarters or a nontaxable cash allowance.

--Subsistence, which is the value of meals provided by the Government or a nontaxable cash allowance paid when meals are not provided.

--Tax advantage, which is the amount of additional cash income a service member would need in order to have the same take-home pay he or she now has if all the regular military compensation were subject to Federal income tax.

Since retirement is based on the basic pay element of RMC only, the multiplier used for uniformed services personnel must necessarily be greater than the multiplier used for civilian employees if benefits are to be comparable, even if other provisions were standardized.

In a recent report, "Military Compensation Should Be Changed to Salary System" (FPCD-77-20, Aug. 1, 1977), we recommended that the uniformed services pay and allowances system be converted to a salary system. If a salary system were adopted, under a standardized retirement program uniformed services personnel would have no apparent need for a retirement formula different from that applicable to civilian employees.

Retirement contributions

Since its inception, the uniformed services retirement system has been noncontributory, meaning that members do not make contributions from their pay toward the cost of retirement, as do most Federal civilian employees. The Congress makes annual appropriations to meet current benefit payments. Our legislative research did not show why the system is noncontributory.

The argument has often been advanced that uniformed services personnel make an "imputed" retirement contribution. That is, basic pay or RMC is lower than otherwise would be paid by an amount equal to the retirement contributions being made by civilian personnel. We found no support for this contention in our review of the system's historical development. Similarly, in 1976 the third "Quadrennial Review of Military Compensation" concluded that it is not demonstrable that basic pay or RMC is reduced by an imputed retirement contribution.

Vesting

Uniformed services members are not vested in the retirement system until they serve 20 years. Members who separate before 20 years of service receive no retirement benefits.

Most retirement programs for Federal civilian employees provide for full vesting after 5 years of service with deferred benefits payable at a later date if the employee leaves the Government before retirement age. Moreover, ERISA requires private plans to meet one of three vesting standards: (1) full vesting after 10 years of service, (2) 25-percent vesting after 5 years of service, with 5 percent added during each of the next 5 years and 10 percent added each year thereafter until 100-percent vesting is achieved after 15 years, or (3) 50-percent vesting when age plus credited service total 45, with an additional 10 percent for each of the next 5 years thereafter. We found no evidence that the Congress has ever considered vesting before 20 years of service for uniformed services personnel.

Disability retirement

The uniformed services retirement system provides retirement benefits to members who cannot perform their duties because of disabilities as do civilian retirement systems. But, as with other provisions, disability provisions of the uniformed services system differ significantly from those of civilian systems. (See app. XXIII for specific comparisons.)

While disabled soldiers have received disability payments in some form since colonial days, the current disability retirement provisions were established by the Career Compensation Act of 1941. That act established the first uniform law governing disability retirement in all branches of the uniformed services. The act provides for retirement of officers and enlisted members with a 30 percent or more permanent disability rating (according to the VA's rating schedule) if physically unfit to perform the duties of their grade. If the member has served less than 8 years, the disability must be the "proximate result of performing active duty" before retirement benefits will be granted. The 8-year requirement is waived during war or national emergency.

If the disability is not permanent, the member is placed on temporary disability retirement and is subject to physical examinations at least every 18 months. After 5 years, the member must either be retired for permanent disability, removed from the temporary disability list and returned to active duty, or separated (without retirement benefits but often with severance pay). There are no subsequent examinations or other verifications of continuing disability for members rated as permanently disabled.

The disability benefit is determined by multiplying the member's final basic pay by 2.5 percent for each year of service or by multiplying the percentage of disability by the member's final basic pay, whichever is greater. Benefits for a permanent disability range from 30 to 75 percent of basic pay. However, the minimum is 50 percent while on the temporary disability list.

We found only general reasons for the existence of the uniformed services disability retirement program--(1) to insure a physically fit armed force which could provide effective leadership, (2) to provide a continuing payment to members forced by physical disability to retire from military service, and (3) to provide some measure of economic security for those who endure the hazards of service in wartime and for those who choose the military service as a career, etc. We could not find, however, any rationale for the specific benefit provisions.

Survivor benefits

Survivorship provisions of the uniformed services retirement system have the same objectives as corresponding provisions in civilian systems--to provide a reasonable level of benefits to surviving family members upon the death of a covered employee.

Survivor benefits for the uniformed services retirement system were adopted through the 1953 Contingency Option Act which provided the Retired Serviceman's Family Protection Plan (RSFPP). RSFPP benefits were payable only to the survivors of retirees, and participation in the plan was optional. Very few retirees participated in RSFPP, apparently because of its cost.

In 1972 the Congress enacted the Survivor Benefit Plan (SBP) which was designed to provide survivor benefits comparable to those for retirees under the civil service retirement system. In general, SBP provides 55 percent of the retiree's benefit to a surviving spouse and eligible surviving children. SBP was designed to provide survivor protection at a reasonable cost where it did not previously exist and enhance it where it did. It was also felt that a well rounded, balanced compensation system was essential to efficient personnel management commensurate with an all volunteer force. The compensation system had to be competitive with those of other employers, or it would not be possible to retain the most qualified career personnel.

Participation in SBP is automatic unless a retiree elects not to participate or to participate at less than full coverage.

Unlike the civil service retirement system, which provides survivorship protection to employees after 18 months of service, SBP is available only to retirees and members with 20 years or more of service who are still on active duty. However, uniformed services personnel participate in social security, which provides survivor benefits under certain conditions after 6 calendar quarters of covered employment. At age 62, the amount of social security attributable to a retiree's military service is deducted from the surviving spouse's SBP annuity.

SBP and the civil service retirement system pay the same benefits to surviving spouses of retirees, but major differences exist in benefits for surviving children. Both systems have the same formula for reduction of the retiree's benefit if survivorship is elected, and surviving spouses under each program receive 55 percent of all or whatever portion of the retiree's benefit the retiree had specified as the base for the survivor benefit. Under SBP, a retiree has three options for payment of the 55-percent survivor annuity--spouse only, payments to the spouse until the spouse becomes ineligible (death or remarriage before age 60) and then to the children, or children only. There are no concurrent payments to both a surviving spouse and surviving children under SBP. Moreover, an additional reduction in the retiree's benefit is required if the retiree selects the second option, and a reduction is also made if the retiree chooses children's benefits only under the third option. Children's benefits are payable under the civil service system regardless of whether the retiree elects survivorship coverage for his/her spouse, and spouses' benefits and children's benefits are calculated under a separate formula and are paid in addition to the surviving spouse's 55-percent annuity.

We could find no explanation of why the uniformed services survivorship program differs so significantly from the civil service system, particularly since SBP was intended to provide comparable benefits.

Reserve retirement

The Army and Air Force Vitalization and Retirement Equalization Act of 1948 created a retirement program for members of the reserve components. The purpose of the program is to provide an incentive for personnel to remain in the reserves.

To qualify for reserve retirement, a reservist must have

--completed 20 years of creditable service in the Armed Forces,

--served the last 8 years of service in a reserve component, and

--not be retired from active military duty.

Reserve retirement benefits are computed under the same formula as that used for the active forces but with a different definition of years of service to reflect the unique form of service in the reserves. Moreover, benefits are not payable until age 60 regardless of when the 20 years of service are completed.

In determining reserve retirement eligibility, the term creditable years of service is defined as a year on active duty or any year in which, through a combination of active and inactive duty, the reservist earns at least 50 points. If the member earned fewer than 50 points in any year, it does not count as a year of satisfactory service for reserve retirement eligibility, but the points do count in the computation of retirement benefits. In computing annuities, the term constructed years of service is applied, and it is defined as total points earned over the reservist's career divided by 360. For example, a reservist who had earned at least 50 retirement points each year for 20 years and accumulated a total of 2,520 points would at age 60 receive retirement benefits based on 7 years of constructed service (2,520 divided by 360).

By deferring benefit payments to age 60, the reserve retirement program differs significantly from the active duty retirement program in which benefits may begin immediately upon completion of 20 years of service. Further, the benefits payable at age 60 are based on pay rates in effect at that time, while deferred benefits under Federal civilian retirement programs are based on pay rates in effect when the service was completed. We were unable to determine why the reserve retirement provisions differ so greatly from the Government's other retirement programs.

Interrelationship with other Federal retirement systems

The uniformed services operate a closed personnel management system; members enter at a relatively young age, and relatively few entrants remain until retirement. Each branch of the uniformed services generally grants retirement credit for members transferring from one service to another. However, the Armed Forces do not always give retirement credit for service performed by NOAA members. No credit is granted for Federal civilian service under the retirement system, even though military service is generally creditable, without cost to the employee, under civilian retirement systems.

In general, uniformed services retirement benefits are payable in addition to any benefits that may be earned under other Federal retirement systems. Military service generally may not be used to earn retirement credit under both the uniformed services system and a civilian system. However, military reservists and disability retirees may receive credits for any active duty service under both the uniformed services and civilian systems.

Many uniformed services retirees are reemployed in civilian capacities by the Government. (The Civil Service Commission estimated that, as of June 30, 1975, approximately 142,000 uniformed services retirees were employed in the civilian service.) In accordance with the Dual Compensation Act of 1964, all are paid the full salary of their civilian positions, earn retirement credits under civilian systems, and, in most cases, also receive their full uniformed services retirement benefits. The act provides that all retired enlisted personnel and reserve officers may receive full retirement benefits in addition to their Federal civilian salaries. A retired regular officer receives only a portion of his/her retirement benefit--currently, the first $4,532 plus half the balance--and the pay of the civilian position.1/ The amount of $4,532 was originally $2,000 when the law was enacted, and represents the original $2,000 plus subsequent cost of living adjustments. The amount will continue to be increased by future cost of living adjustments. Regular officers whose retirements were based on combat disabilities are excluded from the dual compensation offset provisions. Of the 142,000 uniformed services retirees in civilian positions, only 5,164 were retired regular officers subject to the dual compensation restriction.

The Dual Compensation Act as originally proposed made no distinctions between regular officers, reserve officers, and enlisted personnel, as they all were to be subject to the dual compensation provisions. However, an amendment, which became part of the law, excluded reserve officers and enlisted personnel. At that time, about 95 percent of the uniformed services retirees were reservists and enlisted personnel; therefore, a small percentage of reemployed retired personnel were affected by the law as finally passed. The $2,000 amount included in the law as part of the formula for reduction of retired regular officers benefits was determined to be the approximate average nondisability retirement benefit of enlisted personnel at the time the 1964 law was being considered. The formula, one-half of the remainder, was chosen as a reasonable compromise between the view that retired officers should retain all of their retirement and the view that they should have none of their retirement while working in civilian jobs.

1/The Dual Compensation Act was amended by the Civil Service Reform Act of 1978 to provide a former member of the uniformed services may not receive retired pay and salary in excess of the rate of pay for level V of the Executive Schedule, currently $47,500. Generally, this limitation applies only to members retiring after the effective date of the Reform Act.

In researching the legislative history of the 1964 act, the only reason we found for the distinction between regular and reserve officers was that regular officers receive more advancement in their term of service and are allowed to obtain 30 years of service while the vast majority of reserve officers retire after 20 years. While reserve officers have never been legally required to retire after 20 years of service, reservists do not have the same statutory tenure as regular officers and therefore tend to be separated first during reductions in force. This may or may not have justified distinguishing between reserve and regular officers in 1964. However, we believe it is questionable whether the distinction continues to be justified today.

When retired uniformed services personnel reenter active duty, their retirement benefits are suspended. In our opinion, when a "retired" uniformed services member becomes employed in a Federal civilian capacity, he/she has not retired but merely changed positions within the Government. We believe that both salary and retirement benefits attributable to Federal service should not be paid to a Federal employee during active service. Moreover, the ability of many uniformed services retirees to secure other Government employment would seem to negate somewhat the stated objectives of the uniformed services retirement system (see p. 23) such as retaining qualified members and the need to provide, on the basis of 20 years of military service alone, a degree of financial security.

VA benefits

In addition to benefits from the uniformed services retirement system, military personnel may also be eligible for benefits from VA programs. In general, however, VA benefits do not constitute a form of retirement but are considered to be payments to veterans who have faithfully served their country. VA disability and survivor programs may be considered to complement rather than duplicate retirement benefits.

VA benefits provide compensation for service-connected disabilities incurred or aggravated in the line of duty during wartime or peacetime service, if the member was not separated under dishonorable conditions. Amounts paid are based on the extent of earning capacity impairment and/or individual needs. If a member is receiving military retirement (disability or nondisability) he/she must waive an equal amount of retirement benefits to receive disability compensation from VA.

Certain veterans may receive compensation for nonservice-connected disabilities. The veteran must have been discharged from the military under conditions other than dishonorable after 90 or more days of service, including at least 1 day of wartime service. Also, the veteran must be 65 or be totally and permanently disabled from nonservice-connected causes. Payments are subject to income limitations with the amount varying inversely with countable income. The annual income limit for those eligible under age 78 is $3,600. Maximum payment for a single veteran under age 78 is $185 a month, while members over age 78 receive a 25-percent differential. In determining annual income, all sources of income are included unless they are specifically excluded by law. Some of the exclusions are welfare or relief payments, VA compensation, spouse's earned income, and 10 percent of all payments under public and private retirement programs (including social security).

Payments under VA's Dependency and Indemnity Compensation (DIC) program are available to survivors of veterans who died from service-connected causes. DIC is payable to the widow or dependent child(ren) if the service member died from (a) a disease or injury incurred or aggravated while on active duty or on active duty for training, (b) an injury incurred or aggravated while on inactive duty training, or (c) an otherwise compensable disability. The amount of the DIC payment is based on the military pay grade of the deceased. Additional payments are made for dependent children and spouses in need of aid and attendance. DIC payments are deducted from any survivor benefits payable from the uniformed services retirement system.

CIVIL SERVICE RETIREMENT SYSTEM

The civil service retirement system which covers approximately 2.7 million employees is the largest staff retirement system for Federal civilian personnel. In fiscal year 1977, the system paid approximately $9.3 billion in benefits to 1.5 million retirees and survivors.

The system was established in 1920 as the first retirement program for employees in the competitive civil service. It was born out of a pressing management need to remove from employment permanently tenured personnel who could no longer perform efficiently because of age or infirmities.

Permanent tenure in Government employment was provided when the classified service was established in 1883. Subsequently, many employees had grown old and become inefficient in their work and incompetent for continued service. However, because most elderly workers had not been able to make financial provisions for their old age, and because isolated instances of removing them had drawn adverse public reaction, it was impossible to induce responsible managers to dismiss them. As a result, an unofficial, unauthorized pension system evolved. It consisted simply of retaining on the rolls, under various pretexts, all superannuated employees with many years of service and paying them full salary for little or no work. This practice impaired the efficiency of the Government's operations and retarded the advancement of competent employees.

Upon its enactment, the civil service retirement system provided automatic coverage to all employees in the classified civil service; full-time employees of the District of Columbia government (excluding teachers, school officers, firemen, and policemen); and employees of the U.S. Capitol Buildings and Grounds, the Library of Congress, the Botanic Gardens, and superintendents of the national cemeteries. In addition, the President, by Executive order and upon recommendation of the Civil Service Commission, could extend coverage to any noncompetitive employee or group of employees not in the classified service.

The system provided only two types of retirement--mandatory and disability. Mandatory retirement was generally set at age 70. However, employees separated at the mandatory retirement age were eligible for an annuity only if they had completed at least 15 years of service. Disability retirement annuities were provided to covered employees with a minimum of 15 years' creditable service who, before reaching mandatory retirement age, became totally disabled for useful and efficient work (in either the position occupied or any other positions to which they would have been assigned).

Both mandatory and disability retirement annuities were based on length of service and average salary during the last 10 years of covered employment and were equal to approximately 2 percent of the 10-year salary average for each year of service up to 30. Annuity amounts ranged from a minimum of $180 to a maximum of $720 a year.

The system was financed by employee contributions of 2.5 percent of basic salary and, as needed, by annual appropriations. Employee contributions were deposited in a "civil service retirement and disability fund," which was maintained by the Treasury Department and invested in interest-bearing Government securities. Service credit was granted for all competitive and noncompetitive civilian service in Government departments, branches, and independent offices and for all military and Coast Guard service prior to August 1, 1920.

There were no provisions under the original system for deferred annuities, survivor annuities, or optional retirements. Nor were there any provisions regarding the reemployment of annuitants.

As is apparent from the preceding discussion, the civil service retirement system was originally designed primarily to assist management in improving productivity by providing for the orderly and humane removal of superannuated and incapacitated employees.

There have been many changes to the civil service retirement system over the past 58 years. The present system consists of several different sets of provisions which bear little resemblance to those contained in the original legislation. Most employees are covered by the system's general provisions, but separate provisions (allowing higher annuities and/or earlier retirement ages) exist for Members of Congress, congressional staff, law enforcement and firefighter personnel, and air traffic controllers.

The following sections discuss the development of the general provisions of the system and contain analyses of the special benefits provided to certain groups.

Covered employment

Employment eligible for coverage under the system has expanded greatly since 1920, and, in many respects, this growth has occurred on a patchwork, arbitrary basis.

In general, the system now provides coverage to civilian officers and employees appointed or elected to a position in or under the executive, legislative, or judicial branches of the Government, including Government-owned or controlled corporations, the government of the District of Columbia, and Gallaudet College. Coverage is mandatory, except for Members of Congress and congressional employees.

Certain employees, however, are specifically excluded from coverage either by law or regulation. These include the President, Federal judges, employees subject to another Federal retirement system, and certain temporary, part-time, and intermittent employees.

There are also certain exceptions to those exclusions. When covered employees (except alien employees whose duty station is located in a foreign country) accept employment in excluded positions without a break in service or after a break of 3 days or less, they retain coverage under the civil service system. Examples of this are covered employees who transfer to the TVA or the Federal Reserve Board, both of which have their own retirement systems. In addition, coverage is retained by certain covered employees who transfer to public international organizations. However, such coverage is limited to a maximum of 8 years.

Between 1920 and 1940 the Congress extended coverage under the system to certain groups of employees who had been excluded by the original law. In general, these included postmasters, employees of the Federal Bureau of Investigation, State Department employees serving abroad who were not in the Foreign Service, and, upon their election, to congressional employees and employees of the U.S. courts.

In January 1942 the Congress enacted legislation which had the effect of eliminating "competitive status" as a factor in determining coverage under the system. The legislation extended coverage to elected and appointed officers and employees in or under the executive, judicial, and legislative branches of the Government and to officers and employees of the District of Columbia government. The only individuals specifically excluded from coverage were those subject to another Federal or District retirement system which, in most cases, had been established after the civil service system. Elective coverage was retained for congressional employees but was withdrawn for employees of the U.S. courts. In addition, coverage was made optional for Presidents, Vice Presidents, and Members of Congress.

The coverage granted to Presidents, Vice Presidents, Members of Congress, and heads of executive departments and agencies by the January 1942 legislation was rescinded 2 months later. The apparent reason for withdrawing this coverage was because of adverse public opinion and the war. Some Members of Congress felt that controversy over the matter could interfere with "attaining that unity so necessary to victory" in war.

In July 1946 legislation was enacted which again extended coverage to heads of executive departments and agencies. At that time only a small number of positions in the executive branch were not covered by the system and it was felt that individuals holding these positions should not be discriminated against.

Members of Congress were also again extended coverage, at their option, in 1946. The legislative history indicates that, by allowing Members to participate in the system, a sense of security would result and would contribute to an independence of thought and action by Members. It was also believed that coverage would bring a larger number of younger Members with fresh energy and new viewpoints into the legislative service.

Between 1946 and 1958 the Congress terminated six Federal retirement systems and placed the covered employees under the civil service system. The terminated systems included the Panama Railroad and Panama Canal Company retirement systems, a retirement system covering noncitizen employees of the Panama Canal Company and the Canal Zone Government, the Alaska Railroad retirement system, a retirement system for employees of the Comptroller of the Currency's office and a system for faculty members of the U.S. Naval Academy and the Naval Postgraduate School.

During this period the Congress also extended retirement coverage to officers and employees of Gallaudet College, a nonprofit institution partly funded by Government appropriations. While the Congress recognized that Gallaudet employees were not Federal employees, it accorded them coverage because their work "is so closely allied to and associated with the Federal Government and the District of Columbia government as to constitute them Federal employees."

In 1974 the Congress established, in the District of Columbia, a private, nonprofit corporation known as the Legal Services Corporation. The enabling legislation provided that the corporation would not be considered a department, agency, or instrumentality of the Federal Government. It further provided that the officers and employees of the corporation would not be considered Federal except for purposes of compensation for work injuries, life and health insurance, and civil service retirement. We could find no explanation in the legislative history of why these employees were granted retirement coverage for service with a private non-Federal corporation.

Under certain circumstances and conditions, credit may be granted for service not covered by the system. The Civil Service Commission, as administrative agency for the system, decides on questions regarding creditable service. For example, credit may be granted to newly covered employees for previous service under another Government retirement system (military or civilian), in the Peace Corps, Volunteers in Service to America, and the Pan American Sanitary Bureau.

Optional retirement

The optional retirement provisions applicable to most employees covered by the system provide for voluntary retirement at age 55 with 30 years of service, at age 60 with 20 years, or at age 62 with 5 years. 1/ In each case, at least 5 years of covered civilian service is required.

Optional retirement, introduced in 1930, allowed an employee who had completed 30 or more years of service to retire 2 years earlier than the mandatory separation age for the position occupied with no reduction in annuity.

The rationale behind this provision was that in large groups of employees certain individuals become superannuated and consequently inefficient earlier in life than most others in their group. Therefore, the Congress felt efficiency in Government service would be enhanced by affording such individuals an opportunity to retire a few years early with just remuneration for long service. It was believed that only the mentally and physically impaired would take advantage of this option. This was because the ages at which the option was available would preclude most individuals from securing employment in the private sector.

1/The Civil Service Reform Act of 1978 provides optional retirement for any individual who is removed for less than successful performance from the Senior Executive Service after completing 25 years of creditable service or after completing 20 years of service and attaining age 50.

In 1942 the system's optional retirement provisions were liberalized. The new provisions permitted voluntary retirement at age 60 with 30 years of service, at age 62 with 15 years, or (on a reduced annuity) between ages 55 and 60 with 30 years. At the same time, the head of an employing agency was given the right to file a retirement claim for certain employees age 60 or older who were eligible for optional retirement. This right could be exercised only if the employee was unable to satisfactorily and efficiently perform the duties of his position or a similar one. The employee, however, had the right of appeal to the Civil Service Commission, and the Commission's decision was final. This provision was practically never used and was eliminated from law in 1948.

Our research indicated that changes in optional retirement were made because most other public retirement systems provided earlier retirement options and because the changes would reduce the number of employees retiring on disability, thereby effecting a savings in administrative costs.

In 1956 the provision for optional retirement at age 62 with 15 years of service was changed to age 62 and 5 years of service. The reduction in annuity of employees electing to retire at age 55 with 30 years of service was eliminated in 1967. At the same time, the service requirement for optional retirement at age 60 was changed from 30 to 20 years.

For several years preceding these changes, Federal employee organizations had sought voluntary retirement with full annuity after 30 years of service at age 55, or preferably at any age. They held that this provision would make it more feasible economically for workers with partial disabilities or declining capacity or interest to withdraw from active service and thereby improve Government operations. In addition, they contended that 30 years is a full career, justifying retirement without penalty, and that the existing law discriminated against employees who entered the service at an early age. It was also argued that early retirement eases unemployment problems by making room for new hires.

A 1966 report to the President by the Cabinet Committee on Federal Staff Retirement Systems recommended the adoption of an age 55, 30 years' service option with unreduced annuity. The report also recommended a reduction in the minimum service requirement at age 60 from 30 years of service to 20 years. It suggested that this would provide a meaningful intermediate option between 55/30 and 62/5 voluntary retirement provisions and establish a more consistent relationship between age and service. There was a seeming inequity in that a 55 year old employee with 30 years of service could retire immediately, as could a 62 year old employee with only 5 years of service, while a 61 year old with 29 years of service would have to wait another year before he could retire.

Benefit formula

In general, benefits under the system are expressed as a percentage of the average annual salary earned during the employee's 3 consecutive highest paid years, "high-3," with basic annuity maximum of 80 percent of high-3. The percentage is calculated under a 3-step formula as follows:

(1) 1.5 percent of high-3 multiplied by first 5 years of service, plus

(2) 1.75 percent of high-3 multiplied by the number of years of service between 5 and 10, plus

(3) 2 percent of high-3 average salary multiplied by all years of service over 10 years.

If a larger annuity will result, 1 percent of high-3 plus $25 may be substituted for any one or all of the above steps. This option is generally applicable in cases where an employee's high-3 average salary is less than $5,000.

An annuity formula was first used under the system in 1926. Under the formula, an employee's basic annuity was computed by multiplying his average salary during the last 10 years of service (not to exceed $1,500) by his years of service (not to exceed 30) and dividing the resulting product by 45. This established a maximum annuity of $1,000, but no minimum was set.

Several changes which liberalized the annuity formula were made over the years. In 1930 the salary base was changed to a 5-year average (limited to $1,600), and annuities were calculated under two alternate methods with retirees receiving the higher of the two amounts. Under the method applicable to all but the lowest salaried employees, the 5-year salary average up to $1,600 was multiplied by years of service (not exceeding 30) and the product divided by 40. This method produced a maximum annuity of $1,200.

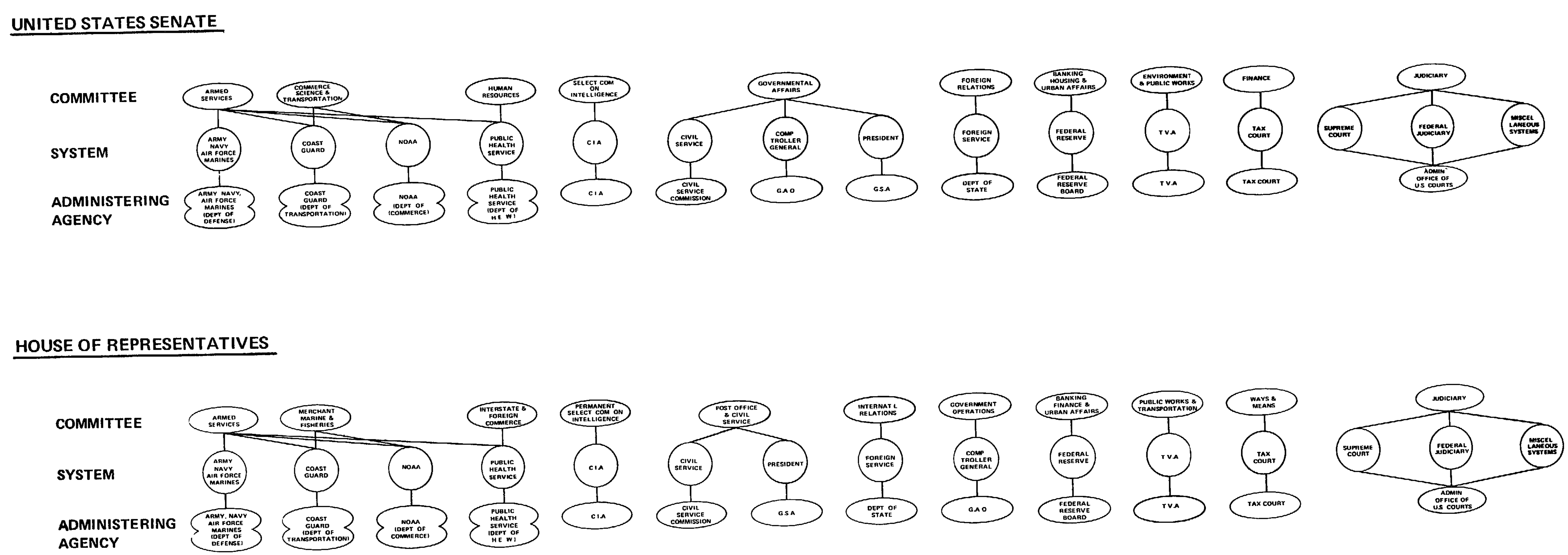
A third alternative computation method was added in 1942. This method eliminated the restriction on high-5 average salary; increased the years of service that could be used in the calculation to 35, and divided the product by 70. This method generally operated whenever high-5 average salary exceeded $2,800 and in certain $2,400 to $2,800 cases and where service ranged between 30 and 35 years. The apparent purpose of the method was to provide more equity to higher salaried employees with long service by granting them annuities more proportionate to their salaries. Under the previous formula, some higher salaried employees with 30 years of service received annuities as low and sometimes lower than 20 percent of their active-service salaries. In contrast, it was pointed out that employees retiring with 30 years of service under the Foreign Service retirement system could receive annuities equal to 60 percent of their salaries (with no limits) and that military officers with 30 years received 75 percent of their final basic pay at retirement.

A single computation formula was substituted by legislation enacted in 1948 for the three alternative methods. The new formula provided for computing an employee's basic annuity by multiplying his years of service by 1.5 percent of his high-5 average salary or 1 percent of his high-5 plus $25. This legislation also established the basic annuity maximum at 80 percent of high-5.

The current 3-step calculation formula, using high-5 salary as the base, was adopted in 1956. The formula represented an apparent compromise between the formula contained in a union-supported bill and a formula recommended by the Civil Service Commission. The union-supported bill provided for applying the 1948 formula to only the first 5 years of service and for using 2 percent of high-5 for all remaining years. This would have provided a basic annuity of 57.5 percent of high-5 after 30 years of service. In place of this, however, the Commission proposed a formula under which the basic annuity after 30 years would have been 52.5 percent of high-5. The compromise ultimately adopted provided 56.25 percent of high-5 for 30 years of service.

In 1969 the salary base for computing annuities was changed from the high-5 average to a high-3 average. The rationale for this change was that the high-5 average had tended to keep employees working beyond the time they normally would have or should have retired. This tendency was strengthened by the regularity of annual general pay

CONGRESSIONAL COMMITTEE JURISDICTION OVER FEDERAL RETIREMENT PROGRAMS



increases. Since the highest 5 years of earnings were usually the most recent years of employment, employees eligible for retirement postponed retiring in order to improve their high-5 average which, with pay raises, would increase appreciably with each additional year of service.

Disability retirement

Employees who have completed 5 years of creditable service under the civil service system are eligible for a retirement annuity at any age if they cannot, because of disease or injury, perform usefully and efficiently in the grade or class of position last occupied. An employee unable to do one essential function of his job is considered to be fully disabled; the system does not provide for partial disability.

A disabled retiree is guaranteed a minimum annuity equal to the lesser of (a) 40 percent of his high-3 average salary or (b) an annuity computed under the general retirement formula (see p. 41) after increasing his actual service by the number of years elapsing between the date of separation and the date on which he would reach age 60. An annuity computed under the general formula based on a disabled employee's actual service is allowed if it is greater than the guaranteed minimum annuity.

Retirees considered to be temporarily disabled must undergo periodic medical examinations until they reach age 60, recover from their disability, or are determined to be permanently disabled. Subsequent examinations are not required for retirees determined to be permanently disabled. Both temporary and permanent disability annuitants under age 60 are considered to be economically recovered if, in each of 2 successive years, their income from wages and/or self-employment equals at least 80 percent of the current rate of pay of the position occupied at the time of retirement. Annuities for disability retirees who are medically or economically recovered and not reemployed by the Government are generally terminated 1 year after recovery, and the annuitant may be eligible for benefits under the systems' discontinued service or deferred retirement provisions.

The changes leading from the original disability provisions of the system in 1920 to the current provisions occurred mostly on a piecemeal basis, and, in general, we could not find the specific rationale used to justify the changes. The major changes occurred as follows:

1926--The term "totally disabled for useful and efficient service" was redefined to apply only to service in the grade or class of the position occupied by an employee rather than to any Government service as provided by the original law.

1930--The minimum service requirement for a disability annuity was reduced from 15 to 5 years.

1939--The period of time during which an annuity could be paid to a recovered disability annuitant who had not been reemployed was established at one year.

1946--Provision added entitling recovered disability annuitants to benefits under the system's deferred retirement and involuntary separation provisions. At the time, the latter provisions provided for a reduced annuity beginning at age 55 or an unreduced annuity beginning at age 62. (Under the original law, a recovered disability annuitant who failed to secure reemployment under the system had no further rights to retirement benefits.)

1948--Requirement for annual medical examination of temporarily disabled annuitants was changed to terminate such examinations when the annuitant reached age 60.

1956--Minimum disability annuity and economic recoverability provisions were established.

Discontinued service and deferred retirement

Employees terminated before reaching normal retirement eligibility may, under the following conditions, be eligible for an immediate discontinued service or deferred annuity.

1. If they were involuntarily terminated through no fault of their own and are age 50 with 20 years of service, or any age with 25 years of service, benefits are payable immediately. Benefit amounts are calculated under the general formula but are reduced by one-sixth of 1 percent for each month the retiree is under age 55.

2. If they have completed 5 years of civilian service and elect to leave their retirement contributions in the fund, deferred benefits, calculated under the general formula, are payable at age 62.

The original retirement system provided no protection for employees with substantial service who were involuntarily separated through no fault of their own. Responding to the need for such protection, the system was amended in 1922 to offer certain employees a choice of either a reduced immediate annuity or a deferred full annuity when the employee reached mandatory retirement age, provided the employee had completed at least 15 years of service and had attained age 55 at the time of involuntary separation.

In 1926 the discontinued service benefits were extended to cover employees with 15 years or more of service who were involuntarily separated between ages 45 and 55. Such employees were given the right to a deferred annuity (beginning at the mandatory retirement age) or could elect to receive a reduced annuity beginning as early as age 55.

The principle of providing annuity protection for persons separated before attaining normal retirement eligibility was materially broadened by legislation passed in 1942. In effect, the legislation established the concept of vested rights for employees covered by the system. It authorized retirement benefits for employees separated at any age after serving 5 years or more, regardless of the reason for the separation. When separated involuntarily for reasons other than misconduct or delinquency, an employee could elect (1) a reduced annuity beginning at age 55 (or immediately if he had already reached 55) or (2) a deferred annuity at the full rate commencing at age 62. If an officer or employee resigned or was removed for cause, he acquired title only to a deferred age-62 annuity. In addition, the legislation prohibited employees with 5 or more years of service from receiving a refund of their contributions (based on service subsequent to enactment) upon separation.

It was reasoned that civil service retirement, like the social security program which had been established a few years earlier, was primarily an old-age benefit and, therefore, when employees separated, their contributions should be retained in the fund until they reached retirement age. Furthermore, it was believed that some retirement security should be provided those employees who, after 5 years of service, left Government for employment in the private sector where they were covered by social security. Some had suggested that credits should be transferred from the civil service system to social security. However, it was felt that the administration of such an arrangement would be expensive, cumbersome, and complicated; therefore, the Congress established a vested, deferred annuity for all employees completing 5 years of service under the civil service system.

The system's involuntary and deferred retirement provisions were amended in 1948. The right to an immediate age-55 annuity upon involuntary separation for employees with 5 or more years' service was eliminated. However, an immediate, reduced annuity was authorized for any employee involuntarily separated after completing 25 years of service, regardless of age. Also, the refund provision was amended to give the employee the option of receiving a refund of contributions if separated for any reason (voluntarily or involuntarily) before completing 20 years of service.

The involuntary separation provisions were liberalized in 1956. The provision entitling employees to an immediate reduced annuity upon involuntary separation with 25 years' service was retained. However, a new provision provided the same entitlement to employees involuntarily separated after attaining age 50 and completing 20 years of service. According to a Senate Committee report, the purpose of the latter provision was to alleviate the void which existed for employees involuntarily separated after completing 20 or more years but less than 25 years. At the time, employees separating with 20 or more years of service could not withdraw their contributions and were entitled only to a deferred annuity at age 62. Thus, an employee who was involuntarily separated at age 50 after 24 years of service would have to wait 12 years to receive an annuity. But, if the same employee had 25 years' service upon separation, his annuity would have begun immediately. The legislation also eliminated the provision which barred employees separating after 20 years of service from withdrawing their contributions.

In 1973 a special provision was enacted which pertained to employees of an agency undergoing a major reduction in personnel. 1/ Under this provision, employees of such an

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1/As amended by the Civil Service Reform Act of 1978, this provision also pertains to an agency undergoing a major reorganization or a major transfer of function.

agency who have 25 years of service or who have attained age 50 and served 20 years may voluntarily elect to retire on an immediate reduced annuity. However, use of this option is restricted. Before employees can retire under the provision, the Civil Service Commission must determine that the agency's reduction in force is a "major" reduction and designate the geographic area(s) or occupation(s) of the agency to which the early retirement option will apply. The Commission also must stipulate the period of time during which employees may elect to retire under the provision.

The special provision was intended to help mitigate employee hardships and management disruptions which often accompany a major reduction in personnel. It was pointed out that major reductions usually resulted in the termination or down-grading of those employees who had the least seniority or retention preference. Accordingly, many younger employees were separated while older employees, some of whom may have desired to retire but were not eligible to do so were retained.

Mandatory retirement

Public Law 95-256, enacted on April 6, 1978, removed the mandatory retirement age for most civil service employees, effective September 30, 1978. Special mandatory retirement provisions still exist for employees of the Alaska Railroad, U.S. citizen employees of the Panama Canal Company and the Canal Zone Government, air traffic controllers, and law enforcement and firefighting personnel. The President, however, is authorized to waive the automatic separation requirement for any individual when, in his judgment, it is in the public interest.

Prior to enactment of Public Law 95-256, most civil service employees were required to retire at age 70 or as soon thereafter as they completed 15 years of service. Members of Congress, congressional employees and certain employees in the judicial branch appointed to hold office for a definite term of years were previously excluded from the mandatory retirement provision. We were unable to determine why the distinction was made for these employees.

Employees of the Alaska Railroad and U.S. citizen employees of the Panama Canal Company and the Canal Zone Government are required to retire at age 62 or as soon thereafter as they complete 15 years' service. When the separate retirement systems for these employees were abolished and the employees brought under civil service retirement coverage (see p. 38), they were allowed to retain their earlier mandatory retirement ages. The reason for these exceptions was not apparent, particularly since 7 years earlier, the Congress had eliminated the mandatory retirement age of 65 for mechanics, letter carriers, and Post Office clerks and 62 for railway postal clerks under the civil service system and had established age 70 as the mandatory retirement age for these employees. Public Law 95-256 also removed the mandatory retirement age for these employees.

Air traffic controllers are required to retire at age 56, and law enforcement and firefighter personnel must retire at 55 or as soon thereafter as they complete 20 years of service. These and other unique retirement provisions applicable to employees under the system are discussed on pages 51 through 59.

Survivor benefits

In general, the system provides annuities to surviving spouses and children of employees with at least 18 months of covered service. The spouse receives 55 percent of the employee's earned annuity at the time of death, subject to a minimum amount equal to 55 percent of the lesser of (1) 40 percent of the high 3 years' salary average or (2) the annuity that would have been paid had the employee continued working until age 60 at the same high-3. Annuities to surviving spouses are paid for life unless they remarry before age 60. Each qualifying unmarried child to age 18 (22 if a full-time student) receives the lesser of

--60 percent of high-3 divided by the number of qualified children,

--$5,443 divided by the number of qualified children, or

--$1,814.

Higher annuities are paid for children of an employee not survived by a spouse. Such children receive the lesser of

--75 percent of high-3 divided by the number of qualified children,

--$6,532 divided by the number of qualified children, or

--$2,177.

If, at the time of retirement, an annuitant accepts a reduced annuity, a survivor annuity will be paid to his or her surviving spouse. The reduction will be equal to 2.5 percent of the amount, up to $3,600, that the retiree specified as the base for the survivor benefit plus 10 percent of any specified amount over $3,600. The survivor's annuity will be 55 percent of all or whatever portion of the retiree's annuity before reduction that the retiree specified as the base for the survivor benefit.

An unmarried annuitant who is in good health may also accept a reduced annuity and designate an individual with an insurable interest to receive a benefit of 55 percent of the reduced amount. The reduction is equal to 10 percent of the retiree's annuity plus an additional 5 percent for each full 5 years the beneficiary is younger than the retiree. The total reduction cannot exceed 40 percent.

Whether or not a survivor benefit is elected at retirement, children of deceased annuitants are entitled to a survivor annuity under the same conditions and in the same amounts as the children of a deceased employee. Survivor benefits are adjusted semiannually to reflect increases in the Consumer Price Index by the same percentage adjustment received by retirees.

Survivor benefits were added to the system in 1939, and the provisions have changed many times since then. The 1939 provisions allowed any employee retiring under the system's mandatory or optional provisions to elect a reduced annuity for himself and an annuity payable to a named survivor upon his death. The retiree could designate anyone as a survivor beneficiary; there was no requirement of relationship or dependency. The amount of a survivor's annuity varied depending on such factors as the age and sex of the retiree and designated survivor at time of retirement. In no case, however, could the value of the two combined be greater than the actuarial value of a retiring employee's full life annuity.

Major changes to the survivor program were made in 1948 in an apparent attempt to provide protection comparable to that of social security. These changes added survivor provisions for married employees with 5 years of service or more (50 percent of earned annuity for spouse and additional amounts for children), allowed certain unmarried retirees to provide a survivor annuity for a person having an insurable interest in him, and provided benefits to the children of certain deceased retirees. Benefits were generally payable only to the survivors of male employees and retirees, and normally surviving spouses' annuities could not begin before age 50 unless there were eligible surviving children under age 18. Retirees who were receiving discontinued service or deferred annuities were not eligible to participate in the survivor program. As a further restriction, unmarried disability retirees also could not participate.

In 1949 retiring female employees were given the right to provide a benefit for their surviving spouses. However, such benefits were payable only when such spouse was incapable of self support because of a disability and had been receiving more than half his support from his wife.

Other major amendments were made in 1956, again apparently aimed at establishing some comparability with survivor benefits provided by the social security program. These changes allowed all retirees, except unmarried disability retirees, to participate in the program and allowed widows and widowers to receive benefits at any age.

In 1962 survivor protection for the spouse of a retired married employee was made automatic unless the employee, in writing, elected otherwise. Both spouses' and insurable interest annuities were set at 55 percent of the retiree's annuity. Also at this time, a new provision was added which allowed a surviving child annuitant who was a full-time student to continue to receive an annuity until age 22. Additionally, the current annuity reduction formulas for retirees electing to participate in the program were instituted.

In 1966 the program was changed to continue the annuities of widows or widowers who remarried after reaching age 60. (Previously, benefits had ceased upon remarriage.) Additionally, any annuity terminated because of remarriage before age 60 could be restored if the remarriage was later terminated because of death, annulment, or divorce.

Minimum benefits for surviving spouses were established in 1969 along with a reduction from 5 years to 18 months in the period of service required for benefits under the program. According to a Senate committee report, the purpose of these changes was to provide more adequate survivor protection, particularly to younger employees with low earnings and short service. It was pointed out that, although the retirement system was primarily a long-term staff retirement plan, 3 million employees relied upon its protection for survivor benefits as well as for retirement purposes.

In 1971 widowers of deceased female employees were extended the same benefits accorded widows, thereby rescinding the dependency requirement that had been in effect since 1956.

The survivor program was amended in 1974 to eliminate the annuity reduction for married retirees if the marriage terminated before the retiree's death. Similar legislation was enacted in 1978 for unmarried retirees whose designated beneficiaries predeceased them.

Members of Congress
and congressional staff

Members of Congress, and to a lesser extent, congressional staff, receive different benefits under the civil service system than do other participants. Their annuities are calculated using more generous benefit formulas and, in many cases, other different provisions.

A special optional retirement provision for Members of Congress was introduced in 1946 by the same legislation which extended Members optional coverage under the system. The provision gave Members the option of retiring at age 62 after having completed a minimum of 6 years' service as a Member. The legislative history provided no explanation for this special provision, other than stating that granting Members of retirement age or with other infirmities the right to participate in the system was in recognition of the arduous labors imposed on all Members.

The 1946 law also established a separate retirement benefit formula for Members of Congress. Under the formula, a Member's annuity was computed by multiplying his years of service as a Member by 2.5 percent of his average annual basic salary as a Member. Benefits for any creditable non-Member service were computed under the less generous annuity provisions applicable to Federal employees in general.

Elective coverage under the system was extended to congressional employees in 1937. Until 1954 these employees were covered by the same benefit provisions as other employees, but, in that year, a separate annuity provision was adopted. Under the provision, retiring congressional employees could elect to have their annuities computed by a special formula or by the general formula applicable to all other employees. The special formula provided an annuity equal to (a) 2.5 percent of high-5 average salary for each year of service (not exceeding 15) as a legislative employee, including allowable military service, plus (b) 1.5 percent of such average salary multiplied by all other years of allowable service.

The purpose of this new provision was to recognize the uncertain tenure of congressional employees and their limited opportunity to establish an adequate retirement annuity based on years of service. The legislative history stated that, while special legislation had been approved from time to time to correct certain inequalities and problems in the retirement system relating to other groups of Federal employees, nothing had been done about the problem of the uncertain tenure of congressional employees.

Members of Congress were granted an additional special retirement option in 1954--the option to retire, on a reduced annuity, at age 60 with 10 years' service as a Member. At the time, other system participants were required to have served 30 years and to have attained an age between 55 and 60. In commenting on this and the other amendments, however, a committee report stated that the benefits provided were not "any more liberal than the comparable present retirement provisions for other Federal employees."

The optional retirement provisions of age 62 with 15 years of service for employees and age 62 with 6 years' service for Members of Congress were eliminated in 1956. In their place a new optional provision was substituted which permitted both employees and Members to retire at age 62 with 5 years of service. However, Members of Congress were given the additional option of retiring without a reduction in annuity at age 60 after completing 10 years. The corresponding provision of age 60 and 30 years' service relating to most other covered employees remained unchanged.

A significant survivor benefit available only to Members of Congress was added by legislation enacted in 1956. This legislation established survivor protection for the widow or widower of a former Member of Congress who separates with entitlement to a deferred annuity. Under this provision, the surviving spouse of a former Member who has title to a deferred annuity but who dies before such annuity commences is entitled to an immediate annuity equal to 50 percent of the Member's deferred annuity. Survivors of other former employees who die before payment of a deferred annuity begins are entitled only to a refund of employee contributions.

In 1960, legislation authorized payment of an immediate reduced annuity to any Member of Congress, age 50 or older, who was separated from service, other than by resignation or expulsion, after service in nine Congresses. The provisions for an annuity if a member or employee is involuntarily separated after 25 years' service, regardless of age, or after 20 years' service and attainment of age 50, were retained. The apparent purpose of the 1960 legislation was to protect Senators who, after having served three terms in the Senate--a total of 18 years--failed to be reelected.

The 1960 legislation also liberalized eligibility requirements for a deferred annuity for Members of Congress. Under a new provision, any Member who separated for any reason after 20 years' service, 10 of which were service as a Member, could receive a reduced deferred annuity beginning at age 50.

Also in 1960, the application of the special and general annuity formulas with respect to Members of Congress and congressional employees was revised and their current benefit computation method was established. Prior to this, the two formulas operated completely independently of one another. An individual's annuity based on Member and/or congressional employee service was computed under the special 2.5 percent formula. The general 3-step formula applicable to other personnel was used to compute the annuity for all other creditable service regardless of when it was performed. The revised provision, in effect, integrated the two formulas so that the annuity of a retiring Member or congressional employee is computed under a modified version of the general 3-step formula, based on total creditable service. The formula operates as follows:

1. 2.5 percent of high-5 1/ average salary multiplied by years of

    (a) service as a Member or congressional employee and

    (b) allowable military service, plus

1/Computation base changed from high-5 to high-3 in 1969 for all employees covered by the system. (See p. 42.)

2. 1.75 percent of high-5 average salary multiplied by years of other service which, when added to years of 2.5-percent service, do not exceed 10 years (if 2.5-percent service total 10 years or more, the 1.75-percent factor is not applied), plus

3. 2 percent of high-5 average salary multiplied by years of service not used in steps (1) and (2).

The effect of the change was to eliminate the 1.5-percent factor used in the general formula for each of an employee's first 5 years of service. The change was made because the previous independent application of the two annuity formulas was considered to be at variance with one of the generally accepted principles of a staff retirement plan, that a greater, not a lesser, benefit should be provided for additional years of service.

In apparent recognition of the more generous benefits available to Members of Congress and congressional staff, their required rates of contribution to the system are slightly higher--8 percent and 7.5 percent, respectively, as compared to 7 percent for most other covered employees.

Law enforcement officers and firefighters

About 52,000 employees of various Federal agencies and the District of Columbia Government whose primary duties are (1) investigating, apprehending, or detaining persons suspected or convicted of Federal crimes or (2) controlling and extinguishing fires or maintaining and using fire apparatus and equipment are, by law, eligible for earlier and more generous civil service retirement benefits. These employees may voluntarily retire at age 50 after 20 years of such service, and their annuities are computed at the rate of 2.5 percent of average pay (average high 3 years' annual pay including administratively uncontrollable overtime for law enforcement officers) for each of the first 20 years of service plus 2 percent of average pay for each year of covered service thereafter. Covered employees and employing agencies each contribute 7.5 percent of pay toward retirement. Since January 1, 1978, such employees have been required by law to retire at age 55, or after completing 20 years of covered service, whichever comes later. The head of an agency can, however, retain an employee to age 60.

The early retirement policy was enacted more than 30 years ago to improve the quality of Federal law enforcement service by helping to maintain a young, vigorous work force. The more generous annuity formula is designed to make earlier retirement economically feasible, not to reward these employees for performing demanding or hazardous services.

Many occupational groups of employees are eligible for the special retirement benefits. Examples of the types of Federal positions included follow.

Investigation and apprehension of criminals--Such employees as special agents in the Federal Bureau of Investigation, Internal Revenue Service, Secret Service, and Drug Enforcement Administration. Customs and immigration border patrol officers and airplane pilots, game wardens, postal inspectors, and Bureau of Indian Affairs and Panama Canal Zone police also receive the benefits.

