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Severance pay for Federal personnel was legislated to provide involuntarily terminated employees with recognition for their service, compensation for the lost job and its consequences, and help in the transition to a new career. The Federal Government's severance pay programs are divided into two major categories: for Federal civilian employees and for uniformed services personnel. Findings/Conclusions: The armed services nondisability severance program is sometimes viewed as a substitute for vesting for officers who are separated with less than 20 years of service. There are inequities in severance pay entitlements of military and civilian personnel and in benefits available to members of the uniformed services. For example: military nondisability severance pay is available only to officers, not enlisted members; Army and Air Force officers separated for substandard performance sometimes receive more severance pay than officers separated for nonpromotion; basic pay used in calculating military severance pay does not fully reflect a member's compensation; most military officers are limited to a maximum severance pay of \$15,000 unlike civilians who are not limited to a fixed dollar amount; military officers can receive severance pay if separated for unsatisfactory performance while civilian employees are eligible only if they are not at fault; and payments for civilian employees cease if they are rehired while this limitation does not apply to military members. Recent legislation may affect employees' entitlement to the concurrent receipt of severance pay and unemployment insurance. Recommendations: The Congress should: revise the uniformed services' severance pay programs so that separation pay will be calculated and applied uniformly for all

services, provide a severance pay program for enlisted personnel, base the military severance pay formula on the average regular military compensation of the grade of the separated member and bring eligibility criteria in line with the civilian severance program, eliminate the practice of providing severance pay to members separated for unsatisfactory performance, and provide uniform severance pay limitations for all Federal personnel reemployed by the Government. It should also clarify the Unemployment Compensation Amendments of 1976 as they relate to the concurrent receipt of severance pay and unemployment insurance. (HTW)

BY THE COMPTROLLER GENERAL

Report To The Congress

OF THE UNITED STATES

8564

The Federal Government's Severance Pay Programs Need Reform

Federal civilian employees separated through no fault of their own receive severance pay based on the intent to provide comparability with the private sector. Military severance pay, however, is not uniform throughout the services and provides no benefits to regular enlisted personnel.

Recent legislation has also raised questions concerning severance pay's relationship to unemployment insurance especially since severed employees often receive both concurrently.

Severance pay for all Federal personnel, military and civilian, should be based on like criteria, be equitable to all recipients, and not be confused with the intents of other income protection programs.



FPCD-78-68

DECEMBER 7, 1978



COMPTROLLER GENERAL OF THE UNITED STATES
WASHINGTON, D.C. 20548

R-161037

To the President of the Senate and the
Speaker of the House of Representatives

This report discusses the need to provide more consistent severance pay benefits for Federal military and civilian personnel and to clarify recent legislation which may affect the concurrent receipt of severance pay and unemployment insurance. We initiated this review because of our concern that Government severance programs be fair and equitable to the employee and the Government.

We made our review pursuant to the Budget and Accounting Act, 1921 (31 U.S.C. 53), and the Legislative Reorganization Act of 1970 (Public Law 91-510).

Copies of this report are being sent to the Chairman, Civil Service Commission; the Director, Office of Management and Budget; and the Secretaries of Defense and Labor.

A handwritten signature in black ink, appearing to read "James A. Stacks".

Comptroller General
of the United States

D I G E S T

GAO recommends that the Congress (1) revise the Federal Government's severance pay programs so that they are based on like criteria and are equitable to all recipients and (2) clarify the intent of the Unemployment Compensation Amendments of 1976, as they relate to the concurrent receipt of severance pay and unemployment insurance.

SEVERANCE PAY SHOULD SERVE
A WELL-DEFINED PURPOSE

Severance pay has traditionally been paid by employers to terminated employees in recognition of their service and as a measure of compensation for the loss of their jobs and disruption of their lives. The armed services nondisability severance program, however, is sometimes viewed as a substitute for vesting. Military members who are separated with less than 20 years of service have no vesting rights. Only officers receive nondisability severance pay, and it is often considered to be compensation for the lost job and disrupted career as well as a partial substitute for the retirement benefit which would have been received after 20 years of service. (See pp. 14 and 15.)

As a matter of equity and fair treatment, an employee covered by a pension plan normally becomes vested after a reasonable period of service. His future retirement benefit is then protected, in some measure, against termination of employment.

SEVERANCE PAY CRITERIA SHOULD BE
THE SAME FOR ALL FEDERAL PERSONNEL

Severance pay should compensate all Federal personnel, military and civilian, based on the same criteria. Yet there are significant inequities in the severance pay entitlements of military and civilian personnel, and in the benefits available to members of the uniformed services: (See pp. 19 to 24.)

- Military nondisability severance pay is available only to officers, not enlisted members. Enlisted members are rarely separated involuntarily. However, since they are subject to such separation, it would seem appropriate to provide them with the same benefits accorded officers separated for the same reasons.
- Army and Air Force officers separated for substandard performance sometimes receive more severance pay than officers separated for nonpromotion.
- Severance pay for Federal civilian employees is based on salary and years of service. Military severance pay is based on years of service and basic pay. Basic pay does not fully reflect the member's regular military compensation (the equivalent of a civilian salary).
- Most military officers are limited to a maximum severance pay of \$15,000--regardless of their years of service. Federal civilians are not limited to a fixed dollar amount, but may draw severance pay equalling up to 52 weeks of salary--depending on their length of service.
- Military officers can receive severance pay if separated for unsatisfactory performance. Federal civilian employees are eligible for severance pay only if they are separated through no fault of their own.

--Federal civilian employees receive severance payments at regular pay-period intervals. Payments cease if they are rehired by the Government. Military members receive severance pay in a lump-sum amount and are not subject to the same limitation.

GAC recommends that the Congress

--revise the uniformed services' severance pay programs so that the various separation pays will be calculated by the same formula and applied uniformly to all services,

--provide a severance pay program for enlisted personnel,

--base the military severance pay formula on the average regular military compensation of the grade of the separated member and bring uniformed services eligibility criteria in line with the Federal civilian severance program,

--eliminate the uniformed services' practice of providing severance pay to members separated for unsatisfactory performance, and

--provide uniform severance pay limitations for all Federal personnel re-employed by the Government.

RECENT LEGISLATION COULD CREATE
INEQUITIES IN THE WAY SEVERANCE
PAY AND UNEMPLOYMENT ARE PAID

There are wide variations in the States' treatment of severance pay and retirement benefits when unemployment insurance is being computed. When severance pay was enacted for Federal civilian employees, the Congress acknowledged that even though Federal workers were entitled to unemployment

compensation if involuntarily separated, severance pay was still justified to help compensate them for the loss of their jobs, seniority, and benefits, and for the disruption of their lives. (See pp. 24 and 25.)

