DOCUMENT RESUME

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[Review of RCA Retirement Benefits Questioned by Terminated Employee]. PSAD-78-116; B-164292. May 26, 1978. 5 pp. + enclosure (4 pp.).

Report to Rep. Lou Frey, Jr.; by Richard W. Gutmann, Director, Procurement and Systems Acquisition Div.

Issue Area: Federal Procurement of Goods and Services: Reasonableness of Prices Under Negotiated Contracts and Subcontracts (1904).
Contact: Procurement and Systems Acquisition Div.
Budget Function: National Defense: Department of Defense - Procurement & Contracts (058).
Organization Concerned: Department of Defense: Defense Contract Administration Services Region; RCA Corp.
Congressional Relevance: House Committee on Armed Services. Rep. Lou Frey, Jr.

Frank A. Aaron, a terminated employee, questioned the manner in which the RCA Corporation administered and implemented its employees' retirement plan. Aaron alleged that RCA committed fraud by pocketing Government-reimbursed employer contributions to the retirement fund and that employees were not receiving applicable benefits under the company's retirement plan. Aaron, who worked on Government contracts during his entire RCA career, complained that his own contributions, if left in the RCA plan and compounded at 8% interest, would be sufficient to pay for the deferred benefit of $270 per month which he would get if he left his contributions in the plan. Aaron's claim against the pension fund was in accordance with the terms of the plan documents. The pension plan itself does not violate any Government regulations and is operated in a manner similar to most contributory, defined benefit pension plans. The allegations were unfounded. (RRS)

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UNITED STATES GENERAL ACCOUNTING OFFICE
WASHINGTON, D.C. 20548

PROCUREMENT AND SYSTEMS ACQUISITION DIVISION

May 26, 1978

The Honorable Lou Frey, Jr.
House of Representatives

Dear Mr. Frey:

This report is in response to your February 27, 1978, request calling our attention to correspondence you received from Mr. Frank H. Aaron of Satellite Beach, Florida, who questioned the manner in which the RCA Corporation administered and implemented its employees' retirement plan. He alleged fraud committed by the company (1) on the Government whereby the company made profits in excess of the amounts specified by contracts because it retained contributions made by the Government to the RCA retirement plan, and (2) on employees who may not be getting all applicable benefits under the company's retirement program.

We received documentation from and discussed Mr. Aaron's allegations with representatives of the RCA Corporation and the Defense Contract Administration Services Region, both in New York City.

We found that Mr. Aaron's allegations are unfounded both with respect to the statement that RCA is overcharging the Government for retirement plan costs and that RCA employees are being defrauded under the retirement program. Plan benefits are paid in accordance with the RCA Retirement Plan. Details of our review follow.

BACKGROUND

The amounts of annual contributions to a retirement plan are actuarially determined using assumptions such as salary increases, investment earnings, and employee turnover and mortality; and constitute the cost for funding future benefits specified in a plan. When a plan is contributory, such as the RCA plan, the annual funding is in part provided by employees.

Mr. Aaron was employed for about 18 1/2 years by the RCA Service Company, a division of the RCA Corporation. He worked until September 12, 1975, at the Air Force Eastern Test Range, Patrick Air Force Base, Florida, and at the National Aeronautics and Space Administration (NASA), Goddard Space Center, Greenbelt, Maryland. Mr. Aaron joined the RCA

Retirement Plan to which both the employer and employees make contributions.

Mr. Aaron's employment was terminated on September 12, 1975. On February 12, 1976, he was advised of the following options available under a pension program amended to comply with Employee Retirement Income Security Act requirements.

1. He may elect to leave his contributions in the plan and receive a monthly benefit in the amount of $270.00 with payments beginning on October 1, 2000, his normal retirement date, or

2. He may elect to withdraw his contributions, plus credited interest, of $7,440.25 as of December 31, 1975. Even though he withdraws his contributions, Mr. Aaron would receive $800 annually at age 65 from the RCA contributions to the retirement fund.

The RCA Corporation in 1976 has consolidated sales of $4,364 million of which $368 million, or 6.9 percent, consisted of sales to the Government. Contributions to the RCA pension program were about 5.3 percent of payroll costs for 1976. We estimated that the Government's share of annual contributions to the RCA Pension Program was about $10 million. Mr. Aaron worked on Government contracts during his entire RCA career and retirement plan costs contributed by the employer would have been reimbursed by the Government.