Detention of criminals--All employees working inside the walls of a Federal or District of Columbia detention facility. Covered positions include not only correctional officers but also cooks, plumbers, carpenters, paint foremen, mailclerks, telephone operators, accountants, and secretaries. Also covered are research chemists, pharmacologists, physicists, photographers at drug addiction centers, and parole hearing examiners in the Department of Justice.

Fighting fires--Employees fighting both structural and forest fires. The eligibility criteria have also been interpreted to cover such positions as tanktruck operators, certain airplane pilots, and certain foresters.

Supervisory and administrative personnel--Employees who transferred from covered operating positions to positions responsible for supervising operating-level employees or to positions where operating experience is required to perform the various administrative duties. Included are program administrators in headquarters organizations, accountants, personnel officers, administrative officers, and training course developers and instructors.

Civil Service Commission regulations specifically exclude employees in positions whose primary duties involve (1) maintaining law and order, (2) protecting life and property, or (3) guarding against or inspecting for violations of law or investigating persons other than those suspected of violating criminal laws. Also excluded are employees whose duties only occasionally or incidentally require the investigation, apprehension, or detention of persons suspected or convicted of violating Federal criminal laws.

In a February 1977 report 1/ to the House Committee on Post Office and Civil Service, we evaluated the adequacy, reasonableness, effectiveness, and costs of the special, early retirement policy for Federal law enforcement and firefighter personnel. We concluded that the continued need for the special retirement policy is questionable and recommended that the Congress reevaluate the need for the special benefits.

The special benefits may have been needed in 1947 when they were enacted to make certain Federal jobs more attractive and to make it economically feasible for employees in those jobs to retire at a younger age. But the continued need for special retirement is now questionable for several reasons.

--Federal pay rates and regular civil service retirement benefits have been increased substantially, thus reducing the average retirement age for all civil servants.

--Covered employees are not retiring much earlier than employees who are not eligible for the additional benefits but the costs of covered employees' benefits are considerably greater.

--Many covered employees could continue to perform their jobs satisfactorily after age 50 and others could be reassigned to less demanding jobs.

--Civil service disability retirement or Federal workers' compensation benefits are available to employees who can no longer perform their duties.

Over the special retirement policy's 30-year history, including periods when there were substantial differences between the special and regular retirement benefit structures, covered employees have never retired much earlier

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1/"Special Retirement Policy for Federal Law Enforcement and Firefighter Personnel Needs Reevaluation" (FPCD-76-97, Feb. 24, 1977).

than employees under regular civil service optional retirement provisions. The following table compares the average age at retirement for covered employees with the average age of civil service employees retiring under the regular 55/30 option and all employees who retired with 30 or more years of service.

Fiscal year	Covered employees	Other civil service employees: 55/30 option	Other civil service employees: All with 30 years or more service
1947	No retirees	58.6	63.7
1949	59.9	58.1	63.3
1950	58.8	58.0	63.2
1955	59.3	57.9	63.1
1960	59.8	57.8	62.6
1965	58.4	57.7	62.5
1970	57.3	57.7	61.1
1971	57.8	57.8	61.0
1972	56.9	57.1	61.1
1973	56.8	57.2	60.2
1974	56.7	57.2	60.0
1975	56.2	57.0	59.6
1976	55.5	56.8	59.4

The special benefits are considerably more liberal and costly than those provided to other civil service employees. Law enforcement officers and firefighters, by law, receive 50 percent of average pay after 20 years' service and 70 percent of average pay after 30 years, while other civil service employees receive 36.25 percent and 56.25 percent, respectively.

To achieve the current 1- to 3-year reduction in the average retirement age of covered employees, the Government pays heavily. Based on Commission actuarial estimates, the Government's annual normal cost was $311 million in 1976--$118 million (61 percent) more than the cost of providing regular optional benefits to these employees (conservatively assuming a 3-percent annual salary adjustment and a 4-percent annual annuity adjustment). A comparison of the normal cost of the special benefits and the normal cost of all civil service retirement benefits, expressed as a percentage of payroll, follows.

Normal cost	Special benefits	All civil service retirements
Static (assumes no inflation, no general pay increases)	19.7	13.6
Dynamic (assumes 3-percent pay and 4-percent cost of living increases)	43.6	28.7

The special retirement policy is an expensive method of marginally reducing retirement ages. Mandatory retirement will, of course, further reduce the average retirement age. However, we question whether a further reduction in retirement age would be cost effective. Mandatory retirement at age 55 will still permit most covered employees to work a full 25- to 30-year career and to receive greater benefits than regular civil service employees with similar earnings and years of service. Also, many of the covered employees who will be mandatorily retired will be supervisors and administrators who generally do not need to be any more vigorous than any other Federal supervisor or administrator.

Maintaining a trained, alert, and vigorous work force is difficult, but this problem exists to varying degrees in most Federal occupations. Problems such as this are normal and should be resolved by using available personnel management techniques, other retirement provisions, and, if needed for recruitment and retention purposes, special rates of pay. Employees who cannot perform satisfactorily before the regular retirement age should be reassigned to less demanding duties or, as a last resort, retired under existing retirement or Federal workers' compensation disability programs.

Air traffic controllers

Legislation enacted in 1972 granted special retirement benefits to Federal air traffic controllers. Since 1972 controllers have been allowed to retire on an immediate, unreduced annuity at age 50 with 20 years of service or at any age with 25 years' service. Their benefits are calculated under the general formula applicable to other covered employees; however, benefit amounts are subject to a minimum of 50 percent of high-3. Controllers generally must retire at age 56, but the Secretary of Transportation has the authority to retain a controller with exceptional skills and experience for an additional period of up to 5 years.

The rationale for earlier retirement eligibility provisions for controllers is the same as that for law enforcement and firefighter personnel--to help maintain a young, vigorous work force. Similarly, the minimum annuity of 50 percent of high-3 is intended as an economic incentive for controllers to retire early. But, in contrast to the law enforcement and firefighter provisions, controllers who choose to work longer do not receive greater retirement benefits than do other employees who work full careers. To illustrate, after 20 years, the general benefit formula provides 36.25 percent of high-3 and after 25 years, 46.25 percent, whereas controllers retiring at either point would receive 50 percent. A benefit of 50 percent of high-3 is available after about 27 years of service under the general formula. Thus, controllers with 27 years or more will receive no greater benefits upon retirement than other retirees covered by the general benefit formula.

Based on retirement statistics reported by the Civil Service Commission, most controllers do not retire early and take advantage of the more liberal benefit formula. In 1976 retiring controllers, on the average, were 55.2 years old and had completed 32.5 years of service and, therefore, were eligible to retire under the system's regular provisions.

According to legislative history, the mandatory retirement age of 56 was established on the rationale that most controllers did not have the physical and emotional strength required to perform their jobs and insure air safety for the traveling public past age 55.

Reemployment of annuitants

In general, civil service retirees (other than retired Members of Congress) who are reemployed by the Government continue to receive their annuities, but their salaries are reduced by the amount of the annuity. Reemployed annuitants do not contribute to the retirement fund, and reemployment for less than a year does not earn additional retirement benefits. However, annuitants reemployed on a full-time basis for a year or more in positions subject to the retirement system are entitled to a supplemental annuity upon subsequent separation if they make retroactive contributions. A supplemental annuity is computed under the general formula based on the salary received during the reemployment period. Reemployed annuitants who serve for 5 years or more may, upon separation, pay their retirement contributions retroactively and have their annuities recomputed based on their total covered service.

The original civil service retirement law was silent with regard to the reemployment of annuitants, and the current provisions are the result of numerous changes to reemployment policies that have occurred over the years.

The first reemployment provision under the system, enacted in 1926, barred individuals retired for age (mandatory retirement) from reemployment in a position subject to the retirement system. It also provided for termination of annuities upon reemployment of discontinued-service annuitants (involuntary retirement) who returned to Government work.

When the optional retirement provision was introduced in 1930, it also barred reemployment of annuitants who had voluntarily retired.

Reemployment restrictions were modified in 1942 when a provision was added which allowed reemployment of individuals who had retired voluntarily or mandatorily if the appointing official determined such individuals possessed special qualifications. The reemployed individual's annuity was terminated and recalculated under the retirement law in effect at the time of his subsequent separation from service. The purpose of this amendment was to enable the Government to retain or recall persons with outstanding abilities and long experience in a particular field. The amendment was also intended to enable the Government to utilize the services of knowledgeable and experienced retired employees in time of emergencies.

In 1948 reemployment rights were completely revised and a new provision was established under which such rights depended upon an annuitant's age at date of reemployment.

An annuitant who was age 60 or over could be reemployed only if it was determined he possessed special qualifications. Upon such reemployment, (a) the individual continued to receive his annuity, (b) his salary was reduced by the amount of annuity, (c) no retirement deductions were withheld from his salary, and (d) his annuity was not increased by reason of reemployment service. The primary reason for this amendment was to prevent older annuitants from seeking reemployment solely for the purpose of acquiring new or additional benefit rights.

Annuitants under age 60 were not required to possess special qualifications as a reemployment prerequisite. If such annuitants were reemployed in a Government position not subject to the retirement system, their annuities were suspended during the period of reemployment and reinstated at the same rate upon separation. If the annuitants were reemployed in positions covered by the system, their annuities were terminated and their retirement rights were determined under the law in effect at the time of their subsequent separation from service.

Most of the current reemployment provisions were enacted in 1956. The 1956 amendment also removed age as a factor in determining reemployment rights and established a separate provision to govern the reemployment of retired Members of Congress.

When retired Members are reemployed in either elective or appointive positions, their annuities are suspended, and they again become covered by the system as if they had not retired. Reemployed Member retirees make contributions in the amount required for the position they hold, and, upon separation, their annuities are reinstated and recomputed with credit for the additional service. If a former Member elects, retirement benefits for the additional service may be computed as if the service had been performed before his separation as a Member.

We could find no explanation of why the system's reemployment provisions for retired Members of Congress are so different from the provisions applicable to other personnel. Moreover, a third type of reemployment practice exists under the system whereby retirees (other than Members of Congress) who become Federal judges are allowed to receive both full salary and full annuity.

FOREIGN SERVICE RETIREMENT SYSTEM

The Foreign Service retirement system, which is administered by the Department of State, covers approximately 9,400 employees, including most Foreign Service personnel and employees of the United States Information Agency 1/ and the Agency for International Development. In 1976 the system paid about $67 million in benefits to 4,600 employee annuitants and survivor beneficiaries. In comparison to the civil service retirement system, the Foreign Service system provides higher benefits at an earlier age for less service.

1/See footnote on p. 16.

Development of the system

The system was established in 1924 by the same legislation which merged the diplomatic and consular services to form the Foreign Service. Several legislative proposals had previously been made to extend coverage under the civil service system (established in 1920) to employees of the diplomatic and consular services, but these attempts were not successful. The proposals were not only to extend civil service coverage, but also to modify several of the system's provisions for Foreign Service personnel, including removal of the $720 maximum benefit limitation existing at the time.

Employees already covered by the civil service system objected to the provision which would have made the larger annuities for Foreign Service personnel payable out of the civil service retirement fund. They contended it would be an unwarranted use of their money, even though Foreign Service personnel would have had to contribute more than other employees. The question of the actuarial soundness of the proposals was submitted to a Government Board of Actuaries which concurred in the objections and recommended the establishment of a separate retirement fund to be administered by the Department of State.

The employees of the diplomatic and consular services were not covered by the civil service retirement system when it was established because participation was limited to employees in the competitive civil service. Interestingly, this limitation was removed in 1942 and, had these employees not been covered at that time by the Foreign Service system, civil service system coverage would have been extended to them.

Except for different limitations on the maximum benefit amounts, the original Foreign Service benefit provisions were essentially the same as those in the civil service system. In fact, under present Foreign Service retirement law there is a requirement for maintaining conformity between substantially identical provisions of the two systems. Whenever a civil service retirement provision is amended, the corresponding Foreign Service provision is also amended by Executive order. The significant differences between the two systems are discussed below.

Benefit formula

Originally, Foreign Service retirement and disability benefits were based on the following schedule, with the related percentages being applied to an individual's average annual salary for his last 10 years of service.

Years of service	Percent of average salary
30 and over	60
27 to 30	54
24 to 27	48
21 to 24	42
18 to 21	36
15 to 18	30

This schedule of benefits was identical to that which existed under the original civil service system, with one exception. Under the civil service system, benefit minimums and maximums were assigned to each range of years of service and in no case could annual benefits exceed $720. This limitation meant that average salary in excess of $1,200 was not considered in computing benefits. In contrast, the only limitation in computing Foreign Service retirement benefits was that the average salary amount used could not exceed $9,000, meaning that annual benefits could be as much as $5,400 (0.60 x $9,000).

The application of the civil service schedule, with its limitations, resulted in significant inequities. This is apparent from the following example. Consider the case of two employees retiring after 30 years of service, one with an average salary of $1,200 and the other with an average salary of $9,000. Under the original system, each employee would have received a pension of $720. In the case of the lower salaried employee, this amount would have equaled 60 percent of average salary, but only 8 percent for the higher salaried employee. Under the Foreign Service system, both employees would have received a pension equal to 60 percent of their average salaries. The inequities of the civil service benefit schedule with respect to higher salaried employees were recognized and corrected over time, first by increasing the average salary ceiling and later by eliminating it altogether (See pp. 41 to 43.)

In 1939 the Foreign Service benefit schedule was eliminated and replaced by a benefit formula which provided 2 percent of average salary for each year of service, up to a maximum of 30 years. Since that time, there have been few modifications to the system's benefit formula. The maximum years of service which can be used in computing an annuity have been increased to 35 and the average salary is now based on the highest average salary earned for any 3 consecutive years.

A comparison between Foreign Service and civil service retirement benefits for equal periods of service reveals that Foreign Service retirees receive slightly greater benefits. The civil service system provides an annuity equal to 56.25 percent of high-3 average salary after 30 years of service and 66.25 percent after 35 years, in contrast to the Foreign Service system which provides 60 and 70 percent, respectively, of high-3 average salary. Furthermore, under the Foreign Service system, an individual can voluntarily retire at age 50 with 20 years' service on an immediate annuity of 40 percent, whereas, under the civil service system, an individual with only 20 years' service must be at least age 60 to retire voluntarily.

Voluntary retirement

Voluntary retirement after 30 years of service, regardless of age, was introduced into the system in 1931, about 9 months after a voluntary retirement provision was established under the civil service system. The provision was revised in 1939 to require, in addition to completing 30 years' service, attainment of age 60. Retirement after 30 years and before reaching age 60 was still permitted, but the annuity was reduced for each month the individual was under age 60. The age requirement was lowered to 50 in 1941 and, with the establishment of a "selection-out" system in 1946, the service requirement was lowered to 20 years.

The selection-out system was established by the Foreign Service Act of 1946 and is applicable to all nonprobationary Foreign Service officers in classes 1 through 7. The system requires involuntary retirement of any officer who fails to be promoted within a prescribed period of time or who fails to meet the established standard of performance for his class. The act authorized the Secretary of State to prescribe regulations governing the maximum period of time during which any officer (below the class of career minister) may remain in class without promotion. According to a House committee report on the act, the purpose of selection-out is, "to provide for rapid advancement of men of ability by the separation of officers relatively less qualified for advancement."

The act also authorized voluntary retirement for any officer age 50 or over who had completed 20 years of service. According to the House committee report, this provision was "necessitated by the selection-out system." It was stated that voluntary retirement after 20 years of service would lighten the pressure of the selection-out system.

Retirement benefits upon selection-out depend on an officer's class at the time of separation. Foreign Service officers below the level of career minister are ranked in classes ranging from 1 through 8, with class 8 generally being the probationary entry level class. Officers in classes 1, 2, or 3 who are involuntarily retired receive an immediate annuity, regardless of age. The annuity is computed by multiplying 2 percent of the individual's high-3 average salary by his years of service. Officers selected-out of classes 4, 5, 6, or 7 are entitled to the following benefits:

(1) A severance payment equal to one month's salary (based on the officer's final salary rate) for each year of service, but not exceeding a total of 1 year's salary, payable from the retirement fund and

(2) Refund of contributions made to the retirement fund, plus interest.

If an officer has at least 5 years of creditable service, excluding military service, he may elect to receive a deferred annuity beginning at age 60, in lieu of a refund of his contributions.

Any officer in classes 4, 5, 6, or 7 who is eligible for voluntary retirement may be granted such retirement in lieu of involuntary retirement. In addition, any officer in class 4 or 5 who is not eligible for voluntary retirement upon the expiration of the maximum time-in-class period will not be separated until he is eligible for voluntary retirement.

The following table shows that a limited number of Foreign Service officers have been selected-out in recent years under the maximum time-in-class and standard of performance provisions.

Number of Foreign Service
Officers Involuntarily Retired
During Fiscal Years 1974 Through 1977

Fiscal year	Reason	Class 1	2	3	4	5	6	7	Total
1974	Maximum time in class	5	1	1	1	0	0	1	9
	Substandard performance	4	15	0	0	0	0	1	20
	Total	9	16	1	1	0	0	2	29
1975	Maximum time in class	0	0	2	0	1	0	1	4
	Substandard performance	0	1	0	0	0	1	0	2
	Total	0	1	2	0	1	1	1	6
1976	Maximum time in class	0	0	0	0	0	0	0	0
	Substandard performance	0	5	2	0	0	1	0	8
	Total	0	5	2	0	0	1	0	8
1977	Maximum time in class	0	1	7	1	0	2	0	11
	Substandard performance	0	0	0	0	0	0	0	0
	Total	0	1	7	1	0	2	0	11

While these statistics do not reflect the number of officers that may have retired voluntarily in order to avoid being selected out, they do indicate that very few officers are involuntarily retired. In fact, data for the period of 1969-73 showed the average age and length of service of individuals retiring voluntarily to be 56 years old and 28 years of service. In view of this and the fact that over 40 percent of the personnel covered by the retirement system are not subject to selection-out, 1/ it is questionable whether the selection-out system justifies the 50/20 early retirement provision for all covered personnel. It would seem that the need to provide early retirement benefits for those selected out could easily be accommodated by such involuntary retirement provisions (age 50 with 20 years service or any age with 25 years service) as under the civil service system. (See pp. 45 to 47.)

Mandatory retirement

Generally, all Foreign Service personnel have been mandatorily retired upon reaching age 60, except that career ministers, career ambassadors, and career ministers for information were not required to retire until age 65. Effective October 1, 1976, the mandatory retirement age for career ministers and career ministers for information (except those appointed by the President and confirmed by the Senate) was to be gradually reduced to age 60 over a 30-month period. However, a U.S. district court decision on June 28, 1977, declared the age 60 mandatory retirement provision to be unconstitutional and void. The court said it found no rational basis for subjecting Foreign Service personnel to a lower mandatory retirement age than the age 70 requirement applicable to most civil service employees. In fact, it held that age 60 mandatory retirement for Foreign Service personnel was patently arbitrary and irrational since they did not appear to serve under any more difficult conditions or for significantly longer periods of time than many civil service employees. However, Public Law 95-256, which removed mandatory retirement at age 70 for most civil service employees (see pp. 47 to 48), does not apply to the Foreign Service.

FEDERAL RESERVE BOARD RETIREMENT SYSTEM

The Federal Reserve System made up of 12 regional banks coordinated by a Board of Governors was established in 1913.

1/Employees of the Agency for International Development and Foreign Service staff officers (4,191 of the 9,449 covered personnel) are not subject to the selection-out system.

It is the mechanism through which the Nation's supply of bank credit and money is controlled.

The Federal Reserve retirement system consists of two plans--one for employees of the Board of Governors and one for bank employees. Board employees are considered to be Federal personnel in all respects, but bank employees have both Federal and private characteristics. Our discussion in this section of the report is limited to the plan for Board of Governors' employees. (The bank employees' plan is discussed beginning on p. 116.)

About 1,300 employees are covered by the Board plan which is virtually identical to the civil service retirement system. Board employees do not participate in the civil service system solely because of timing. When the civil service system was established in 1920, its coverage was limited to employees in the "classified" (competitive) civil service, which excluded employees of the Federal Reserve. Subsequently, in 1934 the Federal Reserve established a separate retirement plan which covered employees of both the Board and the banks.

In 1942 the Civil Service Retirement Act was amended to cover all employees in or under the executive, legislative, and judicial branches of Government, except those who were covered under another retirement system. Because the Federal Reserve system had been established 8 years earlier, employees of the Federal Reserve were again excluded from civil service coverage. Civil service regulations provided, however, that employees who transferred from a position covered under the civil service system to a position covered under another Government retirement system with less than a 3-day break in service would retain civil service coverage. This resulted in some Federal Reserve Board employees being covered under their own retirement system while others were covered under civil service. Then, on January 1, 1944, the Board of Governors adopted special benefit and contribution provisions for its employees which were substantially the same as those provided under civil service. As stated in the Federal Reserve plan, these provisions were adopted,

> "In order that employees of the Board of Governors may be accorded financial benefits comparable to those granted to employees who are subject to the Civil Service Retirement Act * * *."

Whenever the benefit and contribution provisions of the civil service system are changed, conforming amendments are made to the Federal Reserve Board plan.

TENNESSEE VALLEY AUTHORITY RETIREMENT SYSTEM

Employees of TVA are covered by the TVA retirement system and/or social security, except for about 250 employees covered by the civil service retirement system.

Development of the TVA retirement system

Shortly after TVA was created in 1933, it initiated a study into a possible retirement plan for its employees. TVA was in the excepted (noncompetitive) civil service, and therefore its employees were not eligible to participate in the civil service retirement system. During the study, however, TVA explored the possibility of seeking civil service coverage. After studying the civil service system, TVA chose not to pursue this course of action because it believed the system was not very well suited for its needs. TVA viewed itself as a Federal agency which was more comparable to a private corporation than to a regular executive department because its employees were drawn largely from private enterprise and, in many instances, returned to the private sector. TVA believed that, because of this, social security coverage would eventually be extended to it, and therefore a separate retirement system that could readily be synchronized with social security was needed. Also, TVA wanted some features in its system that were not available in the civil service system at that time. They were:

--A special service benefit provision which permitted an employee leaving TVA through no fault of his own after 10 years of service (now 5 years) to receive the benefits purchased by both his own and TVA's contributions.

--A lump sum death benefit equal to one-half of a year's salary (subsequently increased to as much as 2 years' salary).

--Options to be elected at the time of retirement with regard to the exact terms of the benefits due, such as differing survivor annuity options. (Survivor benefits were first introduced in the civil service system in 1940.)

TVA's retirement system was adopted by the Board of Directors effective November 1, 1939. The retirement system covers all individuals employed at an annual rate of pay except (a) members of the Board of Directors of TVA, (b) members of the civil service retirement system, (c) any person employed for a predetermined period of 6 months or less, (d) any person employed part time, and (e) persons whose services are engaged on a contract basis. Most construction workers are excluded by the above definition because they are hourly paid employees. Employees transferring to TVA from positions covered by the civil service retirement system without a break in service of more than 3 days are required to remain in the civil service system. At the time of our review, about 250 TVA employees were in the civil service system.

If TVA had not established its own retirement system by 1942, its employees would have been brought under civil service retirement coverage. Public Law 77-411 extended civil service retirement coverage in 1942 to employees who had previously been denied such coverage because they were not in the classified (competitive) civil service. However, agencies such as TVA, which in the meantime had established their own retirement systems, were excluded.

Social security coverage

A 1946 TVA study concluded that social security coverage was desirable for all TVA employees, mainly because of intermittent employment. Most of TVA's hourly trades and labor employees worked interchangeably for TVA and private contractors, accumulating social security benefit rights when working for private employers, but not when working for TVA. Employment of annual employees was also unstable during TVA's early years.

Based on the study, TVA began seeking social security coverage for all its personnel, and, effective January 1, 1951, such coverage was extended to its hourly trades and labor employees. In 1956 social security coverage was extended to annual employees, along with integration of the TVA system with social security under a plan approved by the Secretary of Health, Education, and Welfare.

Retirement system benefits

The TVA retirement system is a contributory plan and provides benefits for normal retirement (age 65), early retirement, involuntary retirement, disability retirement, and survivor benefits upon the death of a member before or after retirement. The standard employee contribution rate is 6 percent of basic pay in addition to social security contributions, but may be adjusted depending on when the employee entered the system. TVA employees may reduce their contributions to the retirement system by 3 percent on that part of their salaries not in excess of the social security base and may also direct their contributions to a fixed benefit fund, a variable annuity fund, or both.

The normal retirement benefit is composed of two amounts--an annuity, the employee-financed portion of the benefit; and a pension, the employer-financed portion. The annuity is based on the employee's total contributions and age at retirement. The pension is an amount equal to 1.3 percent of the employee's high-3 average annual salary multiplied by years of service and reduced by a social security offset. The offset equals 2 percent of the employee's annual social security benefit at age 65 not in excess of $1,050, multiplied by the years of creditable service (not in excess of 30, exclusive of any unused sick leave credit) rendered after December 31, 1955. There is no maximum benefit amount.

An early retirement benefit is payable to any employee who has completed 10 years of creditable service, or to an employee who has attained age 60. If the employee is at least age 60, the early retirement benefit is computed under the same method used for a normal retirement benefit. If the employee retires between the ages of 55 and 60, he can accept either a deferred benefit or a reduced immediate benefit. If the employee leaves TVA before age 55 with at least 10 years' creditable service, he is entitled to a deferred benefit, which is payable at any age between 55 and 65.

Any employee whose service is discontinued through no act of delinquency of his own and who has 5 or more years of creditable service is eligible for an involuntary retirement benefit. The benefit is computed under the same method as an early retirement benefit, except the employee can get an actuarially reduced immediate benefit at any age.

Any employee, with at least 5 years of creditable service, who becomes disabled, is entitled to an immediate benefit under the disability provisions, unless he is eligible for a higher benefit under the early retirement provisions. The disability retirement benefit is composed of an annuity and a pension. The annuity is the actuarial equivalent of the employee's accumulated contributions. The pension is equal to 1.1 percent of the member's high-3 average annual salary multiplied by years of service. However, under an alternative formula, a 30-percent minimum is provided, except for older employees with short service. If the employee becomes entitled to social security, the TVA pension is subject to reduction.

Upon the death of an employee in service, a benefit is payable to the estate or to a surviving beneficiary. This benefit may be in the form of (1) a lump sum payment consisting of the employee's contributions, with interest, and a percent of final salary which is based on length of service, including credit for unused sick leave, or (2) if one person is designated as the primary beneficiary, a life annuity which is the actuarial equivalent of the lump sum credit. Several options are available to the employee upon retirement to provide a survivor benefit to a designated beneficiary. Each option is designed to provide a retiree <u>and</u> the survivor the actuarial equivalent of the total benefit that would have been paid to the retiree alone if survivor benefits had not been elected.

A TVA employee who retires before age 62 on an early retirement benefit may elect to have his pension increased until he attains age 62 by an amount equal to the actuarial equivalent of the primary social security benefit payable to him at age 62. At age 62 his TVA pension will be reduced by the full amount of such previously estimated social security benefit. TVA refers to this as the level-income plan.

The TVA financed portion of retirement and survivor benefits has been adjusted each year since 1968 for cost of living increases. An increase is made in January following each year that the CPI average exceeds by at least 1 percent the average for the last year on which an increase was based. The benefit adjustment is the percentage increase in the CPI, with a maximum of 5 percent in any 1 year. There is no provision for cost of living adjustments of employee-financed benefits.

Comparison of TVA and civil service system benefits

Retirement benefits provided under the TVA retirement system, together with social security, are better than civil service benefits in some cases, but not as good in others. One feature of the civil service retirement system which is better than the TVA retirement system is the cost of living benefit adjustments. Only the pension portion of TVA's retirement program is CPI adjusted and then only up to a maximum of 5 percent a year, whereas there is no maximum on the civil service annuity adjustments. However, most of TVA's annuitants also receive social security benefits which are CPI adjusted, and tax free.

On page 75 are comparisons of benefits payable to TVA employees and employees covered by the civil service system under different hypothetical situations. The assumptions made in the calculations include (1) retirement on December 31, 1976, (2) annual salary at retirement of $15,000, (3) pay increases during employment of 4 percent annually, and (4) social security coverage for TVA employees since 1956.

In July 1975 TVA contracted with a consulting firm to study the advantages and disadvantages of withdrawing from social security and replacing the TVA retirement system with the civil service retirement system. The overall recommendation in the firm's November 1975 report was:

> "Based upon our analysis, we believe that an attractive and satisfactory benefit program could be established if the TVA withdrew from the current Social Security program and transferred the TVA Retirement System into the Federal Civil Service Retirement System. In order to maintain an attractive and balanced program, we believe that a modest supplemental disability and dependent children's program would be required. This could be done with a self-administered plan funded through a * * * trust fund at relatively minor cost.
>
> "At the present time the transfer to the FCSRS [Federal Civil Service Retirement System] could be done at a considerable cost savings to the TVA and its employees, and this is the underlying reason for the recommended change. However, this cost savings may be temporary, and it is possible that the change could eventually cost the TVA more than it is now paying to its current program. It is impossible to know at this time * * *."

The report stated the underlying reason for the recommendation was

> "* * * that it would result in an attractive and satisfactory benefit program at a considerable cost savings to the TVA and to most of its employees. Candidly, this is because the required employee and employer contribution for the FCSRS is far less than the amount needed to pay for the plan, and the System is being subsidized by the nation through general revenues. If TVA

switched over, it would be eliminating its own program, which it is paying for in full, and it would be substituting a program that is currently subsidized by the general taxpayers throughout the nation. The danger that exists is that it is questionable how long the entire nation will continue to subsidize the FCSRS."

TVA chose not to act on the consultant's recommendation because of the uncertainties surrounding the future allocation of the cost of the civil service retirement system. (See pp. 154 and 155 for a discussion of civil service costs and the fact that they are not being fully charged to participating agencies.)

Interrelationship with other Federal retirement programs

The TVA retirement system does not recognize service performed under any other Federal retirement system, except military service performed between contiguous periods of TVA employment. To establish military service credit, an individual must make contributions to cover such service, computed on the basis of the employee's salary immediately preceding the date of entry into the military service. The civil service retirement system is the only Federal system that recognizes TVA service as creditable.

Employees transferring from a position covered by the TVA retirement system to a position covered by the civil service retirement system can withdraw from the TVA system and have their TVA service credited under the civil service system by making the required contribution. The required contribution is the minimum amount required for TVA coverage, which currently is 3 percent of salary up to the social security base, and 6 percent thereafter.

On December 31, 1975, TVA had on its payroll 310 retired Federal workers. The number of retirees and the system from which they retired are shown in the following table.

Retirement system	Number of retirees
TVA	26
Uniform services	283
Civil service	1
Total	310

Selected Retirements

Hypothetical situation	Monthly retirement benefit (note a)		Employee cost of retirement benefit (note a)		Amount of social security benefit		Employee cost of social security
	(Male)	(Female)	(Male)	(Female)	(age 62)	(age 65)	
1. Age 65, 30 years' TVA service, minimum employee contributions to TVA fixed fund	$609	$605	$11,059	$11,884	-	$421	$7,023
2. Age 65, 30 years' TVA service, standard employee contributions to TVA fixed fund	658	648	15,094	15,919	-	421	7,023
3. Age 55, 30 years' TVA service, minimum employee contributions to TVA fixed fund, level-income plan	b/614	b/622	10,207	10,926	$258	-	7,023
4. Age 55, 30 years' TVA service, standard employee contributions to TVA fixed fund, level-income plan	b/651	b/657	14,243	14,961	258	-	7,023
5. Age 55 and over, 30 years' service, retiring under the civil service retirement system	676	676	17,623	17,623	-	-	-

a/Before 1964 TVA retirement contribution rates were based on sex and age at entry into the system. Since 1964 they have been the same for men and women.

b/At age 62 when social security payments begin, the TVA retirement benefit will be reduced by $258.

TVA retirees can, under TVA policy, be rehired with no reduction in salary or retirement benefits, provided they are not rehired at an annual rate of pay for a predetermined period of more than 6 months. TVA's stated policy is to obtain services in this way only if it is not practical to use TVA employees. Retirees rehired at an annual rate for a predetermined period of more than 6 months are considered restored to service. Such individuals' benefits stop, and they once again become members of the TVA retirement system.

The civil service retirement law (5 U.S.C. 8344(a)) provides that annuitants who are reemployed by TVA are subject to a reduction in salary equal to the amount of their annuity allocable to the period of reemployment. The Dual Compensation Act of 1964, discussed on page 32, applies to uniformed services retirees employed by TVA. Retired enlisted personnel and reserve officers receive full pay and full retirement benefits, whereas retired regular officers receive only part of their retirement benefits along with their full pay.

Information was not readily available on the number of TVA retirees employed by other Federal agencies. However, if a TVA retiree is hired by another Federal agency, neither his salary nor his retirement benefits are subject to a reduction.

FEDERAL JUDICIARY RETIREMENT SYSTEM

The Federal judiciary was created by the Judiciary Act of September 24, 1789, in accordance with Article III, Section I, of the Constitution, and includes justices of the Supreme Court and judges of the circuit, district, and special courts of the United States. Justices and judges are appointed by the President, with the advice and consent of the Senate. As provided by the Constitution, they hold office during good behavior and receive compensation which shall not be diminished during their continuance in office.

Judges who preside over district courts in United States territories and possessions (other than in Puerto Rico) are not considered to be "article III" judges and are appointed to 8-year terms rather than for life. These territorial judges perform the same functions and have the same responsibilities as do U.S. district court judges. When Alaska and Hawaii became States, for example, territorial judgeships were phased out and U.S. district court judges were appointed. Full life tenure was also extended to judges of the district of Puerto Rico in 1966.

Separate retirement programs exist under the Federal judiciary retirement system for article III judges and for territorial judges. Benefits under both programs are generally superior to those being received by personnel under other Federal retirement programs. In addition, survivor benefits under the system differ in many respects from survivor programs provided to other Federal personnel.

Article III judges

The first retirement program for the Federal judiciary was enacted in 1869. That legislation provided that a judge had to resign from the bench after completing 10 years of judicial service and reaching age 70. The judge would then receive the same salary for life that he was receiving at the time of his resignation. Judges were not required to contribute toward the cost of the program.

Many changes have been made to the judges retirement system over the years since 1869.

1877--Mandatory resignation was removed and judges were allowed an option to resign after reaching age 70 and completing 10 years of service.

1909--Judges who resigned after reaching age 70 and completing 10 years of service received, for life, the annual salary they had received 10 years prior to resignation.

1911--Provision was restored which allowed a resigning judge to continue to receive the salary he was receiving at time of resignation.

1919--New provision was added allowing a judge to retire from active service after reaching age 70 and completing 10 years of judicial service. Retiring judges were subject to recall to perform such duties as they were able and willing to undertake. Both resigning and retiring judges continued to receive the salary received at the time of resignation or retirement. (The retirement provision did not apply to justices of the Supreme Court until 1937.)

1939--Disability retirement was added. A permanently disabled judge was allowed to retire after 10 years of service at any age and to continue receiving his salary. A judge with less than 10 years of service received one-half his salary.

1948--Judicial Code was amended to provide that resignation resulted in loss of office, while retirement did not. Retired judges were allowed to receive the current salary of the office and receive the same salary increases granted to active judges. Revisions to disability benefits based payments on the current salary of the office.

1954--Voluntary retirement provision was changed to allow a judge to retire after attaining age 65 and completing 15 years of judicial service. A judge retiring under this provision received the current salary of the office. Upon reaching age 70, however, he could resign from office and continue to receive the salary he was receiving at time of resignation.

At the time of our review, there were 181 retired and resigned judges on the system's rolls. Of these, 175 had retired and 6 had resigned. Information provided by the Administrative Office of the U.S. Courts showed that, on the average, most retired judges were appointed when they were about 53 or 54 years of age, served about 16 to 18 years, and retired at about age 69 to 71. Retired judges are designated "senior judges," and, according to a report by the Chief Justice of the United States, 91 percent of the senior judges were performing substantial judicial duties.

The 1948 provision allowing retired senior judges to retain their office and to perform such judicial duties as they are willing and able to undertake was cited in the legislative history as justification for their receiving the full current salary of the office. Such rationale appears reasonable to us since, in effect, the judges have not retired from office but have agreed to accept a reduced workload. Furthermore, as mentioned above, the Constitution prohibits the diminution of a judge's salary while he is in office. The apparent rationale for resigned judges (relatively few in number) continuing to receive the salary of the office at time of resignation--a retirement benefit far superior to that received by other Federal personnel--is to encourage aging judges in declining health who can no longer effectively perform judicial duties to leave office. On the other hand, we found no explanation of why judges' disability benefits are computed under a more generous formula from that used in other retirement systems.

Territorial judges

The retirement program for territorial judges is similar to that for article III judges in that a judge resigning from office after reaching age 70 and completing 10 years of service receives, for the rest of his life, the same salary being received at time of resignation. However, other provisions differ significantly.

--Territorial judges are not subject to recall; thus a territorial judge cannot "retire" and receive the current salary of the office. He may, however, resign at age 65 after 15 years of service. (Article III judges may retire to senior judge status at this point, but they cannot resign and receive benefits until age 70.)

--If a territorial judge is removed from office because of disability, or fails to be reappointed, he is entitled, upon reaching age 65, to an annual annuity equal to one of the following:

a) If he completed 16 years (two terms) or more of judicial service, he will receive the salary he was receiving at the time he left office; or

b) If his judicial service totaled less than 16 years but not less than 10 years, he will receive that proportion of salary which the total number of years of judicial service bears to 16. No benefits, either immediate or deferred, are payable for less than 10 years of service.

We could find no specific rationale in the legislative history for the benefit provisions for territorial judges. We found general reasons such as (1) some retirement provisions were needed to attract individuals to the bench, (2) separate provisions under the judicial retirement system were needed for territorial judges since they were not article III judges and were not appointed for life, and (3) benefits should be payable as early as age 65 since age 70 retirement was out of line with other Government retirement systems and systems in private industry.

A 1942 amendment to the civil service retirement system provided coverage under that system to all elective and appointive officers of the judicial branch provided they were not subject to another retirement system. By agreement between the Civil Service Commission and the Administrative Office of the U.S. Courts, territorial judges were allowed to elect to participate in either the civil service system or the territorial judges retirement provisions of the judicial system. Territorial judges were also allowed to transfer from coverage under the civil service system to coverage under the territorial judges plan.

In February 1977 the Commission informed the Administrative Office of the U.S. Courts of a change in its policy regarding the option of territorial judges to participate in the civil service system. The Commission advised that the option had been allowed without any clear authority in law and that future territorial judge appointees will no longer be considered subject to coverage under the civil service system. New appointees will automatically be covered under the territorial judges plan. A new judge appointed from a Federal position subject to the civil service system will be considered to have separated from the Federal Government and to have been reemployed in a new Federal position subject to the judicial retirement system. Two territorial judges currently participate in the civil service system, and they will be allowed to continue under that system until resignation.

Survivor benefits

Before 1954 there were no survivor benefits under the judiciary system. In that year legislation was enacted establishing a noncontributory plan whereby widows of Supreme Court justices would receive an annuity of $5,000 a year. The amount was based on benefits being provided to the widow of President Coolidge by a 1937 law. The "Coolidge" annuity was extended to all Presidential widows and increased to $10,000 in 1958 and further increased to $20,000 in 1971. In 1972, the annuity for widows of Supreme Court justices was increased to $10,000.

A survivorship program was established in 1956 for other Federal judges. According to the legislative history, the program was enacted because most other civilian public servants had the opportunity to participate in the survivorship program of the civil service retirement system. The survivorship program was expected to assist in attracting qualified individuals to the bench.

Under the 1956 survivorship program, judges could elect to participate within 6 months after taking office. The program required judges to contribute 3 percent of their salary, both before and after retirement, to a survivors annuity fund. The annuity payable to a widow consisted of 1.25 percent of the judge's average salary for his last 5 years of service, multiplied by his years of judicial, congressional, and military service and up to 15 years of other Government service. To this was added 0.75 percent of the average salary multiplied by his years of other Federal service. The maximum annuity payable was 37.5 percent of salary. The benefits to a surviving widow were not payable until age 50 unless there was a surviving child, or children. Benefits were also payable to surviving children under age 18.

Recommendations for reform of the judicial survivors annuity program were advocated as early as 1960. The judges and others considered the program to be inadequate. In 1962 it was reported that participation in the program varied substantially from earlier forecasts and, in 1963, the 3-percent contribution rate was found to be inadequate to fund the program's benefits. Legislation was proposed in 1969 to merge the survivor program with the civil service system. The Judicial Conference supported the merger as the best solution to the funding inadequacies of the program; however, the Congress did not enact the proposed legislation. One feature of the proposal--to give Supreme Court justices the option to participate in the judicial survivors program--was enacted in 1972.

In 1973 the Judicial Conference reaffirmed its support of a merger of the judicial survivor program with the civil service system. But the legislation, which was supported by the Civil Service Commission, again failed.

Legislation to merge the two systems was introduced for the third time in 1975. An amendment to the bill, designed to reform the judges' program without merging it into the civil service system, was approved in October 1976. The law provided that, effective January 1, 1977, any Federal justice or judge, territorial judge, Director of the Administrative Office of the U.S. Courts, Director of the Federal Judicial Center, or administrative assistant to the Chief Justice could participate in the system. Participants were to pay 4.5 percent of their salaries, before and after retirement, into the judicial survivor's annuity fund. The legislation also authorized matching agency contributions to be paid to the fund. Major benefit changes were:

--A surviving spouse receives an annuity not to exceed 40 percent of the judicial officials' high-3 year average salary. The annuity is computed at 1.25 percent of the average salary multiplied by the years of judicial, congressional, military and other Federal service (not to exceed 15 years). To this is added 0.75 percent of average salary multipled by the number of years of service over 15.

--A surviving spouse may receive an annuity at any age.

--Cost of living increases will be granted in amounts of 3 percent for every 5 percent increase in the salary of the former office of the judicial official.

The legislative history did not state why the new judicial survivor program differs in many respects from civil service survivor benefits or specifically why the proposals to merge the two programs were not enacted.

Reemployed annuitants

Because the Constitution prohibits reducing a Federal judge's salary while in office, judges' salaries cannot be reduced if they are receiving annuities earned under other Federal retirement systems. They are allowed to receive both full salary and full annuity. In contrast, if a retired Federal civil service employee becomes a territorial judge, his salary is reduced by the amount of his civil service annuity.

Legislation has been introduced in recent Congresses to bar civil service annuity payments to Federal judges in active service but to date it has not passed.

The judicial retirement system does not prohibit payment of annuities and salaries to judges who have resigned from office and have been reemployed by the Government.

TAX COURT JUDGES RETIREMENT SYSTEM

The United States Tax Court was established in 1924 as an independent agency in the executive branch. The court, consisting of 16 judges, adjudicates controversies between taxpayers and the Internal Revenue Service. It is augmented by Tax Court commissioners who adjudicate controversies involving $1,500 1/ or less, and also by retired Tax Court judges, when needed. Tax Court judges have their own retirement system while Tax Court commissioners are covered by the civil service retirement system.

Before 1953 Tax Court judges were covered by the civil service retirement system. In that year, a separate Tax Court judges retirement system was established on the basis that other Federal judges had their own retirement system which provided substantially better benefits than Tax Court judges received under the civil service system. The legislative history indicated that the civil service system was considered inadequate for attracting appointees with needed maturity and experience to the court. The separate retirement system was also believed necessary to attract qualified personnel from the private sector to prevent the Tax Court from having a pro-Government bias.

The Tax Court judges retirement system is an elective, noncontributory retirement plan. Judges not electing to participate are automatically covered under the civil service retirement system. Once an election is made to participate, it becomes irrevocable and all benefits under the civil service system are waived. 2/

Judges retiring under the normal provisions of the Tax Court judges retirement system receive the salary of the office. Generally, this requires a minimum of 15 years' service. The system provides disability benefits based on length of service, but guarantees a minimum of 50 percent of the salary of the office. One of the major reasons cited for the liberal retirement benefits is the "recall" provision. Retired judges are subject to recall for 90 calendar days each year, and, if a retired judge who is physically and mentally able to perform upon recall fails to do so, all rights to retired pay are forfeited for a 1-year period. The 18 judges who have retired under the system have served 58 percent of their available time on recall.

The 1953 law did not provide for separate survivor benefits for Tax Court judges. For survivorship protection,

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1/At the time of our review legislation had passed both the House and Senate increasing this amount to $5,000.

2/Public Law 95-472, approved October 17, 1978, now permits revocation of such elections at any time before the first day an individual is entitled to benefits under the system.

a judge had to remain fully covered by the civil service system, or to participate in the Tax Court judges system and the survivorship provisions of the civil service system. To be covered by the survivorship provisions of the civil service system, a judge was required to make the full employee contribution.

In 1961 legislation was enacted which established survivor benefits under the Tax Court judges system. Judges electing to participate contribute 3 percent of salary, both before and after retirement. Survivor benefits are based on length of Government service, with a maximum of 37.5 percent of high-5 average annual salary.

Justification cited for establishment of the survivor's system was that other judges had their own survivorship protection, and the civil service system was geared to employees who served the Government for most of their working careers. Basically, the same reasons used to justify establishment of the Tax Court judges retirement system were used to justify the survivorship plan.

A provision requiring a Tax Court judge to waive all rights to any benefits under the civil service system when electing coverage under the Tax Court judges system has created inequities. The requirement is in sharp contrast to the provisions in the retirement systems for the Directors of the Administrative Office of the U.S. Courts and Federal Judicial Center which permit the directors to recapture civil service credit for service as a director if they leave their positions for other Government service. One Tax Court judge, who elected coverage under the Tax Court judges system, resigned in 1965 before meeting the system's eligibility requirement, and later obtained other Federal positions. However, because of his previous election, he is not permitted to participate in the civil service retirement system. The former judge had also been covered by the civil service system for several years before his appointment to the court but cannot receive a civil service benefit for that service. 1/

Establishment of the separate retirement system for Tax Court judges has not significantly changed the proportion of judges appointed from the private sector. In 1953, 3 of the

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1/See footnote 2 on p. 83.

16 judges were from the private sector and 13 were from the public sector. At the time of our review, six of the judges were from the private sector, nine were from the public sector, and one position was vacant.

Of the 45 judges appointed between 1924 to 1953, 21 were from the private sector and 24 were from the public sector. Since establishment of the Tax Court judges retirement system in 1953, 22 judges have been appointed; 11 from the private sector and 11 from the public sector.

The Constitutional provisions which give Federal judges life tenure and prohibit the diminution of their salary while in office do not apply to Tax Court judges. However, because of the similarity between the Federal judiciary and the Tax Court in regard to duties performed by retired judges, we believe that it is reasonable to provide full salary to both types of judges when they continue to serve or are available to serve when needed. In our opinion, such judges have not, in fact, retired. As indicated previously, however, we found no such justification for judges' disability and survivor benefit provisions being different from those of other Federal personnel.

COMPTROLLERS GENERAL RETIREMENT SYSTEM

The U.S. General Accounting Office (GAO) was created in 1921 as a nonpolitical, independent agency. GAO's basic purposes are to help the Congress, its committees, and its Members carry out their legislative and oversight responsibilities; perform legal, accounting, and auditing functions assigned by the Congress; and recommend ways to make Government operations more efficient and effective.

GAO is under the control and direction of the Comptroller General of the United States, who is appointed by the President, with the advice and consent of the Senate, for a 15-year term. To insure his independence, the law provides that the Comptroller General can be removed from office only by joint resolution of the Congress for specified causes and in no other manner than by impeachment. Also, the law prohibits a Comptroller General from being reappointed.

Before 1953 the position of Comptroller General was covered by the civil service retirement system. However, 1953 legislation established the Comptrollers General retirement system which, in many respects, provides greater benefits than the civil service system. The system provides a normal retirement benefit upon completion of the 15-year term or at the mandatory retirement age of 70 if the individual has completed at least 10 years of service. The benefit is equal to the salary of the office at time of retirement. However, if the individual is under age 65 the annuity is reduced.

The system was noncontributory, and had no provisions for future annuity adjustments prior to enactment of Public Law 95-512 on October 25, 1978. The act made the retirement system contributory for future Comptrollers General. Those electing survivor coverage will be required to contribute 3.5 percent toward their retirement benefits (in addition to the 4.5 percent for survivor benefits which are subsequently discussed), and those not electing such coverage will be required to contribute 8 percent. The act also provided for future annuity cost of living adjustments based on increases in the CPI. However, the annuity of a retired Comptroller General is limited to the current salary of the office.

According to the legislative history, the Comptrollers General system was established because benefits under the civil service system were considered inadequate for appointees who lacked prior Government service and who did not continue in Federal service after leaving office. (The civil service system would provide benefits of 26.25 percent of high-3 salary after 15 years of service.) Because of the similarity in character, tenure, and independence of the Office of the Comptroller General to that of Federal judges, benefits under the Comptrollers General retirement system were patterned after Federal judiciary retirement benefits.

The 1953 legislation provided that Comptrollers General would automatically be covered by the new system and could receive no retirement benefits under any other law of the United States. In 1966, however, the system was amended to provide that Comptrollers General appointed after January 1, 1966, who at the time of appointment were, or had been, subject to the civil service retirement system, would remain subject to that system unless a written election was made to participate in the Comptrollers General retirement system. Such an election can be made at any time but not later than 60 days after completion of 10 years' service as Comptroller General. An election to participate in the Comptrollers General system and, thereby, waive benefit rights under any other Federal retirement system, is irrevocable.

The time limitation in which a Comptroller General covered by the civil service retirement system can elect coverage under the Comptrollers General retirement system is inconsistent with the provisions imposed on Tax Court judges, who can elect coverage under the Tax Court retirement system at any time while serving as a judge. We found no apparent reason for the different provisions.