After March 31, 1980, Public Law 94-566 will reduce weekly unemployment insurance benefits by the amount of any retirement or similar periodic payments based on an individual's previous work. Depending on interpretation, this law may affect the concurrent receipt of severance pay and unemployment insurance; i.e., Federal civilian workers may have their weekly unemployment insurance benefit reduced by any periodic severance payments they receive, while military and most private sector personnel, because they receive their severance pay in lump-sum amounts, will not be subject to a similar reduction. (See pp. 24 to 26.)

The Congress should clarify the Unemployment Compensation Amendments of 1976 (Public Law 94-566, 26 U.S.C. 3304 note) as it relates to the concurrent receipt of severance pay and unemployment insurance.

Also, if the Congress does in fact want to prevent severed employees from concurrently receiving severance pay and unemployment insurance, then attention should be focused on the inequities that will arise as a result of some persons receiving severance pay at regular pay-period intervals while others are paid in lump-sum amounts. This question could also be considered by the National Commission on Unemployment Compensation, which was established by Public Law 94-566. (See p. 29.)

AGENCY COMMENTS

The Department of Defense agreed that inconsistencies and inequities exist in the military's severance pay programs, but believed it would be premature and inappropriate to endorse any specific severance pay revision at this time. (See p. 22.)

The Civil Service Commission, overseer of the severance pay program for most Federal civilian employees, agreed that severance pay and unemployment insurance were designed for different purposes, and did not believe that it was the intent of the Congress to include severance pay in the unemployment insurance reduction provisions of Public Law 94-566. (See p. 29.)

The Department of Labor, administrator of the Unemployment Insurance Program, agreed that the intent of the Unemployment Compensation Amendments of 1976 (Public Law 94-566) needs to be clarified. (See p. 30.)

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ABBREVIATIONS

CSC	Civil Service Commission
DOD	Department of Defense
GAO	General Accounting Office
NOAA	National Oceanic and Atmospheric Administration

CHAPTER 1

INTRODUCTION

Severance pay for Federal personnel, military and civilian, was legislated to provide involuntarily terminated employees some recognition for their service; to extend a measure of compensation for the lost job, seniority, and disrupted life; and to help in the transition to a new career. Generally, severance pay serves the same purpose in the private sector.

The Federal Government's severance pay programs are divided into two major categories (1) a plan for Federal civilian employees and (2) programs for uniformed services personnel.

The Federal Employees Salary Act of 1965 was the first legislation to provide severance pay to most Federal civilian employees. In an overall effort to provide pay and benefit comparability between Government and private industry workers, the act (5 U.S.C. 5595) provided severance pay for most executive and some legislative branch civilian employees separated through no fault of their own. The severance pay computation formula was devised following a Bureau of Labor Statistics study 1/ of practices in the private sector.

Executive branch civilian employees number around 2,815,000 2/ and comprise approximately 98 percent of the total Federal civilian work force (approximately 2,868,000).

Some form of military severance pay has been in existence since the early 1800s. The Congress, at that time, enacted the act of May 14, 1800, to reduce the Army for purposes of economy and the good of the service. All discharged officers and enlisted personnel were given 3 months' separation pay to use as compensation for services and expenses for returning home.

1/"Major Collective Bargaining Agreements: Severance Pay and Layoff Benefit Plans," U.S. Department of Labor, Bureau of Labor Statistics, Bulletin No. 1425-2, Mar. 1965.

2/Includes all Federal civilian workers except those employed by the legislative and judicial branches, the Central Intelligence Agency, and the National Security Agency as of April 1978.

Military severance pay is currently divided into three categories--nondisability, 1/ reserve readjustment, and disability. The rules by which severance payments are made under these categories sometimes vary among the services and among individual personnel according to grade. The provisions for payment and the eligibility requirements for these various types of separation are codified in title 10, U.S. Code.

Data for fiscal years 1973 through 1977 show that the Government spends a substantial amount each year on severance pay. Costs for those years were as follows:

	<u>FY</u> <u>1973</u>	<u>FY</u> <u>1974</u>	<u>FY</u> <u>1975</u>	<u>FY</u> <u>1976</u>	<u>FY</u> <u>1977</u>
	------(millions)-----				
Executive agencies (note a)	\$19.2	\$25.4	\$24.5	\$50.7	\$65.8
Armed services (note b):					
Nondisability severance	9.2	9.3	14.6	30.1	11.9
Reserve read- justment	17.0	70.3	28.9	50.6	26.8
Disability sever- ance	<u>19.1</u>	<u>17.8</u>	<u>19.0</u>	<u>20.2</u>	<u>25.5</u>
Total	<u>\$64.5</u>	<u>\$122.8</u>	<u>\$87.0</u>	<u>\$151.6</u>	<u>\$130.0</u>

a/Expenditures reported by the Office of Management and Budget and the Civil Service Commission. Increased Department of Defense (DOD) civilian severance payments were largely responsible for the sizable increase in expenditures from fiscal years 1975 to 1976, though very little detailed analysis was available.

b/Obligated funds reported by DOD. Post-Vietnam fluctuations in nondisability severance and readjustment payments largely reflect involuntary personnel cutbacks in years when normal attrition could not produce mandated reductions.

SCOPE OF REVIEW

We evaluated how well the Government's severance programs are serving their intended purpose and the rationale

1/"Nondisability" includes regular officer severance pay for nonpromotion and unsatisfactory performance.

for the criteria being used to determine severance pay benefits. We examined pertinent legislation, policies, and practices and interviewed DOD and Civil Service Commission (CSC) officials. We also reviewed current data from various literature and relevant studies made by the Department of Labor, the Interagency Committee, the Quadrennial Reviews of Military Compensation, and the Defense Manpower Commission.

Government agencies exempted from the severance pay provisions of 5 U.S.C. 5595 are not discussed in this report due to the small percentage of affected employees and the lack of readily accessible information.

CHAPTER 2

AN OVERVIEW OF GOVERNMENT AND

PRIVATE SECTOR SEVERANCE PAY PROGRAMS

Severance pay has traditionally reflected the employer's humanitarian efforts to provide help to the individual whose job has been unavoidably terminated. However, the criteria and formulas for compensating severed workers vary by employer. Federal civilian employees, military personnel, and private sector employees are subject to different severance pay programs.