SUMMARY OF MR. AARON'S COMPLAINT

Mr. Aaron believes that RCA is defrauding the Government by retaining contributions made by the Government which are forfeited by employees when their employment terminates (before or after vesting) before retirement. At the same time, he believes RCA is defrauding the employees retirement program or, in effect, the employees who terminate prior to retirement. Mr. Aaron complains that his own contributions (he could have withdrawn $7,740.25), if left in the plan and compounded at 8 percent interest, would be sufficient to pay for the deferred benefit of $270 per month which he would get if he left his contributions in the plan. Therefore, he believes RCA is contributing nothing to his pension.

THE GAO'S CONCLUSIONS AFTER INVESTIGATING MR. AARON'S COMPLAINT

The GAO has investigated Mr. Aaron's complaint and has found the handling of Mr. Aaron's claim against the pension fund by RCA to be in accordance with the terms of the pension plan documents. Furthermore, the pension plan itself does not violate any Government regulations and is operated in a manner similar to most contributory, defined benefit pension plans.

RCA contributes each year to the pension plan based on an actuarial calculation. Although in recent periods RCA's contributions have been about 81 percent of total contributions (with the employees contributing the other 19 percent), no specific amount of employer contributions is allocated to any individual member. The contributions are made irrevocably on behalf of all participants in the plan. Some members will get more or less of the employer contributions based primarily on the following factors: age entering the plan, age terminating from or retiring from RCA employment, salary progression, and longevity. It is usual for a participant of a contributory plan, whose employment terminates a long time before his deferred benefit becomes payable, to receive a relatively small share of the employer contribution. The retirees who work until normal retirement age generally receive the largest share of employer contributions. This is a form of pooling of risk as is common in insurance and pension plans of all sorts.

The contributions made by RCA and reimbursed in part by the Government were determined anticipating that a percentage of employees would terminate employment before retirement. If more employees terminate than anticipated, actuarial gains result. These gains were adjusted for immediately by RCA instead of being spread over future years. RCA allocates actuarial gains to the cost centers experiencing terminations in excess of those anticipated.

Since the terminations Mr. Aaron referred to in his letter occurred at Government installations, these credits were properly allocated to Government contracts. Instead of the RCA Corporation "pocketing" such excess contributions, the Government, quite properly, is the beneficiary of subsequent credits.

The company's pension plan costs are regularly reviewed by the Defense Contract Administration Services Region, New York, to determine contractor compliance with the Armed Services Procurement Regulation (ASPR). The most recent review, as shown in a report dated July 13, 1977, indicated that the RCA Corporation is accounting for pension plan costs in conformance with ASPR, and termination gains were properly credited to Government contracts.

Under the RCA Retirement Plan, employees terminating after 8 years of membership in the plan have vested rights in the employer's contributions and are entitled to benefits derived therefrom. Mr. Aaron, having been employed for about 18 1/2 years, has vested rights and is entitled to a minimum benefit derived from employer contributions. His statement about employer contributions not going to any terminated employee, vested or not vested, is inaccurate.

If a terminated employee having vested rights elects to take out his own contributions plus credited interest, he is still entitled to an additional benefit derived from employer contributions. Thus, on the basis of RCA's February 12, 1976, letter, Aaron is entitled to receive from the RCA Retirement Fund $800 annually starting at age 65 even though he elects to withdraw contributions.

The RCA Corporation, on May 5, 1978, provided us with revised calculations concerning the benefits accruing to Mr. Aaron. The revisions do not alter our conclusions regarding Mr. Aaron's allegations. Copy of a detailed RCA letter is enclosed.

Mr. Aaron believes that he would be able to purchase an annuity equivalent to the one offered by RCA with his own contributions invested until his normal retirement date. He is apparently assuming that he could invest $7,740.25, due to him, at current yields of 8 percent for 25 years. The RCA Retirement Fund currently guarantees a 5 percent earnings rate.

He fails to realize that any income earned on investment, such as certificates of deposit, is taxable and that there is generally no guarantee of about 8 percent yield on the investment for more than 6 years.

Insurance companies currently offer deferred annuities with earning rates higher than 5 percent to both individuals and to groups. However, they do not guarantee that they will continue to pay the higher rates.

SUMMARY

Mr. Aaron's allegations that (1) the RCA Corporation is pocketing Government reimbursed employer contributions to the retirement fund, and (2) employees are not obtaining applicable benefits under the company's retirement program are without foundation.

Sincerely yours,

R. W. Gutmann
Director

Enclosure