The provision barring a retiree from receiving benefits under the Comptrollers General retirement system and retirement benefits under any other law of the United States is inconsistent with retirement provisions in other special systems covering Presidents and Federal and Tax Court judges. Presidents and Federal judges are permitted to receive their special retirement benefits and any other retirement system benefits to which they are entitled. Tax Court judges electing to receive benefits under their system waive all civil service benefits, but not benefits earned under other Federal retirement systems or social security. It is unclear whether the prohibition against a retired Comptroller General receiving retirement benefits under other laws would apply to social security. Such a determination would have to be made by the Social Security Administration.

Before 1959, the system did not provide survivorship benefits. However, in 1959, 3 years after Federal judges were provided survivor benefits, similar protection was provided to widows and children of Comptrollers General. Survivor coverage is elective and contributory. An election must be made within 60 days of a decision to participate in the Comptrollers General retirement system.

Prior to enactment of Public Law 95-512, survivor coverage required a contribution of 3 percent of salary and retirement annuity, as well as a deposit, with interest, of 3 percent of basic pay received during any former Federal civilian service. In the event a deposit for past service is not made, survivorship benefits are reduced by 10 percent of the amount of such deposit. Public Law 95-512 increased the contribution rate for survivor coverage to 4.5 percent, and made other changes in the survivorship plan similar to the changes made for Federal judges in October 1976.

RETIREMENT SYSTEMS FOR THE DIRECTORS OF THE ADMINISTRATIVE OFFICE OF THE U.S. COURTS AND FEDERAL JUDICIAL CENTER

The Administrative Office of the U.S. Courts was created in 1939 to consolidate the administrative duties of the Federal courts under one agency in the judicial branch and to replace the Department of Justice, the prosecutorial arm of Government, as the administrative authority of the Federal court system. The office is headed by a Director and a Deputy Director, both appointed by the Supreme Court. The Federal Judicial Center was created in 1967 to further the development and adoption of improved judicial administration in the courts. The Center is headed by a Director appointed by a Board composed of the Chief Justice of the United States, two judges of the U.S. courts of appeals and three judges of the U.S. district courts, and the Director of the Administrative Office of the U.S. Courts.

All positions in the Administrative Office of the U.S. Courts and the Federal Judicial Center are covered by the civil service retirement system. However, the directors may elect coverage under separate retirement systems established for them in 1976. The legislative history indicated the major reason for establishing these systems was to attract high caliber individuals.

The Directors retirement systems are noncontributory, and after completing 15 years service and attaining age 65, provide a life annuity equal to 80 percent of salary at the time of retirement. Earlier retirements are available with reduced annuities. The systems also provide disability benefits of at least 50 percent of the salary at retirement.

Benefits provided under the Directors retirement systems are more liberal than civil service benefits. For example, under the civil service retirement system, an individual receives an annuity equal to 26.25 percent of his high-3 average annual salary for 15 years' service. For disability, the civil service retirement system generally provides a minimum of 40 percent of the high-3 average annual salary. On the other hand, the Directors systems have no cost of living adjustment provisions.

The Directors retirement systems do not provide survivorship benefits. However, individuals covered by the Directors systems are permitted to elect survivorship coverage under the Federal judiciary retirement system.

Individuals electing to participate in either of the Directors retirement systems must do so within 6 months after accepting appointment to the position. By electing to particcipate in either of the Directors systems, civil service coverage is waived. However, the systems include a special provision whereby individuals leaving the position, by means other than retirement, are permitted to recapture civil service credit for service as Director. This can be done by making a contribution to the civil service retirement fund equal to the amount that would have been deposited had the individual been covered by the civil service retirement system, plus interest.

Other Federal retirement systems do not have the special "recapture" provision. The only explanation we found for including the provision in the Directors retirement systems was to make the positions more attractive to highly qualified individuals.

The position of Administrative Assistant to the Chief Justice of the United States was created in 1972. The Administrative Assistant is automatically covered by the civil service retirement system but may elect coverage under the retirement system for the Director of the Administrative Office of the U.S. Courts. The legislative history indicated the position needed an individual with high administrative and managerial talents and a legal background with experience and knowledge of the Federal court system. The special retirement benefits were intended to attract and retain individuals with such qualifications.

As mentioned earlier, service under the Directors retirement systems may be creditable under the civil service retirement system; however, civil service retirement credit is not recognized under the Directors systems. Civil service retirees accepting appointments to positions covered by the Directors retirement systems have their salaries reduced by the amount of their annuities; however, individuals retiring under the Directors retirement systems can obtain a civil service position and receive full salary and annuity.

The only explanation we found for establishing the Directors retirement systems was to attract high caliber professionals. However, many civil service positions require and are filled by high caliber individuals who are covered by the standard civil service benefits.

CENTRAL INTELLIGENCE AGENCY RETIREMENT SYSTEM

The Central Intelligence Agency was established in 1947 to coordinate intelligence activities of several Government departments and agencies. The agency evaluates intelligence relating to national security, but has no police, subpoena, or law enforcement powers or internal security functions.

Until 1964 all full-time CIA employees were covered under the civil service retirement system. However, in 1964 a separate retirement system was established for certain CIA employees. The system provides a retirement benefit after attaining age 50 and 20 years' service. The benefit equals 2 percent of high-3 average annual salary for each year of service, up to a maximum of 70 percent.

The CIA retirement system is largely patterned after the retirement system for Foreign Service personnel, particularly the optional retirement provisions. However, several other provisions are the same as the civil service retirement system, as are many Foreign Service provisions. To maintain consistency, the law allows the CIA system to be changed by Executive order whenever changes are made to conforming provisions of the civil service system.

The CIA system's benefits are more generous and are available at an earlier age than those available under the civil service system. It was established on the basis that the rigorous demands of certain positions in the CIA could not adequately be met by older employees. The more generous retirement benefits were designed to make early retirement more attractive and to keep the retirees from suffering financial hardship. The CIA also wanted, because of the duties involved, a mandatory retirement age lower than that of the civil service system. Work performed by certain CIA employees was considered to be as rigorous and difficult as work performed by Foreign Service officers and certain personnel of the FBI, who were covered under retirement provisions offering earlier and more generous retirement benefits. Another reason given for establishing the separate system was that CIA agents were obligated to serve anywhere in the world, often at unhealthful locations.

The CIA system's mandatory retirement age is 60 for GS-17s and below and 65 for GS-18s. The Director, if he determines it is in the public interest, may extend the mandatory retirement age for a participant for up to 5 years. The mandatory retirement age in the Foreign Service system was also age 60 until this provision was ruled unconstitutional and void by a U.S. District Court on June 28, 1977. (See p. 67.)

The CIA Director can also mandatorily retire individuals who are at least age 50 and have completed the service requirements for voluntary retirement. In addition, the Director can mandatorily retire participants who have completed 25 years of service without regard to age if the participant has completed at least 10 years' service with the CIA, and if at least 5 of those years are qualifying service under the CIA system. However, according to CIA officials, Directors rarely invoke these mandatory retirement provisions. The provisions are similar to civil service provisions which provide for involuntary retirement after 25 years' service without regard to age, or at age 50 with 20 years' service. Involuntary retirement provisions in the Foreign Service system vary depending on the employee's class. (See pp. 64 and 65.)

According to CIA officials about one-third of their employees are covered by the CIA system. The remaining employees are covered by the civil service system. Employees covered by the CIA system include those whose duties are determined by the Director to be in support of agency activities abroad that are hazardous to life or health or so specialized because of security requirements as to be clearly distinguishable from normal Government employment. Participants who complete 15 years' service with the CIA, and whose service is judged by the Director to be qualifying for the CIA system, may elect to remain in the system for the duration of their employment with the CIA. Such election is not subject to review or approval by the Director.

To be eligible for coverage under the CIA retirement system, individuals must be citizens of the United States, at least age 25 but less than 60 years of age, and have completed 60 months of qualifying service. All new employees are covered by the civil service retirement system until they complete the required qualifying service. Prior to 1976, the Foreign Service had a similar arrangement under which Foreign Service staff officers and employees appointed by the Secretary of State had to complete 10 years of qualifying service before transferring from the civil service retirement system to the Foreign Service system. However, the 10-year requirement was repealed in 1976. The civil service system has no minimum age or service requirements for participation.

Unlike any other Federal retirement system, the CIA system has a limitation on the number of employees that can be retired under the system at any one period, exclusive of disability retirements. For the period between July 1, 1974, and June 30, 1979, the limitation is 1,500 employees. Apparently, the limitation was imposed because the Director has the authority to extend retirement coverage to employees and, without a limitation, the Congress would have no control over the number of employees that could be extended such coverage.

The CIA considers its retirement system to be an inherent part of its personnel management system and strongly feels that the preferential benefits are needed to maintain a young and vigorous force. Because of the unavailability of information, we were unable to adequately evaluate the need for preferential benefits.

CIA officials expressed concern over the possible loss of administrative responsibilities for covered employees if the CIA system were merged with other Federal retirement programs. They viewed such a loss as an infringement on the statutory responsibility of the Director of Central Intelligence to protect intelligence sources and methods. As mentioned earlier, all CIA employees were covered by the civil service retirement system between 1947 and 1964. In our review of the legislative history, we found no mention of administrative problems as a reason for a separate CIA system.

CIA employees, with a minimum of 1 year of service, can supplement their civil service or CIA retirement annuities by participating in the Government Employees Voluntary Investment Plan (VIP). The CIA maintains the plan for its employees but makes no contributions.

VIP is comprised of two savings funds--a growth fund and an income fund. The growth fund depends upon the rate of return on investments, whereas the income fund has a guaranteed minimum rate of interest (8.15 percent in 1976). Employees can participate in either or both funds. A participant can invest as little as $5 biweekly or as much as 10 percent of base salary. All income and capital gains are reinvested.

VIP is a qualified pension plan; therefore, the tax consequences do not appear until the participant withdraws his investments following resignation or retirement. All gains in VIP attributable to participation in the plan before January 1, 1974, are taxed as capital gains and all gains attributable to participation after that date are taxed as ordinary income but under a special "10-year averaging."

The CIA maintains, and we agree, that VIP should not be considered a Federal pension plan.

PRESIDENTS RETIREMENT SYSTEM

The executive powers of the United States are vested in a President who is elected to a 4-year term of office. The President is Commander-in-Chief of the Armed Forces, and has the power, by and with the advice and consent of the Senate, to make treaties and to appoint ambassadors, other public ministers and consuls, justices of the Supreme Court, and all other officers of the United States whose appointments are not otherwise provided for by the Constitution.

A pension for former Presidents was first authorized by legislation enacted in 1958. The act also provided various other benefits, including a pension for the widow of a former President. Several reasons were cited for establishment of the separate retirement system for Presidents. Basically, the reasons were to provide individuals who served as President an income that would enable them to meet all demands upon them without financial difficulty. A Senate report on proposed legislation to establish the Presidents' retirement system recognized there are many ways in which a former President can earn a large income, but maintained that, by providing a retirement benefit, former Presidents could be expected not to engage in any business or occupation which would demean the office of President.

The system provides a life annuity to former Presidents equal to the rate of pay for executive level I (Executive Department Secretaries), currently $66,000. Each adjustment to the salary results in a like adjustment to a former President's annuity. The annuity is suspended if a former President holds an appointed or elected office or position in the Federal or District of Columbia Governments for other than a nominal rate of pay. The system is noncontributory, and vesting is immediate.

Two former Presidents receive, in addition to the annuity provided under the Presidents retirement system, a civil service retirement annuity. The legislation establishing the Presidents system was silent regarding the possibility of a President receiving two Government pensions. The Senate, however, during a debate in December 1970, discussed this possibility but took no action to preclude it.

The Presidents retirement system also provides a survivor benefit for former Presidents' widows. However, unlike many other Federal retirement systems, it does not provide survivor benefits to children. A widow is authorized a benefit equal to $20,000 a year, with no subsequent cost of living adjustments, for the remainder of her life unless she remarries before age 60. However, to receive the benefit, she must waive her rights to any other annuity or pension to which she is entitled under any other Act of Congress. Moreover, like the Presidential pension, a widow's annuity is suspended if she accepts a Federal or District of Columbia position at other than a nominal rate of pay.

Allowing Presidents who had previously been covered by the civil service system to continue under that system might not result in an annuity less than the current executive level I salary. For example, a total of 19 years' service (4 years as President and 15 years of other Government service) would result in an immediate annuity of $68,500 under the civil service system, provided the minimum age requirement (age 62 in this particular example) was met. If some of the prior service was as a Member of Congress the annuity would be greater because of the higher multiplier used for Member service. If the individual elected to provide a survivor annuity based on the $68,500, his annuity would be reduced to $61,920, but the widow's annuity would be $37,675, or 88 percent greater than the $20,000 survivor annuity paid under the Presidents retirement system. Eight years' service as a President, excluding any other Governmental service, would result in an immediate annuity of $25,500 under the civil service system, provided the individual was at least age 62. The civil service system would also provide, if applicable, survivor benefits for former Presidents' children.

Vice Presidents are covered under the provisions of the civil service retirement system applicable to Members of Congress.

NONAPPROPRIATED FUND INSTRUMENTALITY RETIREMENT SYSTEMS

The Departments of Defense and Transportation estimate they have over 20,000 nonappropriated fund instrumentalities (NAFIs) employing about 193,000 personnel. Their mission is to carry on programs for enhancing the morale, welfare, and recreational activities of active and former military, Coast Guard, and authorized civilian personnel. The programs are financed for the most part by funds generated from retail exchange operations. However, a good deal of the real estate, equipment, utilities, and maintenance required to support these programs is acquired with appropriated funds.

NAFIs are units of the Federal Government, and their personnel meet the general criteria used to define Federal employees. However, legislation exempts many NAFI personnel from the provisions of certain laws administered by the Civil Service Commission, including the civil service retirement system, and from the Federal Employees' Compensation Act.

Organizational structure

The authority for establishing and operating DOD and Coast Guard NAFIs has been delegated to the heads of various components of the Departments of Defense and Transportation. The number and types of units administered by these organizations vary and can generally be classified into four broad categories: 1/

--Resale and revenue sharing
Instrumentalities operating retail operations are generally referred to as exchanges and include department stores, restaurants, gasoline filling stations, barber shops, newsstands, shoe repair shops, laundries, and tailor stores. Receipts in excess of costs are distributed to general welfare and recreation NAFIs.

--General welfare and recreation
Instrumentalities operating general welfare and recreation programs are financed by appropriated funds, by funds received from resale and revenue sharing units, and by funds generated from operations. The type of programs involved are bowling centers, craft and hobby shops, golf centers, outdoor recreation areas, and child care programs.

--Membership association
Instrumentalities operating general welfare and recreation programs for their voluntary members are funded primarily by members. Membership associations generally operate messes and clubs such as officers, enlisted men, aero (flying), boating, amateur radio, scuba diving, etc. No funds are received from resale and revenue sharing units; however, appropriated fund support is provided indirectly through the use of personnel, facilities, utilities, etc.

--Special
Instrumentalities operating support services are primarily financed through user fees and charges. The services provided generally include centralized accounting, procurements, or personnel services for more than one NAFI.

Seven retirement plans cover NAFI employees. The number of units controlled, personnel employed, and principal operating category for each of the seven plans as estimated by DOD and the Coast Guard are shown on the following page.

1/DOD is currently drafting a policy for classifying NAFIs into eight categories. In this report we used four broader categories that include practically all NAFIs.

	Number of units controlled in 1976	Number of employees in 1976	Principal category
Army and Air Force Exchange Service (AAFES)	16,238	60,000	Resale and revenue sharing.
Air Force nonappropriated fund instrumentalities	1,240	40,000	Resale and revenue sharing, general welfare and recreation, membership associations, and special.
Army nonappropriated fund instrumentalities	1,734	33,000	Resale and revenue sharing, general welfare and recreation, membership associations, and special.
Navy Resale System Office (NAVRESO)	178	29,000	Resale and revenue sharing.
Bureau of Naval Personnel nonappropriated fund (BUPERS)	668	19,000	Resale and revenue sharing, general welfare and recreation, membership associations, and special.
Marine Corps exchanges, recreation funds, clubs, messes, and the Marine Corps Exchange Service	189	10,000	Resale and revenue sharing, general welfare and recreation, membership associations, and special.
Coast Guard nonappropriated fund activities	320	2,000	Resale and revenue sharing, and general welfare and recreation.
TOTAL	20,567	193,000	

NAFI employees can be categorized as follows:

	Number of employees
U.S. civilian	134,000
Foreign national	35,000
Military (note a)	24,000
Total	193,000

a/Military personnel who worked for NAFI units part-time during their off duty hours.

The status of U.S. civilian employees was estimated as follows:

	Number of employees
Full-time	71,000
Part-time	38,000
Intermittent	22,000
Temporary	3,000
Total	134,000

Employment status of NAFI personnel

The Federal Personnel Manual Supplement 831-1 states:

> "To be considered a Federal employee, a person must be: (1) Engaged in the performance of Federal functions under authority of an Act of Congress or an Executive order; and (2) Appointed or employed by a Federal officer in his official capacity as such; and (3) Under the supervision and direction of a Federal officer."

NAFI personnel meet these criteria and hold positions which are similar to those of other Federal employees. NAFI personnel include craftsmen and tradesmen, administrative personnel, customer service clerks, and professionals such as managers, accountants, lawyers, engineers, buyers, and media specialists.

However, Federal legislation (5 U.S.C. 2105) stipulates that employees paid from the nonappropriated funds of certain DOD and Coast Guard instrumentalities are deemed not to be Federal employees for purposes of certain laws administered by the Civil Service Commission and are excepted from the Federal Employees' Compensation Act. The exceptions were made in response to a DOD request, so that the NAFIs could establish personnel management systems competitive in cost and flexibility with those of private, commercial retail operations and recreation activities.

The exceptions from full Federal employee status do not apply to morale, welfare, and recreation employees paid from appropriated funds. Some employees having similar jobs at similar units are considered Federal employees and participate in the civil service retirement system because they are paid from appropriated funds. In addition, DOD commissaries are often considered morale and general welfare activities, even though their employees' jobs are similar to those of NAFI employees. However, since they are paid from appropriated funds, they receive civil service status, pay, and benefits.

Exceptions from full Federal employee status also do not apply to NAFI employees of other than DOD and Coast Guard activities, such as the VA's Veterans Canteen Service. These employees participate in the civil service retirement system.

Some laws are applicable to NAFI employees even though they are excepted from Federal employee status. For example, the seven retirement plans established for these excepted employees are not subject to ERISA because NAFIs are considered instrumentalities of the Federal Government and, as such, are exempt. Furthermore, NAFI employees are required by DOD to restrict their political activities, refrain from striking, and to adhere to standards of conduct similar to those of Federal employees.

Development of NAFI retirement plans

NAFI retirement plans developed independently of each other. They share some common problems, and many inequities and inconsistencies exist among them. DOD has initiated action to alleviate some of the problems, but much more needs to be done.

Historically, the heads of DOD components were responsible for creating, maintaining, and supporting programs, services, and activities which have a direct bearing on the morale of military personnel and their dependents, and on civilian employees of the defense establishment. DOD afforded local commanders considerable latitude in the creation, operation, and control of NAFIs. As a result, separate and distinct NAFI personnel management systems developed throughout the services--each having somewhat different personnel administration policies and procedures.

Amendments to the Social Security Act in 1950 permitted NAFI employees coverage under the act. Each of the seven organizations established retirement plans for their employees at various dates--AAFES established the first one in 1946 and the Air Force the last one in 1976.

In 1970-71, the Permanent Subcommittee on Investigations, Senate Committee on Government Operations, held hearings on alleged irregularities and improprieties in various military clubs and exchanges. In response to those hearings, DOD studied the personnel management practices of its NAFIs and concluded there was no justification for the differences in local wage rates and benefit provisions for NAFI employees which existed both within and between installations. In September 1974, DOD issued broad policy guidance for achieving equitable treatment of NAFI employees in seven areas of personnel management, including retirement benefits.

In connection with developing retirement benefits, the Office of the Assistant Secretary of Defense (Manpower and Reserve Affairs) established a DOD working committee in September 1972. The committee developed minimum standards for NAFI employee retirement plans covering such elements as annuity amounts, eligibility, retirement age, service credits, as well as funding and fund reviews. The committee also established a maximum level of benefits, prohibiting new plans or changes to existing plans from exceeding those provided by the civil service retirement system.

The working committee's efforts at establishing standards and monitoring compliance have resulted in major changes in retirement benefits and probably will result in additional changes in the future. However, many inequities, inconsistencies, and common problems continue to exist under the seven separate retirement plans. The differences, which exist throughout the entire range of retirement plan elements, are discussed below.

Benefits

About 30 percent of all NAFI employees participate in retirement plans. Those excepted include foreign nationals, who are generally covered by agreements with foreign countries, certain part-time employees, including military personnel, and temporary or intermittent employees. A general description of the features mandated by DOD follows:

--Four types of retirement are provided--optional, deferred, mandatory, and disability.

--To be eligible for a retirement annuity, the employee must have completed at least 5 years of service.

--Retirement credit will be given for NAFI employment and for military service of up to 5 years when such military service interrupts NAFI employment. No credit will be given for other Federal civilian service. Credit will be allowed for unused sick leave at the time of retirement.

--The formula for computing an employee's annuity will be based on the highest average annual pay for any 3 consecutive years and on the number of years of service.

--Annuities will be subject to offset by a percentage of social security benefits received.

--An employee's basic annuity cannot exceed 80 percent of his high-3 average salary. However, an annuity in excess of 80 percent can be realized through crediting unused sick leave and/or considering social security retirement benefits.

--Death benefits in the form of annuities to surviving spouses are to be paid automatically in the event that employees die before retirement and after completing at least 60 months of service. They are also to be paid to surviving spouses of retirees if such coverage was elected at the time of retirement. No benefits must be paid to surviving children.

The NAFI plans provide most of their benefits within the DOD established minimum and maximum levels; however, some exceptions exist.

--AAFES provides about 1,200 of its management personnel (out of a total of 26,000 employees eligible for retirement plan participation) benefits which exceed the DOD maximum. The special benefits are granted as additional compensation in lieu of higher pay to encourage employees to accept and fulfill employment conditions, such as (1) assignments to any worldwide exchange location at any time for any tour of duty set by the employer, (2) continuous development and improvement in executive ability, and (3)involuntary retirement without recourse to employee grievance procedure at any time after 20 years of service and age 45.

--The Army plan does not comply with most of the DOD minimum benefit levels. However, Army officials advised us they are currently studying the changes needed to bring their plan in line with minimum DOD levels.

Furthermore, even within the DOD established minimum and maximum levels, significant benefit dissimilarities existed among plans.

Eligibility

DOD requires NAFIs to provide retirement benefits to all regular full-time civilian employees who are U.S. citizens, permanent resident aliens of the United States employed in the United States, or permanent residents of Panama employed in the Canal Zone.

Foreign nationals employed overseas are generally not eligible because DOD's policy requires that benefits for locally hired non-U.S. citizen employees be based on customs and practices in the area of employment and the provisions of country-to-country agreements.

Military personnel covered by the uniformed services retirement plan and temporary and intermittent employees are also excluded.

The seven plans meet DOD's eligibility standards for full-time employees but differences exist among the plans. Participation in five plans is voluntary while participation in the Army and AAFES plans is mandatory. One year prior service is an eligibility requirement of Coast Guard, Army, and Air Force plans but not for the other four plans.

Part-time employees are also treated differently. Four plans permit their voluntary participation. The Army plan requires participation while the AAFES and Air Force plans exclude them.

Retirement age and service requirements

A comparison of retirement age and service requirements of the seven NAFI plans illustrating various differences among the plans as well as the departures from DOD standards follows:

Type of retirement	DOD standard Age	DOD standard Years of service	AAFES Age	AAFES Years of service	AAFES supplemental Age	AAFES supplemental Years of service	NAVRESO Age	NAVRESO Years of service	AIR FORCE Age	AIR FORCE Years of service	MARINE CORPS Age	MARINE CORPS Years of service	ARMY Age	ARMY Years of service	BUPERS Age	BUPERS Years of service	COAST GUARD Age	COAST GUARD Years of service
Normal retirement	62	5	62 a/62	5 3	62	5	62	5	62	5	62	5	62	5	62	5	62	5
Voluntary early retirement (with full benefit) (note b)	60 55	20 30	60 55	20 30	60 55	20 30	60 55	20 30	No provision		60 55	20 30	No provision		60 55	20 30	60 55	20 30
Optional early retirement (with reduced benefit)	52	5	52	5	No provision		52	5	52	5	52	5	52 50	5 20	52	5	52	5
Involuntary early retirement	c/50 c/any	b/20 b/any	c/50 c/50	20 25	45	20	No provision		No provision		No provision		No provision		No provision		No provision	

a/Option for a reduced annuity based on employee contributions only.

b/DOD does not require these benefits as minimum levels but rather permits them as maximum levels.

c/Annuity is reduced if under age 55.

Contributions

DOD did not set an employee/employer contribution rate but required:

--All plans to be funded in accordance with sound actuarial principles to assure adequate protection of the interests of beneficiaries and participants.

--The employee and employer to share the current cost of the plan.

--The use of only nonappropriated funds.

--Any and all restrictions on benefits applicable to civil service employees to be automatically applicable to NAFI retirement plans initiated after January 1, 1976.

The contribution rates established by the seven plans follow:

--Five plans 1/ require an employee contribution of 7 percent of pay less contributions made to the social security program.

--The Army plan requires employees to contribute 3 percent of the first $6,600 of pay and 6 percent of any remainder.

--Each of the seven plans requires the employer to pay, based upon an actuarial valuation, all costs not covered by employee contributions based upon actuarial valuation. In 1976, employer contributions ranged from about 6 percent paid by the Air Force to about about 12 percent paid by AAFES (the AAFES supplemental plan does not require any employee contribution). Employers also match the employees' contribution to the social security program.

1/One of the plans, Marine Corps, requires employees to contribute 1.15 percent of salary up to the maximum social security wage base. Since the current social security contribution is 6.05 percent, the employee contribution totals 7.20 percent. As the social security rate increases, the employee contribution will be increased in the same manner.

Qualification for vesting

DOD established 5 years' service and attainment of age 30 as the only qualifications for an employee to acquire vested rights in a retirement plan. Three of the seven plans provide the same vesting qualifications; however, four plans--NAVRESO, BUPERS, Coast Guard, and Army--do not require a minimum of 30 years of age.

Disability retirement

DOD requires payment of an annuity to active employees with at least 5 years' creditable service who become totally and permanently disabled. The benefits can be treated as part of the retirement plan, a separate plan, or both. However, amounts due for disability under the Longshoreman's and Harbor Worker's Act (NAFI employees are eligible for workers' compensation benefits under this act) are required to be offset from disability annuities.

Five plans meet these standards, two do not.

--BUPERS requires 12 months' participation in a group life insurance plan as a condition for disability annuities payable from this plan.

--The Army does not offset annuities by the amounts awarded under the Longshoreman's and Harbor Worker's Act.

Preretirement survivor benefits

DOD requires the payment of an annuity to a surviving spouse upon the death of an employee who has completed 60 months of creditable NAFI service. No children annuities are required. The surviving spouse must have been married to the employee for at least 1 year immediately preceding the employee's death or be the parent of a child born of the marriage. The annuity is 55 percent of the greater amount computed by

--the retirement formula without reduction for age of employee at time of death or

--the lesser of

--forty percent of the employee's high-3 average compensation or

--annuity formula after increasing credited service for the period from the employee's date of death to age 60.

The surviving spouse's annuity is reduced by social security benefits. Annuities are discontinued upon the spouse's death or remarriage before age 60. The annuity is reinstated if the remarriage is terminated by death, annulment, or divorce.

The Air Force and Marine Corps plans provide the DOD minimum levels. Differences from the minimum levels as provided by the other five plans were:

--The eligibility requirement for the AAFES, NAVRESO, BUPERS, and Coast Guard plans is 18 months' service. DOD permits this as a maximum level.

--The Army plan requires that the spouse be married 6 months prior to an employee's death rather than the 1-year DOD requirement.

--The Army plan provides the spouse an annuity equal to the retirement benefit which would have been payable to the deceased employee had he retired on the date of death and elected to have a 100 percent survivor annuity.

--The Army plan provides annuities (1) to the spouse for life without regard to DOD's remarriage provisions and (2) to the surviving dependent children to age 18 or upon marriage, in the event there is no qualifying spouse.

Postretirement survivor benefits

DOD requires that the annuity be made available for the surviving spouse of a retiree. This is an optional feature which, if accepted by the retiree, results in a reduction (either actuarial or a uniform 10-percent reduction) in his annuity. An unmarried employee can also elect to provide survivor benefits to his children, or anyone with an insurable interest.

The survivor's annuity is generally 55 percent of the retiree's annuity with variations depending upon the type of retirement (normal retirement age, early retirement, disability retirement); the portion of the employee's annuity elected as a base for survivor benefits; and the unmarried employee's elected beneficiaries.

The AAFES and Marine Corps plans provide the DOD minimum level. The Air Force plan has only one variation from the DOD minimum level--survivor income options include either 25 percent, 55 percent, or 75 percent of the retiree's annuity. The NAVRESO, BUPERS, and Coast Guard plans have DOD minimum levels except that no offset is applied against survivor's annuity when a survivor becomes eligible for social security benefits. The Army plan provides survivor income calculated differently than DOD's standards.

Retirement benefit formula

The minimum and maximum retirement benefit formula established by DOD is based upon the high 3 years' average basic pay times the rate per year of service determined by the sum of:

--Maximum

--one and one-half percent per year for 5 years,

--one and three-quarters percent per year for over 5 years to 10 years, and

--two percent per year for over 10 years.

--Minimum

--one and one-half percent per year for 10 years, and

--two percent per year for over 10 years.

Eighty percent of high 3 years' average pay exclusive of any credit for unused sick leave is the maximum annuity permitted. The computed annuity must be offset by up to 100 percent of social security retirement benefits at the rate of 2.5 percent for each year of service.

DOD requires retirement credit for service performed for NAFIs but not for military service except for up to 5 years of such military service as interrupts NAFI service.

A comparison of retirement benefits as a percentage of high 3 years' average pay under the maximum and minimum DOD levels follows:

Years of service	Percent of high 3 years' average pay: Maximum (note a)	Percent of high 3 years' average pay: Minimum	Percent of social security benefit offset
20	36.25	35.00	50.00
25	46.25	45.00	62.50
30	56.25	55.00	75.00
35	66.25	65.00	87.50
40	76.25	75.00	100.00

a/Generally 1.25 percent more of the high 3 years' average pay is available at the maximum level, which is the level established for most annuities under the civil service retirement system.

The seven plans differ in retirement formulas as follows:

--The AAFES basic plan provides the maximum level. However, the supplemental plan for AAFES executive management employees provides 2.5 percent for each year of service times the high 3 years' average pay less the amount payable from the basic plan. The supplemental plan permits a maximum of 75 percent of high 3 years' average pay.

--NAVRESO, BUPERS, and Coast Guard plans provide the maximum DOD level. However, they include premium pay such as overtime and Sunday work in the high 3 years' average pay rather than basic pay only. The three plans differ from DOD standards on social security offsets but are expected to comply at some future date.

--The Air Force and Marine Corps plans provide the minimum DOD level. However, the Marine Corps includes premium pay such as overtime and Sunday work in the high 3 years' average pay rather than basic pay only, according to an official.

--The Army plan follows neither standard but rather is based on 5 years' average pay. The annuity formula is 0.8 percent of the first $6,600, 1.8 percent of the excess for each year up to 20 years' service, plus 2 percent of the average salary for each year of service from 20 to 40 years; there is no social security offset, and the annuity cannot exceed $20,000. We were advised that the Army plan is being studied for possible changes to bring it in line with DOD standards.

Six of the seven plans restrict retirement credit for up to 5 years of such military service as interrupts NAFI service. AAFES provides additional credits for up to 5 years of military service which precedes civilian service, but also restricts the total credit to 5 years.

Portability

Under certain conditions, DOD standards permit the transfer of pension rights and credits. Employees who transfer to another NAFI because of transfer of functions between the NAFIs or through a reduction in force by one NAFI with reemployment by another within 90 days retain their rights and credits. Otherwise, there is no required portability among NAFI plans.

Six plans incorporate the DOD minimum standards, while the Coast Guard plan and the AAFES supplemental plan do not provide for any portability features.

Pension rights and credits are not transferable between the civil service and NAFI plans. Thus, employees paid with appropriated funds and subject to the civil service system cannot transfer pension rights and credits when they change positions in a NAFI to those paid with nonappropriated funds. Similarly, employees paid with nonappropriated funds cannot transfer pension rights and credits when they change positions to those paid with appropriated funds.

A BUPERS official said that in the last 2 years the source of funds used to pay employees in 80 positions was changed from appropriated to nonappropriated and in 10 positions from nonappropriated to appropriated. Employees in these positions lost their pension rights and credits simply because of the change in the source of funds. A similar situation occurred under the Army's plan.

Cost of living increases

DOD does not require cost of living increases in computing retirement annuities. As a maximum, DOD permits benefits to be adjusted semiannually on the basis of the percentage increases in the Consumer Price Index during the preceding 6-month period.

Consolidation of NAFI plans

Administrators of most of the NAFI plans told us they preferred that the separate plans be continued and generally opposed consolidation of NAFI plans into one NAFI system or including NAFI personnel in a system with other Federal employees. The administrators maintained that inconsistencies among the plans had caused no problems but acknowledged that there is a trend toward conformity of NAFI retirement benefits with those of the civil service retirement system.

The administrators expressed concerns that a consolidated NAFI plan might provide higher benefits and therefore higher costs for some NAFIs, particularly those providing the minimum DOD benefit levels. They believe an improved plan might threaten the existence of some smaller NAFIs which could not bear the burden of increased operating costs. Similarly, they stated that inclusion of NAFI personnel in a Federal retirement program would cause the NAFIs to lose control over benefit levels and attendant costs. They also stated that including NAFI personnel in a Federal retirement system might cause pressure for granting full Federal status to the employees in terms of pay and other benefits. They contend this would significantly increase costs and force many NAFIs out of business.

In our opinion, the inequities and inconsistencies among NAFI retirement plans should not be continued. NAFI employees and retirees are treated quite differently depending upon the retirement plan that is applicable to their employment for no apparent reason other than that the plans developed independently of each other. Moreover, benefits provided by the NAFI plans and social security combined are in many cases more generous than benefits received by other Federal civilian employees from the civil service retirement system. We found no justification for NAFI employees to receive superior benefits, or for that matter, lesser benefits, than other Federal personnel.

Inclusion of NAFI employees in a Federal retirement program would be consistent with DOD's findings in the early 1970s that there was no justification for differences in benefit provisions for employees of the various NAFIs and the adoption of retirement plan standards by DOD that, in most cases, closely approximate the civil service retirement system. Moreover, employees in Federal NAFIs outside DOD and the Coast Guard participate in the civil service system as do certain NAFI and other morale, welfare, and recreation employees who are paid with appropriated funds.

QUASI-FEDERAL EMPLOYEE RETIREMENT SYSTEMS

Fifteen of the systems included in our review cover certain employees of the farm credit and Federal Home Loan Bank system. In addition, employees of Federal Reserve banks participate in a retirement program with Federal Reserve Board employees but under separate provisions. Employees covered by these retirement programs have both private and public characteristics. Therefore, the issues involved in deciding on the desirability of including the systems in a centralized Federal retirement program primarily concern the relationship of the employees and their organizations to the Federal Government.

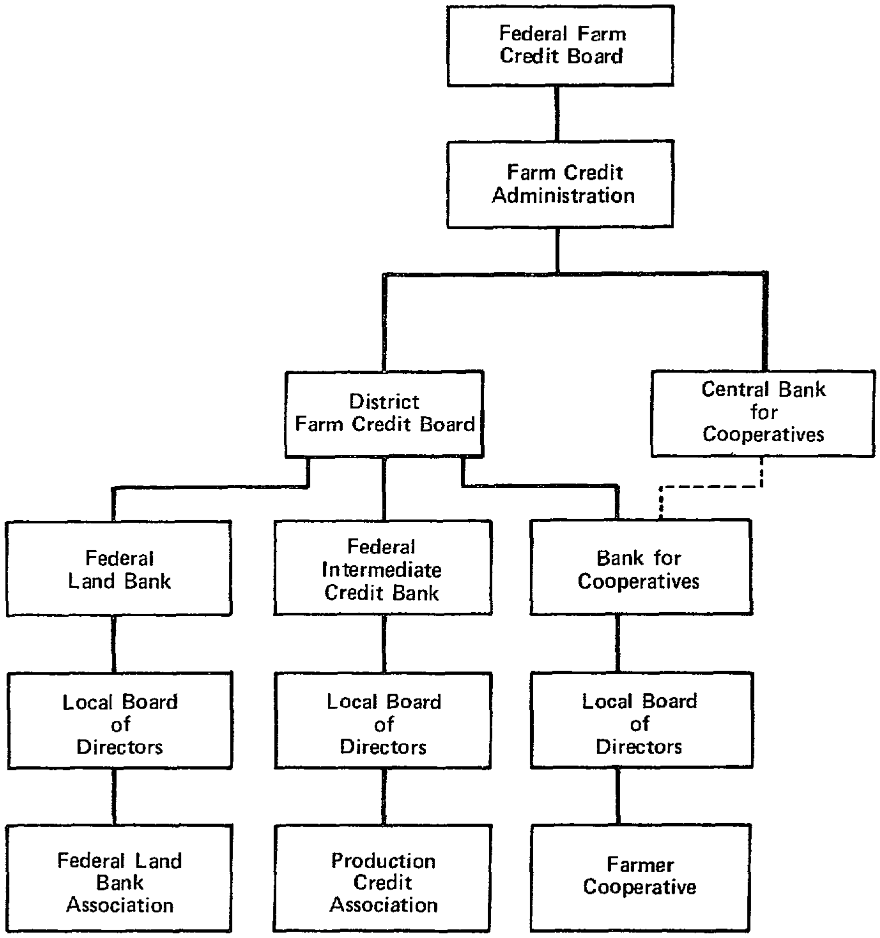
All the "quasi-Federal" plans are administered and maintained by organizations considered to be Federal instrumentalities and, on that basis, have generally been exempted from the provisions of ERISA, which applies only to private employer plans.

Two of the programs were revealed to be employee savings plans rather than retirement programs and, therefore, were eliminated from further review.

Farm credit system

The farm credit system is a network of organizations--Federal land banks and Federal land bank associations, Federal intermediate credit banks and production credit associations, and banks for cooperatives--designed to provide credit to farmers and ranchers. The United States is divided into 12 farm credit districts and at the same location in each district there is a Federal land bank, Federal intermediate credit bank, and a bank for cooperatives.

The Farm Credit Administration, an independent agency in the executive branch, charters and supervises the system's operations. The Federal Farm Credit Board establishes general policies for guidance of the Administration and has responsibility for approving the rules and regulations (including personnel regulations) which govern the operations of the farm credit system. The Board is composed of 13 members, 12 of whom are appointed by the President of the United States, and one appointed by the Secretary of Agriculture to serve as his representative. The following chart depicts their organizational structure.



The organizational structure is the same in all 12 farm credit districts.

There are several local boards of directors, associations, and farmer cooperatives within any given district.

The Farm Credit Administration does not receive any appropriated funds. Its expenses are paid by the institutions under its supervision. However, the Administration is subject to spending limitations passed in annual appropriations bills. The Administration's employees are Federal and are covered by the civil service retirement system.

Development

The farm credit system was created by the Federal Farm Loan Act of 1916. The act provided for the establishment and initial capitalization of the 12 district Federal land banks. The act established local Federal land bank associations through which the land banks make long-term loans secured by first mortgages on farm real estate. In essence, the associations are agents for the 12 Federal land banks. All of the Government capital in the Federal land banks had been repaid by 1947.

The Agricultural Credits Act of 1923 established the 12 district Federal intermediate credit banks. They were organized as banks of discount to provide a permanent and dependable source of funds for institutions making loans to farmers and ranchers. However, they were not very effective during their early years because the primary lenders did not have sufficient capital. To alleviate this problem, the Congress passed the Farm Credit Act of 1933 establishing the production credit associations. The act provided the initial capital and detailed staff to help farmers organize such associations. In effect, the associations are retail outlets for short and intermediate term credit they obtain at wholesale from the Federal intermediate credit banks. In addition, the 1933 act provided for the organization and initial capitalization of 13 banks for cooperatives (one in each of the 12 farm credit districts and a central bank for cooperatives now located in Denver, Colorado). These banks were designed to meet the specialized credit needs of farmers' marketing, supply, and farm business service cooperatives. All the Government capital in the Federal intermediate credit banks, the production credit associations, and the banks for cooperatives has been repaid.

When a Federal land bank or a production credit association grants a loan, the borrower must purchase stock in an amount equal to at least 5 percent of the loan. The farmers and ranchers who share ownership of the system elect the local boards of directors of their associations. Each of the 12 farm credit districts has a seven member district Farm Credit Board. These members also serve as directors of all three banks--Federal land bank, Federal intermediate credit bank, and bank for cooperatives--within the provisions of the law and regulations established by the Farm Credit Administration. The local boards of directors of the Federal land bank associations and production credit associations each elect two of the seven district board members, and the cooperatives which borrow from the banks for cooperatives elect two of the seven members. The seventh member is appointed by the Governor of the Farm Credit Administration with the advice and consent of the Federal Farm Credit Board.

The system obtains most of its loan funds by selling securities to private investors in the Nation's money markets.

The securities are not guaranteed by the Federal Government; however, all sales must be approved by the Governor of the Farm Credit Administration. In 1975, the farm credit institutions loaned more than $27 billion and had a combined net worth of $3.5 billion.

The Federal land banks, the Federal intermediate credit banks, the banks for cooperatives, and, in certain cases, the production credit associations may issue stock which may be purchased by the Farm Credit Administration on behalf of the United States as a temporary investment to help meet emergency credit needs of borrowers.

Retirement coverage

Prior to 1942, farm credit system employees, other than in the Farm Credit Administration, were not covered by a retirement system. However, legislation enacted in 1942 extended civil service retirement system coverage to employees who had previously been denied such coverage because they were not in the classified (competitive) civil service.

The legislative history indicates that, at the time the law was passed, some questions and confusion existed as to which farm credit organizations should be brought under the civil service retirement system. Initially the Civil Service Commission maintained that the retirement system should not apply to employees of the Federal land banks and the banks for cooperatives since virtually all their initial capitalization by the Government had been repaid. About a year later, however, the Commission decided that civil service retirement coverage would be extended to all farm credit banks on the basis that they were controlled by the Government through the high proportion of Government representation on the district boards of directors. At that time, four of the seven district board members were appointed by the Governor of the Farm Credit Administration.

The legislative history does not indicate that consideration was given to extending civil service retirement coverage to employees of the Federal land bank associations and production credit associations. Apparently, these associations were not considered to be controlled by the Government.

The Federal land bank associations and production credit associations are farmer organized for the purpose of borrowing money under the farm credit system. They are controlled by statute, regulations issued by the Farm Credit Administration, or by the Federal land bank or Federal intermediate credit bank in their district. Federal land bank associations act as agents for the Federal land banks in making mortgage loans. Production credit associations make and service their own loans.

From 1942 to 1959, farm credit bank employees continued to participate in the civil service retirement system. However, in 1959, the Congress passed legislation clarifying the status of farm credit banks and their employees. The law designated farm credit bank employees as private and prohibited new employees from participating in the civil service retirement system. Persons employed by the banks at the time the law was enacted were allowed to continue their participation in the civil service system. The law also authorized the districts to establish retirement systems for new employees and extended social security coverage to employees not covered by the civil service system. The Farm Credit Administration was given the responsibility of approving the proposed retirement plans and any changes or amendments thereto.

Each of the 12 farm credit districts has established its own retirement system. Collectively, during fiscal year 1976, the systems covered about 10,500 farm credit bank and association employees, and paid benefits to about 1,200 retired employees and about 100 survivors of former employees or retirees. About 250 bank employees remain covered by the civil service retirement system.

The district retirement systems are individual systems, separately trusted and funded. Benefits under the various plans differ.

--Two districts require employee contributions, others do not.

--Benefit formulas vary widely from district to district.

--Most of the plans contain portability provisions for movement within the farm credit system, others do not.

--The plans have different vesting requirements.

Because of the many retirement formulas and the integration with social security, it is difficult to make comparisons with the civil service retirement system. However, for comparative purposes, assuming a high-3 or high-5 of $15,000 with 30 years of creditable service, the range of normal retirement monthly annuities would be $375 to $630 (plus social security) compared to $703 under the civil service formula. The average farm credit system monthly annuity under the conditions described above would be about $530.

Employee transfers

Other Federal retirement systems do not grant credit for service with farm credit banks and associations and only some of the farm credit retirement systems recognize service performed under other Federal retirement systems. Most of the farm credit retirement systems recognize service performed in another farm credit district.

Reemployed annuitants

Farm credit bank or association annuitants may be employed in other Federal service without a reduction in salary or annuity, and the same is true for a Federal annuitant employed by one of the farm credit banks or associations. Farm credit bank and association annuitants may also be reemployed under the farm credit system without a reduction in salary or annuity under the following rules.

--An annuitant may be reemployed on a temporary basis (not exceeding 1 year) to any position, including a position in which he will assume the full range of duties and responsibilities that he had prior to retirement.

--An annuitant may be reemployed on a permanent basis, provided he does not assume the full range of duties and responsibilities that he had prior to retirement.

ERISA's applicability to the farm credit retirement plans

The Farm Credit Administration applied for and received an exemption from ERISA for the farm credit retirement systems. The exemption letter from the Department of Labor to the Farm Credit Administration stated that each component of the farm credit system is a Federal instrumentality, thus constituting a Governmental entity exempt from ERISA. Farm credit institutions are specifically referred to as Governmental instrumentalities in the Farm Credit Act of 1971. The letter also mentioned further indications that the components of the farm credit system are Federal instrumentalities: the availability of Federal funding, exemptions from Federal, State, and local taxation, and limitations on the ownership of stock. (It should be noted that Production Credit

Associations and Banks for Cooperatives are not exempt from Federal, State, and local taxation.)

Farm credit system employee status

Prior to 1960, the applicability of certain Federal statutes to farm credit bank employees was uncertain. In a December 1955 letter to the Governor of the Farm Credit Administration, the Comptroller General stated

> "* * * it is our considered view that the status of these employees with regard to the applicability of the Federal statutes, * * * should finally be resolved by legislation."

As mentioned earlier, the Congress passed legislation in 1959 which was intended to clarify the status of farm credit bank employees. The act authorized the district farm credit boards and the boards of directors of each bank therein to employ and determine the conditions of employment of its officers and employees, without regard to certain laws. The exempt laws include Federal civil service statutes and all rules, regulations, and orders issued thereunder; the Federal Employees' Compensation Act; the Hatch Act and the Veterans Preference Act; and the Civil Service Retirement Act, except for the bank employees' continuing coverage under the civil service retirement system.

The purpose of the act was to clarify the status of farm credit system employees by designating them private and removing from applicability certain Federal statutes. However, the act also mandated several requirements for the bank to follow which would indicate that the Congress recognized their Federal nature. The act required that district retirement systems be established for employees not covered by the civil service system. The legislative history indicated that the Congress intended that those systems' benefits, together with social security, were to be substantially the same as benefits provided under the civil service system. The act also required the banks to provide their employees with veterans' preference and imposed limitations against political activity substantially similar to that of Federal employees.

Federal Reserve banks

As discussed on page 68, separate provisions of the Federal Reserve retirement system apply to employees of the Federal Reserve banks from those applicable to Federal Reserve Board employees.

Each of the 12 Federal Reserve banks is a Government controlled corporation organized and operated for public service. Federal Reserve banks differ from privately managed banks in that profits are not the object of their operations and in that their shareholders--the member commercial banks of the Federal Reserve System--do not have the rights, powers, and privileges that customarily belong to stockholders of privately managed corporations. Each bank has nine directors, of which six are elected by the member banks and three are designated by the Federal Reserve Board of Governors, which further indicates the public nature of these banks. One of the three directors appointed by the Board is designated as chairman and one as deputy chairman. The chairman, by statute, is designated Federal Reserve Agent and has special responsibilities on behalf of the Board of Governors. In addition, appointments of the president and first vice president of each Federal Reserve bank are subject to the approval of the Board of Governors.

The Federal Reserve banks submit their budgets to the Board for approval. The salaries of all officers and employees of the banks and branches as well as certain other major expenditures are also subject to the Board's approval.

The Board of Governors has delegated to the Federal Reserve banks certain of the Board's supervisory functions, including field examinations of State member banks. Consequently, Federal Reserve bank examiners, who are employees of the Federal Reserve banks, are performing functions substantially identical to those performed by certain Federal employees of the Office of the Comptroller of the Currency and the Federal Deposit Insurance Corporation. The Comptroller of the Currency performs examinations at nationally chartered banks; the Federal Deposit Insurance Corporation examines those insured banks that are not subject to examination by another Federal supervisory agency; and the Federal Reserve banks examine State chartered member banks.

Nearly all of the Federal Reserve System's income is in the form of interest on its holding of Government securities. All Federal Reserve System expenses (including the Board of Governors and the banks) are deducted from this income, and the balance is returned to the Treasury at the end of the year.

Retirement coverage

When the Federal Reserve retirement system was amended in 1944 to provide Board employees benefits comparable to the civil service system (see p. 68), bank employees continued to be covered by the retirement plan previously established in 1934.

The bank plan is quite different from the Board plan and the civil service system. The bank plan does not require employee contributions, and bank employees have also participated in social security since 1951.

Normal retirement benefits are payable under the bank plan at age 60 with 30 years of service or at age 65 with 10 years. Bank employees may retire as early as age 50 with 10 years' service, but their benefits are reduced substantially (up to 60 percent) when they retire early.