THE FEDERAL CIVILIAN SEVERANCE PAY PROGRAM

Section 9 of the Federal Employees Salary Act of 1965, as amended, 5 U.S.C. 5595, and civil service regulations, contained in title 5 of the Code of Federal Regulations, part 550, subpart G, prescribe the conditions under which an employee is entitled to severance pay. The law and regulations also prescribe the method for computing the total amount of severance pay to which an employee is entitled, called the severance pay fund, and the manner in which payment is to be made. A part-time or full-time employee is entitled to severance pay if he/she

- has been employed continuously for at least 12 months before separation and
- is involuntarily separated from the service, not by removal for cause on charges of misconduct, delinquency, or inefficiency.

A fund is established for employees eligible for severance pay. This fund consists of two elements--a basic allowance and an age adjustment allowance. The basic allowance is computed on the basis of 1 week's basic pay (at the rate received immediately before separation) for each of the first 10 years of creditable service and 2 weeks' basic pay for each additional year of service. The age adjustment allowance is computed on the basis of 10 percent of the total basic severance allowance for each year by which the age of the recipient exceeds 40 years. Severance payments are made at regular pay-period intervals at the basic pay rate received immediately before separation until the fund is exhausted or the employee is rehired by the Government. Federal and State income taxes are the only deductions made

(except social security if the employee was subject to social security at the time of separation).

There is a lifetime, 52-week limit on the number of weeks an employee can ever be entitled to severance pay. If an employee is rehired by the Government prior to exhausting his severance pay fund, severance payments are discontinued. If the employee again becomes entitled to severance pay from a subsequent separation, the agency computes the severance pay fund at the time of separation on the basis of all eligible service, past and present, and the employee's current age and pay. The number of weeks the employee previously received severance payments are then deducted from the lifetime, 52-week limit.

Some involuntarily separated employees are not entitled to severance pay. For example, persons receiving Federal retirement, persons refusing an offer of an equivalent position in their agency within the same commuting area, or persons discharged for cause are ineligible for severance pay.

Example I shows the severance pay fund computation for an involuntarily separated 45 year old employee with 20 years of creditable service and a basic weekly pay of \$100:

I. Basic allowance:

\$100 (weekly salary) x 10 (first 10 years)	= \$1,000
\$100 (weekly salary) x 2 x 10 (years excess of 10)	= <u>2,000</u>
	\$3,000

adjustment allowance:

\$3,000 (basic allowance) x 5 (years over 40) x 10%	= <u>\$1,500</u>
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Severance pay fund:

\$3,000 (basic allowance) + \$1,500 (age adjustment allowance)	= <u>\$4,500</u>
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Weekly severance pay entitlement:

\$4,500 (severance pay fund) ÷ \$100 (weekly salary)	= \$100 weekly for 45 weeks
--	-----------------------------

Example II shows the severance pay fund for the same employee if he (1) receives 20 of his 45 weeks' severance pay but is then rehired by the Federal Government and (2) works for 3 years at his new job and is again separated under circumstances entitling him to severance pay. The employee is now 48, has 23 years of creditable service, and earns a weekly basic pay of \$125.

II. Basic allowance:

\$125 (weekly salary) x 10 (first 10 years)	= \$1,250
\$125 (weekly salary) x 2 x 13 (years in excess of 10)	= <u>3,250</u>
	<u>4,500</u>

Age adjustment allowance:

\$4,500 (basic allowance) x 8 (years over 40) x 10%	= <u>\$3,600</u>
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Severance pay fund:

\$4,500 (basic allowance) + 3,600 (age adjustment allowance)	= <u>\$8,100</u>
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It would take almost 65 weeks ($\$8,100 \div \125) to pay out the entire severance pay fund of \$8,100. However, since total severance pay may not exceed 52 weeks, and since the employee has already received 20 weeks of severance pay, he is entitled to only 32 weeks of severance pay at \$125 a week (\$4,000).

ARMED SERVICES SEVERANCE PAY PROGRAMS

Today, Armed Forces severance payments fall into three basic categories: (1) severance pay for officers separated for nonpromotion and unsatisfactory performance (referred to jointly as nondisability severance pay), (2) readjustment pay for reserve officers and reserve enlisted personnel, and (3) disability severance pay for officers and enlisted personnel. Generally, members eligible for an immediate retirement annuity do not receive severance or readjustment pay.

Defense officials stated that fluctuations in severance and readjustment payments from fiscal years 1973 through 1977 primarily reflect post-Vietnam strength reductions. To achieve mandated personnel reductions, the services involuntarily separated reserve and regular officers at accelerated

rates in those years where other actions, such as cutbacks in procurement and voluntary loss management programs, could not produce the required reductions. Additionally, separation payments for nonpromotion varied from year to year because of nonuniform sizes in the eligible populations, promotion board scheduling, and unique service promotion statutes and policies.

Nondisability severance pay

Nondisability severance pay, enacted by the Officer Personnel Act of 1947, is authorized to officers who are severed from the service for the following reasons:

- Navy and Marine Corps regular commissioned officers who twice fail selection for promotion to grades 0-3 or 0-4. Pay is computed at 2 months' basic pay for each year of service, not to exceed 2 years' basic pay or \$15,000, whichever is the lesser.
- Army and Air Force regular commissioned officers who twice fail selection for promotion to grades 0-3 through 0-5. Pay is computed at 2 months' basic pay for each year of service, not to exceed 12 years or \$15,000, whichever is the lesser.
- Regular Navy ensigns (0-1) and Marine Corps second lieutenants (0-1) who fail promotion to 0-2 because of a lack of professional qualification. Pay is computed on the basis of 2 months' basic pay multiplied by years of creditable service, not to exceed 1 year's basic pay.
- Regular Navy and Marine Corps officers who are unsatisfactory in the performance of their duties. Pay is computed at 2 months' basic pay for each year of service, not to exceed 2 years' basic pay or \$15,000, whichever is the lesser.
- Regular Army and Air Force officers whose performance of duty is substandard or who are found morally or professionally disqualified. Pay is computed at 1 month's basic pay for each year of service, not to exceed 12 years.

Reserve readjustment pay

The act of July 9, 1956, was the first law to establish a specific severance pay program for reserve personnel. It

added a section to the Armed Forces Reserve Act of 1952 that allows payment of readjustment pay to reserve members who, after 5 years or more of continuous active duty, are involuntarily released from active duty or who are released at the end of their tour after having volunteered and not been accepted for an additional tour.