Comparative benefits payable to bank, Board, and civil service retirees under various conditions are discussed below. The calculations were based on the following assumptions:

--All retirements were as of December 31, 1976.

--Annual salary at retirement was $15,000.

--Employees received annual pay increases of 4 percent during employment.

--Employees have 30 years of creditable service.

--Bank employees have been covered by social security since 1951.

Selected Retirements

Hypothetical situation	Monthly retirement benefit	Employee cost of retirement benefit	Monthly social security benefit (age 62)	Monthly social security benefit (age 65)	Employee cost of social security benefit
Age 55, retiring under bank plan	$403	$ -	$279	$ -	$7,311
Age 62, retiring under bank plan	537	-	336	-	7,311
Age 65, retiring under bank plan	537	-	-	421	7,311
Age 55 and over, retiring under Board plan and the civil service system	676	17,623	-	-	-

Employee transfers

Service with either the Board of Governors or the banks is creditable and transferable under both the Board and banks' plans. Bank service is not creditable under any other Federal retirement system, and the banks' retirement system does not recognize service performed under other Federal retirement systems.

Reemployed annuitants

Bank plan annuitants reemployed by one of the banks or the Board before age 65 again become members of the retirement system and their pensions terminate. When they subsequently retire, after at least 3 years' additional service, their annuities are recomputed based on their total service. If they are reemployed for less than 3 years, they receive their original retirement benefit plus an additional amount based on their creditable service after return to employment. Bank annuitants may be employed in other Federal service without a reduction in salary or pension, and the same is true for a Federal annuitant employed by one of the banks.

ERISA's applicability to the retirement system

In 1974, counsel for the retirement plan requested a determination from the Internal Revenue Service, the Department of Labor, and the Pension Benefit Guaranty Corporation that ERISA did not apply to their system. The request was approved in a letter from the Internal Revenue Service dated March 23, 1976. It stated, among other things, that the plan constitutes a governmental plan within the meaning of section 414(d) of the Internal Revenue Code and is exempt from the provisions of ERISA to the extent that governmental plans are exempt. The letter noted that the matter had been discussed with the Office of Employee Benefits Security, Department of Labor, and the Office concurred in the determination.

Savings association retirement fund

Certain organizations of the Federal home loan bank system are covered by a retirement plan known as the savings association retirement fund.

The system operates under the control of the Federal Home Loan Bank Board, an independent Federal agency. The Bank Board is also the operating head of the Federal Savings and Loan Insurance Corporation (FSLIC). The Board's control is of much more than a regulatory nature. It issues all rules and regulations under which the 12 Federal home loan banks and FSLIC are required to operate, reviews and approves the banks' budget, approves the selection of the banks' presidents and establishes their salaries, and audits the operations. In addition, the Board has the power to suspend or remove any director, officer, employee, or agent of any home loan bank. The Board's expenses are paid by assessments against the banks and FSLIC, and charges against institutions examined by its Office of Examinations and Supervision. Board and FSLIC employees are Federal and are covered by the civil service retirement system. Employees of the banks have both Federal and private characteristics, and are covered by the saving association retirement fund. Other employees, such as Federal savings and loan association employees, are also permitted to participate in the system.

Development of the Federal home loan banks

The home loan banks were created by the Home Loan Bank Act of 1932 as Federal instrumentalities to implement the responsibility of the Congress and the Board in the fields of saving and housing finance. The banks are exempt from Federal, State, and local taxation, and operate outside the control of State and local governments. In 1952, the Ninth Circuit Court of Appeals upheld the public status of these banks, stating that although they are operated under delimited private management, the institutions do not possess the purely inherent characteristics and attributes of private corporate business enterprises.

The home loan banks are financial institutions whose main function is to supply their members, principally savings and loan associations and savings banks, with credit and to support their role as savings institutions and home mortgage lenders. The principal source of funds for lending is the public sale of consolidated bank obligations. The obligations are not guaranteed by the United States even though the banks are Federal instrumentalities. However, in case of need, the Secretary of the Treasury is authorized to purchase consolidated bond obligations up to an aggregate amount of $4 billion outstanding at any one time.

Operating expenses of the banks are paid from their own income and are not included in the budget of the United States.

Retirement coverage

From 1932 to 1943 Federal home loan bank employees were not covered by a retirement system. However, in December 1943, the banks established the savings associations retirement fund, as a pension trust to provide retirement coverage for their employees. Commercial institutions within the Federal home loan bank system, unlike member banks within the Federal Reserve system, are permitted to participate in the retirement system.

The Social Security Amendments of 1956 provided social security coverage for Federal home loan bank employees on the condition that their retirement system be coordinated with the social security program and that the coordination plan be approved by the Secretary of HEW. When plans were submitted, they were disapproved because they gave each bank a choice as to whether or not to participate in social security. In 1957, the banks withdrew their plans because they would not all agree to social security coverage. However, such coverage was extended to Bank employees by the Social Security Amendments of 1972. The coverage was made retroactive to 1967, provided that the employees and employers paid an amount equal to the taxes that would have been imposed during the period.

The savings associations retirement fund offers the participating organizations a choice of two overall programs, each with various options. The "comprehensive program" provides retirement and death benefits independent of social security, and the "coordinated program" provides benefits integrated with social security. All 12 Federal home loan banks participate in the comprehensive program and have selected the "no employee contribution" option.

Under the other options selected by most of the 12 banks, the retirement benefit formula is 2 percent multiplied by high-3 multiplied by years of creditable service. This results in a higher normal retirement annuity, even without considering social security, than under the civil service system. However, the plan has substantial reductions for retirements before age 65. For example, an individual can retire with an immediate annuity as early as age 45 with 5 years of creditable service, but the annuity is reduced by 70 percent. Retirees at age 55 receive a 30-percent reduction.

Employee transfers

Federal home loan bank service is not creditable under any other Federal retirement system, and the banks do not recognize service performed under other Federal retirement systems except for Federal Home Loan Bank service performed under the civil service system. Employees retiring from one of the banks with prior Board service may receive a retirement supplement in addition to any benefits to which they are otherwise entitled. The supplement is designed to partially compensate the retiree for not being covered by the savings associations retirement fund during both Board and bank service. Officials of the Board met with Department of Justice and Civil Service Commission officials to see if a similar supplement could be paid (by the banks) to Board retirees with bank service, but at the time of our review a decision on the matter had not been reached.

Reemployed annuitants

Federal home loan bank annuitants may be employed in other Federal service without a reduction in salary or annuity, and the same is true for a Federal annuitant employed by one of the banks. Bank annuitants may also be reemployed by one of the banks without a reduction in salary or annuity; however, it is the general policy of the banks not to reemploy annuitants unless it is absolutely necessary.

ERISA's applicability to
the retirement system

The savings association retirement fund was denied an exemption from ERISA because the plan is maintained by more than one employer, some of whom are not governmental entities. The retirement plan is maintained by the Federal home loan banks, the Office of Finance, and savings and loan associations and other similar institutions. All employer contributions are commingled, and all amounts payable by the retirement plan are a general charge upon all assets of the fund.

An exemption from ERISA would have probably been granted if the savings and loan associations and other similar institutions were not participating in the retirement plan. Without these institutions' participation, the reasons cited by the Department of Labor for granting an exemption to the farm credit district's retirement systems would also apply to the savings association retirement fund. (See p. 115.) The cited reasons were:

--The retirement system is maintained by Federal instrumentalities for their employees.

--The instrumentalities are exempt from Federal, State, and local taxation.

--Limitations are placed on stock ownership.

--Federal funding is available in case of need.

PRIVATELY ADMINISTERED RETIREMENT PLANS

Certain employees of the Smithsonian Institution, the Department of Agriculture Graduate School, and the Uniformed Services University of the Health Sciences are covered by social security and by retirement plans administered by the Teachers Insurance and Annuity Association-College Retirement Equities Fund (TIAA-CREF). TIAA is a private nonprofit company organized in 1918 to provide retirement and insurance plans for educational institutions and their staffs. Participation in TIAA retirement plans is limited to colleges, universities, private schools, and certain other nonprofit educational and research institutions. CREF, established in 1952, is a companion organization and also has nonprofit status.

The basic features of TIAA-CREF retirement plans are as follows:

Participation--

Participation requirements are established by the employer.

Contributions--

The level of contributions, as a percentage of salary, and the extent to which they are shared between employer and employee are determined by the employer. Contributions vary from plans where employer and employee each contribute 5 percent of salary to plans where the employer contributes 15 percent or more of salary and the employee contributes nothing. Contributions are used to purchase fixed and/or variable TIAA-CREF annuity contracts.

Vesting--

Full and immediate vesting of all benefits. The participant owns all retirement and survivor benefits, including those purchased by employer contributions. Generally, however, annuity contracts may not be surrendered for cash.

Retirement benefits--

Participants have the right to retire at any age and begin receiving an annuity under any of several options. TIAA provides fixed-dollar annuities, and CREF provides variable annuities. The amount of an individual's retirement annuity varies depending upon sex, age at time of retirement, accumulated contributions, and, in the case of CREF variable annuities, the market value of all securities in the CREF fund.

Disability benefits--

No special disability benefits are provided. However, as mentioned above, a participant may begin receiving retirement benefits at any age. Additionally, TIAA offers group disability insurance plans which may be coordinated with an employer's retirement plan.

Death benefits--

If a participant dies before retirement, the full current value of his TIAA-CREF accumulations, including all employer contributions and all investment earnings, is payable to his designated beneficiary. Several payment options are available. Depending upon the annuity option elected by a participant at time of retirement, benefits may also be provided to the survivors of a deceased retiree.

Although the TIAA-CREF plans covered by our study are privately administered, we examined why personnel covered by these plans are not covered by a Federal retirement system and why TIAA-CREF was selected by their employers to provide retirement benefits.

Smithsonian Institution

The Smithsonian Institution was established by the Congress in 1846 to carry out the trust obligation of the United States to administer James Smithson's bequest for the "increase and diffusion of knowledge among men." About 90 percent of the Institution's operating funds come from the Government--80 percent by direct appropriation and 10 percent from Federal grants. Its remaining financial support is provided by trust funds accumulated through private contributions.

The Smithsonian has approximately 4,950 employees, 3,635 of whom are paid with Federal funds and 1,315 with private funds. Personnel on the Smithsonian's Federal payroll are covered by the civil service retirement system and may participate in the Government's health and life insurance programs. On the other hand, the Civil Service Commission determined in 1970 that, except for certain special status individuals, personnel paid from the Smithsonian's private funds are not considered to be Federal employees and, therefore, not entitled to civil service retirement coverage or Government health and life insurance protection. They are, however, covered by the Federal Employees Compensation Act (workers compensation) and social security, and participate in a TIAA-CREF retirement plan.

Employment status of private roll employees

The question of whether or not personnel paid from the Smithsonian's private funds are Federal employees, subject to civil service laws, has a long history. Apparently, from 1895 to 1947, such personnel were not regarded as Federal employees. In 1928, the First Assistant Secretary of the Interior (responsible at that time for administration of the civil service retirement law) ruled that employees paid from the Institution's private funds could not be covered by the civil service retirement system because they were not employees of the U.S. Government. This ruling was followed by the Civil Service Commission until 1942, when coverage under the retirement system was greatly expanded to include all Federal and District of Columbia employees, except those specifically excluded by statute or Executive order. At this time, the Commission's Retirement Division reviewed the employment status of the Smithsonian's private roll personnel, but took no action because the Secretary of the Institution was opposed to placing such employees under the retirement system.

In 1945, a new Secretary of the Smithsonian took office, and in 1947 requested that the Commission extend retirement coverage to the Institution's then 35 private roll employees. The Commission approved the request based on a determination that such personnel should be considered Federal employees because they met the test of Federal employment. That is, they were (1) engaged in the performance of a Federal function under authority of an act of Congress, (2) appointed or employed by a Federal officer, and (3) under the supervision and direction of a Federal officer. However, subsequent to this action, a question arose regarding the applicability of other Federal personnel laws to trust fund employees. Debate over this issue and the need for legislation clarifying the employment status of such employees continued until 1970.

At that time, the Commission confirmed the retirement rights which had been granted trust fund employees, and the Smithsonian agreed to terminate its practice of extending civil service retirement coverage to future trust fund employees. Specifically, the Commission and the Smithsonian agreed that (1) personnel paid from the Institution's trust funds who were employed on or after March 2, 1970, would not be appointed as Federal employees and (2) the civil service retirement and insurance coverage extended such individuals employed before March 2, 1970, would continue. There were approximately 32 private roll employees in this latter category at the time of the Commission's ruling, including the Secretary of the Institution. As of June 1978, 8 of these special status employees remained on the Smithsonian's rolls.

According to the Commission's records, the decision that the Smithsonian's private roll personnel are not Federal employees was based on the proposition that (1) the Congress created the Institution as a private corporation to administer the Smithson trust and (2) in the administration of the trust funds the Institution is not acting as an agency of the United States and is not performing a Federal function.

Positions taken by GAO on other aspects of the Smithsonian's operations and functions have tended to reinforce the Commission's decision. In an August 2, 1974, letter (B-167068) to the Chairman of the Subcommittee on Buildings and Grounds, Senate Committee on Public Works, we concluded that an assumption that the Smithsonian is a Federal agency or institution cannot be supported. Also, in a September 4, 1975, letter (B-184705) to the Chairman of the Senate Committee on Rules and Administration, we reported that Smithsonian employees paid from trust funds may be authorized and/or directed to undertake activities that would be inappropriate if performed by Government employees in Government agencies.

In contrast to its decision on the Smithsonian, the Commission has determined that employees paid from trust funds administered by the National Gallery of Art and the John F. Kennedy Center for the Performing Arts are covered by the civil service retirement system. Such employees are not, however, subject to other civil service laws generally applicable to Federal employees. Both the National Gallery and the Kennedy Center were established by the Congress as bureaus of the Smithsonian Institution, but each has its own board of trustees, operates independently of the Institution, and establishes employees' compensation separately from that paid to Smithsonian personnel.

Employment policies and practices

There are no specific criteria differentiating between Federal and trust fund employment at the Smithsonian. According to Smithsonian officials, the determination as to whether an employee will be placed on their Federal or trust fund payroll generally depends on such factors as the source and availability of funds and Federal personnel ceilings. For example, the Institution's Museum of Natural History is predominantly federally funded and the majority of the employees are on the Federal payroll. In contrast, the Freer Gallery of Art is primarily supported by the Smithsonian's trust funds and its employees are, for the most part, on the trust fund payroll.

In the administrative area there is a mixture of Federal and trust fund employees, who are engaged in activities supported by both Federal and trust funds. Additionally, administrative employees often have the option of being employed in a Federal or non-Federal status. Thus, actual duties performed have little or no bearing on whether an employee will be considered Federal or non-Federal.

In examining the Smithsonian's employment records for the first 9 months of 1976, we found 35 employees had switched from the Federal to the trust fund payroll and the exact number of trust fund employees had switched to the Federal payroll with corresponding changes in retirement program coverage. The majority of these switches involved no change in either salary rates or job classifications and Smithsonian officials could not explain why they had occurred.

Reasons for selecting TIAA-CREF

In 1977, the Institution's TIAA-CREF retirement plan covered approximately 593 of its 1,315 trust fund employees. The remaining 722 employees were not covered by the plan either because they had not yet met the minimum service requirements, were part-time employees, or were under age 30 and had not elected to participate.

According to Smithsonian officials, the primary reason TIAA-CREF was selected for its trust fund employees was because its portability features help the Institution attract university and research-oriented personnel from academic institutions having TIAA-CREF plans.

However, we were also told that only about 30 of the 593 trust fund employees participating in the Institution's retirement plan were covered by a TIAA-CREF plan prior to coming to the Smithsonian, but it was expected that many more would retain their coverage after leaving the Institution.

Another reason given for selecting TIAA-CREF was to establish comparability of retirement programs for Federal and trust fund employees. According to Smithsonian officials, their TIAA-CREF plan, combined with social security, is comparable to the civil service retirement system, both in terms of benefits and cost.

It is difficult to compare benefits between a TIAA-CREF plan and the civil service system. TIAA-CREF is a "defined contribution plan," meaning that the benefits received are based solely on the amount of contributions made during an employee's employment. Benefits are determined on an individual, actuarial basis. The civil service system is a "defined benefit plan" with benefit amounts dependent on salary and years of service. Moreover, under a TIAA-CREF plan, a participant may allocate both his and/or his employer's contributions between TIAA and CREF, with the former providing a fixed annuity and the latter a variable annuity. Also, unlike the civil service system, TIAA-CREF plans provide no minimum benefits in the event a participant becomes disabled or dies before retirement. However, Smithsonian trust fund employees are covered by social security and may participate in a TIAA total disability insurance plan, the cost of which is paid in full by the Institution.

With respect to cost, the Smithsonian annually contributes to TIAA-CREF approximately 11 percent of an employee's salary up to the social security covered earnings base (currently $17,700) and 10 percent of salary in excess of this amount. Employees contribute approximately 1 percent of salary up to the social security base and 7 percent thereafter. Additionally, under social security both contribute 6.05 percent of covered earnings. In contrast, under the civil service system, agencies and employees each contribute only 7 percent of salary to the civil service retirement fund. These contributions do not, however, represent that system's "dynamic normal cost." (See pp. 154 and 155.)

It seems that the combination of TIAA-CREF and social security, including the latter's tax free aspects, provide the Smithsonian trust fund employees better benefits than those received by employees under the civil service retirement system.

Reemployed annuitants

Retired military personnel and civil service annuitants may be reemployed on the Smithsonian's trust fund rolls without any reduction in either their annuities or salaries. However, if such personnel are reemployed and paid from the Smithsonian's Federal funds, their annuities or salaries are subject to reductions, as they would be if reemployed by a Federal agency.

In December 1976, Smithsonian officials estimated they had approximately 144 retired military personnel and 10 civil service annuitants on their Federal and trust fund rolls. According to the officials, data was not available on how many of the retirees were being paid from Federal funds and how many from trust funds, but they did state that a manual count indicated at least eight civil service retirees were on the trust fund payroll.

U.S. Department of Agriculture Graduate School

The Graduate School was established by the Secretary of Agriculture in 1921 under the same statutory authority that established the Department of Agriculture. The objective of the School is to improve Government services by providing needed educational opportunities for Federal employees. The School operates on a self-supporting basis primarily from tuition fees and receives no direct Government appropriations.

Employment status

The School employs approximately 886 persons, 69 full time administrative personnel, and 817 part time faculty and committee members. Although the School recognizes itself as a Government instrumentality, it does not consider its personnel to be Federal employees. There are, however, certain facts which would seem to indicate that such personnel could be considered Federal employees. Section 2105 of title 5, United States Code, defines a Federal employee as any individual who (1) is appointed by a Federal officer or employee, (2) is engaged in the performance of a Federal function under authority of law or an Executive act, and

(3) is subject to the supervision of a Federal officer or employee. A test of the employment status of Graduate School personnel against these three criteria revealed the following:

Appointment

The Secretary of Agriculture, a Federal officer, appoints all 15 members of the School's General Administration Board. At least eight members must be employees of the Department of Agriculture. Pursuant to regulations promulgated by the Secretary, the Board is responsible for directing and controlling the School's business affairs and for selecting and appointing all officers of the School, including a Director, Deputy Director, and Assistant Directors as needed. In turn, the Director selects and appoints all agents and employees of the School in accordance with regulations and directives issued by the Board.

Federal function

The Graduate School was established under the same statutory authority which established the Department of Agriculture and gave it the responsibility to "disseminate agriculture information in the broadest sense of the word." The School is considered a non-appropriated fund activity of the Department of Agriculture.

Supervision

The Secretary's regulations governing the Graduate School state, in part, that the School is ". . . under the general supervision and direction of the Department of Agriculture."

We also noted that the Graduate School's bylaws require the General Administration Board, in making regulations concerning the selection and appointment, duties, compensation, and benefits of School employees, to generally parallel the practices and procedures applicable to Federal employees subject to laws administered by the Civil Service Commission.

Why TIAA-CREF was selected

The TIAA-CREF retirement plan selected by the School requires contributions of 21 percent of salary--15 percent by the School and 6 percent by participating employees. In adopting the plan, the School's objective was to provide its full-time employees retirement annuities comparable to those provided under the civil service retirement system for equal periods of service. The School's faculty members are employed on a part-time basis and do not participate in the plan. The following table (obtained from the School) compares retirement annuities, as a percentage of an individual's high 3 years' average salary, provided by the two systems. The annuities shown under the Graduate School's TIAA plan are based on a male participant retiring at age 60 after the indicated number of years of service. In addition, School employees also participate in social security.

	Annuity as a percentage of high-3 average salary	
Years of service	Graduate School	Civil service system
30	56.7	56.25
25	48.7	46.25
20	40.0	36.25
15	30.8	26.25
10	21.2	16.25
5	10.9	7.50

While the Graduate School's retirement plan may provide an initial retirement annuity comparable to that provided under the civil service system, it does not provide any special survivor or disability benefits. However, such benefits are provided by social security and (after 1 year of full-time employment) by the School's TIAA total disability insurance plan.

In addition to its contributions to the TIAA-CREF retirement plan, the School contributes 6.05 percent of each employee's salary up to $17,700 to social security and pays the full cost of the disability insurance plan. The disability insurance premium is approximately $34 a year for an employee who does not participate in the School's retirement plan, and about $72 a year for employees who participate in the plan. The difference in premium rates occurs because, in addition to paying a disability annuity, the insurance plan will continue to contribute to the School's retirement plan 21 percent of a disabled employee's former salary. The contributions continue until the disabled annuitant dies or reaches age 65, whichever occurs first.

Based on the foregoing, it is clear that the combined benefits of the School's TIAA-CREF retirement and disability insurance plans plus social security are greater than those under the civil service retirement system.

Reemployed annuitants

Retired civil service and military personnel who are reemployed by the Graduate School receive no reduction in either their annuities or salaries. At the time of our review, there was only one civil service retiree employed full time by the School.

Also, we could find no requirement for reducing either the annuities or salaries of retired Graduate School personnel who are reemployed by a Federal agency.

Uniformed Services University of the Health Sciences

The University of the Health Sciences was established by the Congress in 1972, within the Department of Defense, to educate career-oriented health professionals for the military services and the Public Health Service. At the time of our review, the University operated as a medical school for training physicians, but consideration was being given to incorporating other health disciplines. There were 99 students enrolled at the school as of February 1978.

The University is managed by a Board of Regents and supported totally with appropriated funds. The school employs a faculty of 23 military and 65 civilian members, and an administrative staff of 139 civilian and 17 military personnel.

There are three retirement systems at the University. Military personnel are covered by the uniformed services retirement system; civilian administrative employees by the civil service system; and civilian faculty members by a TIAA-CREF retirement plan. Additionally, all personnel, except civilian administrative employees, are covered by social security. The following table shows the number of University personnel covered by each retirement system as of December 31, 1977.

Uniformed services	40
Civil service	139
TIAA-CREF	50
	229

Why TIAA-CREF was selected

The legislation establishing the University required that civilian faculty members and administrative employees be provided retirement and other related benefits comparable to those received by employees of health profession schools in the Washington, D.C., area. While the legislative history does not indicate the reason for this requirement, it presumably was intended to aid in recruiting personnel. In contrast, however, we noted that the civilian faculties of two other schools operated by the Department of Defense--the United States Naval Academy and the United States Naval Postgraduate School--are covered by the civil service retirement system.

In complying with the statutory requirement, the University surveyed retirement plans at eight universities and colleges in the District of Columbia and surrounding area. Based on the survey, the University adopted a TIAA-CREF retirement plan for its full-time civilian faculty members and established employer and employee contribution rates (as a percentage of each participant's annual salary) of 10 percent and 5 percent, respectively. Civilian administrative employees were excluded from participating in the plan, apparently because it was assumed that most such personnel would be career civil servants either hired from civil service registers or coming to the school from other Government positions. Therefore, it was considered appropriate for them to be covered by the civil service retirement system. We noted, however, that most of the schools surveyed which had TIAA-CREF retirement plans extended coverage to both faculty members and administrative employees.

Participation in the plan is mandatory for all civilian faculty members upon employment, with two exceptions. Participation is elective for teaching research assistants during their first 4 years of employment, and mandatory thereafter. Civilian faculty members who transfer to the University from Government positions in which they were covered by the civil service retirement system automatically retain civil service coverage if their break in service does not exceed 3 days.

As with other TIAA-CREF plans, no special disability benefits are provided under the University's retirement plan. However, civilian faculty members must participate in the University's TIAA group disability insurance plan. The plan's premium costs are shared equally between the University and participants.

Reemployed annuitants

Federal, military, and civilian retirees reemployed by the University in either an administrative or faculty position are subject to the same laws regarding reductions in salaries and annuities as they would be if reemployed by any Government agency. On the other hand, we could find no requirement for the reduction in either the salary or annuity of an individual reemployed by a Federal agency who has retired under the University's TIAA-CREF retirement plan.

CLOSED RETIREMENT SYSTEMS

Three of the retirement programs included in our review--Panama Canal construction service annuity, Federal lighthouse retirement system, and Panama Canal Zone cash relief program--are "closed systems," that is, no new employees may participate. When all existing retirees and surviving beneficiaries are deceased, the systems will terminate. As discussed below, all three systems are small and rapidly diminishing.

Panama Canal Zone cash relief program

During the period when construction work on the Panama Canal was in progress, many workers for the project were recruited by the Government in the West Indies and adjacent areas. As non-U.S. citizens, these canal employees were not eligible for benefits under existing Federal retirement systems. In recognition of this fact, the Congress enacted legislation in 1937 which provided for cash relief payments to be made to disabled employees who had completed at least 10 years of employment.

The original cash relief payment amounted to $1 a month for each year's service, with a maximum of $25 a month. Increases were granted from time to time, and in 1970, legislation was enacted which provided for future cost of living increases equal to the adjustments granted to civil service system retirees. The law also authorized survivor benefits for widows of former employees with 10 years' service at a rate not to exceed 50 percent of the amount their husbands would receive if still living.

A 1958 law closed the Panama Canal cash relief system to new participants and extended civil service retirement coverage to non-U.S. citizen employees of the Canal Zone Government and the Panama Canal Company. As of May 1978, 1,776 beneficiaries (711 retirees and 1,065 widows) were receiving cash relief payments. The payments averaged $100 a month to retirees and $52 a month to survivors.

<u>Panama Canal construction service annuity</u>

In 1915, the Congress enacted legislation which (1) thanked the six Army and Navy members of the Isthmian Canal Commission for their services in connection with the construction of the Panama Canal and authorized their advancement in rank, (2) provided that other officers of the Army and Navy who had been detailed for duty with the Isthmian Canal Commission for more than 3 years should be advanced one grade in rank with the privilege of immediate retirement at 75 percent of pay for the retiring rank, and (3) authorized the advancement by one grade of all U.S. Public Health Service officers who had been detailed for duty with the Isthmian Canal Commission for more than 3 years.

The 1915 law provided no similar recognition or reward for American civilian employees who had been engaged in the construction of the Canal. But legislation was enacted in 1944 to correct this inequity. This legislation provided that each American civilian employed by the Isthmian Canal Commission or the Panama Railroad Company on the Isthmus of Panama for 3 years or more during the construction period (May 4, 1904, to Mar. 31, 1914) was entitled to an annuity for the remainder of his life as follows:

--40 percent of his average annual basic pay, if such service was for as much as 3 years and not more than 4 years.

--50 percent of his average annual basic pay, if such service was for more than 4 years and not exceeding 6 years.

--60 percent of his average annual basic pay, if such service was for more than 6 years.

The law also provided for a survivor annuity to be paid widows of deceased annuitants and widows of deceased former employees who would have been eligible for an annuity had they been living at the time the legislation was passed. The amount of the widow's annuity was the same as the employee's annuity.

In 1956, the annuities were increased by $25 a month, or 25 percent, whichever was less, but no annuity was increased beyond $180 a month. These annuitants do not receive automatic cost of living adjustments as under most other Federal retirement systems, and there have been no legislated increases since 1956.

At the end of fiscal year 1975, there were 437 annuitants on the rolls. It is estimated that, by the end of fiscal year 1978, that number will be reduced to 256, a 41 percent reduction.

Federal lighthouse retirement system

The origin of the Lighthouse Service as a unit of the United States Government can be traced back to August 7, 1789, when the Congress made the first provision for any public work. The Lighthouse Service was placed under the authority of the Secretary of the Treasury and remained there until 1903. The Department of Commerce and Labor was established at that time, and the Lighthouse Service was placed under its jurisdiction. Later, the Department of Labor was created, and the Department of Commerce and Labor became the Department of Commerce and retained jurisdiction over the Lighthouse Service.

Prior to 1918, there was no provision for retiring the employees of the Lighthouse Service. But in June 1918--2 years before establishment of the civil service retirement system--the Congress created the Federal lighthouse retirement system. The law provided that officers and employees who were engaged in the field service or on vessels of the Lighthouse Service, when reaching age 65 after having completed 30 years of Government service, could retire at their option, and those employees reaching age 70 would be mandatorily retired, regardless of length of service.

Employees meeting these requirements received an annuity equal to one-fortieth of their average annual pay for their last 5 years of service multiplied by their years of service with the Lighthouse Service or in a department or branch of the Government having a retirement system. The annuity could not exceed 75 percent of such average annual pay.

The Lighthouse Service was merged with the Coast Guard in 1939, and at that time provisions were made for the gradual replacement of the civilian personnel in the Lighthouse Service by Coast Guard personnel. The officers and employees of the Lighthouse Service were given the option of obtaining a military rank or retaining their civilian status in the Coast Guard and continuing their coverage under the lighthouse retirement system.

In 1955, the age and service requirements for optional retirement under the lighthouse system were lowered to age 60 with 30 years' service or age 62 with 25 years. In 1967, the age requirement for optional retirement was further lowered to age 55.

The annuities for lighthouse system retirees were increased from time to time, and in 1967 the Congress enacted legislation which provided that annuities would be increased by the same cost of living adjustment percentages as granted under the civil service system. The U.S. Coast Guard administers the retirement system, and benefits are paid from annual appropriations.

In 1950, the Congress added a survivorship provision to the system which provided benefits of $50 a month to widows of former civilian employees of the Lighthouse Service. This amount was based on comparable benefits accorded certain survivors under the civil service system in 1948.

The widows' benefit was increased to $75 a month in 1958, and to $100 a month in 1967. Since 1967, cost of living adjustments equal to those under the civil service system have been granted. The benefits were also increased by an additional $26 in 1975. The Civil Service Commission administers the survivorship portion of the retirement plan.

As of June 30, 1975, there were 295 former lighthouse personnel and 332 widows of former lighthouse personnel on the retirement rolls.

FEDERAL EMPLOYEES COVERED BY THE DISTRICT OF COLUMBIA POLICE AND FIREMEN'S RETIREMENT SYSTEM

About 1,500 Federal law enforcement personnel of the Executive Protective Service, 1/ Park Police, and Secret Service participate in a retirement system designed for municipal police and firemen of the District of Columbia. The system is administered by the District, and in general provides much better benefits than federally administered and controlled retirement systems. Also, personnel covered by the District system contribute less toward the cost of their retirement benefits than protective services personnel covered by the Federal civil service retirement system.

In general, the Federal personnel were extended coverage under the District system by laws enacted in the 1920s and 1940s because they were transferred from the District police force or were doing jobs formerly done by the District police.

Executive Protective Service

The Executive Protective Service, called the White House Police until 1970, was established in 1922 to provide a Federal police force, under the control of the President and the direct supervision of an officer designated by him, to guard the White House and grounds. Prior to 1922, the White House was protected by the District police.

The 1922 law specified that Executive Protective Service personnel were to be appointed by the President from lists provided by the District police and the Park Police. Vacancies were to be filled in the same manner. To avoid transfer inequities, Executive Protective Service personnel were allowed to remain in the District's police and firemen's retirement system.

The appointment restrictions were later repealed and, since 1970, the Executive Protective Service has recruited nationwide.

1/By Public Law 95-179, approved Nov. 15, 1977, the name of the Executive Protective Service was changed to the United States Secret Service Uniformed Division. For purposes of simplicity and ease of understanding, retirement coverage of the former Executive Protective Service is discussed separately.

The Executive Protective Service has about 850 employees covered by the District retirement system.

U.S. Park Police

The U.S. Park Police dates back to about 1800 but did not receive its current name until 1919. Park Police were covered by the civil service retirement system from its inception in 1920 to 1924. A 1924 law removed members of the force from the civil service system and placed them in the District retirement system. The act's legislative history does not state why Park Police were included under the District system; however, it seems to have been to avoid transfer inequities between the District and Park Police forces.

About 540 Park Police are covered by the District retirement system. Most are located in the Washington, D.C., area, but 90 are stationed at field locations, mainly New York City and San Francisco. Park Police recruiting efforts are concentrated in the New York area.

Park Rangers, whose duties include law enforcement, and who, in some areas, work side by side with Park Police, are covered by the civil service retirement system. Organizationally, both the Park Police and Park Rangers are under the Department of the Interior.

Secret Service

A 1940 law permits nonclerical employees of the Secret Service who have 10 years' service directly related to protecting the President of the United States to elect coverage under the District retirement system. The law was amended in 1964 to allow credit for periods of prior service with the District police, Park Police, or Executive Protective Service toward the required 10 years of service.

The legislative history of the 1964 amendment indicates that Secret Service agents assigned to protect the President were generally recruited from the Executive Protective Service and District police force. The legislative history also indicated that the Secret Service was having difficulty recruiting personnel. Executive Protective Service and District police were reluctant to transfer to the Secret Service because they would be placed under the less generous provisions of the civil service system until they satisfied the 10-year requirement.

The Secret Service no longer concentrates its recruiting efforts on employees of the Executive Protective Service and the District's police force, but recruits on a nationwide basis. Further, in 1973, the criteria eligibility for participation in the District retirement system were changed to include positions other than special agents. The new criteria include certain special officers and security specialists assigned part-time to the protection of the President.

About 130 Secret Service agents participate in the District system. Other agents are covered by the special early retirement provisions of the civil service system.

Retirement benefits

Amendments to the District's police and firemen's retirement system have established it as one of the most liberal in the United States. A study by the Maxwell School of Citizenship and Public Affairs, Syracuse University, compared the pension benefits of public employees in nine major U.S. cities and found the benefits provided to District police and firemen to be the best in many respects.

Even the special early retirement provisions of the civil service retirement system, which cover most Federal law enforcement personnel (see p. 141), are less generous than the benefits provided under the District's police and firemen's retirement system.

Permitting certain groups of Federal employees to participate in the District retirement system creates inequities between these employees and other Federal personnel. The majority of Federal employees covered by the District retirement system would not meet the qualifications for coverage under the special early retirement provisions of the civil service system. According to the Civil Service Commission, Secret Service agents would qualify for the special retirement provisions; however, Executive Protective Service and Park Police employees would not, with the possible exception of investigators in the Criminal Investigations Branch of the Park Police.

Another inequitable situation exists. Federal employees who retire under the District's police and firemen's retirement system may be reemployed in a position covered by the civil service retirement system without receiving a reduction in either salary or annuity. For example, recently a former Federal employee who retired under the

Optional retirement	District police and firemen retirement system	Special provisions of the civil service retirement system
Minimum requirements	Age--none; service--20 years	Age--50; service--20 years
Benefit formula	2-1/2 percent of average pay (last 12 months' salary) multiplied by years of service not exceeding 20 plus 3 percent of average pay multiplied by years of service exceeding 20.	2-1/2 percent of high 3 year average pay multiplied by years of service not exceeding 20 plus 2 percent of high 3 average pay multiplied by all service over 20 years.
Annuity adjustments	Annuities are automatically adjusted whenever there is an increase in salary for policemen and firemen in active service. The increase will be the same percentage increase as the active force receives.	Annuities are adjusted semiannually based on the percentage increase in the CPI during the preceding 6-month period.
Employee contributions	7 percent of basic salary.	7-1/2 percent of basic salary.

District's police and firemen retirement system was reemployed in a position covered under the civil service system and is receiving a full salary of about $47,000 and a full annuity of about $18,000 a year. In contrast, a civil service retiree who is reemployed in a civil service position would have his salary reduced by the amount of his civil service annuity.

We believe the Federal Government should control these Federal protective services employees' compensation so that it is equitable, affordable, and consistent with that provided to other Federal law enforcement personnel. In an earlier report (Federal and District of Columbia Employees Need To Be In Separate Pay And Benefit Systems, FPCD-77-71, Jan. 12, 1978), we recommended that the Congress enact legislation making all new protective services employees of the Executive Protective Service, Park Police, and Secret Service subject to Federal pay and retirement systems. We also recommended that the Civil Service Commission and others study and report to the Congress on the desirability and feasibility of transferring existing Federal employees now covered by the District's police and firemen's retirement system to the Federal civil service retirement system. At the time of our review, no action had been taken on these recommendations.

CONCLUSIONS

Federal retirement systems are a hodgepodge of inconsistencies and inequities. Because they have evolved over many years without the benefit of overall policy guidance, it is difficult to clearly identify any Federal management or compensation policies that are being served by the systems as they are now designed.

All the retirement systems have the same basic objectives--to provide employees a continuing income after completion of active service or upon becoming disabled and to provide financial protection to survivors upon the death of employees and retirees. Moreover, most personnel are covered by either the uniformed services or the civil service retirement systems, even though numerous other smaller systems exist.

We believe an overall retirement policy could be broad enough to accommodate the needs of all Federal personnel. For example, we are convinced that the very costly "20-year retirement at any age" provision is not needed for most uniformed services personnel. However, if the military services continue to see a need to remove certain personnel through the "up or out" system, an overall retirement policy could provide for such a need through early or involuntary retirement provisions that would be applicable to all covered personnel, both civilian and military. These provisions would also accommodate the stated needs of organizations such as the CIA, Foreign Service, and others to retire certain employees whose effectiveness has been diminished. In this manner, management objectives could be met while allowing other personnel to serve full, normal careers.

Some of the retirement systems cover positions with fixed, relatively short tenures established by law. Individuals appointed to such positions may have had no prior Federal service. Except possibly for these positions, we believe there is generally no need to grant special or preferential benefits to groups of employees merely because of the type of work they are performing. Able, qualified personnel are needed in all Federal occupations, and any differences in job characteristics and requirements normally are, and should be, reflected in the pay rates received. Personnel who can no longer perform satisfactorily in occupations that require exceptional youth and vigor could be retired on disability if such situations could not be resolved by using other available personnel management techniques such as retraining or reassignment to less demanding duties. We would also suggest that individuals appointed to short tenure positions who have had other Federal service before assuming their positions should continue coverage under the same retirement provisions as other Federal personnel. On the other hand, special provisions, such as a minimum benefit, might be required to provide adequate benefits to those individuals who had no prior service or a limited amount.

Many advantages would accrue from the adoption of an overall retirement policy specifying for all personnel, regardless of position, the retirement practices that will be applicable to Government employment. Such a policy would not only better guarantee consistency in benefit provisions, but would also end the inequities now widespread in areas such as employee contribution requirements, transfer of service credits when personnel change employment within the Government, and reemployed annuitant practices.

There are now no clear criteria governing the eligibility requirements for employees to participate in a Government retirement system or even whether certain of the current retirement programs should, in fact, be categorized as Federal plans. At present, the criteria used are inconsistent, confusing, and often conflicting. Specific criteria setting forth the definition of a Federal retirement system and the employee participation requirements are needed. In our opinion, such criteria could legitimately be broad enough to cover all the retirement systems discussed in this report or narrow enough to include only those systems covering employees paid directly with Federal funds. Determination of the proper criteria is a matter for the Congress to decide as part of the Government's overall retirement policy. Retirement programs and employee groups not meeting the established criteria should be made subject to the laws and regulations governing private pension plans.

AGENCY COMMENTS

In general, the agencies responsible for administering the retirement systems agreed that an overall Federal retirement policy was needed but argued that the separate systems should be continued. They insisted, in some cases, that the special or preferential treatment afforded to particular groups was justified because their conditions of employment were different from those of other Federal personnel.

The following summarizes the agencies' comments. Their specific responses are included as appendixes II through XX.

Uniformed services retirement system

The Department of Defense stated that the uniformed services system exists to complement the management requirements of the active force in meeting defense goals and is similar to other Federal retirement systems only to the extent that each is structured to meet the objectives of the organizational entity. Furthermore, DOD maintained that the uniformed services system operates as an integrated element of both the military personnel management system and the military compensation system.

The Department of Transportation, which is responsible for administering the uniformed services retirement system for Coast Guard personnel, did not concur in the concept that equity among Federal retirement systems is paramount. The Department stated that each Federal retirement program should be viewed as part of the total compensation received by the personnel covered by the program. In this regard, the Department stated that total compensation should take into account differences in the types of services performed and should consider all forms of compensation received.

The Department of Commerce, which is responsible for administering the uniformed services retirement system for NOAA's commissioned corps, believed that there is justification for granting preferential retirement benefits to certain groups of employees if job requirements and the effects of the type of work on the individuals are considered. The Department stated there are inequities throughout Government careers, but believed that to eliminate the inequities after retirement would only be acceptable if inequities were eliminated before retirement.

The Department of Health, Education, and Welfare, which is responsible for administering the uniformed services retirement system as it pertains to the commissioned corps of the Public Health Service, believed that retirement systems covering Federal personnel are due for a close critical analysis and that our report made a good case for a homogeneous system. However, the Department also believed that alternative solutions worthy of consideration included correcting inequities and weaknesses within the existing retirement systems or consolidating similar systems wherever possible, but without the goal of achieving a single Federal program.

Civil service retirement system

The Civil Service Commission agreed that there are many inconsistencies and inequities among Federal retirement systems and stated that some consolidation or integration of these systems would alleviate such problems. However, the Commission stated that some differences in specific benefits in the different retirement programs are not necessarily bad. It maintained that the Congress enacted most of the programs in support of the special personnel management systems to which they are related.

With respect to the need for establishing a Federal retirement policy, the Commission agreed that there is a need for regular coordination among the various retirement systems. It stated that some coordination exists today because many other systems seem quick to make parallel changes anytime changes are made in the civil service retirement system.

Foreign Service retirement system

The Department of State stated that the establishment of a retirement policy for Federal employees would be helpful. However, the Department maintained that the conditions of employment between Foreign Service and most other Federal employees are so unlike that entirely different retirement systems are necessary if Foreign Service management and employee interests are to be served.

Federal Reserve
retirement system

The Board of Governors of the Federal Reserve System stated that, in the abstract, a single retirement program for all Federal personnel seemed desirable. However, the Board felt strongly that the separate retirement system for employees of the Federal Reserve should be continued. The Board maintained that elimination of its system could result in substantial disadvantages in that a well funded and functioning system would be abandoned for the uncertainties of a large centralized system.

Tennessee Valley Authority
retirement system

TVA did not believe that our report supported a basic conclusion that there are no compelling reasons for the various agencies to maintain separate retirement systems. TVA stated that the financial soundness of its system and the design of the system to fit the particular needs of both TVA and its employees justified the system's continued separate existence.

Federal judiciary
retirement system

The Administrative Office of the U.S. Courts stated that it was not opposed to the concept of a single Federal retirement program, but believed that exceptions should be made when considerations of either law or fact argue in favor of separate treatment. The Office believed that such unique considerations were present with respect to Federal judges and agreed with our conclusion that judges are justified in receiving the full salary of their office during retirement since the majority of them continue to perform substantial judicial duties.

Tax Court judges
retirement system

The Tax Court stated that there were substantial reasons for questioning the existence of the variety of Government retirement plans and that it may be desirable to eliminate some of the separate plans and cover most Federal personnel under a single retirement program. However, the Court agreed with our position that Tax Court judges are justified in continuing to receive the full salary of their office since, like other Federal judges, they perform substantial judicial duties during retirement.

Retirement systems for the directors of the Administrative Office of the U.S. Courts and the Federal Judicial Center

The Administrative Office of the U.S. Courts believed that unique considerations exist which jusitfy, for retirement purposes, the continued separate treatment of the Administrative Assistant to the Chief Justice, the Director of the Administrative Office of the U.S. Courts, and the Director of the Federal Judicial Center. The Office stated that these positions require highly qualified individuals and that the special retirement provisions have assisted in their recruitment. The Office also pointed out that the tenures of incumbents in the positions have historically been relatively brief.

Central Intelligence Agency retirement system

The CIA believed that its retirement system should remain a separate statutory system, under Agency control, because of unique security and management factors. The CIA stated that the unique management factors related primarily to insuring the maintenance of a young and vigorous operational cadre.

U.S. Presidents retirement system

The General Services Administration believed that one overall Federal retirement policy and centralized management would provide equitable treatment for all Government employees. GSA also believed that any changes to the retirement benefits provided former Presidents should ensure that such Presidents receive annuities sufficient to meet all of the demands upon them without financial difficulty.

Nonappropriated fund instrumentality retirement systems

The Department of Defense believed that it would be unfair to require NAFI employees to participate in a Federal retirement plan if the costs would be significantly higher than the current NAFI plans, since NAFIs must pay their own way under present regulations. DOD stated that it has initiated a study to determine the feasibility and/or desirability of consolidating the various NAFI retirement systems.

Quasi-Federal employee retirement systems

Farm credit system

The Farm Credit Administration agreed that an overall Federal retirement policy was needed to eliminate the many existing inequities and inconsistencies. It did not believe, however, that the retirement systems should be consolidated. The Administration believed the smaller systems were more easily managed, in all aspects, than would be the case with one consolidated program.

Federal Reserve banks

In addition to its objections as mentioned on page 146, the Federal Reserve Board believed that the inclusion of Federal Reserve bank employees in a Federal retirement program could result in a fundamental change in the nature and concept of the Federal Reserve System. The Board contended that the independence of the country's central banking system has proved to have substantial strengths in the public interest and opposed any actions that would run counter to or could impinge upon the structure and independence of the system.

Savings association retirement fund

The Federal Home Loan Bank Board stated that the integration of all Federal employees into one retirement program appeared to be a reasonable, attainable, and defensible objective. However, the Board believed the inclusion of Federal home loan bank employees in such a system was neither warranted nor desirable. The Board maintained that bank employees were not Federal personnel and that removing such employees from participation in the savings association retirement fund would have a serious cost impact on both the fund and the banks.

Privately administered retirement plans

Smithsonian Institution

The Smithsonian Institution believed it would be disadvantageous to replace its highly successful TIAA-CREF retirement plan with anything else. The Institution stated that the plan is equitable, secure, and efficient.

U.S. Department of Agriculture Graduate School

The Graduate School believed that all Federal employees should have equal benefits and that all fringe benefits, not just retirement, should be considered. The School maintained that its full-time staff were not Government employees and believed that it would be a very serious mistake to include such personnel in a Government retirement system.

Uniformed Services University of the Health Sciences

The Department of Defense believed that the University's TIAA-CREF retirement plan was essential for the recruitment of outstanding faculty members. DOD contended that most medical schools have a TIAA-CREF retirement plan and that such plans are familiar to teaching professionals and are a definite attraction to prospective faculty members. Furthermore, DOD maintained that, generally, University faculty members will not make a career in the Government; therefore, DOD believed it would be disadvantageous to require such faculty members to participate in a Government retirement program designed for full career personnel.

CHAPTER 5

FINANCING PRACTICES OF

FEDERAL RETIREMENT SYSTEMS

Federal retirement systems represent substantial long-term financial commitments. Full recognition of accruing retirement costs is essential not only in determining and allocating the cost of Government operations, but also in determining the present and future financial condition of the United States. However, no uniform practices or principles exist among the Government's retirement systems with respect to the actuarial valuation methods used or the funding provisions followed. The costing and funding procedures used by many of the systems understate the full cost of providing retirement benefits.

ESTIMATING AND FUNDING RETIREMENT COSTS

Because of the uncertainty of such future events as death, disability, or retirement, the ultimate cost of a retirement system can be determined only as actual expenditures emerge throughout the life of the system. By the very nature of a retirement system, there is a time lag between the accrual of benefit rights and the actual payment of benefits. Under most Federal retirement systems, benefit rights accrue during an employee's years of service. That is, each year of service has an associated benefit value.

In actuarial terminology, the value of benefit rights earned (accrued) annually by employees covered under a retirement system is referred to as the "normal cost" of the system. Normal cost is commonly expressed as a percent of payroll, and from a financing point of view represents an estimate of the amount of funds which, if accumulated annually and invested over covered employees' careers, will be enough to meet their future benefit payments.

The conventional approach to funding pension benefits is for the employer (and the employees in a contributory plan) to set aside funds approximating normal cost in advance of the date on which the benefits become payable. Many of the Government's retirement systems are funded on a normal cost basis; however, some systems (for example, the uniformed services system) operate on a pay-as-you-go basis whereby the Government finances benefit payments through annual appropriations.

Estimating the normal cost is a complex actuarial process which requires consideration of a multitude of factors. Basically, however, the process involves mathematically predicting the future experience of the system (for example, salary progression, rate of return on invested funds, probable rates of employees' deaths, disability, retirement, and termination of employment) and translating this experience into cost on the basis of the system's benefit provisions. If reasonable assumptions are not made on all factors affecting future benefit payments, normal cost will be incorrect.

Normal cost is calculated on either a "static" or "dynamic" basis, or a mixture of the two bases. Static calculations do not consider future general pay increases or future annuity cost of living adjustments; dynamic calculations consider such increases. Retirement system funding is generally based on the estimated normal cost; therefore, if the normal cost is understated, the system may be underfunded.

There are no prescribed consistent methods of estimating normal cost for use by the various retirement systems. For many of the systems, the estimated normal cost is understated, and for some it is not calculated at all. Many systems calculate normal cost on a static basis even though annuities are based in large part on employees' final salaries or average salaries in their highest paid years and are adjusted based on increases in the CPI.