From 1956 to 1962 readjustment pay was computed at the rate of one-half month's basic pay for each year of active service, not to exceed 9 months' basic pay. The act of June 28, 1962, changed the formula so as to generally equalize readjustment payments made to reservists with severance payments made to regular officers.

At present, there are two basic provisions for reserve readjustment pay--10 U.S.C. 687, and 10 U.S.C. 679 and 680. Under the provisions of 10 U.S.C. 687, readjustment pay is authorized for members of the reserve components who are involuntarily released from active duty after having completed at least 5 years of continuous active duty. The amount payable is computed by multiplying the years of active service, but not more than 18, by 2 months' basic pay. However, pay may not exceed 2 years' basic pay or \$15,000, whichever is the lesser. The readjustment payment of a member who is released from active duty because his performance of duty has fallen below acceptable standards, or whose release is in the best interests of national security, is computed on the basis of one-half of 1 month's basic pay for each year of active service, not to exceed 18 years. The maximum amount payable to such members is 9 months' basic pay or \$15,000, whichever is the lesser. (Members released from active duty because of moral or professional dereliction are not entitled to readjustment pay.)

Veterans who have received readjustment pay and who also receive disability compensation from the Veterans Administration are subject to a reduction in their Veterans Administration compensation of an amount equal to 75 percent of the readjustment pay.

Under the provisions of 10 U.S.C. 679 and 680, the service Secretaries may make a written agreement with any member of a reserve component under their jurisdiction requiring the member to serve not more than 5 years of active duty (other than for training).

A member released from active duty without his consent before the end of his agreement is entitled to an amount

computed by multiplying the number of years and fraction of a year of his unexpired period of service under the agreement by the sum of 1 month's basic pay, special pay, and allowances to which he is entitled on the day of his release.

Although the law makes both officers and enlisted personnel eligible for readjustment pay, the number of reserve officers serving on active duty far exceeds the number of reserve enlisted members. Consequently, few if any enlisted members actually qualify for readjustment pay.

Disability severance pay

When a member is found to be physically disabled, one of three alternative methods may be used to compensate him:

1. The member may be separated with severance pay if (a) the percentage of disability is less than 30 percent--with some qualifications (according to the VA standard schedule of rating disabilities), (b) the disability is permanent, and (c) the member has less than 20 years of eligible service.
2. The member may be retired for physical disability, provided the disability is considered permanent, if (a) the percentage of disability is 30 percent or more or (b) the member has completed 20 years or more of eligible service.
3. The member may be placed on the temporary disability retired list if (a) the percentage of disability is 30 percent or more, but cannot be determined to be permanent or (b) the member has completed 20 years or more of eligible service.

The Third Quadrennial Review of Military Compensation states that disability severance pay is

"* * * to provide a lump-sum payment instead of long-term retired pay to members separated from active military service because of 'minor' disabilities which make them physically unfit to perform the duties of their office or grade, but which are not so severe as to seriously impair their civilian earning capacity."

The Career Compensation Act of 1949 provided a distinction between life-time disabilities, warranting retired pay, and minor disabilities. Thirty percent disability was

established as the dividing line. To be eligible for disability severance pay, a member generally must have less than 20 years' service and be less than 30 percent disabled. The percentage of disability is determined by the military departments using guidelines set forth by the Congress in the "VA Schedule for Rating Disabilities." The VA Schedule is a guide in the evaluation of disability resulting from diseases and injuries encountered while in the military. The percentage ratings represent the average impairment in earning capacity from civil occupations.

Eligible members receive a lump-sum disability severance pay equal to 2 months' basic pay multiplied by their total years of eligible service, not to exceed 2 years' basic pay. These members can also apply to the Veterans Administration for VA disability compensation and are entitled to all other VA benefits. However, members who have received disability severance pay and who also receive VA compensation for the same disability are subject to a reduction in their VA compensation equal to the disability severance pay they received.

Other uniformed services programs

The Coast Guard's severance pay programs are similar to the Navy's. Severance payments are made for nonpromotion, unsatisfactory performance, readjustment pay for reserve personnel, and disability severance pay.

The Public Health Service pays severance pay for nonpromotion and disability. In addition, officers of the regular corps originally appointed to the senior assistant grade (0-3) or above are evaluated at the end of their first 3 years of service, and if found not qualified for further service, are separated with 6 months' pay and allowances.

The National Oceanic and Atmospheric Administration (NOAA) breaks severance pay into three categories: (1) nonpromotion, (2) unsatisfactory performance, and (3) disability. In addition, officers found to be unqualified for retention during their first 3 years of service may be separated without severance pay.

PRIVATE SECTOR PROGRAMS

Severance pay programs in the private sector vary from company to company and range from very liberal to nonexistent. Generally, severance pay plans provide benefits when a firm finds it necessary to terminate employment for reasons other than cause.

Private sector attitudes on what severance pay should accomplish are not well defined. Several losses that severance pay help offset include:

- Job displacement and wage losses, which are the losses, monetary or otherwise, that employees suffer as a result of not continuing in their predisplacement job.
- Critical benefit losses, such as the loss of life and health insurance plans.
- Loss of skill specialization, which occurs when the job requirements of a particular company necessitate that employees, during their tenure, acquire relatively nontransferable skills. Severance pay is necessary to help those employees purchase new job training or adjust to another area where comparable jobs are available.
- Loss of seniority, which usually occurs when workers start new jobs.

The Department of Labor, in reviewing the benefit plans of major collective bargaining agreements during the early 1960s, observed that approximately 30 percent of those companies studied had severance pay and layoff programs. The most common formula for computing severance pay increased benefits according to length of service--for example, 4 weeks' severance pay for 3 to 5 years of service, 6 weeks' severance pay for 5 to 7 years of service, etc.

The Conference Board, in a 1974 profile of employee benefits, concluded that severance pay programs had become somewhat more common since the mid-1960s, but that the severance pay formulas of those companies with severance pay programs had remained basically unchanged. In profiling severance pay programs in the private sector, the report stated:

"Average practice with respect to severance pay is not well-established, although an average survey company is somewhat more likely than not to have a plan--but only for its office employees. The amount of severance pay depends on length of service, but the extent to which service is recognized depends on individual plan design. Many plans are designed primarily with short-service people in mind. Defined (somewhat

arbitrarily) as plans that pay the maximum benefit for five years' service, or less, this design typically provides no more than two weeks' pay. This short-service design is especially widespread among the financial companies. The large industrials generally recognize longer periods of service in the severance pay calculation, and so provide for larger maximum amounts typically (median) 12 weeks' pay for office employees after 13 years' service.