A retirement system is considered fully funded if funds on hand and to be received are equal to the system's liability for benefit payments to present retirees and the anticipated liability for active employees, expressed in terms of present value.1/ However, when the fund balance and future receipts are less than the liability, an unfunded liability is said to exist. (Under a pay-as-you-go system, all of the liability is unfunded.)

The unfunded liability has not been calculated for some of the retirement systems; however, in 1976, three of the major systems reported unfunded liabilities in

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1/Present value is a concept which recognizes the time value of money. It is a technique for determining the amount of money which, if invested today at a given interest rate, would be sufficient to provide monthly benefits in the future.

excess of $273 billion. As shown in the following chart, this was an increase of 75 percent since 1970.

	1970 Liability (note a)	1970 Fund balance	1970 Unfunded liability	1976 Liability (note a)	1976 Fund balance	1976 Unfunded liability	Percent of increase in unfunded liability
	-------	-------	-------	(millions)	-------	-------	
Uniformed services	$103,426	$ -	$103,426	$165,900	$ -	$165,900	60
Civil service	75,236	22,432	52,804	150,470	43,470	107,000	103
Foreign Service	528	53	475	b/1,252	185	b/1,067	125
	$179,190	$22,485	$156,705	$317,622	$43,655	$273,967	75

a/Net liability after deducting future agency and employee contributions and future amortization payments covering specific liability increases.

b/As of Sept. 30, 1976.

Under current financing arrangements, the unfunded liabilities of these systems will continue to grow. As shown in the following table, the unfunded liabilities are estimated to be at least $348 billion by the end of fiscal year 1986. The estimated 1986 unfunded liabilities of the civil service and Foreign Service retirement systems were computed, based on assumed future general pay increases of 5 percent, cost of living adjustments of 4 percent, and a 6 percent rate of return on investments. At the time of our review, the unfunded liability of the uniformed services retirement system was not available on a basis which considered estimated future general pay increases and cost of living adjustments.

Estimated Unfunded Liability

Retirement system	1976	1986	Percent of increase
	(millions)	(millions)	
Civil service	$107,000	$169,000	58
Uniformed services	165,900	a/178,000	7
Foreign Service	1,067	1,902	78
Total	$273,967	$348,902	27

a/Projections available only through 1982.

Annual outlays for Federal retirement benefits are substantial and rapidly increasing. For example, in 1976 the three major systems paid benefits in excess of $15 billion, an increase of 178 percent since 1970. The following table shows the 1970 to 1976 increase by system.

Retirement system	Outlays 1970	Outlays 1976	Percent of increase
	(millions)		
Civil service	$2,752	$ 8,284	201
Uniformed services	2,853	7,296	156
Foreign Service	16	67	319
Total	$5,621	$15,647	178

The increases in outlays were caused by a variety of factors, but the primary reasons were (1) growth in the number of beneficiaries, (2) increases in the pay rates upon which the benefits are based, and (3) annuity cost of living adjustments.

Following is a discussion of the various methods used for computing normal cost and funding the retirement systems included in our study.

Civil service
retirement system

Costs accruing under the civil service retirement system are determined on a static basis, even though the law provides for annual pay increases and semiannual cost of living annuity adjustments. Since 1969, Federal white collar pay has increased about 77 percent and annuity adjustments have totaled about 100 percent. In its most recent actuarial valuation, the Board of Actuaries determined the system's static normal cost to be 13.64 percent of pay.

Public Law 91-93, enacted in October 1969, established the present funding policies of the civil service retirement system. It increased both agency and employee contributions to 7 percent of pay, and also required the Government to make direct appropriations to liquidate, in 30 annual installments, any increase in the unfunded liability resulting from pay increases, liberalization of retirement benefits, or extension of retirement coverage to new groups of employees. In addition, the Secretary of the Treasury is required to transfer to the civil service retirement fund annual payments for interest on the unfunded liability and for the cost of allowing credits for military service. In fiscal year 1976, the agencies and their employees each contributed about $2.7 billion to the retirement fund. Government appropriations and the Treasury transfers totaled about $4.7 billion.

The combined employee/employer contribution of 14 percent of pay covers the system's static normal cost; however, it covers only about half the true cost. The Office of Management and Budget estimates the dynamic normal cost of the system to be 27.4 percent of pay. 1/ When preparing cost analyses under OMB Circular A-76, 2/ Federal agencies will be

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1/In a previous report ("Federal Retirement Systems: Unrecognized Costs, Inadequate Funding, Inconsistent Benefits," Aug. 3, 1977) we stated that OMB estimated the dynamic normal cost of the civil service retirement to be 31.7 percent of pay; however, OMB subsequently revised the estimate based on changed economic assumptions.

2/This circular provides guidance to Federal agencies in making decisions and cost comparisons pertaining to in-house vs. contracting out for needed products and services.

required to use a Government cost factor of 20.4 percent of pay (27.4 percent, less a 7-percent employee contribution).

In fiscal year 1976, the total payroll for employees covered by the civil service system was approximately $39.2 billion. Based on this payroll figure, the following table indicates the difference in the estimated costs accruing under the system depending on whether such costs are determined on a static or dynamic basis.

Computation method	Percent of pay	Amount
		(billions)
Dynamic	27.40	$10.7
Static	13.64	5.3
Understated cost	13.76	$ 5.4

Foreign Service retirement system

This system is funded in much the same manner as the civil service system. Participants contribute 7 percent of their pay, and the employing agency makes a matching contribution. In addition, Public Law 94-350, approved July 12, 1976, authorized annual appropriations to the retirement fund equal to the amount that the system's normal cost exceeds employee and employer contributions.

The normal cost of the Foreign Service system as determined by the latest actuarial evaluation was 18.6 percent of payroll. As in the civil service system, this figure is a static calculation that does not include the effect of future general pay increases or annuity adjustments. At the time of our review, a new valuation was being made which was to include assumptions of future annual annuity cost of living adjustments. However, it did not provide for future general pay increases. Consequently, normal cost will continue to be understated.

The Government makes direct appropriations to amortize any increase in the unfunded liability resulting from (1) pay increases, (2) liberalization of retirement benefits, or (3) extension of retirement coverage to new groups of employees. The Secretary of the Treasury also annually credits to the retirement fund an amount equivalent to the interest on the unfunded liability and the cost associated with allowing credit for military service. For fiscal year 1976, amortization payments, interest on the unfunded liability, and military service credit payments totaled $54.5 million.

Uniformed services retirement system

This system is noncontributory, meaning that the Government pays the entire cost of providing benefits. 1/ The system operates on a pay-as-you-go basis, and benefits are financed through annual congressional appropriations. 2/ As a result, the Department of Defense budget reflects some of the cost of operating the military services in prior years, but does not include any accrual of retirement costs for current military personnel.

The table on the next page shows actual and projected outlays and accrued liabilities through fiscal year 1978.

1/Military personnel are also covered under social security and provided certain death and disability coverage by the Veterans Administration.

2/During the Second Session of the 95th Congress, legislation (H.R. 12392) was introduced which provided for funding of the system on a dynamic normal cost basis.

	Outlays (note a)	Basic pay (note b)	Retired pay as a percent of basic pay (note c)	Accrued liabilities
	(millions)	(millions)		(millions)
1970	$2,853	$12,306	22.2	$103,426
1971	3,389	12,545	24.4	113,389
1972	3,889	13,145	28.7	121,392
1973	4,392	14,705	28.4	130,373
1974	5,137	14,954	30.0	148,016
1975	6,239	15,186	35.9	163,352
1976	7,300	15,489	42.3	165,900
1977	8,238	16,017	48.8	168,300
1978	9,036	16,452	51.9	170,600

a/Actual costs, fiscal year 1970 to 1976; projected costs, fiscal years 1977 and 1978.

b/Budget figures.

c/Based on budgeted figures and excludes reserve retired pay and survivor benefits.

In April 1978, House bill 12392 was introduced providing for establishment of a Department of Defense Military Retirement and Disability Fund. The bill provides that the pre-existing unfunded liability of the uniformed services retirement system be liquidated by annual appropriations to cover payments attributable to service performed prior to creation of the Fund. The accruing liability for future retirement benefits of current active and reserve forces is to be funded on a dynamic basis. The bill had not been acted upon at the time of our review.

U.S. Tax Court judges retirement system

Tax Court judges retirement benefits are financed by annual congressional appropriations. These benefits are financed on a pay-as-you-go basis, and normal cost is not calculated. The unfunded liability for judges benefits has not been determined.

The system also provides an elective survivor benefit plan. Judges electing to participate in the survivor plan contribute 3 percent of pay before and after retirement, and any survivor benefit payments in excess of such contributions are financed by annual congressional appropriations. The unfunded liability of the survivor benefit plan as of September 30, 1976, was $715,000.

Federal Reserve retirement system

The Federal Reserve retirement system consists of two separate retirement plans. One is for employees of the Board of Governors and the other is for Federal Reserve bank employees.

The cost for benefits provided Board of Governors employees is funded through employee contributions of 7 percent of pay and contributions by the employer equal to the difference between employee contributions and normal cost. In calculating normal cost, the actuary has always included an economic assumption regarding future general pay increases.

Employee contributions during calendar year 1976 totaled about $1.5 million, while the employer contributed about $2.7 million. In addition, $1.2 million was required to fully fund a 5.4 percent annuity cost of living adjustment effective March 1, 1976, and this was covered by previously accumulated excess reserves of the plan.

According to the plan's 1976 annual report, the employer's required contribution was 11.1 percent of basic pay, based on assumptions of 4 percent future annual salary increases and a return on investments at the rate of 5.5 percent. This contribution when combined with the 7-percent employee contributions covers the current normal cost, but not the costs of annuity adjustments based on changes in the CPI. Under the system any annuity adjustments granted because of changes in the CPI are to be funded immediately by the employer, thus calling for lump sum payments in the amount determined by the actuary.

The cost for retirement benefits provided Federal Reserve bank employees is funded through employer normal cost contributions. (Employees do not contribute.) For calendar year 1976, the bank plan's normal cost was 11.48 percent of pay, which required a contribution of about $35 million. While retirement benefits for bank employees are not automatically adjusted for increases in the CPI, annuity increases are granted from time to time. Such increases are funded immediately.

Based on the required normal cost contributions and lump sum payments, the system's actuary expressed the opinion that funds on hand and those to be received will be sufficient to provide benefits to all retired and active members; in other words, the system (both Board and bank plans) reports no unfunded liability.

Federal judiciary retirement system

Federal judiciary retirement benefits are financed on a pay-as-you-go basis from funds appropriated for Federal judicial salaries. Normal cost is not calculated, and no determination has been made of the amount of the unfunded liability.

The system also provides an elective survivor benefit plan which is financed jointly by contributions of 4.5 percent of salary each by participants and the Government. A 1976 law also required the Government to make a direct appropriation to fund the plan's unfunded liability as of January 1, 1977. As of March 1, 1976, the unfunded liability of the survivors plan had been determined to be $8.5 million. By a fiscal year 1977 supplemental appropriation, $31.1 million was provided to the survivor program to fund the unfunded liability and to cover other costs estimated to be associated with benefit improvements made by the 1976 law over the next 75 years.

Tennessee Valley Authority retirement system

The TVA retirement system is financed by employee and employer contributions. The system provides retirement benefits composed of two amounts--an annuity, the employee-financed portion of the benefit, and a pension, the employer-financed portion. The standard employee contribution is 6 percent of salary, but it may be adjusted depending on the member's date of entry into the system. TVA employees are also covered under social security, and a member may elect to reduce his contributions to the TVA retirement system by 3 percent on that part of his salary not in excess of the social security base. In fiscal year 1976, TVA employees contributed $13.9 million to the retirement system.

TVA contributes the amount required to cover the administrative cost of operating the system and to provide all benefits other than those derived from members' contributions. The amount TVA contributes, determined by an annual acturial valuation, consists of a normal cost contribution, a contribution to amortize any unfunded liability, and a contribution to fund retiree cost of living increases. In fiscal year 1976, TVA contributed $24.9 million.

Based on the most recent actuarial valuation of the system, the current employer contribution rate is 10.38 percent of pay. This rate consists of

--6.78 percent of pay to cover normal cost,

--0.42 percent of pay to fund fiscal years 1975 and 1976 cost of living increases, and

--3.18 percent of pay to amortize the remaining unfunded liability.

In computing normal cost, factors for prospective pay increases were included. The system's unfunded liability was estimated to be $85 million.

Comptrollers General retirement system

The normal cost and unfunded liability of the Comptrollers General retirement system are not computed. Prior to enactment of Public Law 95-512 on October 25, 1978, the system was operated on a noncontributory pay-as-you-go basic. However, the act made the retirement system contributory for future Comptrollers General. (See p. 86.) Benefits will continue to be financed annually through congressional appropriations to GAO. If a Comptroller General or retired Comptroller General elects survivorship benefits, 4.5 percent of his salary or retirement pay is deducted each year and paid by GAO to the general fund of the Treasury as miscellaneous receipts. Similarly, contributions made by future Comptrollers General toward their own retirement benefits will be processed in the same manner. Prior Federal service may also be considered in computing a survivor annuity. If a Comptroller General elects to have such service considered for survivor annuity purposes, he must contribute 4.5 percent of salary earned during his previous service plus interest to the general fund of the Treasury.

Director of the Administrative Office of the U.S. Courts and Director of the Federal Judicial Center retirement systems

The normal cost and unfunded liability of these retirement systems are not computed, and funds are not maintained.

Benefits are paid by the Administrative Office of the United States Courts from annual appropriations. Employee contributions are not required. However, employees may elect to participate in the survivor benefit plan of the Federal Judiciary retirement system, which requires matching 4.5-percent contributions from the employees and the Government.

U.S. Presidents retirement system

The normal cost and unfunded liability of the U.S. Presidents retirement system is not computed, and a fund is not maintained. The Department of the Treasury pays the pensions for former Presidents and their widows. No participant contributions are required.

Central Intelligence Agency retirement system

Officials of the Central Intelligence Agency did not reveal their retirement system's normal cost, stating that such information is classified. In computing their normal cost, the officials stated that factors of 4 percent for annuity cost of living increases and a 7-percent rate of return on investments were included. A factor for future general pay increases was not included because such increases, as required by law, are amortized over 30 years.

Prior to enactment of Public Law 94-522 on October 17, 1976, the system was funded exclusively from (1) employee/employer contributions (currently 7 percent of pay each), (2) transfers of employee and employer contributions from other retirement systems, and (3) income on investments in U.S. Government securities.

Public Law 94-522 authorized annual appropriations for amounts necessary to:

(1) Finance, in 30 equal annual installments, the unfunded liability created by any statute which authorizes new or liberalized benefits, extensions of coverage, or increases in salary.

(2) Annually meet the normal cost of the system which is not met by employee/employer contributions.

(3) Reimburse the fund for the estimated portion of annuities for the year attributable to military service credit and to pay interest on the unfunded liability.

Agency officials acknowledged they have an unfunded liability but did not reveal the amount. They stated that prior to enactment of Public Law 94-522, contributions to the fund were never adequate to fund the benefits. However, future appropriations by the Congress, in keeping with the appropriation authorities contained in the law, will substantially slow further growth of the unfunded liability.

Closed systems

Included in our study were three retirement systems closed to new entrants--Panama Canal construction annuity, Panama Canal Zone cash relief program, and Federal lighthouse retirement system. The unfunded liability was not determined for any of these systems, and funds are not specifically maintained. Also, normal cost calculations are not made for these systems. Benefit payments to Panama Canal annuitants and widows of former lighthouse personnel are made by the Civil Service Commission, and former lighthouse personnel are paid out of annual appropriations to the U.S. Coast Guard.

Teachers Insurance Annuities Association and the College Retirement Equities Fund

The Teachers Insurance Annuities Association and the College Retirement Equities Fund are privately administered plans. Benefits paid under TIAA are fixed amounts, and benefits paid under CREF are variable amounts depending on the value of the fund's common stock investments. Normal cost calculations are inappropriate for the system as a whole, because individual benefits are determined based on the actuarial equivalent of the employee and/or employer contributions. The employer establishes his contribution rate to the retirement fund. He may also require employee contributions. The employee can elect to have the full amount of the combined contribution used to purchase a fixed annuity from TIAA, or he may direct that a portion or all of the combined contribution be used to purchase a variable annuity from CREF.

Nonappropriated fund instrumentality (NAFI) systems

The Department of Defense mandated that each NAFI plan: (1) be funded in accordance with sound actuarial principles, (2) be reviewed at least biennially by one or more qualified actuaries, and (3) provide for funding current year's cost and within a maximum of 30 years the unfunded cost of all past service credits. In computing normal cost, each NAFI plan includes a factor for general pay increases and annuity cost of living adjustments when such adjustments are provided by the plan. Five of the plans are amortizing their unfunded liabilities over 30 years, one is using 25 years, and one 20.

The normal costs and unfunded liabilities of the NAFI plans are as follows:

Plan	Normal cost Percent of 1976 covered payroll	Unfunded liability Jan. 1976
		(millions)
AAFES	a/7.7	$239.5
Air Force	5.1	16.2
Army	10.9	11.8
NAVRESO	8.5	59.7
BUPERS	8.0	5.2
Marine Corps	7.1	5.4
Coast Guard	9.6	0.4

a/Normal cost of the basic retirement plan only. The normal cost of the supplemental plan is 12.1 percent.

Farm credit system retirement systems

Separate normal cost calculations are made for each of the retirement plans within the farm credit system. The latest actuarial valuations for the plans showed normal costs to range from 3.8 to 16.6 percent of pay. In general, the retirement systems are funded by contributions covering their estimated normal cost and contributions amortizing their unfunded liability. Most of the plans do not require employee contributions.

In computing the estimated normal cost, several of the plans reported they had included salary increase factors. The plans do not provide automatic cost of living annuity increases; therefore, a factor for such increases is inappropriate.

As of June 30, 1976, the farm credit retirement plans reported fund balances of about $79 million and unfunded liabilities of about $55 million.

Savings association retirement fund

All 12 of the Federal home loan banks participating in the savings association retirement fund have elected a noncontributory plan for their employees. Each bank contributes monthly to a fund a certain percentage of the aggregate salaries of all its employees. The system's normal cost is computed under static assumptions; however, each bank's contribution is adjusted annually to reflect changes in employment and salary levels. At the time of our review, bank contributions ranged from 10.5 to 20.8 percent of pay. Cost of living increases are granted on an ad hoc basis and funded separately. As of June 30, 1976, the fund reported assets of approximately $224 million and an unfunded liability of about $6 million. The unfunded liability is to be funded over a 40-year period.

RETIREMENT FUND INVESTMENTS

Investment practices vary among the funded retirement systems. Some of the trust funds, such as the civil service and Foreign Service retirement funds, have outward characteristics of private pension funds but with an important difference. The receipts of these funds, consisting of deductions from employees' salaries, agency contributions, direct appropriations, and interest earnings are required by law to be invested in Federal securities. Some Federal retirement systems (e.g., TVA and Federal Reserve retirement systems) do not have this restriction.

When a retirement system's funds are required to be invested in Federal securities no cash is involved, only bookkeeping entries. The primary purpose of funding such systems is to formally recognize cost. Funding such systems promotes sound fiscal and legislative responsibility and enhances budgetary discipline. When funds are needed to make benefit payments, the Treasury obtains the cash through its normal channels of tax receipts or borrowing from the public. Full funding of such systems would not cause a financial hardship for the Government; however, funding retirement systems with assets invested in the private sector would require immediate cash.

Assets of the TVA retirement system, Federal Reserve retirement system, TIAA/CREF, and the farm credit district retirement plans are basically invested in the private sector. The investments include, among other things, fixed-income securities and common stocks.

Varied investment policies also exist among the seven NAFI retirement systems. The policies are as follows:

--The AAFES, Army, and Marine Corps funds are placed in insurance companies' general accounts, generally with minimum rates of return guaranteed.

--The NAVRESO, BUPERS, and Coast Guard funds are handled by NAVRESO, whose objective is to place 65 percent of these funds in equity securities and 35 percent in fixed-income securities. Funds are placed in the general account of an insurance company and in the investment account of an investment company.

--The Air Force funds are invested exclusively in federally backed fixed-income securities.

EFFECTS OF NOT RECOGNIZING AND FUNDING FULL RETIREMENT COSTS

The Congress, employees, and the taxpayers may be misled by unrealistic estimates of Federal retirement costs. When the full costs are not recognized, there may be a tendency to adopt benefits which could jeopardize the eventual affordability of the retirement systems. Also, the lack of full cost recognition results in the understatement of the cost of Government programs, and without full funding, the Government's retirement system liabilities are not totally reflected in the public debt.

The understatement of civil service retirement system costs results in subsidies to agencies whose operations are intended to be self-supporting. Most agencies whose employees are covered by the civil service system are required to make a matching contribution of 7 percent of pay to the retirement fund. This combined employer-employee contribution of 14 percent covers the static normal cost of 13.64 percent of pay, but not the 27.4 percent dynamic normal cost. Therefore, agency budgets (operating costs) are understated by approximately 13.4 percent of pay--27.4 minus 14. Understating retirement costs of self-supporting agencies means, in effect, they are subsidized by an amount equal to their share of unrecognized and unallocated retirement costs. Recognition of the civil service retirement system's dynamic normal cost and allocating the difference between such cost and employee contributions to participating agencies would eliminate the subsidies that are currently accruing to self-supporting agencies.

CONCLUSIONS

Federal retirement systems lack uniform actuarial valuation methods and funding provisions. Some Federal systems do not even calculate normal cost, and of those that do, differing cost methods and economic assumptions are often used. The estimated normal cost of many systems is understated primarily because the valuations are performed on a static basis. Some systems are financed on a contributory basis, some on a noncontributory basis, some provide for fully funding benefits as they accrue, some provide for partial funding, and others are completely unfunded.

We believe that the inconsistent and inadequate costing and funding methods used for most Federal retirement programs should be corrected. 1/

AGENCY COMMENTS

Most of the administering agencies did not comment on our conclusions regarding the financing practices of Federal retirement systems.

The Central Intelligence Agency agreed that there should be standardized methods of financing the systems and standardized methodology for actuarial valuations.

1/Some action was taken in this area during the 95th Congress. Senate Resolution 244 was adopted requiring a study of the major Federal retirement systems to determine, based on dynamic assumptions, the extent of their present and future unfunded liability, the method of financing each system, and the actions necessary to insure the solvency of each system. Also, legislation (H.R. 9701) was passed requiring Federal pension plans to adopt ERISA's financial reporting standards.

The Civil Service Commission agreed that the cost of most Federal retirement systems is understated and believed that cost estimates for any proposed changes to the systems should be made on a dynamic as well as on the current static cost basis. However, the Commission stated that variations in financing the various systems may be necessary depending on the different types of benefits the particular system offers.

The Department of State agreed that all retirement costs should be recognized but not necessarily apportioned among the various agencies because of the complexity of such a procedure.

The Tennessee Valley Authority stated that its retirement program has been conscientiously funded from the beginning and that, unlike most other Federal retirement systems, the TVA system has no unrecognized costs.

CHAPTER 6

SOCIAL SECURITY FOR FEDERAL EMPLOYEES

The principle that the workers of the Nation should, to the extent practical, be assured that a basic level of family income will continue when earnings are impaired by disability, old age, or death is deeply imbedded in public policy. Some 9 out of 10 jobs are covered under the social security program, which provides this basic protection. Many thousands of staff retirement systems now use social security as a base, while providing supplementary benefits that are tailored to the special circumstances of the covered group. Generally social security's protection continues without interruption if the worker goes into different employment.

Employees who are not covered by an employer-sponsored retirement program and self-employed persons may, by law, establish tax-sheltered programs to provide additional retirement income. Thus, national policy guarantees, in effect, that workers will have the opportunity to supplement the basic protection provided by social security.

One of the major inconsistencies of Federal retirement programs is that social security coverage is provided to some personnel and denied to others. Social security is a large and growing national institution which was designed to be supported on a universal basis. We found no persuasive reasons why Federal personnel should not be covered by social security and their retirement programs redesigned to supplement social security benefits.

EVOLUTION AND CONCEPTS OF SOCIAL SECURITY

The social security system is composed of two parts: the Old-Age, Survivors, and Disability Insurance (OASDI) program and the Hospital Insurance (HI) program. These programs, providing monthly cash benefits (OASDI) and protection against hospital costs (HI), are the Nation's primary means for assuring that families continue to receive a basic level of income when the worker's earnings are impaired by disability, old age, or death. The objective is to provide a "floor of income protection" that will prevent widespread dependency in the Nation. The supplementation of social security's floor of protection (e.g., with pensions, insurance, and other forms of thrift) is desirable from the standpoint of the individual, as well as the

Nation. In a 1975 report, the Quadrennial Advisory Council on Social Security described the interrelationships of social security and other income maintenance programs as follows:

> "The social adequacy and individual equity of OASDI can only be evaluated in the context of America's three-tiered structure for income maintenance. Without the undergirding of means-tested programs for those with the lowest earnings or the supplementation through private means for those who have had higher earnings, OASDI might be judged deficient for many recipients. * * * it is essential that a balance be maintained among social security, means-tested programs, and private plans for income maintenance and capital accumulation."

Unlike a conventional insurance program--where assets are accumulated to meet future liabilities--social security is financed through a year-to-year transfer of income between generations. Today's workers, and their employers, are taxed to support current beneficiaries (yesterday's workers). The system is self-supporting in the sense that it is designed to pay benefits and administrative expenses without subsidy from the general fund of the treasury. Tax receipts are approximately equal to annual expenditures. Social security's trust funds are merely contingency reserves, intended to help the system remain self-supporting through brief periods in which benefit payments exceed tax revenues. The system's ability to fulfill future obligations is limited only by the amount of payroll (or other) taxes the Congress enacts.

The payroll tax

Throughout its history, social security has been financed by an earmarked payroll tax levied equally on covered workers and their employers. In 1978, workers contribute 6.05 percent of the first $17,700 of wages (the "maximum covered earnings") and a matching amount is paid by their employers. The self-employed contribute 8.1 percent of covered earnings. Both the tax rate and the maximum covered earnings are scheduled to rise in future years as shown shown on the following page.

Calendar year	Maximum covered earnings	Employees and employers, each			Self-employed
		OASDI	HI	Total	
1978	$17,700	5.05	1.00	6.05	8.10
1979	22,900	5.08	1.05	6.13	8.10
1980	25,900	5.08	1.05	6.13	8.10
1981	29,700	5.35	1.30	6.65	9.30
1982-84	(note a)	5.40	1.30	6.70	9.35
1985	(note a)	5.70	1.35	7.05	9.90
1986-89	(note a)	5.70	1.45	7.15	10.00
1990 and after	(note a)	6.20	1.45	7.65	10.75

a/In the year after an automatic benefit increase, the maximum amount of covered earnings will automatically increase in proportion to the increase in average wages in covered employment. The new amount is rounded to the nearest multiple of $300.

The concept of a maximum covered earnings limit is an integral part of the social security system. It gives clear recognition to the fact that social security's floor of protection is only one of three elements in the Nation's income-maintenance system--the other two being: (1) private pensions, savings, etc., and (2) public assistance programs. The 1975 Quadrennial Advisory Council, in abandoning a proposal for a substantial increase in the covered earnings limit, reported that

> "* * * [It] would cause social security to interfere with the private savings element. It would certainly extend coverage to a level of income where "enforced" savings seems inappropriate, and where it could further reduce needed capital formation."

Benefits

Because of the worker's payroll tax "contributions," social security benefits are considered an earned right (i.e., not based on a test of need). A worker's eligibility for benefits is based on two criteria: (1) a minimum period in covered employment, and (2) age or disability status. Dependents and survivors of eligible workers may also be eligible for benefits.

The size of a worker's monthly benefit is determined by a multistep process. First, the worker's covered earnings are indexed to reflect their value relative to average earnings of all covered workers for years between 1950 and the second year before benefit eligibility. Next, the worker's indexed earnings are averaged over a specified number of years to determine average indexed monthly earnings (AIME). 1/ The AIME is then applied to a benefit formula in order to determine the worker's Primary Insurance Amount (PIA)--the monthly benefit for a disabled worker, or a worker retiring at age 65. For workers initially qualifying for benefits in 1979, the formula for computing the PIA is shown below: 2/

> 90 percent of the first $180 of AIME, plus
> 32 percent of the next $905 of AIME, plus
> 15 percent of AIME above $1,085

The actual benefit paid to a social security recipient is determined as a percent of the PIA. As shown in the detailed summary of OASDI benefits beginning on page 173:

--Workers retiring at age 65 receive a benefit equal to 100 percent of their PIA. Those retiring between ages 62 and 65 take a reduction of up to 20 percent in their PIA.

--The spouse of a retired or disabled worker receives a benefit equal to 50 percent of the wage-earner's benefit (not necessarily the PIA) if spouse's benefit is claimed at age 65. The benefit rises to 100 percent when the wage-earner dies.

1/Because social security is still in a transition period, the number of years used in computing the AIME varies according to the worker's date of birth and sex. In general, as the system ages, the AIME for retirement benefits will be based on the highest 35 years of covered earnings. The AIME for death and disability benefits will be based on the highest "n" years of earnings, where "n" is equal to the number of years elapsing between 1950 or age 26 (if later) and before the year of death or disability (but never less than 2).

2/Established by the Social Security Amendments of 1977. Transitional provisions allow workers reaching age 62 before 1984 to elect benefits based on previous computation schedules.

--A spouse with covered earnings receives his or her own benefit as a worker, or the spouse benefit, whichever is higher.

In contrast to a reward for long service, social security "insures" workers against a loss of earnings in old age. However, except for persons age 72 and over, full benefits are paid only to beneficiaries who are substantially retired from work. 1/ Social security's "retirement test" permits a beneficiary, age 65 or over, to earn up to $4,000 in 1978 without any loss of benefits. Beneficiaries under age 65 can earn up to $3,240 in 1978 without a loss of benefits. For each $2 of employment earnings in excess of the exempt amounts ($4,000 and $3,240), $1 of benefits is withheld. The amount of exempt earnings for beneficiaries 65 and over is scheduled to increase $500 a year from $4,000 to $6,000 in 1982. Thereafter, it will be increased annually to reflect changes in average wage levels, in the same manner as the exempt amount for beneficiaries under age 65 is increased now.

Social security tries to meet the goals of both individual equity (providing benefits related to contributions) and social adequacy (lifting all beneficiaries out of poverty), but with emphasis on the latter. The antipoverty-welfare element is a major departure from the philosophy of a staff retirement plan and accounts for features such as:

(1) The spouse's benefit--The benefit awarded at retirement to a worker with a spouse who has no earnings record, when both are over age 65, is 150 percent of the benefit paid to an unmarried worker who has made identical contributions.

(2) Benefits for a divorced wife--After 10 years of marriage and upon reaching age 65, a divorced wife is entitled to 50 percent of the retired worker's benefit. The retired worker's benefit is not reduced and, if remarried, the spouse may also be receiving benefits.

(3) Benefits formula weighted toward low-income workers--The social security benefit formula provides wage-related benefits. But, as illustrated in the following chart, the ratio of benefits to average earnings is greater for low wage earners than for high wage earners.

1/Beginning in 1982, beneficiaries age 70 and over will be exempt from any limitation on employment earnings.

Average annual earnings (note a)	PIA as percent of average annual earnings (July 1977)
Up to $1,320	147.2
4,800	78.9
6,600	70.9
9,000	63.9
12,000	54.7

a/Twelve times the average monthly earnings used for social security computation purposes.

Summary of OASDI Benefits Under Law (note 1)
(As of Jan. 1, 1978)

Insurance Benefits for Workers

Old-age. "Fully insured" 2/ workers retiring at age 65 are entitled to a monthly benefit equal to the PIA.

--A reduced benefit which is graded down to 80% of the PIA may be claimed at age 62 (minimum age).

--Benefits are increased by 3% of the PIA for each year a worker delays retirement after age 65 and before 72.

1/For the sake of brevity, numerous qualifications of the Social Security Act have been omitted from the table.

2/Fully insured: Requires one quarter of coverage for every year elapsed after 1950 (or year of attainment of age 21 if later) and before the year of attainment of age 62 (or year of death or disability, if earlier). Minimum requirement is 6 quarters, and maximum is 40 quarters (10 years).

Disability. "Disability insured" 1/ workers are entitled to a monthly benefit equal to the PIA, if they are prevented from engaging in any substantial gainful activity by reason of a physical or mental impairment which can be expected to last for 12 months (or death).

Dependents of Workers Receiving Old-Age or Disability Benefit

A spouse or divorced wife (i.e., married 10 years before divorce) is entitled to a benefit of 50 percent of the worker's PIA if claimed at 65, graded down to 37-1/2% if claimed at age 62, the minimum age. 2/

A child who is (a) under 18 or (b) disabled prior to age 22 and still disabled or (c) 18 to 21 and a student is entitled to a benefit of 50% of the worker's PIA.

A wife who has in her care a child (except those claiming benefits only under (c) above) is entitled to a benefit equal to 50% of the worker's PIA.

Lump Sum Death Benefit

$255 is payable at the death of a "fully or currently insured" worker.

1/Disability insured: Requires fully insured status and at least 20 quarters of coverage in the 40 quarters prior to disability. Reduced requirements for disability prior to age 31.

2/Beginning in 1982, benefits payable to spouses or surviving spouses will be reduced by the amount of any pension based on their noncovered public (Federal, State, or local) employment. In the case of a nondependent husband or widower, this reduction was effective beginning December 1977.

Survivors of Insured Workers

A widow(er) or surviving divorced wife 65 or older of a "fully insured" worker is entitled to the benefit the worker would be receiving, if alive. The corresponding benefits for a widow(er) who is between 60 and 65 will be reduced in accordance with age--71.5% of the benefit at age 60.

--A severely disabled widow may claim a benefit before age 60 which is graded down to 50% at age 50.

--Benefits may be reduced if survivor is a public pensioner. 1/

--An unremarried widow(er) or surviving divorced wife who has the care of a surviving child (except those claiming benefits as an 18 to 21 year-old student) is entitled to a benefit equal to the child's benefit, regardless of age.

A dependent surviving parent of a "fully insured" worker is entitled to 82-1/2% of the worker's PIA. If two such parents are entitled to benefits, each receives 75% of the PIA. A parent who remarries after the worker's death is ineligible.

A surviving child of a "fully or currently insured" 2/ worker who is either (a) under 18 or (b) disabled prior to 22 and still disabled or (c) 18 to 21 and a student is entitled to 75% of the worker's PIA.

Maximum Family Benefits

Family benefits payable on the covered earnings of any one worker are limited by the benefit tables, generally to between 150% and 188% of the worker's PIA.

1/See footnote 2, p. 174.

2/Currently insured: Requires 6 quarters of coverage within the 13-quarter period ending with death or entitlement to old-age benefits.

While it is generally agreed that social security should only provide a "floor" of income protection, there are diverse opinions as to what level of income constitutes a suitable floor. The middle viewpoint is that social security, together with other income and assets, should be sufficient to yield a reasonably satisfactory minimum standard of living for the great majority of individuals.

Monthly benefits for three types of workers retiring in July 1976 are shown below. The benefits are also shown as a percent of earnings in the year before retirement (referred to as "replacement rates"). Because of the weighted benefit formula, the replacement rates are higher for workers with low earnings.

	Monthly benefits			Replacement rates		
	Low	Median	Maximum	Low	Median	Maximum
Worker Retiring:						
At age 65	$208	$320	$387	56%	43%	31%
At age 62	166	252	304	45	34	25
Worker Retiring at age 65 with dependent spouse:						
Age 65	312	480	581	85	65	47
Age 62	286	440	583	74	60	43
Worker retiring at age 62 with dependent spouse:						
Age 65	270	410	494	73	55	40
Age 62	244	370	446	66	50	36

Notes: Hypothetical workers: low-earnings worker assumed to earn half of the median earnings for males during each year of the averaging period; median-earnings and maximum-earnings workers assumed to earn the median income for males and maximum income subject to social security tax, respectively, over the averaging period.

The replacement ratio is the constant dollar value of the 1976 benefit divided by the constant dollar value of the 1975 wage for retiring workers with assumed earnings histories.

Because benefits are not subject to income tax, the replacement rates for "take home" pay are somewhat higher than those shown in the table, particularly at higher income levels. The after-tax effects partially offset the weighting of benefits toward low-income workers.

For the same year, the Bureau of Labor Statistics (BLS) estimated three annual budgets for a retired couple. 1/ The higher budget was $10,048 ($837 per month), the intermediate was $6,738 ($562 per month), and the lower was $4,695 ($391 per month). Workers retiring at age 65 with a dependent spouse, except for the low-earners, received benefits from social security alone that were in excess of BLS's lower budget. Social security benefits for low-income workers were substantially below BLS's lower budget.

Millions of workers are covered under staff retirement plans which overlay the basic protection of social security. In 1967, only 1 out of 5 social security beneficiaries had their OASDI benefits supplemented by another pension. But the number is expected to increase--in 1972, 65 percent of all private nonfarm workers were employed in establishments offering pension plans, compared with only 58 percent in 1968.

Persons not covered by employer-sponsored retirement programs are allowed, by law, to establish individualized, tax-sheltered programs to provide additional retirement income to supplement their social security. Self-employed persons may tailor investment programs, known as "Keogh" plans, to meet their specific needs and set aside 15 percent of their earnings, up to $7,500 a year in the plan. The contributions are tax deductible, and all income derived from investments in the plan accrues tax free until they are withdrawn. Retirement withdrawals may begin at age 59.5 but must begin at age 70.5. Keogh plans were first authorized in 1962. Similarly, tax-sheltered Individual

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1/The retired couple is defined as a husband, age 65 or over, and his wife. They are assumed to be self-supporting and living in an urban area; they are in reasonably good health and able to take care of themselves. The budget costs are specified to portray three relative levels of living--termed lower, intermediate, and higher. The lower budget is not intended to represent the income necessary for subsistence at the poverty level, but simply represents a level lower than the intermediate budget.

Retirement Accounts are available to employees and the self-employed under guidelines similar to those for Keogh plans. However, contributions to these plans are limited to $1,500 a year. Individual Retirement Accounts were first authorized in 1974 and, by 1976, almost 2 million persons had established such accounts for their retirement years.

Growth of social security coverage

When enacted in 1935, social security was a modest program of old-age insurance. The advantages of universal compulsory coverage were not readily apparent and many large groups of workers were excluded from the program. Among them were:

--Farm workers and self-employed individuals (because of difficulties in securing earnings reports).

--State and local government employees (because of the Constitutional issue of levying a Federal payroll tax on such governments).

--Federal employees (because most workers were already covered under a well-established staff retirement plan, and the advantages of including them under social security were not apparent).

Over the years, social security's benefits have been greatly improved: benefits for dependents and survivors were added in 1939; disability benefits in 1956; and health insurance in 1966. As experience was gained under the program, approaches that would make possible or facilitate coverage for groups that initially posed problems were worked out, and coverage was extended to more and more groups. Some 9 million additional jobs including certain farm, domestic, and self-employed persons were added in 1950; State and local government employees were granted optional coverage in 1951; and other farm and self-employed persons were added in 1955. Social security coverage was extended to members of the uniformed services in 1957.

Today the social security system is vast--95 out of 100 young children and their mothers are protected by its survivor insurance; 4 out of 5 persons between ages 21 and 64 are protected by its disability insurance; and 1 out of 7 Americans--more than 33 million persons--receive monthly social security benefits. In 1977 about 107 million persons--9 out of 10 of the Nation's workers--contributed payroll taxes into the system; and $84.6 billion was disbursed in benefits.

As of 1974, the majority of persons not covered by social security comprised two groups.

--About 32 percent of all State and local government employees; 3 percent were excluded by law, and 29 percent had declined voluntary coverage.

--About 90 percent of the Government's civilian work force in jobs covered by Federal staff-retirement systems. Nine out of 10 of those employees were covered by the civil service retirement system.

The following table, based on a June 1974 estimate, summarizes the percentages of the Nation's jobs covered and not covered by social security.

Percent of United States Jobs Covered by Social Security
June 1974 (estimated)

Job category	Covered jobs	Noncovered jobs: Coverage not elected	Noncovered jobs: Excluded from coverage
	(percent of U.S. jobs)		
Federal Government:			
Civilian	0.33	-	2.79
Military	2.46	-	-
State and local government	8.91	3.83	0.36
Industry and commerce	64.37	-	a/0.40
Nonprofit organizations	3.55	0.25	0.18
Nonfarm self-employed	5.52	0.17	0.89
Farm operators	1.66	0.35	0.06
Farm employees	1.16	-	0.36
Domestic employees	1.03	-	0.44
Railroad employees	0.68	-	-
Ministers	0.23	0.02	-
Total percent of jobs	89.90	4.62	5.48

a/Consists of newsboys under age 18.

The Social Security Amendments of 1977 resolved a number of the system's financing problems. But, after the turn of the century, the ratio of retirees to workers will be rising sharply, putting further strains on the system. To finance the benefits projected for that period, social security payroll taxes will probably have to be increased again.

The long-range problem relates to demographic changes. There are now 30 beneficiaries per 100 workers, and by the year 2030 the ratio is expected to change to 45 beneficiaries per 100 workers. Unless the ratio is improved by an increased birthrate or immigration, an increased proportion of women participating in the work force, or a later retirement age, social security taxes, as currently legislated, are projected to be inadequate. To change social security to a pre-funded system would require a huge buildup of funds that would dislocate the whole economy. To partially prefund social security, or to defer all costs to the next generation of workers, raises questions about the program's impact on individual savings, and capital formation.

To lessen the likelihood of future tax increases, some authorities believe that social security coverage should be extended on a mandatory basis to all Federal and noncovered State and local employees. Prior to the Social Security Amendments of 1977, the Quadrennial Advisory Council on Social Security estimated that, if all public employees were brought under social security, there would be a long-term reduction in the cost of OASDI of 0.25 percent of covered wages and a short-term reduction of 0.70 percent. By way of comparison, the 1977 OASDI tax rate (employer and employee combined) was 9.9 percent of covered wages. Such proposals are not new. Of seven major studies undertaken since 1938, all have recommended some type of social security coverage for Federal civilian employees.

Aside from the desire to increase short-term revenues, proposals for expanding social security to cover additional employees rest on four premises:

--The equity of universal financing for social security's welfare aspects. Many persons believe that the cost of financing such provisions should be shared by all and that noncovered workers enjoy a privileged tax position.

--The desire to eliminate duplication and "windfall" benefits for those employees who, through limited secondary employment, qualify for social security.

--The value of portability in providing continuous protection for workers moving between covered and noncovered employment.

--The desire to assure noncovered workers the same basic level of protection afforded others in the Nation.

The Social Security Amendments of 1977 directed the Secretary of Health, Education, and Welfare, in consultation with Treasury, the Office of Management and Budget, and the Civil Service Commission, to study and report to the Congress before 1980 on the feasibility and desirability of extending social security coverage to Federal and other noncovered employees.

SOCIAL SECURITY AND THE FEDERAL STAFF RETIREMENT SYSTEMS

Many Federal personnel are covered by social security, including those in the uniformed services, TVA, nonappropriated fund activities, and quasi-Federal organizations. However, most Federal civilian jobs are excluded from social security protection and covered under one of several Federal staff retirement systems. Of the 35 active retirement programs listed on pages 2 to 4, social security coverage is not permitted during Federal employment under the retirement systems of the civil service, Foreign Service, Federal Reserve Board, Federal judiciary, U.S. Tax Court judges, Comptroller General, Director of Administrative Office of the U.S. Courts, Director of Federal Judicial Center, Central Intelligence Agency, and the President. These systems are complex and loosely coordinated retirement programs intermingling staff retirement and social insurance concepts. But such concepts are difficult to harmonize.

Social insurance emphasizes the concept of "social adequacy." It protects society against widespread economic dependency by providing a floor of income protection that is contingent upon "risk." Staff retirement systems are generally designed to support organizational objectives. They emphasize benefits that will (1) help maintain a competitive employment position, (2) induce workers to remain with the organization through the peak of their productivity, (3) keep appointment and promotion opportunities open, and (4) ease adjustments in the size or composition of the work force as needed to fulfill organizational objectives. Federal retirement systems continue to place main emphasis on the retirement benefits and protection of long-service employees. They do not always provide the basic level of protection that would be available under social security.

The exclusion of most Federal civilian workers from social security raises basic concerns of social adequacy and individual equity, both amplified by the considerable mobility of workers between Federal and private employment.

Social adequacy

Federal civilian employment exposes large numbers of Amercian workers to serious gaps and deficiencies in survivorship and disability protection. Social security provides full-scale survivorship and disability protection for young workers after 6 calendar quarters (18 months) of covered work. But under most Federal staff retirements systems:

--Survivor benefits are available after 18 months, but disability protection is not provided until completion of 5 years of service. According to the Civil Service Commission, as of June 30, 1976, about 16 percent of the workers subject to the civil service retirement system have less than 5 years of service. While the incidence of disability is low among these younger workers, its effects on the family can be disastrous.

--Survivorship and disability protection stops if the worker leaves Federal employment before retirement. Large numbers of workers, some having lost social security protection earned in previous employment, reenter the private sector without survivorship or disability protection, and remain without such protection for some time. In most situations, the worker's protection is impaired. Social security benefit amounts will not reflect their recent earnings and may be quite low because of the length of time spent in noncovered work.

--Many years of service are required before family survivorship protection (spouse and dependent children) is equivalent to that provided by social security. On the other hand, most Federal systems pay an immediate annuity to a surviving spouse without a dependent child. Social security benefits, in the absence of a dependent child, are not payable until the widow(er) attains age 60 or, if severely disabled, age 50. 1/

1/For further information, see our earlier report, "Changes to the Federal Employees Group Life Insurance Program Are Needed," FPCD-77-19, May 6, 1977, which showed that Federal and non-Federal employers' death benefit programs are generally comparable except for younger employees and retirees over age 65 where social security puts the non-Federal sector ahead.

Individual equity

There is also concern that the existing situation places an unfair cost on the majority of other workers who are covered and contribute to social security throughout their working lives. Many Federal civilian workers, through secondary employment, become entitled to social security benefits which are in the lower benefit range but which represent a very high return on the worker's contributions. Because social security averages earnings over a substantial period of years (ultimately 35), and since retired Federal workers usually have relatively few years of covered earnings, their average earnings for social security purposes are artifically low. Benefits in this range are heavily weighted because they are intended for people who have had low earnings over a working lifetime. The cost of such "windfall" benefits must be borne by all covered workers and their employers.

The Civil Service Commission reported that, in 1972, 58.3 percent of Federal retirees, age 65 and over, were receiving social security benefits in addition to their civil service annuity.

COMPARISONS OF BENEFITS AND FUNDING OF SOCIAL SECURITY AND FEDERAL STAFF RETIREMENT SYSTEMS

Since most Federal employees who are excluded from social security coverage participate in the civil service retirement system, our specific comparisons with social security are limited to that system for purposes of simplicity. In general, however, the findings are applicable to other Federal staff retirement systems as well.

As shown on the following page, over 79,000 employees retired under the civil service retirement system in fiscal year 1976. On the average, they retired at age 58 after 25 years of service and received annuities of $631 a month. Seventy percent elected a survivor option. The annuities (automatically adjusted to keep pace with changes in the cost of living) will continue to be paid throughout the lives of these retirees and, where elected, reduced annuities will be paid to their survivors.

Provision under which retired	Number added to roll: Total	Number added to roll: Percent female	Age	Average service	Monthly annuity	Electing survivor option: Percent	Electing survivor option: Average monthly survivor annuity
			(years)				
Mandatory, 15 years' service	1,509	34.2	70.4	26.0	$575	57.2	$349
Disability	31,170	25.6	54.7	22.0	538	72.4	323
Voluntary:							
30 years' service, age 55	14,010	14.1	56.8	33.4	909	78.9	538
30 years' service, age 60	8,634	18.8	63.6	34.7	901	74.4	545
20-29 years' service, age 60-61	3,499	38.3	60.7	25.3	565	64.8	332
12-29 years' service, age 62	8,863	37.2	64.9	21.1	435	62.0	262
5 years' service, age 62	1,491	41.1	65.2	8.8	146	59.0	90
Subtotal	36,497	24.2	61.1	28.9	728	71.6	435
Deferred	4,255	44.1	61.6	12.2	137	31.2	110
Involuntary:							
20 years' service, age 50	1,188	47.1	54.4	22.5	517	62.8	301
25 years' service	3,184	21.9	52.8	29.5	817	72.6	474
Subtotal	4,372	28.8	53.2	27.6	735	69.9	427
Special provision:							
Law enforcement & fire fighters	1,599	1.4	55.5	30.7	1,283	92.9	755
Air traffic controllers	60	0.0	55.2	32.5	1,324	90.0	745
Members of Congress	7	0.0	60.7	17.6	1,192	85.7	456
Total	79,469	a/25.8	a/58.2	a/25.2	a/$ 631	a/69.8	a/$395

a/Figure is an average.

The table on the previous page offers several interesting observations about the differences between social security and Federal retirement. For example, of the workers joining the civil service retirement roll:

--<u>About 30 percent did not elect the survivor option</u>. Civil service provides the worker a choice between: (1) a full annuity, without survivor benefits; and (2) a reduced annuity with survivor benefits. Married workers are automatically enrolled in the survivor option unless written request to the contrary is made at the time of retirement. Critics have pointed out that the decision could encompass spite, lack of care, a desire to receive the unreduced benefit, or plans which may not be fulfilled. Inevitably, there are situations in which a surviving spouse is left unprotected. Social security permits no such option. The surviving spouse is effectively guaranteed benefits in old age.

--<u>About 15 percent were retired on the basis of management objectives</u>. Mandatory retirement and the special provisions for air traffic controllers, law enforcement, and firefighter personnel, are intended to maintain a productive work force; involuntary retirement is used to facilitate reductions in the size or composition of the work force; and deferred retirement 1/ is used to help the Government maintain a competitive employment position. Social security is not designed to support management objectives.