"The 'leading edge' company provides a severance pay plan for both office and non-office employees, with payments up to 26 weeks' pay or more if an employee is terminated after extensive company service." ^{1/}

Though the Conference Board found that some plans considered the employee's age in determining benefits, more often than not, length of service was the primary consideration in determining benefits.

CONCLUSIONS

The Federal civilian severance pay program was legislated as part of an overall effort to establish pay and benefits for Government employees comparable to those prevailing in the private sector, and to eliminate any double standards which might put Federal employees at a disadvantage.

To this end, the Government has provided its civilian employees a severance pay plan that compares favorably with the more liberal private sector programs. Achieving true severance pay comparability is difficult because very little uniformity exists in the private sector. Many companies do not even have a severance pay plan. Also, severance pay in the private sector is more commonly provided for office employees than for nonoffice employees. The Government provides most of its civilian employees, regardless of profession, a severance pay plan based on an identical salary, age, and length of service formula.

The military's severance pay programs are descended from laws enacted in the 1800s. Since that time, military

^{1/}"Profile of Employee Benefits," The Conference Board (New York, New York, 1974), p. 83.

severance pay has evolved into a program aimed at compensating members whose careers have been terminated and helping them readjust to a civilian job--in effect, the same purpose as the Federal civilian severance pay program.

We see no reason why military members and Federal civilian employees should be treated differently if they lose their jobs for reasons other than cause. A Federal civilian employee may have his position abolished after 12 years of service and receive severance pay, while an enlisted military member may be denied reenlistment after 12 years of service and not be eligible for severance pay. We believe that all Federal personnel should be treated the same. Military personnel who are involuntarily separated for reasons other than cause, or who are denied reenlistment for reasons other than cause, should receive severance pay similar to that provided for Federal civilians. (See ch. 3.)

CHAPTER 3

FEDERAL SEVERANCE PROGRAMS INEQUITABLE

Severance pays for Federal military and civilian personnel were legislated to serve a similar purpose. Yet the separation benefits provided for members of the various uniformed services are based on different criteria and result in members receiving different treatment. Specifically, military severance pay, influenced by the early retirement system and the fact that members are not vested until they complete 20 years of service, fails to provide equitable benefits to individuals involuntarily forced to begin new careers. 1/

Pending revision of the current military retirement system, severance pay should be redesigned to provide payments based on a uniform age, pay, and length of service formula similar to that provided Federal civilian personnel.

ARE MILITARY SEVERANCE PROGRAMS SERVING A DUAL ROLE?

Severance pay has traditionally been paid by employers to terminated employees in recognition of their service and as a measure of compensation for the loss of their jobs and disruption of their lives. The severance program covering most executive branch employees has kept this goal intact. The armed services nondisability severance program, however, is sometimes viewed as a substitute for vesting. Unlike Federal civilians, military personnel have no vesting rights until they reach retirement eligibility. Federal civilians, after completing 5 years of service, have a vested right to retirement benefits. If service is terminated after 5 years but before eligibility for an immediate annuity, the employee is eligible for a deferred annuity beginning at age 62.

Lack of vesting before 20 years of service is a problem for the military. The provisions of the current military nondisability retirement system are such that it is viewed as a "winner-take-all" system. Only about 11 percent of the enlisted and 29 percent of the officer personnel entering the service remain to retirement. 2/ Enlisted members falling short of the required 20 years

1/Vesting represents the right of an employee to part or all of the benefits of a pension plan due to him or her on leaving.

2/Report of the President's Commission On Military Compensation, Apr. 1978, p. 43.

receive nothing, while officers are entitled to severance pay--but it is not a substitute for vesting and should not be considered as such. As a matter of equity and fair treatment, personnel covered by a pension plan normally become vested after a reasonable period of service. Their future retirement benefit is then protected, in some measure, against termination of employment.

Previous study groups
recommended changes

Several study groups have been formed to review the military retirement system and make recommendations for change. Two well-known studies were done by the Interagency Committee and the DOD Retirement Study Group. 1/ Both groups proposed some form of vesting and severance pay for involuntarily separated members (officers and enlisted). Also, both proposals would offer involuntarily separated members a choice between a deferred annuity or a lump-sum equity payment.

The Interagency Committee, established by the President in 1971, did not propose a severance pay for members voluntarily separating. 2/ However, voluntarily separating members with 10 but less than 20 years of service would receive their choice of either a deferred annuity at age 60 (2-1/2 percent of basic pay times years of service) or a lump-sum equity payment (5 percent of basic pay times years of service).

Severance pay would be reserved for those members being involuntarily separated with 5 but less than 20 years of service (computed at 5 percent of basic pay times years of service). Involuntarily separating members with 10 but less than 20 years of service, in addition to their severance pay, would also receive their choice between a deferred annuity at age 60, or a lump-sum equity payment.

The DOD Retirement Study Group, established by the Secretary of Defense to review the recommendations of the Interagency Committee, believed the most serious drawback

1/Proposals made by these groups for compensating members separated prior to retirement are outlined in app. V.

2/The Interagency Committee and the DOD Retirement Study Group used the term "readjustment pay" in lieu of severance pay.

to the Interagency Committee proposal was that the choice of a lump-sum payment for members voluntarily separating with more than 10 years of service might serve as a disincentive for continued service.

The Study Group's proposal for vesting and severance pay was different than the Interagency Committee's in two respects (1) voluntarily separating members with 10 but less than 20 years of service would not be given a choice between a deferred annuity or a lump-sum equity payment, but would be eligible only for the deferred annuity and (2) whereas the Interagency Committee proposal would provide involuntary separatees with 10 but less than 20 years of service a choice of either a deferred annuity or a lump-sum equity payment, the Study Group would provide the same benefits to members with only 5 years of service.

The DOD Study Group's vesting and severance pay modifications were incorporated into the Retirement Modernization Act, which was introduced in the House of Representatives in the 93rd Congress and again in the 94th Congress.

Both proposals, then, would be considerably more generous than the present system to both voluntarily and involuntarily separated officers and enlisted members with less than 20 years of service. For example, under the DOD Study Group proposal, an Army captain (O-3) voluntarily separating after 14 years of service would receive, at age 60, a deferred monthly annuity of \$551.36 (based on October 1, 1977, pay rates). An involuntarily separated captain (O-3) with 14 years of service would receive either a deferred monthly annuity of \$551.36 at age 60 or a lump-sum equity payment of \$13,232.52. In addition to the deferred annuity or equity payment, he would also receive a severance payment of \$13,232.52.