--<u>About 39 percent retired for disability</u>. Civil service's definition of disability requires only that a worker, because of physical or mental impairment, be unable to perform useful and efficient service in his or her present position.

1/After completing 5 years of service, an employee leaving work covered under the civil service system is entitled to either a refund of retirement contributions or a deferred annuity payable at age 62.

(Other forms of work are not considered. 1/) Social security, on the other hand, defines disability as the inability to engage in any substantial gainful activity. Disability benefits were paid to less than 16 percent of the workers joining the social security roll in fiscal year 1976.

--Less than half retired under voluntary age-service provisions. Under social security, an employee's full work career is expected to span the period between the ages of 22 and 65 (43 years). Old age "retirement" benefits, however, may be claimed at age 62 after 10 years of covered work when the program matures in 1991--fewer years now. 2/ Civil service's voluntary retirement provisions are based on age-service requirements. On the average, employees retiring under these provisions are age 61.1 and have completed 28.9 years of service. Many may also be entitled to social security benefits in the future (43-year career minus 28.9 years of Federal service equals 14.1 years available to work in employment covered under social security).

Contribution rates and benefit structures

In general, the monthly benefits provided under civil service are greater than those provided under social security, but civil service employees--and the Government, as employer--also pay considerably more for the benefits. However, meaningful comparisons of contributions and benefits are difficult in view of the differing objectives, philosophies, and characteristics of the two programs.

1/For additional information on civil service disability practices, see our reports entitled, "Civil Service Disability Retirement: Needed Improvements," FPCD-76-61, Nov. 19, 1976, and "Disability Provisions of Federal and District of Columbia Employee Retirement Systems Need Reform," FPCD-78-48, July 10, 1978.

2/See footnote 2 on p. 173.

Civil service retirement benefits can be viewed as deferred compensation earned during active employment. Benefits are paid from a fund and interest earnings accumulated during employees' working years. Most civil service employees currently contribute 7 percent of their earnings to the retirement fund, and these contributions are matched by the employing agencies. In addition, the Government makes direct appropriations and other transfers to the fund for certain costs not covered by contributions. (See chapter 5 for a comprehensive explanation of how the system is financed.) In 1976, the additional Government contributions amounted to about 13 percent of employees' pay; thus, total contributions of approximately 27 percent of pay were made to the fund during the year to finance future benefit payments. Actual benefit payments during the year were only 14.1 percent of payroll. In contrast, social security benefit payments are not prefunded. Payments during the benefit period are financed by taxes on the Nation's work force.

Civil service employees' 7 percent contributions are applied to their total salaries, and benefits are based on years of service and average salary for the 3 consecutive highest paid years. Under social security, an employee's OASDI contribution rate is lower, and limited to "covered earnings" (5.05 percent of earnings up to $17,700 in 1978). Retirement benefits are based on the average indexed monthly earnings for the highest 35 years. 1/

Equivalent workers contribute much more under civil service than they would under social security, particularly if their earnings are in excess of social security's "maximum." Social security's high-35 average is lower than civil service's high-3 average. It includes early work years at typically low salaries, and averages only covered earnings--not necessarily total career earnings. The social security benefit formula (1) is not directly tied to a worker's final salary, (2) provides proportionately greater benefits to persons with low earnings, and (3) changes annually.

Shown below are comparative replacement rates for civil service employees retiring at ages 62 and 65 (assuming they entered Federal employment at age 25) and the social security recipients discussed on page 176.

1/See footnote 1 on p. 171.

Replacement Rates (note a)
(1976 retirement)

	Social security: Low earnings	Social security: Median earnings	Social security: Maximum earnings	Civil service
	(Percentage of final earnings)			
Worker retiring:				
At age 65	56	43	31	73
At age 62	45	34	25	67
Worker retiring at age 65 with spouse:				
Age 65	85	65	47	b/71
Age 62	74	60	43	b/71
Worker retiring at age 62 with spouse:				
Age 65	73	55	40	b/65
Age 62	66	50	36	b/65

a/In contrast to civil service benefits, social security benefits are not taxable and include free hospital insurance. Thus, in terms of income available after taxes and purchasing hospital insurance, civil service replacement rates would be somewhat lower than shown.

b/Civil service retiree assumed to have elected a reduced annuity in order to provide survivor benefits.

In the above examples, civil service's replacement rates are higher for single workers at all income levels and for married workers with median and maximum earnings; social security's are higher for low-paid workers with dependent spouses. However, civil service benefits are based on years of service; social security benefits stress social adequacy. The two are not directly comparable. Further, the level of earnings has no bearing on the civil service replacement rates; whereas, under social security, the replacement rates are weighted to favor lower paid workers.

Social security's high wage earner (worker with maximum covered earnings throughout career) had a final salary of about $15,000 at age 65--slightly less than the average earnings in 1976 of Federal white collar employees under the General Schedule.

The replacement rates are based on gross income. Replacement rates based on spendable income (net of taxes, retirement contributions, and health insurance) would be substantially higher for social security beneficiaries--their benefits are tax exempt. Civil service annuities are taxed and annuitants must also pay for health insurance. The benefit structures of civil service and social security have other differences, namely:

Civil service	Social security
Workers with 30 years of service may retire with no reduction in benefits at age 55. Some are allowed to retire with 20 years' service at age 50 with no reduction.	Workers retire with full benefits at age 65. Retirement with reduced benefits is permitted at age 62.
Benefit payments are not affected by subsequent earnings in non-Federal employment.	Benefits may be reduced or withheld because of subsequent employment.
Benefits are paid only to the retiree during his or her lifetime. Survivorship provisions are optional and, if elected, will reduce the retiree's benefit.	Benefits are paid to the family. In addition to the worker's benefit, additional amounts are paid to all eligible dependents (subject to a family maximum).
The surviving spouse receives an immediate annuity equal to 55 percent of the retiree's benefit (except when death occurs after retirement and the worker rejected the survivorship option).	The surviving spouse is eligible for the worker's full benefit at age 65, or a reduced benefit at age 60. Benefits are payable at earlier ages only if the spouse is disabled or caring for a dependent child.

Civil service	Social security
The worker's spouse loses all eligibility for benefits upon divorce.1/	The worker's spouse retains eligibility for all benefits after divorce--providing the marriage lasted 10 years.
Benefits are taxed after they exceed the amount of the worker's contributions. Health insurance is paid for by the annuitant.	Benefits are tax exempt. Hospital insurance is paid for by social security.

HEALTH INSURANCE FOR THE AGED AND DISABLED

The 1965 enactment of Medicare inaugurated a national policy of providing, under the social security system, hospital insurance and low-cost supplementary medical insurance for persons aged 65 and over--the age group with the highest incidence of illness and disability, the lowest income, and the least adequate private health insurance coverage. The Social Security Amendments of 1972 extended this protection to two groups of "high risk" persons under the age of 65: (1) disabled persons, after 2 years on the OASDI benefit roll, and (2) persons with chronic kidney disease, requiring dialysis or renal transplant.

Federal civilian employees--most of whom are excluded from social security, and hence prepaid Medicare coverage--are offered health insurance under the Federal Employees Health Benefits (FEHB) Act of 1959. Roughly 85 percent of Federal employees have enrolled in the FEHB program and are entitled to continue participation during retirement (with the same benefits and at the same cost as an active employee) if:

--They retire on disability or an immediate annuity after 5 or more years of service.

--They are enrolled under the FEHB program for

1/Public Law 95-366 enacted on September 15, 1978, authorizes the Civil Service Commission to comply with the terms of a court decree, order or property settlement in connection with the divorce, annulment, or legal separation of a Federal employee who is eligible for benefits under the civil service retirement system.

(1) the 5 years of service immediately preceding retirement or

(2) all service since the first opportunity to enroll.

Medicare

Medicare is composed of two related health insurance programs:

(1) Part A--Hospital Insurance (HI) is a basic plan providing protection against the costs of hospital and related care.

(2) Part B--Supplementary Medical Insurance (SMI) is a voluntary supplement to HI covering payments for physicians' services and certain other medical and health services not covered in the basic plan.

The HI program, the more costly part of Medicare, is self-supporting and is financed on a current-cost basis through social security payroll taxes. In 1978, the HI tax rate for employer and employee each was 1.0 percent of earnings up to the tax base of $17,700 a year. (For scheduled increases in both the tax rate and base, see p. 170.) The SMI program is financed primarily by enrollee premiums and by contributions from the general fund of the Treasury.

Hospital insurance protection is provided to:

--All individuals aged 65 or over who are eligible for social security monthly benefits (without regard to the "earnings test").

--All disabled beneficiaries after 2 years on the social security benefit roll.

--Persons with chronic kidney disease requiring dialysis or renal transplant, if fully or currently insured under social security and the spouse or dependent of such a person. 1/

1/Currently insured status requires 6 quarters of coverage within the most recent 13-quarter period. Fully insured status requires 1 quarter of coverage (acquired at any time) for every year elapsed after age 21--up to a maximum requirement of 40 quarters.

--Non-OASDI enrollees. Noninsured persons over age 65 who are enrolled in SMI can elect to enroll in HI under the same conditions applicable to SMI. The entire cost is paid by the enrollees. The monthly standard premium rate for July 1977 through June 1978 was $54.

SMI protection is available for all individuals entitled to HI coverage and practically all other persons reaching age 65, including Federal employees and annuitants. SMI coverage is voluntary, with the enrollee paying a standard premium rate and the Government paying the remainder. For the period July 1977 through June 1978, enrollees paid a monthly premium of $7.70, and the Government pays additional monthly amounts of $16.90 for persons age 65 and over and $42.30 for disabled and kidney disease enrollees.

The Federal Employees Health Benefits Program

Over 75 private plans participate in the FEHB program, offering Government employees and retirees a wide variety of services. All plans offer self-only and self and family coverage, and some offer high and low benefit options. The program is financed on a current basis by premiums paid in part by employees and annuitants and in part by the Government. The Government's share of the cost of an enrollment is equal to 60 percent of the average high option premium of six representative plans, but no more than 75 percent of the total premium of the plan selected by the enrollee. Survivors of employees and retirees may continue coverage in the same cost-sharing ratio as long as their annuities are sufficient to meet their share of the cost.

The 1977 premium rates of the Government-wide Service Benefit Plan, which covers more than half of the people protected under the program, were as follows:

	Monthly premuim (note a)		
Type of enrollment	Government contribution	Employee/annuitant premium	Total
High option:			
Self only	$21.57	$20.57	$42.14
Self and family	53.27	46.64	99.91
Low option:			
Self only	7.95	2.65	10.60
Self and family	23.04	7.68	30.72

a/Biweekly premiums converted to monthly amounts for comparison purposes.

Most Federal employees elect to continue the FEHB program in retirement. In fiscal year 1977, for example, over 83 percent of the employee annuitants added to the civil service system's retirement roll retained their insurance coverage, as shown below:

Provision under which retired (note a)	Number added to roll	Average monthly annuity	Percent with health benefits
Mandatory, 15 years' service	1,773	670	83.1
Disability	33,036	578	79.9
Voluntary:			
30 years' service, age 55	16,649	953	87.2
30 years' service, age 60	9,312	938	90.7
20-29 years' service, age 60-61	3,834	603	83.8
12-29 years' service, age 62	10,049	464	80.3
Subtotal	74,653	695	83.2
Involuntary:			
20 years' service, age 50	877	593	73.1
25 years' service, any age	2,749	815	82.7
Subtotal	3,636	761	80.3
Special provisions:			
Law enforcement & firefighters	1,227	1,380	97.6
Air traffic controllers	69	1,342	100.0
Members of Congress	53	1,970	81.1
Total	79,638	709	83.4

a/Excluded are 1,787 annuitants retiring under the provisions of 5 years' service--age 62 (of which 96 elected the FEHB program)--and 4,143 annuitants electing a deferred annuity. These categories did not, in general, qualify for continued participation in the FEHB program.

The civil service annuitant retiring for disability in 1977 would have to pay over 8 percent of his or her annuity for high option family coverage under the Service Benefit Plan.

The FEHB program provides a cost advantage for retirees, whose health care costs are substantially higher than those of younger people, and a cost disadvantage for active employees. (The older group makes greater use of health care and its more costly services, particularly hospitalization.) The dramatic difference in the cost of insuring active employees and annuitants is shown by the benefit experience of the 1966 FEHB programs (Medicare began on July 1, 1966).

	Patient category	Average benefits paid per covered person Jan. 1, 1966 to Dec. 31, 1966
A.	Employees and dependents	$67.87
	Annuitants and dependents	144.49
B.	Employees only	83.71
	Annuitants only	189.46
C.	Employee dependents	60.78
	Annuitant dependents	97.67

The FEHB program no longer reports the benefit experience of employees and annuitants as separate categories. The program's actuaries told us, however, that as a general rule the health insurance industry considers the liability of insuring persons aged 65 and over to be 2 to 3 times greater than the liability of insuring persons in the 20 to 30 age group.

In 1976, annuitants and their dependents accounted for almost 26 percent of all persons covered by the FEHB program (an increase from less than 8 percent in 1966). The cost increase which would be expected to accompany the increased share of annuitants has, however, been ameliorated--at least to some extent--by the introduction of Medicare. When an individual is entitled to benefits under both the Medicare and FEHB programs, Medicare pays first and the FEHB plan generally will pay any difference between the Medicare payment and the individual's financial obligation.

Comparison of Medicare and FEHB benefits

While both the Service Benefit Plan and Medicare are designed to enable persons to obtain essential health care services without depleting their financial resources, the programs' benefit provisions are dissimilar. Medicare is oriented to the aged, and thus does not include the full range of maternity and related benefits provided by the Service Benefit Plan. On the other hand, Medicare provides better protection against the expense of care in a skilled nursing facility. A comparison of the protection afforded older Americans under the two plans is shown on page 196.

The Service Benefit Plan provides virtually complete protection against the cost of inpatient hospital care, including the costs of surgery, physicians' visits, and medication. Medicare provides substantial protection against the expense of short-stay hospitalization and offers better coverage for persons requiring continued treatment in an extended care facility. Except for the Service Benefit Plan's coverage of prescription drugs, the two plans are roughly comparable in their coverage of outpatient services and doctors' visits.

Comparison of Major Benefits Under Medicare and the Government-wide Service Benefit Plan (July-Dec., 1977)

Provision	Medicare	High option Service Benefit Plan
Inpatient hospital care	Up to 90 days in each benefit period with patient paying a deductible of $124 for the 1st 60 days plus a co-insurance amount of $31 a day for each day in excess of 60 during a benefit period. --An additional 60 hospital days are provided as a lifetime reserve with patient paying $62 a day co-insurance. --Inpatient psychiatric hospital service included, but subject to a lifetime limitation of 190 days.	Up to 365 days for each hospital confinement, including inpatient psychiatric hospital service.
Skilled-nursing facility (SNF) care	Up to 100 days in a benefit period for continued treatment in an extended care facility after transfer from a hospital where the patient stayed 3 or more days. The first 20 days are covered in full. In each of the remaining 80 days patient pays $15.50 co-insurance. 1/	Convalescent care excluded.
Home health care	Posthospital home health services for up to 100 visits in a year following discharge from a hospital or SNF, if services are furnished under an approved plan. SMI: Provides home health care services without hospitalization requirement.	Up to 90 days' home health services after discharge from a hospital; patient remains under physicians' care and services are furnished under an approved plan.
Physician's and surgeon's services	SMI: Covered, subject to $60 deductible per year and 20% co-insurance, except that hospital inpatients are fully insured for services of radiologists and pathologists.	Pays usual, customary, and reasonable charges for surgery, inpatient and certain outpatient visits. Office visits and certain other physicians' services subject to deductible and 20% co-insurance. 2/
Prescription drugs	Covered only when furnished in a hospital or extended care facility.	Covered in or outside a hospital. Prescription drugs outside a hospital are covered subject to deductible and 20% co-insurance. 2/
Miscellaneous	Service Benefit Plan provides coverage for outpatient hospital treatment related to "medical emergencies" and for certain therapeutic or diagnostic services. Medicare and the Supplemental Benefits of the Service Benefit plan cover, subject to 20% co-insurance, certain outpatient hospital services, and other medical services such as: diagnostic tests, limited ambulance services, prosthetic devices, and physical therapy. 2/	

1/Medicare nursing home benefits are very limited--less than 2 percent of Medicare's benefit payments of $25 billion in 1978 were for nursing home care. The Medicaid program pays for most long-term care.

2/Co-insurance provisions of the Service Benefit Plan begin after the covered person has incurred $100 of expenses for covered services (the deductible).

--The enrollee's liability is limited. After the total co-insurance payments on behalf of the enrollee and any covered family members amount to $4,000 in a calendar year, the plan pays 100% of the covered expenses.

--A subscriber who is enrolled in Part B (SMI) of Medicare is exempted from the deductible and the co-insurance requirement. The Service Benefit Plan pays up to 100% of usual, customary, and reasonable charges for covered services and supplies not paid by Medicare. (As of January 1977, aged persons not enrolled in HI but enrolled in SMI numbered 385,000. Of these, 64,000 were Federal civil service annuitants.)

The differing emphasis of the two programs is readily explained by the distribution of the Nation's health care expenditures among age groups in 1975 as shown below.

Type of expenditure	Age group: under 19	19 to 64	65 and over
	(percentage of total expenditures)		
Hospital care	33.6	48.7	44.3
Nursing home care	1.5	2.0	25.2
Physicians' services	33.0	21.2	16.0
Other professional services including dental care	13.0	11.5	3.3
Drugs and drug sundries	13.1	10.4	8.7
All other health services	5.9	6.3	2.6
Total	100.0	100.0	100.0

Note: Totals may not add because of rounding.

As shown, over 85 percent of the health care expenditures for older Americans involve either hospital or extended care or physicians' services. The preference for either Medicare or FEHB, therefore, centers on the degree of risk one is willing to assume between inpatient hospital/surgical costs and the expense of extended care. It also depends on the need to provide health insurance protection for dependents under the age of 65. Whatever the reason, the great majority of Federal annuitants continue their coverage under the FEHB program.

Comparatively few Federal annuitants spend their entire working lifetimes in Federal employment. Some will have the years of social security coverage needed to be insured under Medicare at age 65, but many long-service employees will not. If those who retire by age 55 work and become fully insured under social security, at age 65 they will receive the same level of Medicare protection as workers who have contributed to social security throughout their working lifetimes. This raises a question of equity between the public and private sectors, and among Federal personnel, such as the uniformed services and TVA, who contribute to Medicare during their Federal employment.

Federal retirees who do not secure Medicare coverage through non-Federal employment or as the spouse of an individual covered by social security will not receive the basic, prepaid health insurance protection afforded to virtually all other persons in the country. Also, the divorced spouse of a Federal retiree loses any health insurance protection he or she may have had under the FEHB program. In contrast, a divorced spouse who was married for at least 10 years to a worker covered by social security may receive both a spouse's benefit and medicare protection. These situations raise a question of social adequacy and the propriety of an arrangement under which Federal employees are exempted from the public policy of protecting individuals, and society, against the adverse effects of dependency because of ill health in old age and during long-term disability.

Because Federal civilian employees are not covered under social security and its Medicare provisions, they must pay increased health insurance premiums during active employment and continue to pay the premiums in retirement. Some of them may enter old age without health insurance.

Many of the workers entering and leaving Government employment lose the continuity of Medicare's disability protection that is afforded workers who move from one job to another in private industry. Aside from the possibility of social security protection earned in part-time work, some of these workers are exposed to substantial gaps (perhaps 5 or more years) in Medicare's disability protection--a hazard unparalleled in private employment.

ALTERNATIVE APPROACHES FOR INTEGRATING FEDERAL RETIREMENT PROGRAMS WITH SOCIAL SECURITY

The issue of social security coverage for all Federal personnel has been examined often, and numerous proposals to include all employees under social security have been advanced. Proposals have ranged from allowing voluntary participation in social security in addition to a staff retirement plan to compulsory social security coverage for all Federal employees supplemented by a staff retirement plan. However, most proposals, including the 1975 recommendation by the Quadrennial Council on Social Security for compulsory coverage for Federal employees, have not outlined a plan for integrating social security benefits with the staff retirement plans now in effect.

This part of our report places into perspective the basic approaches for accommodating a Federal staff retirement system to social security. An essential point to recognize is that the two systems have differing objectives. Social security is primarily oriented toward the family and emphasizes the principle of social adequacy. It bases benefits on "lifetime" earnings, defines "retirement" as the withdrawal of aged workers from the work force, and places the financing burden on future generations. On the other hand, most staff retirement systems are primarily oriented toward the worker and emphasize the principle of individual equity. Benefits are based on earnings, and "retirement" is simply the act of leaving a job after a specified period of employment. Most systems are financed in advance through employee and/or employer contributions during the worker's career.

It must also be recognized that social security coverage for all Federal workers will, in general, require an increase in the Government's immediate cash requirements. As explained more fully in chapter 5, the receipts and funds of most of the Government's "funded" retirement systems must be invested in Federal securities. Most contributions to the funds are only bookkeeping entries, and cash is generally needed only when benefit payments are made.

At present the annual receipts of the Government's funded systems exceed their current obligations to beneficiaries; the excess is accumulated in the trust funds. The "cash assets" of the trust funds are converted to long-term debt (in effect Treasury borrows from the trust funds) thereby decreasing the Government's current cash demand. Social security benefits are not prefunded, but are paid from current contributions by covered employees and their employers. If all Federal employees were covered by the program, their and the Government's contributions would be used to make benefit payments. In short, there would be an increased flow of cash out of the Treasury. The Government would need to reduce other current expenditures, increase borrowing, or raise taxes. 1/

We have identified four basic approaches for accomodating a Federal staff retirement system to social security: (1) the "fully additive" approach, (2) the "offset" or "envelope" approach, (3) the "step rate" or "integrated formula" approach, and (4) the "complementary" approach.

1/Should the additional social security receipts from the Government and its employees be used to increase the social security trust funds--rather than expended in benefits--the long-term debt would be preserved.

The "fully additive" approach

Under the "fully additive" approach, the staff plan is not changed and social security is added. Although this approach was generally used to extend social security coverage to the uniformed services in 1956, 1/ it would appear to be in excess of the needs of Federal personnel--and a costly, and probably unaffordable, alternative to both the Government and its civilian employees. For example, in 1978, under the fully additive approach civil service employees would have been required to contribute 13.05 percent of salary up to $17,700 (6.05 percent for social security and 7 percent for civil service retirement) and 7 percent of salary in excess of $17,700. This approach would go beyond filling the gap in the protection of those who shift between Federal employment and other work and would, in many instances, provide benefits in excess of a worker's final salary.

The "offset" or "envelope" approach

In the "offset" or "envelope" approach, all or some portion of the worker's primary social security benefit is subtracted from his staff plan pension. For example, assume that a staff plan is designed to provide benefits of 60 percent of final average salary at age 65 after 40 years of service. If the plan is designed with a "30 percent offset," and the primary social security benefit provides a replacement rate of 40 percent for an employee, then the staff plan would provide a benefit of 48 percent of final salary (60% minus 12% equals 48%), for a combined total benefit of 88 percent.

The offset method has the obvious advantage of stating retirement benefits as a percent of final salary, but it may also cause the staff plan to provide greater benefits to

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1/When social security coverage was extended to the Federal uniformed services in 1956, no reduction was provided in the retirement benefits under the existing uniformed services retirement system. One consideration was that both military retirement and social security benefits were applicable only to base pay, which represented only a part of a member's total compensation. On the other hand, military members whose basic pay is less than the social security ceiling may receive gratuitous social security wage credits of up to $1,200 a year.

higher income workers. For example, if the social security recipients (age 65) described on page 176 retired under a "30 percent offset" plan, the benefits paid by the staff plan would be as follows:

	Replacement rates		
	Low earnings	Median earnings	Maximum earnings
	(Percentage of final earnings)		
Staff plan basic benefit	60.0	60.0	60.0
Less: 30% offset	16.8	12.9	9.3
Staff plan pays	43.2	47.1	50.7
Social security benefit	56.0	43.0	31.0
Total benefits	99.2	90.1	81.7

Treasury regulations do not permit private pension plans to make a full (100%) offset from uniform percentage-of-pay benefit formulas. Otherwise, the plans have considerable latitude in establishing offset levels. The vast majority deduct a maximum of one-half the primary social security amount.

An increasing number of plans base the amount of the offset on the employee's years of service. The Federal TVA retirement system, for example, reduces the member's pension by 2 percent of the first $1,050 of the social security benefit for each year (up to 30 years) of creditable TVA service.

The "step rate" or "integrated formula" approach

The "step rate" or "integrated formula" approach is another attempt to provide employees an equitable totality of benefits upon retirement. It provides one percentage benefit on the part of salary subject to social security and a higher benefit on the remainder or "excess portion" of salary. For example, the plan might offer a benefit for each year of service of 1 percent of salary subject to social security tax plus 2 percent of the part of salary in excess of covered wages.

The growth of final pay plans (as distinguished from plans using career average salaries) and the enactment in

1972 of automatic increases in social security's tax base present a number of problems for step-rate plans, and many have been replaced by offset formulas. Although a step-rate plan could be designed with an automatic shift in the salary "breakpoint" to match changing social security maximums--it would unquestionably be a complex undertaking if a final-pay plan, together with social security, were to provide a consistent replacement ratio.

The "complementary" approach

In the "complementary" approach, the staff plan supplements social security and, where desired, provides a "bridge" between the plans. For example, it may offer

--benefits to protect the surviving spouse during periods in which social security benefits are not payable, and/or

--supplementary benefits to workers retiring before they are entitled to social security benefits.

The "bridge" benefits are simply additive, provided as a fixed sum, or as a percentage of pay. The staff plan generally avoids any "tie in" with social security's benefit formula.

The independence provided under the "complementary" approach offers three important advantages for accommodating a Federal staff retirement system to social security. These are:

(1) Cost control--In the "complementary" approach, benefit liabilities (and hence, funding requirements) are determined by the provisions of the staff plan itself. The liabilities of coordinated plans (such as those using the step-rate or offset method) are directly affected by changes in the social security formula.

(2) Ease of administration--The "complementary" approach avoids the administrative burden of using data from two systems (e.g., what portion of the social security benefit to offset for Federal service; whether to recompute benefits due to a change in the Social Security Act, etc.).

(3) Enhancement of staff retirement objectives--The "complementary" approach safeguards the visibility and

objectives of a staff retirement plan. Since social adequacy is provided under the social security system, the staff plan is free to emphasize individual equity and organizational incentives, and its funding and benefits can be shaped accordingly.

If social security were stationary, the problem of designing a "complementary" plan to produce a desired totality of benefits would be relatively simple--a completely independent set of benefits could be established so that the two plans together would produce whatever results were desired. In the past, however, social security's benefit structure has not been stationary, predictable, or technically logical--integrated plans (using the offset or step rate method) have been superior to the "complementary" approach in providing a guaranteed totality of benefits.

The Social Security Amendments of 1977 converted social security's benefit structure to a "wage indexed" system. Beginning in 1979 a worker's earnings will be indexed to reflect annual increases in average earnings levels. This should have the effect of assuring that similarly situated beneficiaries generation to generation will receive the same relative level of benefits. To the extent that social security's replacement rates have been stabilized, the "complementary" approach should be a particularly viable alternative for accommodating Federal staff retirement systems to social security.

Implementation

It would be relatively simple to implement social security coverage for the entire Federal work force if such practical considerations as traditions already established, entitlements already earned, etc., were ignored. But such considerations are hard realities, and they must be reckoned with. In the absence of a specific coverage plan, therefore, we have limited our discussion to an overview of three implementation approaches.

The first, and simplest, way to handle the problem of integration might be to mandate social security coverage only for all new employees--leaving older employees under the provisions of the present staff plans, and bringing new employees under the coverage of a coordinated plan. The principal advantages and disadvantages of this approach would be as follows:

Advantages	Disadvantages
--Quickly accomplishes the goal of protecting short-term employees.	--Does not eliminate gaps in protection of present employees leaving Federal work force.
--Provides additional revenues to social security.	--Dual benefit problem for present employees remains.
--Minimizes impact on current work force.	--Requires continued administration of present staff retirement systems.
--Transition to complete coverage of the work force.	

The disadvantages of the first approach relate entirely to employees remaining under the present staff retirement systems, and might be ameliorated through several measures. For example:

--Gaps in protection: Credits could be transferred from the staff retirement system to social security for the Federal service of (1) workers who have employment subject to the present staff retirement system but who die or become disabled before they are eligible for protection under that system and (2) workers who separate from that system before they are eligible for retirement benefits. For example, upon the worker's separation, the staff system would transfer to the social security trust funds amounts equal to the contributions the worker would have been required to pay (plus related employer contributions and interest) if his or her total Federal employment had been covered under social security. In turn, social security would provide the worker retroactive earnings credits and quarters of coverage.

--Dual benefits: Maximum limits might be placed on social security benefits paid to Federal annuitants. This action would alleviate, but not completely solve, the problem of Federal annuitants receiving "windfall benefits" from the social security trust funds. A precedent for this type of provision already exists in the Social Security Act's maximum limit on disability benefits--in combination with Workers' Compensation, disability benefits may not exceed 80 percent of final earnings.

A second way to implement social security coverage for the Federal work force might be to mandate retroactive social security coverage for all workers--bringing all employees under the coverage of a coordinated staff retirement plan at once. Under this approach, the Federal retirement systems would reimburse social security for the contributions, plus interest, that would have been made on behalf of workers had their entire Federal career been covered under social security. The social security system, in turn, would provide retroactive credit for each worker's earnings (and service) under a Federal staff retirement system. The principal advantages and disadvantages of this approach would be as follows:

Advantages	Disadvantages
--Eliminates the "gap in protection" problem.	--Maximizes impact on current work force.
--Bars future beneficiaries from receiving "windfall" social security payments.	
--Avoids transitional period; puts "new" and "old" employees under consistent staff plan provisions.	

A third method that would represent a "middle ground" from the other two approaches would be to allow current personnel to retain any vested benefits they have earned to date under the existing systems and make the coordinated staff plan and social security applicable to all subsequent service. Persons nearing retirement eligibility under the existing plans should possibly be excluded, at their option, if their remaining Federal service would be insufficient to earn social security benefits.

The principal advantages and disadvantages of such an approach would be as follows:

Advantages	Disadvantages
--Provides quick coverage for Federal workers.	--Maximizes impact on current work force.
--Bars windfall benefits for new entrants.	--Does not eliminate coverage gaps for existing short-term workers who leave the Federal work force.
	--May increase windfall benefits for long service Federal workers.
	--Would involve numerous practical difficulties in conversion.

This method was used when social security coverage was extended to TVA employees, effective January 1, 1956. Initially, benefits for service before 1956 were computed according to formulas in use prior to that date; staff plan pensions earned after that date were subject to a social security offset. Subsequent amendments to TVA's retirement system provide for the same benefit formula to be applied to all years of creditable service with the offset applicable to service after 1955. Thus, overall benefits for TVA employees increased with the addition of social security.

CONCLUSIONS

We do not know of any persuasive reason for the continued exclusion of most Federal civilian workers from social security coverage. Because of the exclusion:

- --Some Federal personnel do not receive the basic protection afforded by social security to virtually all other workers in the country. Correspondingly, they do not share in the responsibility inherent in the social security program of meeting the basic needs of the Nation's elderly and disabled persons.

- --Many employees moving between Federal and private employment are exposed to serious gaps in their survivor and disability protection.

--Many Federal retirees, through limited secondary employment, become entitled to social security benefit amounts which were designed for persons who had had low earnings over their working lifetimes. The costs of these "windfall" benefits are paid through contributions by other workers and their employers.

--Federal employees and retirees must pay higher health insurance premiums and are not assured of prepaid Medicare coverage upon reaching age 65.

Without universal social security coverage, it will be very difficult, if not impossible, for the Government to provide comparable and equitable retirement benefits to all its personnel.

AGENCY COMMENTS

Those agencies commenting on the issue of social security coverage for all Federal personnel generally deferred to the study of this issue mandated by Public Law 95-216. The law requires, in part, that the Secretary of HEW, in conjunction with the Civil Service Commission and OMB, conduct a study of the desirability and feasibility of extending social security coverage to all Federal employees.

CHAPTER 7

RETIREMENT PROGRAM PRACTICES IN

THE NON-FEDERAL SECTOR

Many States and private employers cover substantially all their employees under a few large retirement plans, and there is a trend toward additional consolidation of non-Federal plans, particularly in the public sector. Although private companies often have more than one plan, they cover most employees by a single plan.

This chapter discusses some of the approaches and philosophies followed by non-Federal employers in providing retirement benefits to their employees and examines the benefits, as well as the obstacles and problems, that others have encountered in consolidating employee retirement programs.

PUBLIC SECTOR

According to Department of Commerce statistics published in 1972, there were 176 and 2,128 retirement plans administered by State and local governments, respectively. The bulk of the employees, however, were covered by a few large plans. Eighty-seven percent, or about 7.9 million employees, were covered by 3.9 percent, or 89, of the plans. In recent years, growth in the size and number of large plans has been more rapid than that of smaller plans. Moreover, many State plans permit voluntary local government participation.

Since 1970 consolidation of individual plans into a single statewide retirement plan has occurred in Florida, Tennessee, Kansas, and South Dakota. Louisiana and Washington were unsuccessful in their attempts at consolidation; but Washington did centralize the administration of its major plans. Some States, like Hawaii and Nevada, have had consolidated statewide plans for many years.

Consolidation of small locally administered systems, usually police and fire, into larger State administered plans has occurred quite frequently in recent years as exemplified by such actions in Ohio, Washington, and Montana.

Reasons for consolidating

The primary motivation for most governments to consolidate pension plans was to further their goal of providing employees uniform and equitable benefits. Some other positive spillover effects which have been reasonably expected to occur are:

--The elimination of fragmented and piecemeal retirement plan legislation which frees legislators to focus their attention on one system. This should lead to a better coordinated retirement policy and a more equitable benefit design.

--More uniform benefits between groups, which would eliminate or minimize the problems associated with the pressure to increase benefits from competing groups.

--A reduction in administrative expenses through the elimination of duplicate functions that are performed in a multiplan operation.

--A more efficient and effective investment program through

--a unified and coordinated policy and

--the potential for higher rates of return stemming from the availability of larger amounts of investment capital and broader diversification opportunities.

Employees were also expected to profit from the unification of retirement plans because of

--enhanced benefits which often accompanied consolidation,

--improved services to plan members,

--better management control and a more financially viable plan, and

--increased employment mobility flowing from portability features.

Consolidation, however, did not necessarily assure avoidance or elimination of problems associated with a multiplan operation. One State that had a unified system since 1946 was still, in the 1970s, experiencing some of the problems that usually exist in fragmented operations:

--An inadequate organization lacking the positions and personnel with the skill to effectively manage its plan.

--A contribution rate insufficient to cover benefit costs.

--Poor investment management.

--The absence of modern operating procedures.

--The inability to fully communicate with members.

Problems experienced in consolidating

Governments consolidating their systems usually experienced certain transitional problems:

--Training new staff.

--Expanding existing or implementing new accounting and member data information systems.

--Explaining to employees changes in the plan's options, benefits, costs, etc.

Costs associated with meeting those needs may offset the expected reductions in administrative expenses. Three States that recently consolidated their plans experienced these problems, but once the transitional period is over, all expect productivity gains through economies of scale to result in a cost benefit.

Furthermore, administrators have had problems in interpreting some of the provisions included in the legislation establishing the consolidated plan. Ambiguities involving such matters as prior service credits and special eligibility requirements required numerous administrative proceedings and in some cases formal State Attorney General's opinions for clarification. These problems are also transitional and in time will diminish or disappear.

Other difficulties experienced in State consolidations were:

--Problems concerning the size, makeup, and authority of a retirement board.

--Inadequate funding of liberalized benefits.

--Opposition from executive officers and employee groups involved in existing plans who fear a dilution of their influence and authority under a consolidated plan.

--Lack of legislative support preventing and/or delaying consolidation.

The basic objectives of consolidation--establishing a uniform retirement policy and more equitable benefits--were also achieved in some cases without consolidating systems. Two States mandated relatively uniform benefits and operating standards for their individual plans. One State, prior to consolidating its police and fire plans in 1967, required under its statutes uniform benefits and allowances for all of its local plans.

PRIVATE SECTOR

As with the non-Federal public sector, many private companies administer numerous retirement plans; however, the majority of their employees participate in a few relatively large plans. A Department of Labor study showed that more than one-half of the employees covered by all pension plans participate in less than 2 percent of the plans.

A Bankers Trust Company study of corporate pension plans issued in 1975 revealed that about 60 percent of the 190 companies studied cover substantially all their employees under a single plan rather than using separate plans for different groups. However, many companies did have large numbers of plans covering employees in different bargaining units.

We reviewed one consolidation in the private sector whereby a merger of two companies included consolidation of existing retirement plans to provide one benefit package for all employees of the new company. This was done to impress upon employees the fact that they all were working for the same company. The company did not, however, consolidate the plans covering employees of subsidiaries since they were not working directly for the company.

Most companies we visited had coordinated company policies guiding benefit levels to differing employee groups even though they had more than one plan. The companies maintaining separate plans for different types of employees did so to remain competitive in their respective labor markets.

The Bankers Trust study also indicated that in the prior 5 years, there was no trend to or away from consolidated single plan programs in the private sector. Of the 190 employers studied, one changed from a single plan to two separate plans, while another changed from a multiplan program to a single plan. However, this must be viewed in the light of private sector employers having for the most part already consolidated their plans.

Employers in the private sector did point out some possible disadvantages to consolidation.

--The competitive forces among industries prohibit costly benefit increases which could occur if a standard, uniform program means improved benefits for some or all employees.

--The effectiveness of control over splintered bargaining units is diminished.

BENEFIT DIFFERENCES AMONG EMPLOYEE GROUPS

State and local governments and private companies often provide different retirement benefits to various employee groups. State and local governments generally provide higher benefits to teachers and school employees, to policemen and firemen, and to judges and elected officials than they do to their general employees. The differences in benefit levels came about primarily through tradition and separate historical development. Private companies generally provide higher benefits to their salaried employees.

In State plans there is a trend toward conforming teacher and school employee benefits with those of other employees. We found no such trend for other groups.

Practically all of the work force in the private sector and about 75 percent in the non-Federal public sector are covered by the social security system. Most large private pension plans are integrated with social security, while many of the statewide systems are not.

Public sector benefits

States are generally providing different retirement benefits to four broad groups of their employees--those in the "general" category; teachers and school employees; police and fire; and elected officials and judges. The benefits are provided either through a separate plan for each group or through a consolidated plan with nonuniform benefit levels. Recent consolidations in four States eliminated separate teacher plans and provided for more comparability in benefits. In addition, 19 other States provide similar benefits to teachers as those of their general employees.

The following chart illustrates the different benefits provided certain State employee groups.

	Retirement requirements		Benefit formula--percent of salary per year of service	Employee contributions, percent of salary
	Age	Years of service		
State A				
General	58	35	1.6	None
Police and fire	52	25	2.0	None
Elected officials and judges	62	8	a/3.0 to 3.33	8.0
State B				
General	None	25	2.0	7.8
Police and fire	None	25	2.5	12.2
Elected officials and judges	None	10	3.5	7.8
State C				
General	65	5	1.0	5.0
Police and fire	55	5	b/2.0	6.0
Elected officials and judges	65	5	b/3.33	6.0

a/Elected officials earn 3 percent of compensation; judges 3.33 percent.

b/Actual benefit formula is 50 percent of high 3 years' salary based on 25 years required for police and 15 years for judges. Reduced for each year of service less than required, additional years credited at 2 percent per year.

Uneven benefits for each group came about primarily through separate historical development, and the benefits continue mostly through established tradition.

Police and fire personnel receive higher benefits than other employee groups even in those States that have consolidated their retirement plans because:

--Historically, State and local government retirement practices for these employees have followed the Federal Government's practice of providing early retirement to uniformed military personnel.

--Traditionally, retirement benefits for police and fire personnel have been considered a form of added compensation for hazardous duty.

--Police and fire personnel are effectively organized and are a potent political force in State legislatures.

Judges are provided more liberal benefits on the basis that they are frequently appointed or elected at an older age and because it is believed liberal benefits are needed to attract competent lawyers from lucrative private law practices.

Uncertain tenure is cited as a reason legislators and other State elected officials are provided higher benefits. In some States the higher benefits are also provided to supplement what is considered the low compensation received by these officials.

Private sector benefits

Private companies having more than one plan usually provide one for their bargaining unit or production employees and another for their salaried employees.

The two tier system developed in the late 1940s. Previously, companies provided pensions on their own initiative and had a relatively free hand in their design. In 1948, the National Labor Relations Board ruled that retirement plan provisions were subject to collective bargaining. The retirement plans developed for production employees through the bargaining process generally provided a flat dollar benefit based on years of service but without consideration of compensation rates. The retirement plans of salaried employees continued as designed under the old system. Unlike the negotiated plans, they provided benefit amounts based upon both salary and years of service.

Consequently, while both plans provide similar benefits at lower compensation levels, the salaried employees' plans provide higher retirement benefits as pay levels increase. In addition, salaried employees in some instances are eligible for benefits not available to hourly employees such as supplemental benefit plans and company investment and savings plans.

INTEGRATION WITH SOCIAL SECURITY

Public sector

When the Social Security Act was enacted in 1935, it specifically excluded State and local government employees from participation in the system. Amendments to the act in 1950 allowed participation by non-Federal public employees not already covered by other pension plans. By 1954, voluntary coverage was also extended to employees already covered in State and local plans.

Six States do not participate in the social security program. Of the remaining 44 States, 38 allow social security benefits to completely supplement State plans, while six provide for some reductions in benefits based upon the amount received from social security.

For example, one State plan which is integrated with social security provides for offset of State benefits equivalent to 50 percent of the social security retirement benefit. The plan was integrated in 1976 because of:

--The high cost associated with providing two separate and independent retirement programs.

--The unpredictability of future social security benefits and cost.

--The possibility of a retiree receiving from the two nonintegrated plans more disposable income than he received as an active employee.

Non-Federal public employers participating in the social security system highlighted the program's

--portability features,

--broad family survivor and disability protection,

--tax free benefits, and

--cost of living provisions.

Those who opposed participation stressed that the program

--is costly,

--shifts policy formulation to the Federal Government, and

--is of limited value to female and unmarried employees without dependents.

Increases in social security costs in recent years have led some States to consider integrating their systems with social security. With expected continued increases in these costs many States may of necessity take this action. We noted that one State recently completed a study on the need to continue participation in the social security program. The study was precipitated by the high cost of maintaining two separate plans and the high level of benefits. The study group recommended continued participation in social security because such features as disability benefits and tax free status could not be acquired at a more reasonable cost anywhere else. The study group, however, recommended that the State plan's benefits be integrated with social security by an offset formula. The recommended integrated plan would provide net retirement benefits equal to preretirement net income for about two-thirds of the current contribution to the two separate plans. The study had not yet been acted upon by the State legislature at the time of our review.

Private sector

The Social Security Act provides for mandatory coverage of practically all private sector employees. Most private pension plans provide some type of integration with social security and retirement benefits. The Bankers Trust Company study of 271 large single employer plans indicated 180 are integrated with social security. The preponderance of the remaining 91 plans provide flat dollar benefit amounts based upon years of service.

CONCLUSIONS

Most States and large private employers cover substantially all of their personnel under a small number of retirement plans.

There is a trend toward consolidation or merger of small State and local government retirement plans into larger State administered ones or into a single consolidated plan. A similar trend toward consolidation or merger is not apparent in the private sector. However, most private companies already cover substantially all of their employees under one plan.

Many of the reasons compelling State/local governments to merge or consolidate their retirement systems would also be generally applicable to the Federal Government. By far the most important would be to achieve equality of benefits under a unified and coordinated retirement policy. Other advantages, such as increased portability of retirement credits between employment in the various agencies and/or positions which are currently covered by separate retirement plans and a possible minimizing of competition among employee groups for benefit improvements, would also apply to the Federal situation.

As with the Federal Government, the practice by State and local governments of providing various benefit levels to employee groups exists to a large extent because of tradition rather than any meaningful policy analysis. States appear to be moving toward conformity of teacher and school employee benefits with those of general employees. In the private sector, benefit differences occur primarily as a result of collective bargaining with separate employee groups or the need to remain competitive in differing labor markets.

Social security is an important and integral part of practically all non-Federal sector employee retirement packages. The social security program provides a wide range of benefits that at best could only be replaced at higher costs, or as with portability and tax free benefits, could not be replaced at all.

CHAPTER 8

OVERALL CONCLUSIONS AND RECOMMENDATIONS

Federal retirement programs have not received the management attention they deserve in view of their importance and tremendous costs. The lack of an overall Federal retirement policy and independent, piecemeal development have resulted in a patchwork of systems providing different benefits under different conditions to various employee groups. Some of the differences are justified, but in general our review of the historical development of each system discloses no reasons for continuing the inequities that exist.

As requested, our objective in performing this review was to address the issue of whether it is desirable to establish a mechanism to provide coordinated management of the many Federal retirement systems. Based on the results of our review, we believe a centralized focus on retirement matters would help assure that the systems develop on a consistent and financially sound basis. We found no need for each of the systems to have its own independent administrator and separate congressional committee responsible for its oversight and legislative changes.

We recognize that most of the agencies commenting on a draft of this report insisted that the preferential or special treatment being afforded many Federal personnel is generally justified and should be continued. We do not agree, in general, with these positions but believe that, where unique benefits can be justified, they could be accommodated in an overall retirement policy much in the same manner that the civil service retirement system currently contains a series of benefit provisions for different employee groups and different employment conditions.

In addition to the differences in benefit provisions among the systems, there are significant differences in the methods by which the systems are costed and funded. In most cases, the systems' costs are understated. We believe it is imperative that the true costs of Federal retirement be recognized and funded on a consistent basis regardless of whether the systems' benefit provisions are revised.

If all Federal personnel are to be covered by consistent retirement provisions, a decision must be made on whether social security should be part of their retirement plan. Many Federal personnel are not covered by social security, but many others are. Social security is an integral part of non-Federal retirement programs, and we know of no persuasive reasons why all Federal personnel should not also receive the basic protection afforded by social security.

A primary reason for the proliferation of retirement programs in the Government is the lack of definitive eligibility criteria for participation in a Federal retirement system. Many of the smaller retirement programs for civilian employees, for example, were established because criteria no longer in existence for participation in the civil service system precluded their coverage at the time. Moreover, the various criteria used have been inconsistently applied. We found no logical basis whatsoever for instances such as allowing employees of Legal Services Corporation, a private organization, to participate in the civil service system while groups with more direct Federal relationships like the farm credit and Federal Reserve banks, Smithsonian private roll, and Agriculture Graduate School employees were excluded. Similarly, why should certain employees of DOD nonappropriated fund instrumentalities be excluded from the civil service system when many other groups paid with nonappropriated funds are covered? Specific criteria for guidance are sorely needed.

RECOMMENDATIONS FOR CONGRESSIONAL ACTION

We recommend that the appropriate committees of Congress hold hearings to evaluate in depth the issues raised in this report and to set in motion actions necessary to establish an overall Federal retirement policy and a mechanism for coordinating the management of Federal retirement systems. We offer the following suggestions as matters that should be considered.

--Establishment of a Federal retirement policy which outlines the principles, objectives, and standards to be followed in providing retirement benefits to military and civilian personnel. The policy should cover such matters as benefit levels, social security coverage, costing and funding, vesting, and administration. It should serve both management and employee needs. While recognizing that special provisions may be justified for particular groups, the guiding principle should be that all Federal personnel receive consistent benefits.

--Review of existing systems to determine the extent to which they need changes to conform to the established policy, including consolidation of systems wherever practical.

Should be --Adoption ed of actuarial valuation methods and funding provisions that reflect the full cost of accruing retirement benefits and charged to agency operations all costs not covered by employee contributions.

Should be --Development ed of y eligibility criteria for participation in a Federal retirement system. Those systems covering employees who do not meet the criteria should be made subject to the laws governing private pension plans.

--Centralization of committee jurisdiction over retirement matters to better assure consistent application of the retirement policy. needs to be considered In the absence of such centralization, the Congress should establish a temporary joint committee to review all Federal retirement systems and recommend needed changes in policies to achieve the above objectives.

The --Establishment of a permanent, independent board with authority and responsibility for monitoring the development, improvement, and administration of Federal retirement systems. is necessary The membership of the board should include representatives from the private sector and legislative, executive, and judicial branches, each appointed to a fixed term.

U.S. House of Representatives
SUBCOMMITTEE ON RETIREMENT AND EMPLOYEE BENEFITS
OF THE
COMMITTEE ON POST OFFICE AND CIVIL SERVICE
B-345-D RAYBURN HOUSE OFFICE BUILDING
Washington, D.C. 20515
June 23, 1976

Honorable Elmer B. Staats
Comptroller General of the United States
General Accounting Office
Washington, D. C. 20548

Dear Mr. Comptroller General:

At the present time there are approximately fifty one pension programs that have been exempted from the Employee Retirement Income Security Act (ERISA) because they are considered to be Governmental plans administered by agencies or instrumentalities of the United States Government. We, the undersigned, are extremely concerned that the Nation's largest and most diversified employer--the United States Government--does not have a retirement policy to serve as a guide in the overall development and improvement of these programs.

The absence of an overall retirement policy has allowed the various systems to evolve in an independent manner which has been the cause of many problems. This piecemeal development has resulted in inconsistent benefits, duplicate benefits, gaps in retirement protection, inconsistent financing methods, and large unfunded liabilities. These problems were specifically pointed out in an earlier study conducted by the General Accounting Office.