Under the existing system a voluntary separatee would receive nothing. An Army captain with 14 years of service separated for nonpromotion would receive only severance pay (\$15,000).

To date the Congress has not acted on either proposal, and DOD does not plan to resubmit the Retirement Modernization Act proposal or other alternatives until the proposals made by the President's Commission on Military Compensation have been evaluated.

The President's Commission on Military Compensation was established in June 1977 to resolve the differences among prior study groups and to propose a single, integrated plan for military compensation. The Commission, in its April 1978 report, recommended replacing the existing retirement system with a 3-part program that consists of an old-age retirement plan, a deferred compensation trust fund, and a severance pay plan. ^{1/} Under this proposed system, officers and enlisted members with 10 or more years of service would qualify for an old-age annuity patterned after the provisions of the Federal civil service retirement system. In addition, for members completing 5 years of service, the Government would establish a deferred compensation trust fund designed to provide additional incentives to remain on active duty and to assist separated members in their transition to civilian life. At the completion of 10 years of service, the amount in the fund would be vested in the account of the military member. If the member left active duty after that point, the balance of the account would be distributed to the member according to one of several available options. Members who did not leave the service would be able to draw a portion of their account while still on active duty.

The proposed severance pay system would provide involuntarily separated members with 5 to 30 years of service a lump-sum payment based on a formula of one-quarter month's basic pay a year for up to 10 years of service, and one-half month's basic pay a year for 11 to 30 years of service--up to a maximum of 12 months' basic pay.

Aside from the minimum 5 years of service requirement and the lack of an age adjustment factor, the Commission's severance pay proposal, in itself, is similar to the Federal civilian program. However, when combined with the deferred compensation trust fund--designed in part to assist severed members in their transition to civilian life--the proposed severance benefits for terminated military members would exceed those available to Federal civilians separated under similar circumstances.

The Commission's deferred compensation proposal warrants careful consideration because in attempting to alleviate current personnel retention problems, it may create new ones. The present 20-year retirement system is inefficient in part

^{1/}See the "Report of the President's Commission on Military Compensation," Apr. 1978, pp. 61 to 73.

because members have no vested rights until they serve 20 years, and marginal performers with several years of service often remain to the 20-year point solely to become vested in the retirement system. Conversely, for members with marketable skills, the prospect of combined military retired pay and second career income provide a strong incentive to leave the service. As noted in our March 13, 1978, report "The 20-Year Military Retirement System Needs Reform" (FPCD-77-81):

"Retaining employees past the point where they are able and willing to fulfill the duties of their respective jobs can be very expensive in terms of efficiency and the ability to meet an employer's mission. Conversely, there can be substantial and perhaps enormous costs associated with retiring employees too early. If early retirement benefits are so good that an employee retires before he has lost the ability and inclination to do a good job, then the organization has not received full value from its investment in training and experience."

The proposed deferred compensation plan may very well provide a strong incentive for members who normally leave after one enlistment to stay until the 10th year when they become vested in the plan, but retention potential beyond that point lacks certainty. The Commission's proposal would rely on higher Government contribution rates to the plan after 10 years, 1/ the interest that would continue to accumulate, and the deferral of taxes to provide sufficient incentives for members to continue on active duty past 10 years of service. A reasonable possibility exists, however, that the availability of the deferred trust fund money after 10 years of service might provide a catapult that would induce members with marketable skills to leave the military and seek civilian employment.

The deferred compensation trust fund, in our opinion, is a departure from traditional compensation factors in the private sector, and would perpetuate the belief that a gap exists between the pay and benefits of Federal civilian

1/The Commission's proposed contribution to the deferred Compensation account would be as follows: 6 to 10 years of service, 20 percent of basic pay; 11 to 20 years, 25 percent; 21 to 25 years, 15 percent; 26 to 30 years, 5 percent.

and military personnel. Further consideration should be given to using available funds to attract and retain members where personnel shortages exist, rather than establishing a deferred compensation trust fund for all military personnel serving longer than 5 years.

UNIFORMED SERVICES SEVERANCE
PAY CRITERIA NOT EQUITABLE

Though current severance pay laws were intended to provide equitable benefits for members separated before retirement eligibility, some service members still receive inequitable treatment. For example, the Officer Personnel Act of 1947 requires that Navy and Marine Corps officers with less than 20 years of service who perform unsatisfactorily be discharged with the same severance pay as officers discharged for failure to be promoted (2 months' basic pay for each year of commissioned service, not to exceed the lesser of 2 years' basic pay or \$15,000).

The Army and Air Force Vitalization and Retirement Equalization Act of 1948 recognized this shortcoming and tried to make a distinction between Army and Air Force officers separated for nonpromotion and those separated for unsatisfactory performance. Those separated for nonpromotion were to continue receiving severance pay calculated in the same manner as Navy and Marine Corps personnel separated for nonpromotion. Officers separated for unsatisfactory performance would receive severance pay calculated at the rate of 1 month's basic pay for each year of service, not to exceed 1 year's basic pay.

On the surface, the Army and Air Force "substandard performance" formula appears to be less favorable than the formula for Navy and Marine Corps officers discharged under similar circumstances, and for any officers discharged because of failure of promotion. However, increased basic pay rates have distorted the relationship between the two formulas. For example, an Army or Air Force captain discharged after 12 years of service for substandard performance is entitled under the "less favorable" formula to severance pay of 1 year's basic pay (\$19,465.20). ^{1/} The entitlement of a similar Navy or Marine Corps officer discharged for unsatisfactory performance, or of a similar officer of any service discharged

^{1/}Based on Oct. 1, 1978, pay rates.

for failure of promotion, is \$15,000 under the "more favorable" formula of 2 months' basic pay times years of service, not to exceed the lesser of 2 years' basic pay or \$15,000.

Officers of the Coast Guard, National Oceanic and Atmospheric Administration, and Public Health Service separated for nonpromotion or unsatisfactory performance are not limited by a \$15,000 ceiling.

The services should eliminate the practice of paying severance pay to members separated for unsatisfactory performance. Federal civilian employees, like most of their private sector counterparts, do not receive severance pay if they are separated for cause.