Just as the Cabinet Committee on Federal Staff Retirement Systems did more than a decade ago, we recognize that: (1) the issues are complex, (2) conflicting and divergent interests have to be balanced, and (3) changing manpower needs will continue to affect future policies. Please consider this letter as an official request for the General Accounting Office to undertake a comprehensive study of the desirability of consolidating all or part of the fifty one retirement systems administered by the Federal Government into a centralized mechanism charged with the responsibility of eliminating the problems cited above.

With best wishes, we are,

Sincerely yours,

Richard C. White

Richard C. White
Chairman
Subcommittee on Retirement and Employee Benefits

Henry S. Reuss

Henry S. Reuss
Chairman
Committee on Banking, Currency and Housing

Melvin Price

Melvin Price
Chairman
Committee on Armed Services

RETIREMENT SYSTEMS ADMINISTERED

BY THE FEDERAL GOVERNMENT

(1) Civil Service Retirement System
Room 4307
1900 E Street, N.W.
Washington, D.C. 20415

(2) Military Retirement System
Room 20263, Pentagon
Washington, D.C. 20203

(3) Foreign Service Retirement and Disability System
Room 1818
Department of State
Washington, D.C. 20520

(4) Federal Reserve Employees Retirement Plan
33 Liberty Street
New York, New York 10045

(5) Tennessee Valley Authority Retirement System
400 Burwell Building
Knoxville, Tennessee 37902

(6) Federal Judiciary Retirement System
Administrative Office of U.S. Courts
Washington, D.C. 20544

(7) Federal Judicial Survivors Annuity System
Administrative Office of U.S. Courts
Washington, D.C. 20544

(8) Widows of Supreme Court Justices Retirement System
Administrative Office of U.S. Courts
Washington, D.C. 20544

(9) Federal Lighthouse Retirement System
Room 4307
1900 E Street, N.W.
Washington, D.C. 20415

(10) U.S. Tax Court Judges Retirement System
400 Second Avenue, N.W.
Washington, D.C. 20217

(11) U.S. Tax Court Judges Survivors System
400 Second Avenue, N.W.
Washington, D.C. 20217

(12) Comptroller General Retirement System
U.S. General Accounting Office
441 G Street, N.W.
Washington, D.C. 20548

(13) Comptroller General Survivor System
U.S. General Accounting Office
441 G Street, N.W.
Washington, D.C. 20548

(14) U.S. Courts Retirement System
Administrative Office of U.S. Courts
Washington, D.C. 20544

(15) Federal Judicial Center Retirement System
Administrative Office of U.S. Courts
Washington, D.C. 20544

(16) Supreme Court Justice Retirement System
Administrative Office of U.S. Courts
Washington, D.C. 20544

(17) CIA Retirement and Disability System
Central Intelligence Agency
Washington, D.C. 20505

(18) CIA Employees Voluntary Investment Program
Central Intelligence Agency
Washington, D.C. 20505

(19) U.S. Presidents Retirement System
GSA, Room 2140
18th & F Streets, N.W.
Washington, D.C. 20405

(20) Widows of U.S. Presidents Retirement System
GSA, Room 2140
18th & F Streets, N.W.
Washington, D.C. 20405

(21) Savings Association Retirement Fund
Federal Home Loan Bank Board
5 Corporate Park Drive
White Plains, New York 10604

(22) Commissioned Corps of the Public Health Service Retirement System
5600 Fishers Lane
Rockville, Maryland 20852

(23) U.S. Coast Guard Retirement System
U.S. Coast Guard
Washington, D.C. 20591

(24) Retirement Annuity Plan for Eligible Civilian Employees--Army and Air Force Exchange Service
Dallas, Texas 75222

(25) National Oceanic and Atmospheric Administration Retirement System
Rockville, Maryland 20852

(26) Coast Guard Exchange Employees Retirement Plan
Navy Resale System Office
3rd Avenue and 29th Street
Brooklyn, New York 11232

(27) Navy Exchange Employee Retirement Plan
3rd Avenue and 29th Street
Brooklyn, New York 11232

(28) Bureau of Naval Personnel Non-Appropriated Fund Employees Retirement Plan
Department of the Navy (7232)
Washington, D.C. 20370

(29) Group Retirement Plan for Civilian Employees of the U.S. Marine Corps Exchanges, Recreation, Funds, Clubs, Messes, and Exchange Service
Post Office Box 1834
Quantico, Virginia 22134

(30) U.S. Army Non-Appropriated Fund Employee Retirement Plan
Department of the Army
The Adjutant General Center
(DAAG - NFA - IG)
Washington, D.C. 20314

(31) U.S. Air Force Non-Appropriated Fund Retirement Plan for Civilian Employees
AFMPC/DPMSPA
Randolph Air Force Base, Texas 78148

(32) TIAA - CREF Retirement Plan for Private Role Employees of the Smithsonian Institution
Smithsonian Institution
A & I Streets
Washington, D.C. 20560

(33) TIAA - CREF Retirement Plan for Faculty Members of the Uniformed Service University of the Health Service
6917 Arlington Road
Bethesda, Maryland 20014

(34) Panama Canal Construction Service Annuity
Room 4307
1900 E Street, N.W.
Washington, D.C. 20415

(35) First Farm Credit District Retirement Plan
Post Office Box 141
Springfield, Massachusetts 01101

(36) Farm Credit Retirement Plan-Columbia District
Post Office Box 1499
Columbia, South Carolina 29202

(37) The Retirement Plan for Eligible Employees of Farm Credit Institutions in the Fourth District
Riverview Square
Louisville, Kentucky 40202

(38) Farm Credit System Retirement Plan
Post Office Box 50590
New Orleans, Louisiana 70150

(39) Production Credit Association Retirement Plan for the New Orleans District
Post Office Box 50590
New Orleans, Louisiana 70150

(40) Sixth Farm District Group Annuity Plan
Farm Credit Banks of St. Louis
14th and Olive
St. Louis, Missouri 63103

(41) Employees Retirement Plan of the Seventh Farm Credit District
Farm Credit Banks of St. Paul
375 Jackson Street
St. Paul, Minnesota 55101

(42) Ninth Farm Credit District Pension Plan
Farm Credit Banks of Witchita
151 North Main
Witchita, Kansas 67202

(43) Farm Credit Banks of Houston Pension Plan
Post Office Box 2649
Houston, Texas 70001

(44) Farm Credit Banks of Houston Thrift Plan
Post Office Box 2649
Houston, Texas 70001

(45) Berkley Farm Credit Employees Retirement Plan
Post Office Box 529
Berkley, California 94701

(46) Twelfth District Farm Credit Retirement Plan
West 705 First Avenue
Spokane, Washington 99204

(47) Panama Canal Zone Cash Relief Program for Non-U.S. Citizens
Panama Canal Company
425 13th Street, N.W.
Washington, D.C. 20004

(48) TIAA/CREF Retirement Plan for the Graduate School of the U.S. Department of Agriculture
U.S. Department of Agriculture
Washington, D.C. 20250

(49) Federal Land Banks of Columbia Salary Reduction Thrift Plan for Farm Credit Employees
Post Office Box 1499
Columbia, South Carolina 29202

(50) Juciciary of the Territories Retirement System
Administrative Office of the U.S. Courts
Washington, D.C. 20544

(51) Farm Credit District of Baltimore Retirement Plan
Post Office Box 1555
Baltimore, Maryland 21203

ASSISTANT SECRETARY OF DEFENSE
WASHINGTON, D C 20301

MANPOWER,
RESERVE AFFAIRS
AND LOGISTICS

1 AUG 1978

Mr. H. L. Krieger
Director
Federal Personnel and Compensation
Division
U. S. General Accounting Office
Washington, D. C. 20548

Dear Mr. Krieger:

This is in reply to your letter to the Secretary of Defense regarding your draft report dated May 26, 1978, on "A Single Retirement System for All Federal Personnel: Is It Desirable?" (OSD Case #4916, FPCD-78-49).

We have reviewed the draft report, as requested, and are enclosing general comments on the Uniformed Services retirement system. Additionally, detailed comments are enclosed addressing specific portions of the draft report. Based on our review, the Department of Defense does not agree that it is desirable for all Federal personnel, to include uniformed services members, to be covered by a single retirement system. However, we recommend this draft report be referred to the forthcoming Presidential Commission on Retirement for consideration of each of the findings and recommendations.

We appreciate the opportunity to review the draft report and trust our comments will be helpful in your further efforts on the matter.

Sincerely,

ROBERT B. PIRIE, JR.
Principal Deputy Assistant Secretary
of Defense (MRA&L)

Enclosures

[See GAO notes 1 and 2 on page 305.]

DoD General Comments on the Uniformed Services Retirement System

The military retirement system exists to complement the management requirements of the active force in meeting the defense goals of the Nation. In its purpose, it is similar to other retirement systems only to the extent that each is structured to meet the objectives of the corporate or government entity. Any correlation drawn among retirement systems must be based on a corresponding correlation among the actual requirements that each management system must meet. In effect, requirements determine organizational objectives, objectives dictate personnel management goals, such goals establish personnel management requirements, and these requirements determine the nature of a retirement system. Unless there is commonality among the organizations' raison d'etre, it is unreasonable to assume that retirement systems can be similarly structured. To do otherwise, reverses the management process and erroneously uses the retirement system to dictate changes in personnel management, and changes in the requirements of the organization itself. The draft report mistakenly assumes that the organizational criterion of the uniformed services is the same, or similar, to other Federal organizations. This assumption is without objective basis.

The retirement system of the uniform services operates as an integrated element of both the military personnel management system and the military compensation system. It is the management tool by which the Service personnel managers remove members from the active list, either voluntarily or involuntarily, through nondisability retirement, disability retirement, retirement for nonregular service, or the severance/readjustment mechanism. Managers, working against military mission requirements, as dictated by national defense needs, are able to maintain the composition, size, and structure of the active force by exercising the authority of the military retirement system. The draft report fails to recognize the viability of the retirement system as a tool of personnel management.

As an element of the military compensation structure, the retirement system serves an income replacement function and an income maintenance function for members. Those who are required to be retired, at what would normally be the mid-point of a civilian career, must rely upon retired pay to replace income. This income replacement function becomes one of income maintenance to meet old-age needs as members remain on extended active duty and advance in age. Incorporation of the income maintenance function is a necessary element of the retirement system if members are retained past a marketable age level; this provides an income base for old-age. Although the draft report does not address adequacy of retired pay levels, the omission of reference to the function of retired pay represents an inconsistency in the facts upon which conclusions and recommendations are allegedly based.

The report does not present an objective evaluation of the differences in organizational responsibility, the active force management requirements against which each retirement system is designed, the purpose for which each is structured, or the function that each retirement system is to perform. Consequently, there is insufficient analysis presented upon which to base a recommendation for consolidation and integration with other Federal retirement systems. The report is, however, a useful anthology of the various systems covered.

For the past decade, the military retirement system has been the subject of numerous reviews and investigations by the Administration and the Congress. It is noteworthy that each of these independent studies has confirmed the need for a unique system which meets military management needs. As a result of these efforts, the Department of Defense proposed amendatory legislation to the 93rd and 94th Congresses to revise the military nondisability and severance pay systems. The purpose of that proposal was to establish a greater degree of retirement uniformity among the Services, to redesign the retirement system as a more efficient element of the personnel management and compensation systems, to remain fair to members, and to achieve cost avoidance. This proposal has not been presented to the 95th Congress pending evaluation and assimilation of the recommendations from the President's Commission on Military Compensation (PCMC).

The recently completed report of the PCMC recognized that management needs of the uniformed services for military personnel are different from personnel management needs for civilian employees. Even though the Commission recommended adoption of some features of the Civil Service retirement system, the retirement system recommended by the PCMC differs substantially from that for civilian employees. The ongoing review of the Commission's recommendations is expected to result in a legislative proposal to modify the current military retirement system. Such a proposal will necessarily take into account specific force management needs of the military and the inherent differences in the nature of Federal civilian employment and military careers.

On April 3, 1978, the Department of Defense proposed legislation to provide for a Department of Defense Military Retirement and Disability Fund. This legislation would permit the Department to budget and account for the cost of retired pay and survivor benefits on an accrual basis. Under the proposal, the President's budget would reflect the incurred liability of the Department for future retirement benefits of the current active and reserve forces. As proposed, current payments to military retirees and their survivors would be made from the Fund. Accruing liability for future retirement obligations in the Defense budget would be shown as an element of personnel costs of the respective Military Departments. The DoD firmly believes that accounting and budgeting for military retired pay on an accrual basis represents a more realistic and accurate treatment of the actual costs of supporting the armed forces.

The Department of Defense has initiated a study plan to determine the feasibility and/or desirability of consolidating the various nonappropriated fund (NAF) retirement programs currently established within the Department of Defense. Included in the study would be the issue of determining the direct benefits to be gained by consolidation. In addition, the issue of the different benefits will be reviewed to determine if changes should be made to provide for a consistent benefit program for all NAF employees. It would be patently unfair to require the NAF retirement plan to close out and participate in a Federal plan if the costs are significantly higher, since the NAF organization must pay its own way under present regulations. Assuming no change will be made with respect to jurisdiction over NAF retirement programs, the Department of Defense will decide, at the completion of the present study effort, the extent of program consolidation and level of benefits for the various groups of employees.

With respect to the retirement plan coverage for appropriated fund employees, the Department of Defense defers to the U. S. Civil Service Commission. However, the GAO conclusion that a single Federal retirement program would be "much easier to manage" is unsubstantiated. In administering the current Civil Service retirement system, the Civil Service Commission has encountered numerous difficulties which relate to the size and complexity of the program.

The draft report proposes that social security be the base for a revised retirement system for Federal employees. The purpose of the Federal Old-Age, Survivors, and Disability Insurance portion of social security is to provide partial economic security in the event of retirement death or disability. The primary goal of the system was to provide an income security floor; however, it has evolved to more than a security floor program. The benefit coverage provided presumes supplemental benefit coverage from pension plans, individual insurance, savings and other investments. It is a regressive tax, but is even more regressive in terms of the benefits. The benefit ratio is weighted heavily in favor of those who had lower earnings over their covered career. This is intended to prevent widespread dependency on public sources for economic security and is not a retirement system. In its operation, it is similar to an income transfer system and, today, operates as a transfer program rather than a retirement program. In its funding, it should be noted that the system is essentially a "pay-as-you-go system." It should be recognized that the current Federal Civil Service retirement system was designed in a manner which provides for plan features essentially the same as provided to those covered by social security. It is also noted that the Employee Retirement Income Security Act of 1974 addresses the integration of social security into pension systems by prohibiting reductions in private pension benefit payments because of an increase in social security benefits or wage base. It would appear, therefore, that the impetus to bring Federal civilians under social security coverage will be a need to broaden the funding base rather than provide old-age pension benefits.

Recognizing the importance of Federal retirement systems on the personnel covered, the organizations concerned, and the cost involved, the Administration is in the process of establishing a Presidential Commission on Retirement. This forthcoming Commission is scheduled to commence a two-year study of retirement policy for the Nation in July 1978. Presently, the Pension Policy Coordinating Group and its working group are being formed under the Office of the Assistant to the President for Domestic Affairs and Policy.

OFFICE OF THE SECRETARY OF TRANSPORTATION
WASHINGTON, D.C. 20590

ASSISTANT SECRETARY
FOR ADMINISTRATION

June 30, 1978

Mr. Henry Eschwege
Director
Community and Economic
Development Division
U. S. General Accounting Office
Washington, D. C. 20548

Dear Mr. Eschwege:

In response to your letter of May 30, 1978, this is the Department of Transportation's reply to the General Accounting Office (GAO) draft report "A Single Retirement System for All Federal Personnel: Is It Desirable?"

Based upon a review of 38 retirement programs associated with the Federal government, GAO has concluded that action to combine these different programs into a single Federal retirement system is highly desirable, as it would correct the many inconsistencies and inequities that exist and bring the retirement matters under more centralized management.

The Department of Transportation believes it to be appropriate to defer comment on the issue regarding 20-year military retirement as this issue is the subject of the President's Commission on Military Compensation and is currently under review at the Office of Management and Budget and Congressional levels. However, this Department does offer discussion on the issues of inequity and efficiency as follows:

-- The Department of Transportation does not concur with the concept embodied in the report that equity among the several Federal retirement programs is paramount. The military retirement program, and each of the other Federal retirement programs, should be viewed as a part of the total compensation received by the personnel covered by the program.

[See GAO note 1 on page 305.]

-- Total compensation should take into account the difference in type of service that is being or has been performed and should consider all forms of compensation received. In this regard military duty involves the potential for, and performance of combat duty, frequent moves, forced family separations, long work hours, and arduous sea and isolated duty. These differences must be considered when determining the total remuneration. Moreover, many of these duties do not result in increased compensation; there is no overtime or night differential pay for military personnel, there is no reimbursement of the cost of buying and selling homes when transferred or for trips to locate housing at the new duty station. Finally, while senior military personnel eventually may earn and serve in less arduous roles, they then face mandatory retirement in prime career age and, in many instances, face imposed limitation on employment. These differences are significant.

-- The Department of Transporation believes that centralization of the Congressional committee jurisdiction over retirement matters might have some merit. However, centralized administration should be avoided. The draft report noted that there will be no appreciable change in administrative costs if the present system were consolidated and integrated. Therefore, there is no advantage to depriving participants of the personalized service they are now receiving.

-- The draft report recommends inclusion of all Federal employees in the Social Security system. It should be noted that the military are now required to participate in the Social Security system.

-- The Department of Transportation recommends that Congress insure that the need for protection of current entitlements are kept in the forefront of any deliberation on this report. In this regard, the President's Commission on Military Compensation has recommended that adequate grandfather provisions be incorporated into any changes to that program. Such provision is equally vital should any changes result from the recommendations in this report.

If we can assist you further, please let us know.

Sincerely,

for Edward W. Scott, Jr.

UNITED STATES DEPARTMENT OF COMMERCE
The Assistant Secretary for Administration
Washington, D.C. 20230

13 JUL 1978

Mr. H. L. Krieger
Director, Federal Personnel and
Compensation Division
U. S. General Accounting Office
Washington, D. C. 20548

Dear Mr. Krieger:

This is in reply to Mr. Eschwege's letter of May 30, 1978, requesting comments on the draft report entitled "A Single Retirement System for All Federal Personnel: Is It Desirable?"

We have reviewed the enclosed comments of the Associate Administrator, National Oceanic and Atmospheric Administration, and believe they are responsive to the matters discussed in the report.

Sincerely,

Elsa A. Porter
Assistant Secretary
for Administration

Enclosure

[See GAO note 1 on page 305.]

UNITED STATES DEPARTMENT OF COMMERCE
National Oceanic and Atmospheric Administration
Washington, D.C. 20230

Ax21

OFFICE OF THE ADMINISTRATOR

JUL 7 1978

Mr. H. L. Krieger, Director
Federal Personnel and Compensation Division
General Accounting Office
441 G Street, N.W., Room 4001
Washington, D.C. 20548

Dear Mr. Krieger:

The National Oceanic and Atmospheric Administration is grateful for the opportunity to comment on the draft GAO report entitled, "A Single Retirement System for All Federal Personnel: Is It Desirable?"

The report identifies a number of "inequities" and proposes a solution to these through consolidation of the Federal retirement systems. The action suggested overlooks the fact that retirement is only part of a total career compensation package. There are "inequities" throughout governmental careers because of different operating conditions. To eliminate the "inequities" after retirement would only be acceptable if corresponding "inequities" were eliminated before retirement.

There are, however, a number of injustices in the present situation, some of which are identified in the report. These should be examined and corrected. A number of archaic practices could be revised, and there are some opportunities for administrative streamlining. It may be possible, as is suggested, to combine administratively the differing systems. Nothing should be done, however, without consideration of the effect on the total career contract.

We agree that the Federal retirement problem is severe enough to merit top Congressional scrutiny, and we concur with the recommendation. The general conclusion of the report which calls for centralization, standardization, and equalization of retirement benefits could, however, cause numerous serious personnel management problems, if adopted solely in the name of administrative neatness and the elimination of "inequities."

We strongly disagree with the conclusion in the report which states that there is "no justification for granting preferential retirement benefits to certain groups merely because of the type of work performed." There is justification, if job requirements and the effects of the type of work on the individuals are considered.

[See GAO note 1 on page 305.]

APPENDIX V

The data presented for the NOAA Corps is factual. The Corps' retirement system is integrated with Social Security and is administratively centralized by contract with the U.S. Navy, which is in consonance with several of the recommendations of the report.

Sincerely yours,

George S. Benton
Associate Administrator

DEPARTMENT OF HEALTH, EDUCATION, AND WELFARE
OFFICE OF THE SECRETARY
WASHINGTON, D C 20201

JUL 15 1978

Mr. Gregory J. Ahart
Director, Human Resources
Division
United States General
Accounting Office
Washington, D.C. 20548

Dear Mr. Ahart:

The Secretary asked that I respond to your request for our comments on your draft report entitled, "A Single Retirement System For All Federal Personnel: Is It Desirable?" The enclosed comments represent the tentative position of the Department and are subject to reevaluation when the final version of this report is received.

We appreciate the opportunity to comment on this draft report before its publication.

Sincerely yours,

Thomas D. Morris
Thomas D. Morris
Inspector General

Enclosure

[See GAO note 1 on page 305.]

DEPARTMENT OF HEALTH, EDUCATION, AND WELFARE

Comments on GAO Draft Report:

"A Single Retirement System for All Federal Personnel: Is It Desirable?"

We agree with the basic premise of the report, that is, the retirement systems covering Federal employees, civilian and military, are due for a close critical analysis. However, while GAO makes a good case for a homogeneous system, it is not the only acceptable solution. Alternate solutions worthy of consideration are correcting inequities and weaknesses within the existing retirement systems or consolidating similar systems wherever possible but without the goal of achieving a single system.

The portions of the draft report which concern the Commissioned Corps of the Public Health Service (PHS) are accurate. We would like to emphasize that the purpose for providing 20-year retirement for this group of employees is as valid today as it was when established. This provision is necessary as an incentive so officers will stay longer in the Corps. Opportunities abound in the private sector for the medical professionals in the PHS Commissioned Corps. The availability of 20-year retirement is an important factor in retaining these valuable employees in public service.

We are deferring comment on the proposal in the report that social security benefits form the base for any Federal retirement system. This issue will be thoroughly analyzed in the study mandated by Congress in section 311 of Public Law 95-216. This provision called for the Secretary of Health, Education, and Welfare in conjunction with other affected agencies to conduct a study of the desirability and feasibility of extending social security coverage to all Federal employees.

UNITED STATES CIVIL SERVICE COMMISSION

WASHINGTON, D.C. 20415

IN REPLY PLEASE REFER TO

YOUR REFERENCE

JUL 1 4 1978

Mr. H. L. Krieger, Director
Federal Personnel and Compensation Division
U. S. General Accounting Office
Washington, D. C. 20548

Dear Mr. Krieger:

This letter is in response to your request dated May 24, 1978 for our comments on GAO DRAFT Report "A Single Retirement System For All Federal Personnel: Is It Desirable?", FPCD 78-49.

We have reviewed the report and concluded that we are already on record on many of the issues raised, inasmuch as they have been subject of various other GAO reports on which we have previously commented. Most notable among these previous reports was "Federal Retirement Systems: Unrecognized Costs, Inadequate Funding, Inconsistent Benefits", dated August 3, 1977. To the extent that the present report is consistent with the earlier report, we refer you to our previous comments to Congress.

We find the report to be factually correct in most respects, but we do have comments on the major topics discussed.

1. Are Separate Systems and Benefits Needed?

   It is true as GAO indicates that there are many inconsistencies and inequities that exist among the various Federal retirement systems. Some consolidation and integration of these systems would alleviate such problems. The greatest problem of this kind occurs when Federal employees change jobs and as a result move from a position covered under one retirement system to a position covered under another system. While prior Federal service is generally creditable under the subsequent retirement system, various mechanisms exist for barring the crediting of the same service under both systems. Another problem that recurs frequently has to do with annuitants under one Federal retirement system becoming employed in a position covered by another Federal retirement system. Not all retirement systems have the rule which the Civil Service Retirement System does that pay during any reemployment must be reduced by an annuity equivalent.

[See GAO note 1 on page 305.]

THE MERIT SYSTEM—A GOOD INVESTMENT IN GOOD GOVERNMENT

As for GAO's concern that eligibility criteria for participation, in other words, criteria for coverage under the Federal retirement systems, are not as clear as they might be, we think that the existing criteria are quite clear and made quite specific by enabling legislation for most of these systems. For example, coverage under the Civil Service Retirement System is generally universal over Federal employment. Coverage depends on the type of appointment. Generally speaking all employees are covered except those whose appointments are limited to a year or less. In addition, there are certain specific statutory exclusions such as those for members of the Federal judiciary and employees subject to other Federal retirement systems.

It should be understood that differences in specific benefits in the different retirement systems are not necessarily bad. They were put there for very specific reasons by the Congress which enacted most of these systems in support of the special personnel management system to which they were related.

A. Need for Establishment of Federal Retirement Policy

There is certainly a need for regular coordination of activities among the various Federal retirement systems. We try conscientiously to pay heed to this need. Most other retirement systems appear to be aware of this need also and indeed seem quick to make parallel changes in their retirement systems any time changes are made in the Civil Service Retirement System. Therefore, some coordination among the retirement systems already goes on.

B. Need for a Single Retirement Program Administered by One Agency

The Civil Service Commission has traditionally favored some consolidation of other retirement systems with the Civil Service Retirement System. However, it is not entirely clear that all such other systems should necessarily be consolidated with the Civil Service Retirement System, and the Commission must defer to the views of the other agencies which administer such other systems as to whether there is a need for their particular retirement systems.

It is important to recognize that each Federal retirement system was created to support a unique personnel management system. For example, Civil Service Retirement is an important adjunct of Federal civil service personnel management under the provisions of title 5, United States Code. Similarly the Foreign Service Retirement System and the Central Intelligence Agency Retirement

System are important adjuncts of their related personnel management systems. To the extent that these various Federal retirement systems were clearly created in support of particular personnel management systems administered by separate agencies it is not nearly so clear as GAO suggests it might be that administration of these various retirement systems would be improved if they were consolidated into one. It would be difficult for one agency to become fully familiar with the details of the various Federal personnel systems and the retirement systems which support them. Even if the systems were consolidated, presumably, special benefits for special groups in need of provision for economically feasible early retirement might have to remain. Our staff is continuing to study the need for special retirement benefits for Federal law enforcement officers.

C. Need for Centralization of Congressional Committee Jurisdiction Over Retirement Matters

Any Congressional committee with centralized jurisdiction over retirement matters would, like a similar centralized retirement agency in the Executive branch have very broad jurisdiction over retirement systems which support numerous Federal personnel systems. Today these personnel management systems and the retirement systems which support them tend to be reviewed by the same Congressional Committee which reviews the activities of the entire agency concerned with the particular personnel and retirement systems. For example, the Committees on civil service have reviewed both the civil service personnel system and the civil service retirement system, and the Committees on foreign affairs have reviewed both the foreign service personnel system and foreign service retirement system. The committees on civil service and foreign affairs would, we believe, still retain a vital interest in the civil service and foreign service retirement systems, respectively, even if a new committee with centralized jurisdiction over Federal retirement systems were created. Ultimately, whether such a centralized committee on retirement matters could be created in the House and in the Senate, is a matter uniquely for them to decide and we defer to the views of the Congress on whether such a committee ought to be established.

II. GAO Comments Directed at Other Federal Retirement Systems

A. GAO recommends that employees of non-appropriated fund instrumentalities of the Department of Defense should no longer be provided retirement benefits other than those normally available to Federal employees, if it is determined that NAF personnel are indeed Federal employees.

Since 1952 there has been a law that stated that for Civil Service Retirement purposes NAF personnel would not be deemed to be Federal employees. Prior to that time there were various court decisions that had produced contradictory decisions and inclusive decisions as to whether NAF personnel were really Federal employees. As for specific recommendations on whether NAF personnel should be treated as regular Federal personnel and brought under the Civil Service Retirement System, we basically defer to the views of the Department of Defense. However should such personnel be determined by DOD and the Congress to be Federal personnel entitled to coverage under the civil service retirement system such coverage would almost have to be prospective from that time. The cost to the Civil Service Retirement System of having to credit any prior NAF service under the Civil Service Retirement System would be substantial and in the millions of dollars.

B. GAO indicates it sees no special reason for the existence of the so called quasi-Federal employee retirement systems administered by the Federal Reserve Banks, the Federal Home Loan Banks and the Foreign Credit Banks.

As we understand it, these systems were specifically created to facilitate the transfer of banking industry personnel in and out of these agencies without the loss of benefit protection or diminution of the level of such protection. We defer to these banking agencies as to whether or not there is a need for continuing the existence of such programs.

C. The GAO report finds little reason to support the existence of TIAA/CREF retirement system benefits for certain employees of the Smithsonian Institution, the USDA Graduate School and the Uniformed Services University of the Health Sciences.

Such other retirement systems for employees of these institutions as we understand it were created to enable these institutions to sucessfully compete in attracting qualified personnel from the academic community who generally had TIAA/CREF retirement benefits with whatever educational institutions they had previously been employed. The way TIAA/CREF works its benefits and protections are readily transferrable as a member of the academic community moves from one educational institution to another. As for the merits of continuing such special benefit programs in these three institutions, as well as in the University of the District of Columbia which also offers TIAA/CREF benefits to its employees, we defer to the views of the agencies involved.

D. This GAO report reiterates once again the GAO position that Federal employees now in the retirement system for District of Columbia policemen and firemen should be brought under the Federal civil service retirement.

As we stated in the past, the Commission concurs with this position and has been working with the District Government and personnel at OMB, the Executive Protective Service and the U.S. Park Service and the U.S. Secret Service to find a way to accomplish this change in an equitable and cost effective manner.

[See GAO note 3 on page 305.]

F. Those systems covering employees who do not meet eligibility criteria for participation in the Federal retirement systems, says GAO, should be made subject to the laws governing private pension plans.

We are aware that apparently there has been a legal question as to whether the so called quasi-Federal retirement systems and those for non-appropriated fund personnel are subject to the provisions of the Pension Reform Act of 1974 - The Employee

Retirement Income and Survivors Annuity Act. We defer to the administrators of the systems as to whether they should be subject to the provisions of the Pension Reform Act.

III. Financing Practices of Federal Retirement Systems

The GAO report suggests that there is a need for a uniform method of determining liabilities associated with Federal retirement systems and a need for more consistent funding practices among such systems. This is a very complex issue which should be considered very carefully in depth with input from all retirement systems. Variations in financing the various systems may be necessary depending on the different types of benefits the particular system offers. As we have indicated before, we do agree that the present method of determining and presenting retirement costs results in an understatement of such costs. We believe that the systems and proposed changes in the systems should be valued on the costs presented on a dynamic as well as on the current static cost basis. This procedure would enhance cost recognition and budgetary discipline as well as promote sounder fiscal and legislative decision making.

The GAO also recommends in this report that agency operations should be charged with all costs not covered by employee contributions. As we have said before, this issue is one primarily concerned with budgetary and cost allocation considerations policy. Our main concern as a trustee of the Civil Service Retirement and Disability Fund is that the system be capable of meeting its obligations through adequate financing; thus, the source or allocations of government contributions is not of as much concern as the adequacy of total income. The Commission currently has no position on this recommendation.

IV. Social Security for Federal Employees

Lastly, GAO recommends development of an implementation plan for conversion of Federal employee retirement systems to coordination with social security system so that all Federal personnel might be covered under social security. The issue of whether Federal employees should be generally subject to social security and their Federal retirement systems modified to provide benefits in addition to social security is a very complex matter on which we have no position at this time. We are open to the possibility of such a change, however, we do not think it would be possible to reach a final position in this matter until some mechanism for making the transition has been determined which will protect rights of employees and minimize costs to the government. The Congress has directed an interagency study of this question in which the

Commission is to participate under the Social Security Amendments of 1977. No conclusions on the issue of social security coverage for Federal employees can be reached before this study is completed.

It should also be added that a principle reason GAO uses for consolidation of retirement systems under social security - that most such systems are already coordinated with social security - is not supported by the facts. Although several of such systems are coordinated with social security, such retirement systems cover only a minority of all Federal employees. Most Federal employees are covered under the Civil Service Retirement System which, of course, is not presently coordinated with social security.

Sincerely yours,

Alan K. Campbell
Chairman

DEPARTMENT OF STATE
Washington, D C 20520

June 28, 1978

Mr. J. K. Fasick
Director
International Division
U. S. General Accounting Office
Washington, D. C.

Dear Mr. Fasick:

I am replying to your letter of May 24, 1978, which forwarded copies of the draft report: "A Single Retirement System for All Federal Personnel: Is It Desirable?"

The enclosed comments were prepared by the Director General of the Foreign Service.

We appreciate having had the opportunity to review and comment on the draft report. If I may be of further assistance, I trust you will let me know.

Sincerely,

Daniel L. Williamson, Jr.
Deputy Assistant Secretary
for Budget and Finance

Enclosures:
As Stated

[See GAO note 1 on page 305.]

GAO DRAFT REPORT: "A SINGLE RETIREMENT SYSTEM FOR ALL FEDERAL PERSONNEL: IS IT DESIRABLE?"

The Department of State appreciates the opportunity to comment on the portion of the Comptroller General's proposed report to the Congress you forwarded May 24, 1978 entitled A Single Federal Retirement System for All Federal Personnel: Is it Desirable?

The draft report states that there is an absence of an overall Federal retirement policy and you recommend that the appropriate committees of the Congress hold hearings to consider in depth the issues raised in your Report and that the Congress set in motion actions to establish a single retirement system. Specific recommendations include:

1. The establishment of a Federal retirement policy which outlines the principles, objectives, and standards to be followed in designing a retirement system for military and civilian personnel. The policy should cover such matters as benefit levels, financing and funding, vesting, and administration. It should serve both management and employee needs and include a principle that in the absence of any justifiable management purposes, all Federal personnel are to receive equitable benefits.

   Department Comment: The Department believes that the establishment of a retirement policy for Federal employees to include the items listed in the GAO recommendation above would be helpful. We believe, however, that the conditions of employment are so unlike between most Federal and Foreign Service employees with respect to conditions of service, health hazards and length of useful service, that entirely different systems are necessary if Foreign Service management and employee interests are to be served.

2. The centralization of committee jurisdiction over retirement matters to better assure consistent application of the retirement policy.

Department Comment: The Department would wish to defer to the Congress on this issue. We would point out that the Foreign Service Retirement Amendments of 1976, title V of P.L. 94-350, made a comprehensive revision of the Foreign Service retirement system. In areas such as survivorship where the Congress believed Foreign Service and Civil Service benefits should be the same, that Act revised Foreign Service provisions to conform with Civil Service provisions.

In other areas, such as the basic annuity formula and provisions for early retirement and separation, where there is a management reason for a different Foreign Service provision, existing Foreign Service provisions were retained or modified as appropriate. In addition, the 1976 Act added a provision to the Foreign Service Act for the automatic incorporation in the Foreign Service system of future changes in the Civil Service system in areas where the Congress establishes conformity between the two systems.

We believe that this 1976 Act went a long way toward achieving the basic objectives set forth in the draft report with respect to the Foreign Service system, and might serve as a precedent for application to some other retirement systems, and be more practical than the fundamental and monolithic change recommended in the draft report.

The Foreign Service retirement system is closely coordinated with the special features of the Foreign Service personnel system. Both systems are designed to facilitate recruitment and retention of a highly qualified, mobile corps of Foreign Service personnel capable of assuming a wide range of demanding duties, frequently under difficult and dangerous conditions, anywhere in the world, as the needs of the nation may require. The Senate Foreign Relations Committee and the House International Relations Committee are intimately familiar with the kinds of problems the Foreign Service personnel and retirement systems are designed to meet. They applied this knowledge and experience when fashioning the landmark 1976 Act described above. Those Committees are well equipped to continue jurisdiction over these matters.

3. That there be established a central authority responsible for overall administration of the retirement system.

   Department Comment: The only reason to recommend centralized management of Federal retirement programs, in our view, would be to provide improved and more economical administration. This is not supported in the body of the draft report which states that "...centralized administration would not significantly reduce administrative costs, but centralized control might (emphasis added) result in improved and more consistent administrative methods and procedures with improved service to retirees." We believe that centralized management of the retirement systems in and of itself has no inherent virtue. We doubt that "bigger is better", and we believe that this Department is better able to support Foreign Service annuitants than a centralized manager of a single retirement system.

   Retired Foreign Service personnel perform a significant service for the Department in acquainting members of their respective communities with foreign policy issues and problems. An effective and strong United States foreign policy can only be built and maintained by an informed citizenry. Foreign Service retirees, by their participation in local activities, contribute significantly to this end. We believe their continuing ties to the Department in every possible way, including the continued servicing of their annuities by the Department, contribute to the retirees continued interest in foreign affairs and is worthwhile. In particular, we see no point in severing this tie with Foreign Service retirees if overall cost savings are not envisioned.

4. The adoption of actuarial valuation methods and funding provisions that reflect the full cost of the retirement program and charge to agency operations all costs not covered by employee contributions (if the agreed upon policy calls for employees to share retirement program costs).

   Department Comment: The Department agrees that all retirement costs should be fully stated in the Federal budget. However, we believe apportionment of central Civil Service retirement costs now stated in connection with the budget for the Civil Service Commission among all Federal agencies would be unnecessarily complex.

5. The development of an implementation plan for conversion to the new system and the extension of social security coverage to all Federal personnel.

   Department Comment: Since the Department does not agree that a single retirement system would necessarily better meet the needs of the U.S. Government or of U.S. employees, we see no need for an implementation plan for conversion to a single retirement system. We defer comment on the extension of social security coverage to all Federal personnel until a full and complete proposal for such coverage is developed.

Harry G. Barnes, Jr.
Director General of
the Foreign Service

BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM
WASHINGTON, D C 20551

G. WILLIAM MILLER
CHAIRMAN

June 23, 1978

Mr. H. L. Krieger
Director
Federal Personnel and
Compensation Division
United States General
Accounting Office
Washington, D. C. 20548

Dear Mr. Krieger:

Thank you for the opportunity to review and comment on your proposed report on the desirability of establishing a single retirement system for all Federal personnel, transmitted with your letter of May 24, 1978.

While the stated objective seems highly desirable in the abstract, namely, a single retirement system for Federal personnel, when applied to include employees of the Federal Reserve Board and Federal Reserve Banks, the Board is strongly opposed to such a proposal because in practice it would appear to offer substantial disadvantages. This opposition reflects the Board's judgment that certain of the conclusions stated in the report with respect to similarities in the nature of the functions and responsibilities between System personnel and employees of other regulatory bodies are not borne out by the actual circumstances. The report also does not appear to give adequate recognition to the Congressional intent underlying provisions of the Federal Reserve Act granting to the Board, subject to statutory provision, control of the provisions for employment, compensation and expenses of its employees. Similarly, while your proposed report addresses concern over inadequate funding, inconsistent benefit levels and ineffective administration in many of the Federal retirement systems, none of these criticisms can be accurately applied to the Federal Reserve retirement program.

[See GAO note 1 on page 305.]

Mr. H. L. Krieger

The actuarial cost of our plans is fully funded on a "dynamic" basis, and all pension supplements granted in past years have been funded by contributions into reserves in the amounts called for by the actuary's projections of terminal funding needs.

The value of the benefits for persons under that part of the plan known as the "Board Plan" is estimated to be equal roughly to the value of the benefits provided under that part of the plan referred to as the "Bank Plan." Only the design and the sources of benefits differ. The "Board Plan" provides pension, disability, and survivor benefits for Board personnel virtually identical to those granted employees subject to the Civil Service Retirement Act, and with the same contribution required of employees. In establishing the Board Plan, the Board of Governors provided that any changes in the Civil Service retirement plan would be embodied in the Board Plan, unless formal action to the contrary was taken by the Board of Governors. In that part of the program known as the "Bank Plan," benefits are integrated with those available to employees under the Social Security system. These benefits are more closely related to those provided by employers with whom the Reserve Banks compete for personnel.

The administration of our program has been, and continues to be, both effective and responsive to employee claims. In all major respects, a highly competent staff has been able to react to the needs and claims of employees of the System. We feel that these are distinctly positive factors in employee morale and thus in the overall effectiveness of the Federal Reserve System.

One very important feature of the Federal Reserve retirement plans that also must be considered is that they grant service credit for employment in any part of the Federal Reserve System. Obviously, with the essential interchangeability of our personnel between the Board and the Reserve Banks, it is important that there be full portability, for pension purposes, of service throughout the System. This portability is not provided by the Civil Service plan.

There seems to be no persuasive reason for Congress to dismantle a proven, well functioning Federal Reserve retirement program and to trade for the uncertainties of service from a large centralized system. This does not seem in the best interest of the

Mr. H. L. Krieger

Federal Reserve or the important role it plays in the economy. We have a smoothly working program. Its essential characteristics are adequate funding, consistent benefit levels, effective administration and portability within the System. Moreover, there seems to be no singular advantage that would outweigh the cost and disruption of the consolidation itself.

In addition, any move to bring Federal Reserve Bank employees directly under the centralized retirement system your report proposes could be a step toward a fundamental change in the concept and nature of the Federal Reserve System. The independence of this country's central banking system, which is comprised of a unique combination of a Government Board and quasi-government Federal Reserve Banks, has proved to have substantial strengths in the public interest. We oppose actions that run counter to or could impinge upon that structure and its independence from the influences of possible partisan concern.

Various provisions of the Federal Reserve Act also provide a scheme of Congressional oversight that assures appropriate accountability of the System to the Congress.

[See GAO note 3 on page 305.]

Sincerely,

TENNESSEE VALLEY AUTHORITY
KNOXVILLE, TENNESSEE 37902

July 3, 1978

Mr. H. L. Krieger, Director
Federal Personnel and Compensation Division
U.S. General Accounting Office
Washington, D.C. 20548

Dear Mr. Krieger:

We are glad to comment on the draft report on the desirability of a single retirement system for all Federal employees.

The basic conclusion of the report is that there are no compelling reasons for the various agencies to maintain separate retirement systems. It does not seem to us that the report supports that conclusion. To the contrary, the financial soundness of the TVA Retirement System illustrates the merit of structuring Federal retirement systems to fit the needs of each agency and its employees.

The financing of a consolidated Federal retirement program, such as the report urges, is staggering. The combined contributions which TVA makes to the Social Security System and to the TVA Retirement System substantially exceed those we would make to the Civil Service Retirement System at its present rate of contribution. However, the standard contribution to the latter System by agencies and employees provides only about one-half the true cost of the Plan. The merger of TVA's plan under existing circumstances would perhaps provide an initial cost-savings but could result in much higher contribution rates by both TVA and its employees later or, in the absence of such funding, add to the tax burden of financing the unfunded costs. For instance, based on the report's figures showing the true cost of the Civil Service Retirement System as 27.4 percent of payroll and assuming that the 7 percent employee contribution rate does not change, it is not difficult to visualize an agency contribution rate in excess of 20 percent. For agencies operating primarily on user-fees, such as TVA, that increased cost could have substantial impact. In our case, most of the increased cost would have to be passed on to our electric power ratepayers. Having contributed over the years an amount sufficient to properly fund the TVA Retirement System, it would not be an attractive proposition to be faced with the potential obligation of making up past funding deficiencies of other agencies.

[See GAO note 1 on page 305.]

Mr. H. L. Krieger July 3, 1978

In summary, TVA and its members have a sound retirement system and we do not believe that conformity is a proper basis for eliminating it. The System's benefits have been designed to fit the particular needs of both the Agency and the members. The System's independence permits changes to be made in a timely manner based on clearly identified need and after full consideration of the real cost of such changes. The program has been conscientiously funded from its inception and indiscriminate changes in benefits have been avoided. Additionally, unlike most Federal retirement systems, the TVA System has no unrecognized costs. The national recognition of the TVA System reflects favorably on the Federal Government in general and on TVA in particular.

We reviewed the sections of the report dealing with the TVA Retirement System; and we have a few editorial suggestions, as shown on the enclosed pages.

Thank you for giving us the opportunity to comment on the report.

Sincerely,

H. N. Stroud, Jr.
Acting General Manager

Enclosures

[See GAO note 4 on page 305.]

ADMINISTRATIVE OFFICE OF THE UNITED STATES COURTS
WASHINGTON, D.C. 20544

WILLIAM E FOLEY
DIRECTOR

JOSEPH F SPANIOL, JR
DEPUTY DIRECTOR

June 30, 1978

Mr. H. L. Krieger
Director, Federal Personnel
and Compensation Division
General Accounting Office
441 G Street, N. W.
Room 4001
Washington, D. C. 20548

Dear Mr. Krieger:

I am writing in response to the recent request of Mr. Victor L. Lowe for comments upon a draft report prepared by the General Accounting Office regarding a proposed single retirement system for all federal personnel. I appreciate the opportunity to comment upon this draft and Mr. Lowe's offer to include my comments in the final report.

I wish to state at the outset that my office does not oppose the concept of an overall retirement system combining the various existing retirement programs and applicable to federal employees generally, which is suggested in your report. We believe, however, that exceptions should continue to be made in such a consolidated system when considerations of either law or fact argue in favor of separate treatment for any category of federal officers or employees. We further submit that such unique considerations are present with respect to the two categories of officials covered by your report with which my official responsibilities are concerned, namely the judges of the United States and certain other officers of the Judiciary: the Administrative Assistant to the Chief Justice, the Director of the Federal Judicial Center, and the Director of the Administrative Office of the U. S. Courts.

With respect to federal judges, the central fact which must be considered in evaluating the provisions of current law for their retirement, resignation on salary, and survivor benefits is that those judges appointed under Article III of the Constitution (including the justices of the

[See GAO note 1 on page 305.]

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Supreme Court, circuit and district judges of the United States, and the judges of the Court of Claims, Court of Customs and Patent Appeals, and Customs Court) are entitled to hold office for life, assuming good behavior, and may be involuntarily removed from office only through impeachment by the Congress. Thus any system which is designed to induce aged or disabled federal judges to either relinquish their offices voluntarily or to retire from full judicial service must provide sufficient financial protection to them so that they will be reasonably motivated to do so.

In this regard the statement on page 132 (renumbered page 27) of the report that "separate retirement programs" exist for Article III judges should be clarified. Such judges do not in fact retire in the sense that this term is applied to other employees. Under 28 U.S.C. §371(b) they rather have the option, upon attaining the age of 70 and completing at least ten years of federal judicial service or attaining the age of 65 and completing at least 15 years of such service, to retain their office but "retire from regular active service." As noted in your report, judges who exercise this option are then known as senior judges and may be designated and assigned under 28 U.S.C. §294 to continue to perform such judicial duties as they are willing and able to undertake. The Supreme Court in Booth v. United States, 291 U.S. 339 (1934), affirmed that such senior judges continue to hold the judicial office, although their assumption of senior status does create a vacancy in their courts to which the President may by law nominate a successor.

Your report concludes with respect to senior judges that their retention of the right to the full judicial salary is justified because the overwhelming majority of them who are able to do so continue to perform substantial judicial duties. We would concur in this conclusion and would add that their entitlement to the salary of the office logically follows from the fact that they continue to hold the office and may not under the Constitution be deprived thereof or have their salaries diminished except upon impeachment. One further observation should be made, however, with respect to the survivor benefit provisions for such judges which are discussed in your report at page 137 and

[See GAO note 5 on page 305.]

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following. Because federal judges do not "retire" in the normal sense of that word meaning the relinquishment of office, they do not have the opportunity available to federal employees generally to provide for their survivors in conjunction with their own retirement program. See 5 U.S.C. §8331(1)(i), which excludes justices and judges of the United States from participation in any aspects of the civil service retirement system.

The system of judicial survivors' annuities which is set forth at 28 U.S.C. §376 is intended to meet this need. While it is true that this system differs in many respects from the survivor benefits available under civil service retirement, the difference in financing and computation of benefits is necessary in view of the relatively low number of years of judicial service completed by most judges as compared with the years of service creditable toward the retirement of federal employees, spanning their entire careers. As discussed more fully in the attached comments, federal judges are typically appointed to office at the prime of their professional lives and thus have the opportunity to complete only an average of approximately 15 years' service in that capacity (see page 134 of your report). Their survivor benefits based upon years of creditable service must logically be computed under a different formula from that of the civil service retirement system in order to afford meaningful financial protection to judicial survivors.

I should next like to discuss the provisions of 28 U.S.C. §371(a), stating that a justice or judge who resigns after attaining the age of 70 and completing at least ten years of service shall for the remainder of his life receive the judicial salary which he was receiving when he resigned. Your report states at page 135 that no explanation had been found as to why a resigned judge should have such continued entitlement to a government salary. The rationale underlying this section was well explained by the Court of Claims in the case of Johnson v. United States, 79 F. Supp. 208 (1948), which stated that the Congress adopted this statutory provision in order that "superannuated judges might be induced to relinquish their offices if they could be assured for the balance of their lives of the salary attached to it."

[See GAO note 5 on page 305.]

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In its opinion the Court of Claims further described the nature of the continued salary payments made to a resigned judge under this law "not as a pension or a gratuity, but as the consideration offered to induce him to give up his right to hold the office as long as he lives." 79 F. Supp. at 210. It was the view of the Congress that the judiciary would benefit by the resignation of judges of advanced age who no longer possessed the physical vigor or motivation to continue to perform judicial duties. Furthermore it is less expensive to the government to have such judges resign and pay them the salary which they were receiving at the time of resignation than to have them retire to senior status, in which they would be entitled to all future salary increases accorded to judges while not rendering any concomitant benefit in accepting designations for continued judicial service under 28 U.S.C. §294.

A similar explanation is applicable to section 372(a) of title 28 with respect to the entitlement of judges to retire and continue to receive the salary of the office (or one-half of such salary if less than ten years of judicial service have been completed) upon becoming permanently disabled. If such continued salary benefits were not provided, judges who are constitutionally entitled to hold office for life would refuse to certify their disability and would insist upon continuing in active status.

Finally I should like to comment upon the report's observation with respect to the retirement provisions applicable to the Director, Administrative Office of the U. S. Courts, under 28 U.S.C. §611, for which the Administrative Assistant to the Chief Justice is eligible under 28 U.S.C. §677. Similar provisions are applied to the Director of the Federal Judicial Center through 28 U.S.C. §627. The report states at page 181 (renumbered page 40) that the affected positions are not sufficiently unique to warrant special retirement treatment. An opposite conclusion is reached, however, at page 234 (renumbered page 42) with respect to the President

[See GAO note 5 on page 305.]

Mr. H. L. Krieger
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and the Comptroller General of the United States, "who may have had no prior federal service and whose tenures in office are limited by law." While it is true that the incumbents of the three affected judicial offices are not legally limited in their terms of office as are the President and the Comptroller General, I would suggest that the other factors making the latter offices appropriate for special retirement coverage apply as well to the Director of the Federal Judicial Center, the Administrative Assistant to the Chief Justice, and the Director of the Administrative Office.

Each of these offices is such that there will frequently exist the need to recruit individuals out of the private sector to fill them. Such individuals would have to be highly qualified and accomplished in the fields of law or public administration. Thus it is likely that they would be at mid-career and might have had little or no prior service in the government. Although I have made my career in the federal service, my four predecessors in this office had little or no previous government service, before appointment as Director, which would have been creditable toward their retirement. Likewise the present Director of the Federal Judicial Center and the Administrative Assistant to the Chief Justice had both had distinguished academic careers prior to assuming their current offices.

Another characteristic which these positions share with the office of Comptroller General is that the tenure of the incumbents has historically been relatively brief. Indeed only one of my predecessors served in this office as long as the 15-year term allowed to the Comptroller General by statute. The average tenure of each of my four predecessors was less than nine years, and excluding the 17-year tenure of the first Director of the Administrative Office, the others each served an average of only about six years. The Federal Judicial Center in its first nine years of existence was headed by three different Directors. Thus these offices have been able to attract a succession of individuals with diverse backgrounds and have changed hands at quite frequent intervals, bringing fresh viewpoints and ideas to federal judicial administration. Without the special retirement provisions described in the report, it is doubtful that this would have been the case.

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I hope that these comments may be helpful in your evaluation of the draft report. I am also attaching for your further information an excerpt from a letter sent last year to Mr. Lowe on this subject by the late Director Rowland F. Kirks, and some additional materials prepared by my office in response to certain observations in the draft report. If the Administrative Office can be of further assistance in your study of federal retirement programs, please feel free to contact us.

Sincerely,

William E. Foley
Director

Enclosures

[See GAO note 2 on page 305.]

UNITED STATES TAX COURT
WASHINGTON, D C 20217

CHAMBERS OF
C. MOXLEY FEATHERSTON
CHIEF JUDGE

July 20, 1978

Mr. H. L. Krieger
Director, Federal Personnel
and Compensation Division
General Accounting Office
Room 4001
441 G Street, N.W.
Washington, D. C. 20548

Dear Mr. Krieger:

As requested, we are submitting comments on portions of the draft of a proposed report entitled "A Single Retirement System for All Federal Personnel: Is It Desirable?"

We fully recognize that there are substantial reasons for questioning the existence of the variety of retirement plans for Federal employees and that it may be desirable to eliminate some of those separate plans and cover most Federal employees under a single retirement system. Yet, as the GAO report recognizes, there are "compelling reasons" for the maintenance of some separate retirement systems.

[See GAO note 1 on page 305.]

The report finds that the separate retirement system for district and appellate Federal judges should be continued. As we understand it, you have concluded that there are also "compelling reasons" for the continued maintenance of the separate retirement system for judges of the United States Tax Court. This conclusion is predicated on the premise that Tax Court judges, on the one hand, and United States district and appellate judges, on the other, should be treated in the same fashion for retirement purposes. Both categories of judges are subject to being assigned judicial duties after formal retirement. That potential for assignment differentiates their situation from that of other retired Government employees and justifies their continuing to receive the salary of the office, irrespective of whether they are actually serving on recall at any given time.

The purpose of this letter is to set forth in detail our reasons for believing that your conclusions and the predicate on which they are based are sound and that, therefore, the present retirement system for Tax Court judges should not be changed.

Role of the United States Tax Court

At the outset, we should like to describe the functioning of the Tax Court and the responsibilities of its judges. Although the predecessor of the Tax Court, the Board of Tax Appeals, was initially established as a part of the executive branch of the Government, Congress, in 1969, made the Tax Court a court of record and removed it from the executive branch. Tax Reform Act of 1969, sec. 951. In doing so, Congress gave legal effect to the role of the Court which, as a matter of fact, had already existed.

Throughout the existence of the Tax Court, including the period when it was known as the Board of Tax Appeals, it has functioned only as a court of law. While the Court was still located in the executive branch, the judicial character of its work was described in the following manner:

> Whatever label might be used to characterize this Court for various purposes, its proceedings are, and were intended by Congress to be, in every sense of the word, judicial. It is required by statute to act, and does act, solely in a judicial manner,

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> and exercises only judicial power. We hear and decide only real controversies between adverse parties, following procedures that are inherently judicial. We make no independent investigation of the facts as do some agencies labeled "administrative" either upon our own motion or upon the motion of one of the parties; our findings of fact are based solely on evidence submitted to us by the parties in accordance with prescribed rules. We do not appear as parties in court to enforce our orders or the law as do so-called administrative agencies. Our findings of fact carry the same weight as those made by a District Court sitting without a jury. Our decisions are final and may be attacked, in the same manner as District Court decisions, only by appeal to a United States Court of Appeals. [Fairmont Aluminum Co. v. Commissioner, 22 T.C. 1377, 1384-1385 (1954), affd. 222 F.2d 622 (4th Cir. 1955), cert. denied 350 U.S. 838 (1955); footnotes omitted.]

The Tax Court applies the rules of evidence applicable in the United States District Court for the District of Columbia (sec. 7453, I.R.C. 1954 2/) which, under the Federal Rules of Evidence, apply generally in the district courts; its decisions are appealable to the courts of appeals in substantially the same manner as are the decisions of the district courts (sec. 7482);

2/ All statutory references are to the Internal Revenue Code of 1954, unless otherwise indicated.

and within the limits of its jurisdiction, it serves the same role as the district courts (Brittingham v. Commissioner, 451 F.2d 315 (5th Cir. 1971)). In the Brittingham case, the court of appeals described the authority and responsibilities of the Tax Court in the following passage:

> * * * comity dictates that courts of coordinate jurisdiction not review, enjoin or otherwise interfere with one another's jurisdiction. The Tax Court, within its limited jurisdiction, is of equal stature with the district court. In connection with those cases before it, it has the same power available to it as the district court. The decisions of each are fully reviewable by the same Court of Appeals. The proper exercise of restraint in the name of comity keeps to a minimum the conflicts between courts administering the same law, conserves judicial time and expense, and has a salutary effect upon the prompt and efficient administration of justice. * * * [451 F.2d at 318.]

The Tax Court hears and decides the overwhelming bulk of Federal tax litigation. Although a taxpayer who is unable to settle his controversy with the Internal Revenue Service can pay the tax and sue for a refund in the district court or the Court of Claims, the Tax Court is the only Court in which he can dispute a deficiency without first paying it. Most taxpayers bring their cases to the Tax Court. In the fiscal year ended June 30, 1976, the latest year for which statistics are available for all courts, 889 cases were commenced in the district courts; 144 in the Court of Claims; and 11,360 in the Tax Court. In recent years, the volume of litigation in the Tax Court has increased dramatically. For a number of years, 6,000 or 7,000 cases were commenced each year, but in the past year, the number of new cases exceeded 12,000. As of April 30, 1978, the Tax Court had 21,537 pending cases.

For years, the Tax Court has had jurisdiction to hear and decide income, gift, and estate tax cases. In recent years, Congress has enacted special provisions for handling small tax cases in order to make it easier for small taxpayers to bring their controversies to this Court, and by legislation we have been required to issue declaratory judgments with respect to rulings on employee retirement plans, exempt organizations, and certain foreign transfers of property. This declaratory judgment jurisdiction with respect to exempt organizations is concurrent with the Court of Claims and the United States District Court for the District of Columbia. In addition, this Court has been given jurisdiction over certain disclosure actions. Part of that jurisdiction is exclusive and part is concurrent with the United States District Court for the District of Columbia.

Thus, within its statutory jurisdiction, the Tax Court judges have the same powers and responsibilities as the district court judges, and by statute (sec. 7443(c)(1)) they receive the same salaries. As the GAO report points out: "Because retirement is an integral part of employee compensation, differing benefit provisions mean differing rates of compensation for employees who are performing similar or equivalent functions and who are otherwise paid the same." Since the Tax Court judges perform the same or similar services as the judges of the United States district courts, and since it is the avowed legislative purpose to provide the same compensation for both types of judges, it follows that similar retirement systems must be maintained for both the Tax Court and district court judges.

The Court still consists of 16 presidentially-appointed judges (the number established in 1926), and the Court hopes that it can handle its augmented workload with no increase in the size of the Court (except additional commissioners (special trial judges) as needed). To that end, each judge is being called upon to assume an even heavier workload. With such demands upon the judges, this is certainly no time to make their positions less attractive.[3/]

Selection of Tax Court Judges

The judges of the Tax Court are selected and appointed in substantially the same manner as other Federal judges. Tax Court judges are appointed by the President with the advice and consent of the

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3/ In this connection, I invite your attention to "The Report of the Commission on Executive, Legislative and Judicial Salaries," dated December 1976, which comments in some detail on the need for, and difficulty in, attracting qualified lawyers to serve as judges. This report deals with salary differentials, but the reasons therein discussed for providing adequate judicial salaries also support continuation of the retirement system for Tax Court judges.

Senate. Although the judges are appointed only for a term of years (15 years at the present time), they, in effect, serve for life since, at least for the past 30 years, all judges have been reappointed until they are eligible for retirement. Even after retiring, the Tax Court judges, although they are required to serve for a period of only 90 days a year, generally do in fact continue to serve on recall and work full time until they are unable to do so because of physical or mental conditions.

For many years, it has been the practice to appoint to the Tax Court only those attorneys who have, either in private practice or Government service, achieved professional recognition in the field of Federal taxation. In the past, the Secretary of the Treasury made recommendations for appointment to the President for his consideration. To assist him in selecting the most qualified persons, the Secretary has generally received the suggestions and evaluations of a committee composed of presidentially-appointed officeholders who are specialists in the field of Federal taxation. He has also invited and received the comments of the American Bar Association. On June 5, 1978, President Carter issued Executive Order No. 12064 creating an advisory commission to identify and evaluate qualified candidates for appointment to the Tax Court, and he will consider the recommendations of that commission in making his appointments.

To secure the necessary experience and professional recognition, the selected appointees must be mature individuals. The average age, at the time of appointment, of all judges now serving on the Court was 47; the youngest was 38, and the oldest was 58. The average age, at the time of appointment, of the judges now on the Court from private practice was 47; the youngest was 42, and the oldest was 58. An attempt is generally made to have the Court representative; that is, there is generally a fairly even balance between those attorneys from private practice and those who have served in the

Government, and some consideration is also given to choosing as judges attorneys from the various areas of the country.

Since World War II, the private practice of tax law has been lucrative. Appointees to the Court from private practice generally accept a large reduction in compensation when they are appointed. 4/ If the geographical distribution of Tax Court appointments is to be preserved, an appointee from outside the Washington area must (unlike district and appellate court judges) uproot his family and move to Washington. Appointees from Government invariably have worked in the tax field for years and are at a point in their career where, as a general rule, they could move to lucrative private practice positions. On electing the Tax Court retirement system, they forfeit the rights to civil service retirement benefits. Although several reasons (including the satisfaction he expects to receive from

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4/ The Report of the Commission on Executive, Legislative and Judicial Salaries, Background Studies on Compensation (December 1976), page 7, states the average salary of judges on acceptance of their appointment was 33 percent less than their prior private practice income.

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the performance of the judicial work) ordinarily lead a judge to make the decision to accept such reduction in compensation, and incur the expense and disruption of moving their homes, a significant consideration is the Tax Court judicial retirement plan.

Since judges of this Court are required to retire at age 70, the average tenure of the present judges from private practice cannot exceed 23 years; for one judge, his tenure cannot exceed 12 years, and the maximum tenure for any of such judges is 28 years. Obviously, those judges cannot serve on the Court for a sufficiently long period of time to earn an adequate retirement under the civil service retirement system. One inducement for such judges to accept the position is the prospect that they can continue to serve on the Court as long as they are able, physically and mentally, and they will continue to receive the salary of the office.

Eliminate the right to retire on full pay (with or without recall), and few able private practitioners can afford financially to accept a Tax Court appointment and

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make a career commitment. Once a district or appellate judge is appointed, he is forbidden by statute from engaging in the practice of law. 28 U.S.C. 454. The possibility of his earning supplemental compensation from other business activities while serving as a judge is circumscribed and regulated by the Code of Judicial Conduct. Tax Court judges are subject to similar restrictions. If they participate in the Tax Court retirement system, they are prohibited from practicing tax law. The restriction on private practice can be justified so long as the judge has the right to continue to receive the pay of the office; without such compensation, it would be unfair to deny the judge the right to practice his profession.

Any change in the Tax Court retirement system would make it likely that appointees from private practice will accept Tax Court appointments only with a view to temporary service followed by a return to private practice. Creating that kind of "revolving door" situation would be abhorrent to the concept of the Tax Court as the type of independent judicial body which the Congress has sought to create.

It may be suggested that retirement benefits should not be used to make up for inadequate current compensation, but it is unrealistic to expect Congress to fix the judicial salary at such a level that the salary, standing alone, would induce highly qualified persons to leave the private practice of law and accept a judicial position.[5/] Without the inducement of the judicial retirement plan, the character of the Court would be changed. It is certain

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5/ The Report of the Commission on Executive, Legislative and Judicial Salaries, Background Studies on Compensation (December 1976), page 10, states:

> Judges get 100% of final pay but make no contribution. Were it not for this difference, we would have been inclined to propose larger salary increases for the judiciary--because theirs is a long-term career position, not an interlude; and the evidence is overwhelming that Federal judges can earn more in the private sector, and the evidence, as well as the public, generally is substantially more supportive of higher salaries for the judiciary. The Commission notes that although Federal judges receive full pay throughout retirement, the great majority nevertheless continue to perform judicial duties during that time.

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that the Court could not continue to attract highly qualified individuals from private practice who would make the long-term commitment contemplated for a judicial appointee; and it would become impossible to maintain the necessary balance between those from private practice and those with Government experience.

Furthermore, it should be recognized that many of the judges now on the Court have had opportunities to leave the Court but have remained, in part, because of the retirement plan. In the past years, for example, several judges have had opportunities to enter private practice and earn compensation equal to two or three times their Tax Court salaries. It would be unfair to the judges who have come on the Court or remained here with the expectation of participating in the present retirement plan to modify that plan to their detriment.

Congressional Recognition

Twenty-five years ago, the Congress recognized the need for establishing a special retirement plan for judges of the Tax Court, and since then, Congress has, from time to time, recognized the continuing need for the maintenance of such special provisions. The initial special provisions for Tax Court judges were enacted in 1953. In discussing the reasons for such legislation, the Ways and Means Committee report indicated that one reason was to treat Tax Court judges in a manner similar to other Federal judges; it declared that other reasons were:

> The civil-service system is a satisfactory one, insofar as the average Government employee is concerned, since he generally enters employment at an early stage in life and by retirement age has met the service requirements for a full annuity. However, it has not been satisfactory for Tax Court judges, since the particular qualifications for appointment require that they be men of maturity and experience prior to entering service, which would result in their receiving an inadequate annuity if they retired at the usual time.
>
> The desirability of making provision for judicial retirement of Tax Court judges has been recognized for some time. Legislation to this end has been proposed by the American Bar Association and is supported by the Treasury Department. It likewise has the support of the American Institute of Accountants. Tax Court judges deal with complicated and important questions, are required to have a knowledge of general law as well as tax and renegotiation law, and have a heavy workload.

> The positions thus call for physical and intellectual stamina. Yet because of the lack of an adequate retirement system there is a natural tendency to continue work beyond the proper limit of physical capacity.
>
> A judicial retirement plan thus would represent a proper concern for the welfare of the judges of the court. It would also facilitate the appointment of qualified persons engaged in the private practice of law who are reluctant to accept in their middle years a position with inadequate retirement benefits. As a result, appointments to the Tax Court in recent years have drawn heavily on experienced personnel already in Government service, who have previously built up service credits for retirement. While this is not undesirable to some degree, a Tax Court heavily balanced with men having prior Government experience may well involuntarily give a pro-Government bias to its considerations. This possibility makes it highly desirable to appoint persons from private life.
>
> * * *
>
> In short, such a plan would serve the best interest of the Government, private taxpayers and the country as a whole. [H. Rept. No. 846, 83d Cong., 1st Sess., p. 4 (1953).]

In 1967, Senator Long, Chairman of the Senate Finance Committee, and Congressman Mills, then Chairman of the House Ways and Means Committee, introduced bills which were designed to make the Tax Court a court under Article III of the Constitution. S. 2041 and H.R. 10100, 90th Cong. However, at the hearings on the Senate bill, Senator Long testified that on further consideration, he had concluded that he did not favor life tenure for Tax Court judges and that therefore he did not favor making the Tax Court an Article III court. He did favor a number of changes which would give the judges of the Tax Court the same powers as judges of the district courts. In part, he also stated:

> The Tax Court judges presently are paid the same annual salary as Federal District judges, namely, $30,000, but in some other respects may not receive the same emoluments as other judges. This bill would provide that the Tax Court judges would in all of these respects be treated the same as other Federal judges. The bill, for example, provides that the retirement system for the Tax Court judges will be tied in with the retirement system for other judges. These provisions also I consider to be good changes. [Hearings on S. 2041 before the Subcommittee on Improvements in Judicial Machinery of the Senate Judiciary Committee, Oct. 1967.]

The Article III bills were not enacted, but in 1969, the other changes favored by Senator Long were enacted. Secs. 951 through 962, Tax Reform Act of

1969. It was then that the Tax Court was removed from the executive branch of the Government and made an Article I court. In other respects, the Tax Court was given many of the powers of a district court, and its separate retirement plan was modified to conform substantially to that applicable to district and circuit judges.[6/] In describing these changes, the report of the Senate Finance Committee stated:

> The bill establishes the Tax Court as a court under Article I of the Constitution, dealing with the Legislative Branch.

6/ In Appendix II, of the GAO report, it is stated:

> Discontinued Service
>
> Eligibility: Any age and 15 years service.

This statement may be read to indicate that Tax Court judges can retire at any age after completing 15 years of service, but such is not the law. Under sec. 7447 (b)(3), a judge who is not reappointed may retire if he has completed 15 years of service and if he has advised the President that he is willing to continue to serve. Otherwise he cannot opt for retirement until he has both reached the age of 65 and had 15 years of service.

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At the present time, the Court of Military Appeals is the only other Article I court. Other courts, however, have enjoyed this status in the past, including the Court of Claims. In accordance with this change, the Tax Court is given the same powers regarding contempt, and the carrying out of its writs, orders, etc., that Congress has previously given to the District Courts.

* * * The amount and method of payment of the Tax Court judges' salaries are made identical with those of District Court judges.

The provisions regarding retirement are revised to require retirement at age 70, whether or not the judge has completed 10 years service by that time. The provisions of existing law authorizing the use of retired judges on recall to relieve heavy case loads are unchanged by the amendments.

As in the case of the District Court, the bill permits a judge to retire at age 65 if he has served at least 15 years, and to retire at a younger age with 15 years service if he is available for reappointment at the conclusion of his term but is not reappointed. The bill requires a Tax Court judge to retire if he is permanently disabled. In general, retirement under these provisions is to be at the full pay of the office.

If the judge has served less than 10 years when he reaches the mandatory retirement age of 70, then his retirement pension is apportioned in accordance with the number of years he has served. If the judge has served less than 10 years and is retired because of disability, then his pension is half the salary of the office. The disability

> provisions are patterned after those of District judges. [S. Rept. No. 91-552, 91st Cong., 1st Sess., p. 304 (1969); footnotes omitted.]

A review of this legislative history shows beyond a doubt that there were good reasons for creating a separate retirement plan for Tax Court judges and that those reasons continue to exist. The subject has been considered by Congress from time to time in the past 25 years, and on each occasion and as late as 1969, Congress has recognized the continuing need for a separate retirement system for Tax Court judges, <u>and has strengthened that system</u>.

<u>General Observations</u>

The performance of judicial services by those retired judges serving on recall is essential both for the district and appellate courts and for the Tax Court. The report concludes that the retirement plan for other Federal judges should not be changed "In view of the fact that retired judges perform substantial duties." We understand the GAO was advised by the judiciary that "91 percent of the retired judges performed substantial judicial service." As pointed out in the

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report, the 18 judges of the Tax Court who have received retired pay since 1953 have served 58 percent of the time on recall. Fifty-eight percent of the time constitutes a very substantial contribution to the work of this Court by the retired judges. Indeed, during the fiscal year ended September 30, 1977, for example, the retired judges serving on recall produced over 8 percent of the Court's published and memorandum opinions. Moreover, all of the 18 retired judges have served the 90-day period for at least 1 year and 14 of the 18, or 78 percent, have served on recall for more than 1 year after retirement. In fact, these 18 retired judges on recall have served approximately 103 man-years.

Although Tax Court judges are required to serve a minimum of 90 days a year on recall, most of them serve practically full time. Because of the nature of the work, any retired judge of the Tax Court who serves on recall serves for the entire year and not just for 90 days. To our knowledge no retired judge has ever limited his services on recall to the 90 days provided in the law. Like most other Federal judges, most retired Tax Court judges continue thus to serve, and have discontinued their service only when their advanced age has made it impossible for them to perform judicial duties.

Even so, as suggested above, most Tax Court judges do not have the opportunity to serve long enough before reaching the mandatory age of 70 to build up adequate retirement benefits under a system keyed to the length of service. Since the average age of the present judges when appointed to the Tax Court was 47, and since a judge is required to retire at age 70, the maximum average tenure is 23 years. If a judge is, in fact, in his 50's when appointed to the Court, his maximum tenure will be less than 20 years. Normally, his minimum tenure for entitlement to any retirement benefits is 15 years. Many of the judges from private practice now serving on the Court have no individual retirement benefits available to them from their private practice.

In summary, we are convinced that sound reasons exist for the continuance of the separate retirement

APPENDIX XII

provisions for Tax Court judges similar to that of other Federal judges. The present program is needed by the Court to attract, for a career commitment, outstanding, mature tax practitioners from both the private and public sectors and thus to continue satisfactorily to perform the increasingly heavy duties that are being imposed upon it. The absence of such a program would be highly detrimental to the proper functioning of the entire system of Federal taxation, which is already under heavy strain and subject to serious questioning by the taxpaying public.

If we can furnish you with any further information, please feel free to call upon us.

Sincerely yours,

C. Moxley Featherston

C. Moxley Featherston
Chief Judge

The Deputy Director
Central Intelligence Agency

Washington, D C 20505

22 June 1978

Mr. H. L. Krieger, Director
Federal Personnel and Compensation Division
General Accounting Office
Washington, D. C. 20548

Dear Mr. Krieger:

This is in response to Mr. J. K. Fasick's letter of 24 May 1978 requesting our comments on your proposed report as to the desirability of establishing a single retirement system for all Federal personnel.

We do not concur in the conclusion that the CIA Retirement and Disability System (CIARDS) should be included in a single consolidated Federal system. We consider that the unique security and management factors require that the CIARDS should remain under Agency control as a separate statutory system.

The justification for maintaining CIARDS as a separate system was spelled out in the Agency's detailed response of 9 March 1977 to Mr. Shelton's earlier (11 November 1976) letter which initiated GAO's review. A copy of the response we made at that time is enclosed as Attachment C. Unfortunately, your draft report does not include most of the rationale supporting our position. As a result, recipients of the report within the Congress would be given a one-sided view supporting your conclusion for one retirement system with little insight into the Agency's position to allow an objective appraisal of the proposal as it concerns CIARDS.

To present a balanced report, we feel it only fair and necessary that the detailed rationale supporting CIA's position be included in the section of your report on CIARDS. Accompanying this letter as Attachment A are our comments on the draft of your proposed report. For your further information is Attachment B, a statement made by the Acting Deputy Director of Central Intelligence on 13 October 1977 during hearings on CIARDS held by the House Permanent Select Committee on Intelligence. We believe you will find in these two attachments important information to supplement the information we gave to Mr. Shelton in March 1977.

If, notwithstanding the views expressed in the attached materials, your final report recommends the merger of CIARDS in a single Federal

[See GAO note 1 on page 305.]

retirement system, we request that the report reflect the Agency's rationale for CIARDS as a separate system and the Agency's stand in opposition to any other arrangement.

A representative of our Office of Personnel is prepared to meet again with Mr. Shelton directly to discuss appropriate revisions of the report to satisfy our concerns.

Sincerely,

John F. Blake
Acting Deputy Director

Enclosures

[See GAO note 2 on page 305.]

General
Services
Administration Washington, DC 20405

JUN 15 1978

Honorable Elmer B. Staats
Comptroller General of
the United States
General Accounting Office
Washington, DC 20548

Dear Mr. Staats:

This is in response to Mr. Fred J. Shafer's letter of May 24, 1978, requesting the General Services Administration's comments on your draft report entitled, "A Single Retirement System For All Federal Personnel: Is It Desirable?"

The draft report is well documented, factual and the recommendation for the development of an overall policy and centralized control of the Government's retirement programs should provide equitable treatment for all Government employees.

Chapter 4 of your draft report suggests that a former President should be covered by the Civil Service retirement system, since equitable benefits would be provided. The examples provided in the report support this suggestion. However, there are two circumstances in which the former President would not receive equitable benefits:

(1) If a President did not have prior Government service, and particularly if he were a one-term President, the benefits would be greatly reduced under Civil Service retirement. (President Carter has only military service which could be counted toward retirement.)

(2) If a President were very young when elected, he would not be eligible for retirement benefits upon completion of his Presidency. (President Kennedy would not have met the minimum retirement age.)

The retirement benefits for former Presidents were enacted to enable them to meet all of the demands upon them without financial difficulty. Changes to the current benefits should be prepared in a way to ensure that <u>any</u> former President would receive a sufficient annuity.

[See GAO note 1 on page 305.]

We agree that the widows of former Presidents should receive an annuity related to her husband's annuity. The present fixed survivor's annuity is inequitable.

Thank you for the opportunity of commenting on your draft report.

Sincerely,

Robert T. Griffin

Robert T. Griffin
Deputy Administrator

FARM CREDIT ADMINISTRATION 490 L'ENFANT PLAZA, S.W WASHINGTON, D.C. 20578

July 7, 1978

Mr. H. L. Kreeger, Director
Federal Personnel and Compensation Division
General Accounting Office
Room 4001
441 G Street, N. W.
Washington, D. C. 20548

Dear Mr. Kreeger:

We wish to thank you for the opportunity to comment on a draft of a proposed report on the desirability of establishing a single retirement system for all Federal personnel. Our personnel and legal staffs have thoroughly reviewed this report and I am enclosing their suggested technical changes and comments to improve the accuracy of the report. In addition to these technical changes, I believe the report raises several issues that are deserving of special comment.

The report properly raises the issue of the "crazy quilt" of provisions of Federal retirement programs relating to benefits, actuarial assumptions, and funding. We agree with the report that the problem is a lack of an overall benefits philosophy by Congress. Such a philosophy should include a statement of what the Federal Government as an employer should provide its employees and their dependents when they retire, die or become disabled; general guidelines as to the overall costs of benefits programs; and the desired relationship between Federal benefits and those in the private sector. All future proposals to change any Federal benefits program should be considered in light of this philosophy. We agree with the report that benefits programs should be dealt with as part of an overall compensation package.

The report in several places states that there is no reason why the various Federal retirement systems should not be combined. This seems to be a reverse logic--change is desirable unless there are reasons for not changing. Normally, in this type of report, reasons should be stated for making changes such as increased cost savings, portability for employees who move from one retirement system to another, or better management. The report seems to be advocating combination on the assumption that "bigger is better." This may be a false assumption for a number of reasons. The smaller, private pension plans such as those of the Farm Credit System are better managed, actuarially sound,

[See GAO note 1 on page 305.]

produce a better yield on investment, amortize all unfunded liability, and provide benefits which are normally consistent with district board philosophy. The larger plans such as civil service retirement, military retirement and social security, have enormous unfunded liabilities, poor return on investment, use improper actuarial assumptions, and do not conform to any overall benefits philosophy from Congress. By these criteria, smaller appears to be better.

The report suggests that a single retirement system would be easier to manage and eliminate the inequities and inconsistencies which exist among the various Federal retirement systems. Again, the history and current financial situation of civil service retirement, military retirement and social security would indicate that these larger plans are not more easily managed than smaller plans such as those of the Farm Credit System. If inequities and inconsistencies are the problem, then some standardization of benefits provisions is the answer. This can be achieved without merging all retirement programs into a single plan. At present, the Farm Credit System is working toward development of common retirement benefits provisions without integration of funds.

Another area that requires comment is the concept of "portability." A significant problem is the portability or transferability of service credit when one moves from one Federal retirement system to another. For example, while military service is creditable under civil service retirement, the reverse is not true. Also, an employee of one of the Farm Credit System district retirement plans cannot receive service credit under civil service retirement. While we are generally in favor of portability of benefits between retirement systems, it must also be recognized that providing service credit is expensive and portability provisions should address those situations where career transfers are likely. It is unlikely that someone would move from Tennessee Valley Authority to the Farm Credit System, but it is likely that someone under civil service retirement would transfer to the Farm Credit System or that Farm Credit System employees would move from one Farm Credit district to another. In exercising our responsibility of supervising the Farm Credit System retirement plans, we have advocated portability of all benefits (not just retirement) and all districts now embrace this concept of portability and all are in the process of implementing a model portability provision which will provide vesting and service credit for those employees who move from one Farm Credit district to another. We would enthusiastically support a change to Federal law which would provide retirement portability between the district retirement plans of the Farm Credit System and civil service retirement.

A final concern which we must express over the draft report is that it incorrectly classifies Farm Credit System employees as Federal employees. Farm Credit System employees are not Federal personnel (see 12 U.S.C., §2227(a)(3)). No provisions of Title 5 apply to any Farm Credit System employees except for the 250 who are "grandfathered" under civil service retirement. While the institutions of the Farm Credit System are Federally chartered instrumentalities of the United States, the employees are not Federal personnel.

We appreciate the opportunity to provide you with our comments on your draft report. If you wish further information or clarification of our comments, please contact our Director of Personnel, Michael E. Hotz.

Sincerely,

Donald E. Wilkinson
Governor

Enclosure

[See GAO note 2 on page 305.]

Federal Home Loan Bank Board

1700 G Street, N W
Washington, D.C 20552

Federal Home Loan Bank System
Federal Home Loan Mortgage Corporation
Federal Savings and Loan Insurance Corporation

Office of General Counsel

June 22, 1978

Mr. H. L. Krieger, Director
Federal Personnel and Compensation
Division
United States General Accounting
Office
Washington, D. C. 20548

Dear Mr. Krieger:

In your letter of May 24 to Chairman McKinney, you requested our review and comment on your draft report "on the desirability of establishing a single retirement system for all Federal personnel". You noted that the portions of the draft report sent to us relate to the Savings Associations Retirement Fund (SARF). SARF, in addition to providing pension coverage for approximately 12,000 employees of savings and loan associations, also provides pension coverage for some 1300 employees of the Federal Home Loan Banks (FHLB).

In our view, integration of FHLB employees into a single retirement system for Federal personnel is neither warranted nor desirable.

Notwithstanding the authority of the Bank Board over the Federal Home Loan Bank System, the fact remains that employees of Federal Home Loan Banks are <u>not</u> Federal employees. Their salaries are not subject to Government prescribed scales, and their employment security is not subject to regulation of the Civil Service Commission. Moreover, to divorce FHLB participation from SARF after 36 years would undoubtedly be very costly. Further, a serious dislocation could thereby be occasioned in SARF, since pension plan contributions for FHLB employees account for approximately 15% of its assets.

While the unfunded liabilities of the civil service and uniformed services retirement systems total billions of dollars and are projected to $347 billion by 1986, the unfunded liabilities of SARF are small in comparsion with most public and private plans. If FHLB employee pension

[See GAO note 1 on page 305.]

coverage were integrated, as you propose, presumably, FHLB pension costs would rise to cover the larger unfunded liabilities of a unified system. Incidentally, it is our understanding that SARF is in full compliance with the Employee Retirement Income Security Act of 1974. Vesting provisions under SARF would probably generate the type of difficulty referred below to in your draft report.

The draft report acknowledges (pages 9 and 10) the difficulties of integrating other retirement systems into one system:

> Implementation of a new retirement system to cover all personnel will not be easy. In addition to the basic policy issues of what benefits the program should provide, who should be covered, who should administer the program, what Congressional committee(s) should have jurisdiction, etc., many practical difficulties inherent in any major change to on-going programs will be involved. For example, decisions will be required on whether the new program should be effective immediately for all personnel or apply prospectively only.

In our judgment, the draft report contains certain inaccuracies which you may wish to amend:

- page 200 - The FSLIC is not part of the Federal Home Loan Bank System, as is inferred here. The Bank Board is the operating head of the FSLIC. The Office of the FSLIC is a constituent element of the Bank Board. For example, the General Counsel of the Bank Board is, ex-offico, the FSLIC General Counsel. All other FSLIC support functions are performed by the Bank Board. In fact many FSLIC statutory responsibilities are performed by Bank Board personnel. FSLIC employees are Federal employees, as the draft report notes in the last paragraph on this page. FSLIC employees are included in the pension coverage of the Civil Service Retirement. It is therefore suggested that any inference that such employees are included in SARF pension coverage, should be dispelled by deletion of the reference to the FSLIC.

[See GAO note 5 on page 305.]

Also the Bank Board does not "select" the FHLB Presidents as alleged on this page. That is the primary responsibility of the board of directors of each Bank, although its selection is subject to approval of the Bank Board.

The last sentence on the page notes that "other employees of the system [the Federal Home Loan Bank System] such as Federal Savings and Loan Association employees, are also permitted to participate in the banks' retirement plan". It is also stated on page 202 of the draft report that "Commercial institutions within the Federal Home Loan Bank System, unlike members with the Federal Reserve System, are permitted to participate in the <u>bank retirement</u> system". (Emphasis supplied)

Although regulated, examined and audited by the Bank Board, Federal savings and loan associations are private institutions and their employees in no way can or should be characterized as Federal employees or "quasi" Federal employees. Also what is referred to as the "bank retirement plan" is the "Savings Associations Retirement Fund" whose pension plan participants include not only employees of Federally chartered, but State chartered savings and loan associations--none of whom, under any standard, could be considered Federal employees. Moreover, pension contributions by some 600 associations accounts for 85% of SARF's assets.

The draft report referring initially to a pension supplement for FHLB retirees with Bank Board service noted:

- page 205 - Officials of the Board held formal discussions with Civil Service Commission and Department of Justice officials in regard to whether a similar supplement could be paid by the banks, to Board retirees with bank service. Commission and Department of Justice officials advised the Board that they believed such an arrangement would be in violation of Civil Service Retirement Act. Apparently, they viewed this supplement as a benefit being paid by another <u>Government source</u> (sic) for the same service, <u>which would be in</u> violation of the act.

[See GAO note 5 on page 305.]

The above discussion is incorrect.

As a participant of the meeting with Justice representatives, in a memorandum of May 7, 1975, prepared shortly after the meeting, I wrote to our then General Counsel as follows:

> Jack Buckley and I met Tuesday with Leon Ullman, First Assistant to the Assistant Attorney General, Office of Legal Counsel and with Nathan Siegel of that Office.
>
> While the meeting focused principally on 18 USC 209, as to whether the supplementing a Board pension (as it applies to Bank to Board transfers) raises problems under that section, there also emerged a basis policy question as to whether such a supplement conflicts with the pension policies of the Civil Service Commission.
>
> Jack has had informal discussions with the Commission staff who have professed no interest in our proposal. The immediate task is to obtain that in writing.
>
> Mr. Ullman said his Office would entertain a request for a ruling on the 18 USC 209 question. He and Mr. Siegel raised the usual questions suggested by 18 USC 209, but also conceded that the close relationship of the Banks and the Board is a factor not ordinarily associated with questions under that section, in view of the absence of the conflict of interest that are present when an employer in private industry is involved. (Emphasis supplied)

[See GAO note 3 on page 305.]

While seeking to integrate all Federal employees into one retirement system appears to be a reasonable, attainable, and defensible objective, there would seem to be little justification to include non-Federal employees in such a system. Moreover, limiting Congressional inquiry to the integration of all Federal employees into one retirement system suggests a "package" more susceptible of acceptance than the introduction into the inquiry of pension coverage for non-Federal employees.

For the reasons stated above, we urge rejection of any proposal that would compel divorcement, after 36 years of the SARF pension coverage for employees of the Federal Home Loan Banks.

If there is any further information that you may wish, please let me know (377-6460).

Sincerely yours,

Anne P. Jones
General Counsel

By: Jerome S. Plapinger
Jerome S. Plapinger
Associate General Counsel

SMITHSONIAN INSTITUTION
Washington, D.C. 20560
U.S.A.

July 10, 1978

Mr. Victor L. Lowe
Director
General Government Division
General Accounting Office
Room 3866
441 G Street, N. W.
Washington, D. C. 20548

Attention: Mr. H. L. Krieger, Director
Federal Personnel and Compensation Division

Dear Mr. Lowe:

Thank you for your May 30, 1978, letter inviting our comments upon your proposed report on the desirability of establishing a single retirement system for all Federal personnel. We have read the report with care and have two comments concerning the references in the report to the Smithsonian.

First, the report correctly concludes, citing earlier GAO and Civil Service Commission rulings, that Smithsonian Trust Fund employees are not Federal employees. We would note, however, that the retirement plan in which those employees participate (TIAA-CREF), unlike the many Federal plans you discuss, is fully funded, and we strongly believe it would be disadvantageous to replace that highly successful plan with anything else. Moreover, we are confident that our TIAA-CREF plan, which is privately administered by the Teachers Insurance and Annuity Association subject to the provisions of ERISA, is quite equitable. Your conclusion that that plan provides "better benefits than those received by employees under the civil service retirement system" should be measured against the reality that that plan, unlike the Federal plan, does not provide cost-of-living increases and requires employees to work until age 65 (contrasted with age 55 for Federal employees) to get full benefits. Thus,

[See GAO note 1 on page 305.]

although the Institution's contribution is slightly higher, when all factors are weighed together, we believe the plan to be equitable, secure, and efficient. Accordingly, we can see no sound reason for discontinuing the Institution's participation in it.

Secondly, in the section entitled "Employment Policies and Practices," your report may give the erroneous impression that decisions regarding civil service versus Trust Fund employment status are optional or arbitrary on the part of the Institution or its staff. To the contrary, source of funding always determines this status, and only rarely is the source of funding optional. Those infrequent instances of discretion generally involve administrative positions, in relation to which efforts are made to maintain a balance approximating the overall institutional ratio of Federal to Trust Fund expenditures. Moreover, the small number of employees (less than 2% annually) changing from civil service to Trust Fund status or vice versa is occasioned by the recognition of the employees' right to compete for any position for which they are qualified. Our view is that any contrary policy would contravene merit promotion and sound management principles.

In conclusion, while we are not in a position to evaluate the desirability of having all Federal employees covered by one retirement plan, we do feel strongly that our benefits plan for Trust Fund employees should not be disrupted.

Sincerely yours,

John F. Jameson

John F. Jameson
Assistant Secretary
for Administration

GS

A CENTER FOR CONTINUING EDUCATION

GRADUATE SCHOOL • U.S. DEPARTMENT OF AGRICULTURE • WASHINGTON, D. C. 20250 • (202) 447-2077

Office of Director

June 28, 1978

Mr. H. L. Krieger, Director
Federal Personnel and Compensation Division
General Accounting Office, Room 4001
441 G Street N.W.
Washington, D.C. 20548

Dear Mr. Krieger:

This is a response to your memo of June 1, 1978, requesting comments on a single retirement system for all Federal personnel. We found your report both informative and comprehensive.

As you know, the Graduate School, USDA, is in a unique position with regard to its relationship to the Federal government. It receives no appropriated money from the Department of Agriculture nor from Congress. Its fulltime employees historically have not been considered to be in the career civil service system. The school is entirely self-supporting from fees from individuals, government agencies, or outside organizations seeking its services.

I am enclosing a recent newsletter which summarizes a number of its contributions to government employees, government agencies, and others who have sought its services over the past 56 years.

Successive Secretaries of Agriculture have appointed members of a General Administration Board which functions somewhat like a board of trustees of a college or university. This Board, in turn, has appointed a director and a deputy director as necessary. These two appointees and others employed fulltime by the Graduate School have not been considered career civil servants. Their salaries and benefits have been paid by fees collected for services rendered.

As a self-supporting, non-degree granting, special purpose school for adults, the Graduate School, USDA, has provided immeasurable ideas, improvements, and growth opportunities to individuals and employing organizations for over 56 years.

The Graduate School has been able to contribute extensively because of the many freedoms enjoyed by the administrators and faculty of the school. Especially noteworthy among these freedoms are: freedom to experiment, to innovate, to anticipate and adapt to rapid changes in government and in society. Its faculty has historically been parttime persons who teach on

[See GAO note 1 on page 305.]

their own time. They receive a nominal honorium, and, in the process of teaching, keep updating themselves and getting ideas from the adult students themselves. They are not professional educators but practitioners who help other adults gain new knowledge, skills, insights, and understandings.

Continuing education has been and continues to be the Graduate School's only preoccupation (no campus, no football team or other embellishments).

Like any responsibile organization, the Graduate School has attempted to provide fringe benefits for its fulltime employees. To the extent we could afford them, we have tried to make our benefits as comparable as possible to those provided by the government.

Retirement benefits are but one type of fringe benefits we provide.

Our fulltime employees are not in the career service so they are not able to transfer to other agencies nor take advantage of the many career advancement opportunities available to civil service career employees.

In addition, since we are a small organization, we have not been able to afford to provide the many health insurance benefits career employees enjoy.

With regard to the Graduate School retirement benefits, it has been the intent of the Graduate School's General Administration Board to provide retirement benefits as close to federal civil service retirement benefits as possible and affordable.

The information provided in a GAO report which compares the percentage of the annuity of the high three years average salary does not take into consideration the effects of social securty, the cost of social security, the fact that the Graduate School plan was based on an annuity pay out for a single life rather than a pay out to the annuitant and survivor. Currently, taxpayers are funding a major portion of the Civil Service Retirement Ssytem through general tax revenues. Under the Graduate School's system, there is no credit for accumulated sick leave as provided in the civil service plan.

The civil service plan provides for a cost of living increase. There is no such provision available in the TIAA plan. The civil service plan is backed by the United States government; whereas, the Graduate School plan is much smaller and backed by a private nonprofit corporation.

[See GAO note 3 on page 305.]

We agree with the GAO report that all federal employees should have equal benefits; however, we feel that all benefits should be considered, not just retirement.

We are vitally concerned with the future contribution of the Graduate School to government employees and government agencies. The organization has existed for over 56 years without directly appropriated funding and without fulltime government employees. We feel it would be a very serious mistake to make the fulltime staff of the Graduate School government employees. We are, therefore, opposed to the Graduate School fulltime staff members participating in the present government retirement system or a new single retirement system which may be set up.

Following are some points of consideration with the civil service plan and the TIAA Graduate School plan.

Should you need additional information or if you have questions about the Graduate School, feel free to call me (447-2077) or our Business Manager, Ken Dickerson (447-3090).

Sincerely,

John B. Holden

John B. Holden
Director

CANAL ZONE GOVERNMENT
BALBOA HEIGHTS, CANAL ZONE
OFFICE OF THE GOVERNOR

JUN 12 1978

Mr. H. L. Krieger, Director
Federal Personnel and Compensation Division
General Accounting Office
Room 4001
441 G Street, NW
Washington, D. C. 20548

Dear Mr. Krieger:

Under date of May 24, 1978, the Director, General Accounting Office requested that we forward our comments to you on the draft of a proposed report entitled "A Single Retirement System for all Federal Personnel: Is it Desirable?"

This report discusses two closed retirement systems of direct interest to the Panama Canal Company and Canal Zone Government. One of these is the Panama Canal Zone Cash Relief Program and the other one, the Panama Construction Annuity Service Program. This report shows that at the end of Fiscal Year 1975, 2,185 beneficiaries (1,024 retirees and 1,161 widows) were receiving cash relief payments. The attrition rate of beneficiaries (by death) under this program is quite high; as of May 31, 1978, there were 711 cash relief recipients and 1,065 survivors for a total of 1,776, this represents a decrease in number of beneficiaries of 19 percent over a three-year period. It is pertinent to note that the average pension for recipients is $100 per month and that of survivors is $52 a month. Under the Panama Canal Construction Service Annuity Program you report that at the end of Fiscal Year 1975 there were 437 annuitants on the rolls and your estimate was that by the end of Fiscal Year 1978 the number would be reduced to 176, a 60 percent reduction. Inasmuch as this program is operated through the U.S. Civil Service Commission, this agency does not have information as to the number of annuitants still on the rolls.

In the case of both the Panama Canal Zone Cash Relief Program and the Panama Canal Construction Service Annuity Program, however, we agree with your conclusion that inasmuch as these two programs are both closed retirement systems, that is, no new employees may participate and when all existing retirees and surviving beneficiaries are deceased the system will terminate, little would be gained by including the two programs in a consolidated federal retirement system. We therefore recommend that they not be included in a consolidated federal retirement system if such a system comes into being.

Sincerely yours,

H. R. Parfitt

H. R. Parfitt
Governor

[See GAO note 1 on page 305.]

EXECUTIVE OFFICE OF THE PRESIDENT
OFFICE OF MANAGEMENT AND BUDGET
WASHINGTON, D.C. 20503

JUN 26 1978

Mr. H. L. Krieger
Director, Federal Personnel and
Compensation Division
U.S. General Accounting Office
Washington, D.C. 20548

Dear Mr. Krieger:

This is in response to your May 24, 1978 request for comments on the GAO report, "A Single Retirement System for all Federal Personnel: Is it Desirable?"

The draft report is a very comprehensive and thorough description of the management of current Federal retirement programs, the differences in coverage and benefit levels among them and the differences in their respective financing practices.

The report offers useful insights on such issues as:

- a single Federal retirement policy
- centralization of Congressional committee jurisdiction on retirement matters
- a central authority responsible for overall administration of Federal retirement programs
- adoption of actuarial valuation methods and funding provisions that reflect the full costs of retirement programs
- charging to agency operations all retirement program costs in excess of any employee contribution
- the extension of social security coverage to all Federal personnel

The proposal to Congress that the appropriate committees hold hearings to consider indepth the issues raised in the draft report is in consonance with this Administration's desire to review pension policy. I am sure that you are aware of the

[See GAO note 1 on page 305.]

actions being taken to establish a Presidential Commission on pension policy. The proposed charter for the Commission includes for review some of the same issues raised by your report. I feel confident that views expressed in the report will be given full consideration by the Commission and that the background material will be invaluable--especially since it has been consolidated in a single volume. Your final report should be very helpful to the Commission in the formulation of its conclusions and recommendations to the President on Federal pension policy.

We thank you for the opportunity you have afforded us to comment on the draft report.

Sincerely,

W. Bowman Cutter
Executive Associate Director
for Budget

Notes

1. The draft report provided agencies for comment contained a preliminary conclusion that consolidation and integration of the Government's many retirement systems into a centralized system was desirable to correct the many inconsistencies and inequities that exist and to bring retirement matters under more concentrated management. In preparing the final report, this conclusion was revised and the concept of a single Federal retirement system was deleted. However, agency comments pertaining to GAO's preliminary conclusion have been included in order that they may be considered in any future proposals for adoption of this concept in whole or in part.

2. The enclosure(s) containing detailed comments on specific portions of the draft report were considered and changes made, where appropriate, in preparing the final report.

3. The deleted comment(s) related to matters in the draft report which have been revised in this final report.

4. The enclosures were sections of our draft report with suggested wording changes. Where appropriate, changes were made in this final report.

5. Page references refer to pages in the draft report and may not correspond to pages in the final report.

(963056)

*U.S. GOVERNMENT PRINTING OFFICE : 1978 0-620-167/14

COMPTROLLER GENERAL OF THE UNITED STATES
WASHINGTON, D.C. 20548

B-179810

The Honorable Gladys Noon Spellman
Chair, Subcommittee on Compensation
and Employee Benefits
House Committee on Post Office and Civil Service HSE02908

The Honorable Henry S. Reuss
Chairman, House Committee on
Banking, Finance and Urban Affairs HSE05400

The Honorable Melvin Price
Chairman, House Committee
on Armed Services HSE00500

This report, prepared in response to your joint request of June 23, 1976, discusses the desirability of establishing a mechanism to coordinate the management of all Federal retirement systems.

Based on a review of 38 retirement systems established or maintained by the Government and its instrumentalities, the report recommends that an overall Federal retirement policy and a coordinated management mechanism be established. Such a policy and centralized management focus are needed to help Federal retirement systems develop on a consistent and financially sound basis.

The report is being issued in two volumes. Volume I contains the report text and appendixes I through XX, which include the request letter and agency comments. Volume II contains appendixes XXI through XXIV, which provide information on the basic benefits provided by the systems discussed in the report.

As arranged with your offices, unless you publicly announce its contents earlier, we plan no further distribution of this report until 30 days from the date of the report. At that time we will send copies to interested parties and make copies available to others upon request.

Elmer B. Staats
Comptroller General
of the United States

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