MILITARY AND FEDERAL CIVILIAN SEVERANCE PROGRAMS DO NOT PROVIDE UNIFORM BENEFITS

Several notable differences exist which result in military and Federal civilian personnel receiving inequitable severance pay benefits: 1/

- Severance pay for civil service and private sector employees is usually based on salary and years of service. Military severance pay is based on basic pay and years of service. Basic pay does not completely reflect the member's total salary. Total military salary is more accurately referred to as regular military compensation, which consists of basic pay, basic allowance for quarters, basic allowance for subsistence, and the tax advantage derived from the nontaxable status of the two allowances.
- Military nondisability severance pay is available only to officers--there are no similar provisions for enlisted members. 2/ Enlisted members are rarely separated involuntarily. However, since they are subject to such separation, it would seem appropriate to provide them with the same benefits accorded officers separated for the same reasons. Federal

1/See app. IV for comparison charts.

2/Legislative research failed to show why there is not a nondisability severance pay program for regular enlisted personnel.

civil service employees, whether general schedule or wage board, part or full time, are eligible for severance benefits if involuntarily separated.

- Military officers separated for unsatisfactory performance are eligible for severance pay. Federal civilian employees can receive severance pay only if they are separated through no fault of their own.
- Most military officers are limited to a maximum severance pay of \$15,000, regardless of their years of service. Federal civilians are not limited to a fixed dollar amount, but may draw severance pay equaling up to 52 weeks of basic pay--depending on their length of service.
- Federal civilian employees receive severance payments at regular pay-period intervals. Payments cease if they are rehired by the Government. Military members receive severance pay in a lump-sum amount and are not subject to the same limitation.

CONCLUSIONS

Severance pay for all Federal personnel, military and civilian, should be based on the same criteria. The legislative intent of both programs indicate this should be the case. The military severance pay system is a patchwork system which may be doubling for purposes never intended, and it often pays members separated for similar reasons unequal amounts. As a matter of equity and fair treatment, all Government personnel separated through no fault of their own deserve severance pay based primarily on a uniform length of service formula.

Before the military's severance pay programs can be viewed as comparable with the Federal civilian program, adjustments must be made in the military retirement system, as we have previously reported. ^{1/} That is (1) some form of vesting should be provided to military members and (2) military members should not be allowed to retire, at their discretion, with only 20 years of service. Until then, military severance programs may be viewed as providing severance pay for purposes not evidenced in the Federal civilian sector.

^{1/}"The 20-Year Military Retirement System Needs Reform," (FPCD-77-81, Mar. 13, 1978).

RECOMMENDATIONS TO THE CONGRESS

We recommend that the Congress

- revise the uniformed services severance pay programs so that the various separation pays will be calculated by the same formula and applied uniformly to all services,
- provide a severance pay program for enlisted personnel,
- base the military severance pay formula on the average regular military compensation of the grade of the separated member and bring uniformed services eligibility criteria in line with the Federal civilian severance pay program,
- eliminate the uniformed services' practice of providing severance pay to members separated for unsatisfactory performance, and
- provide uniform severance pay limitations for all Federal personnel reemployed by the Government.

AGENCY COMMENTS AND OUR EVALUATION

DOD agreed that many inconsistencies and inequities exist in the present military severance pay programs. However, it stated that since legislation will be submitted to the next session of the Congress which will restructure, where appropriate, the military compensation system, it is premature and inappropriate to endorse any specific severance pay revisions because (1) there is no evidence of any compelling urgency for such a change, and (2) the rationale for such change is faulty.

It was not our intent to design a new military compensation system in this review, but we are concerned about the deficiencies and the inequities that currently exist in the uniformed services severance pay programs.

We are pleased to see that DOD intends to submit legislation which they claim will address many of the problems discussed in this report. We urge the Congress to

make sure that such legislation is submitted promptly for its consideration.

We disagree with DOD that the rationale for change is faulty. DOD said the major faults with the rationale were:

- Military careers are shortened for a number of reasons, whereas a civilian career extends until normal old-age retirement.
- Military personnel are subject to military discipline under the Uniform Code of Military Justice, which is a stricter code than that applicable to most Federal civilians.

Civilian careers, like military careers, are sometimes shortened by a reduction in force, and we believe the two should be compensated similarly. It is true that many military members choose to retire after only 20 years of service and at a relatively young age, but we view this as a costly system that must be revised. Furthermore, military personnel who are court martialed and discharged or are released from service early because of a crime under the military code do not warrant the receipt of severance pay in addition to their normal entitlements.

CHAPTER 4

SEVERANCE PAY AND UNEMPLOYMENT INSURANCE

Severance pay and unemployment insurance are not provided for the same purpose, and in our opinion, do not represent duplicative benefits.

Recent legislation, however, aimed at reducing unemployment insurance by the amount of any periodic payments based on an individual's previous work, could affect the concurrent receipt of severance pay and unemployment insurance. Depending on interpretation of the law, Federal civilian workers could have their unemployment insurance reduced by any periodic severance payments they receive, while military and most private sector personnel, because they receive their severance pay in lump-sum amounts, might not be subject to a similar reduction.

FEDERAL AND PRIVATE SECTOR COMPARABILITY

Severance pay for Federal civilian employees was legislated as part of an overall effort to provide pay and benefits to Government employees comparable with those prevalent in the private sector. The legislative history of severance pay for Federal employees indicates that the Congress was aware of the different intents of unemployment insurance and severance pay in the private sector when it considered Government severance pay legislation. The following comment about severance pay and unemployment insurance appeared in a report of the House Committee on Post Office and Civil Service:

"Unemployment compensation is also payable to Federal employees, as it is to those in private enterprise, in accordance with practices of the State in which they reside. Unemployment compensation helps tide individuals over periods of unemployment, but does not compensate them for loss of seniority and other benefits earned in their previous job, nor for the disruption of their existence that is associated with loss of employment." (H. Rept. 792, 89th Cong., 1st sess. 31 (1965)).

At present, the effect of income other than wages on unemployment insurance is determined by the individual jurisdictions (the 50 States, the District of Columbia, and Puerto

Rico). 1/ Severance pay presently has no effect on unemployment insurance benefits in 36 jurisdictions, reduces unemployment benefits in 11 jurisdictions, and eliminates concurrent unemployment payments in 5 jurisdictions.

Public Law 94-566, after March 31, 1980, will reduce individual unemployment benefits by the amount of any pension, retirement or retired pay, annuity, or any other similar periodic payment which is based on the previous work of an individual. The legislative history of this law indicates that the intent is to reduce the unemployment benefits of those persons who are receiving pensions and have retired from the labor force. However, if severance pay is interpreted as a "periodic payment," then all jurisdictions will be required to reduce weekly unemployment insurance benefit payments by the amount of any periodic severance payments received--though the total amount of unemployment benefit entitlement an individual would be eligible for would not be reduced.

This situation could lead to the inequitable treatment of Federal civilian employees who receive their severance payments at periodic pay-period intervals. Military personnel and most private sector employees receive their severance pay in lump-sum amounts and could possibly avoid the weekly reduction of their unemployment benefits based on that technicality.

SEVERANCE PAY AND UNEMPLOYMENT
INSURANCE SERVE DIFFERENT PURPOSES

Severance pay and unemployment insurance do not provide benefits for entirely parallel reasons. To reduce unemployment payments by the amount of any concurrent separation payments may defeat the intent of severance pay in the private and public sectors.

The unemployment insurance program was established in 1935 as part of the Federal-State employment security program authorized under the Social Security Act (42 U.S.C. 501)

1/By law, for unemployment insurance purposes, unemployed Federal civilian and military personnel are to receive the same treatment as their private sector counterparts. Consequently, regulations for severed Federal personnel pertaining to the concurrent receipt of severance pay and unemployment insurance are determined by individual State law.

and the Wagner-Peyser Act (29 U.S.C. 49). The program was designed to provide temporary protection for qualified insured workers who lost their jobs until they could either be rehired or find new employment.

There is no uniformity in the jurisdictions' formulas for determining workers' unemployment benefit rights. However, all jurisdictions require that employees be able, available, and willing to work in order to qualify for benefits. They also require that claimants work a certain number of weeks and/or earn a certain amount of wages in a base period in order to qualify. The weekly benefit amount, that is, the amount payable for each week of total unemployment, varies with the worker's past wages with certain limits. In most jurisdictions, the formula is designed to compensate for a fraction of the full-time weekly wage; i.e., for a fraction of the wage loss, up to a specified maximum benefit amount.

A legislative analysis of unemployment compensation prepared in 1974 by the American Enterprise Institute For Public Policy Research explains the character of unemployment insurance:

"Unemployment insurance belongs to the family of social insurance programs, which can be distinguished from the family of social assistance, or welfare programs. Social insurance is an ingenious device occupying a middle ground between wages and welfare that attempts (not always successfully) to have the best of both worlds. Like welfare, it aims to make its benefits available at the time and to the extent that need is experienced. Like the wage system, it makes income available on the basis of previous work without proof of individual need, that is, without any needs test.

"In the United States unemployment benefits are paid in some proportion to wages, so that the person who is paid higher wages when employed receives higher benefits when unemployed and is thus helped to maintain something close to his accustomed standard of living. This is justified on the score that the taxes paid by the employer into the unemployment insurance fund are also a percentage of wages; consequently the employer has made a larger contribution in the name, as it were, of the higher-wage

employee. Social insurance is thus integrated with the market in a way that social assistance is not." 1/

Like unemployment compensation, the loss of wages is an important reason why employers provide severance pay. However, the concept of severance pay is sufficiently broad to incorporate other rationales as well. When looking at the entire income protection picture some of the different philosophies between severance pay and unemployment insurance become evident:

--Unemployment benefits cease as soon as the recipient is reemployed. This feature underscores the idea that unemployment insurance is to provide temporary income replacement for the unemployed. However, most private sector employees covered by severance pay programs are entitled to their full severance pay benefit regardless of whether they find new employment the day after losing their job, or months later. Often severance benefits are paid in lump-sum amounts, highlighting the employer's desire that the employee receive the full benefit without regard to the success or failure of his job search. Even separated Federal employees rehired by private concerns can continue to collect their severance pay from the Government.

Employers usually feel that severance pay is justified because of the disruption to the employee's work life, loss of seniority, need for retraining or education, costs involved in a job search, and need to pay off debts the employee committed himself to pay when he was employed. Some employers also believe that a reasonable commitment (severance pay) made to employees separated through no fault of their own will help ease any uncertainties the remaining work force may have concerning their future financial security.

1/"Unemployment Compensation: Proposed Permanent Changes," American Enterprise Institute For Public Policy Research, Apr. 30, 1974, p. 6.

- The weekly benefit amount paid under the unemployment insurance program is based on a worker's past wages (within certain limits). That is, unemployment compensation is designed to replace lost wages. Severance pay varies in that length of service is also an important determinant in how much severance pay the employee receives. Employees generally receive a certain number of weeks pay based on years of service. In this way, the employer can provide greater compensation to longer service employees, reflecting the greater commitment the employee made to the employer.

- Unemployment compensation does not consider an employee's age. Some employers, including the Federal Government, include an age allowance in their severance pay formula for older workers who lose their jobs. The age allowance is provided partly in recognition of the fact that older workers have a more difficult time finding new employment than younger workers. Unemployment compensation treats all employees alike, young and old.

- Unemployment compensation, as a social insurance program, is nontaxable to the recipient. On the other hand, all applicable taxes (income, social security, etc.) must be deducted from severance payments. That is, severance pay is treated like other income the employee has earned.

CONCLUSIONS

The 50 States, the District of Columbia, and Puerto Rico have developed diverse procedures for determining unemployment insurance eligibility. However, Federal involvement is increasing. This is exemplified by the passage of Public Law 94-566, which, after March 31, 1980, will reduce unemployment benefits by the amount of any pension, retirement pay, annuity, or other similar periodic payment based on the previous work of an individual.

It is unclear whether severance pay fits the intended definition of a "similar periodic payment." Also, a periodic payment would not apply to military severance pay or the majority of private sector programs that pay severance in lump-sum amounts, but would seem to be aimed more at Federal civilian employees.

Severance pay constitutes a benefit to workers who in many cases have invested numerous years with a single employer. Reducing weekly unemployment benefits by the amount of severance pay an individual receives would probably serve no positive effect. Employers, already required by law to pay unemployment taxes, might stop providing severance pay, since it would cease to be the highly visible gratuity it has traditionally been, and would not increase the severed employees weekly income.

RECOMMENDATIONS TO THE CONGRESS

We recommend that the Congress clarify the Unemployment Compensation Amendments of 1976 (Public Law 94-566, 26 U.S.C. 3304 note) as it relates to the concurrent receipt of severance pay and unemployment insurance.

Also, if the Congress does in fact want to prevent severed employees from concurrently receiving severance pay and unemployment insurance, then attention should be focused on the inequities that will arise as a result of some persons receiving severance pay at regular pay-period intervals while others are paid in lump-sum amounts. This question could also be considered by the National Commission on Unemployment Compensation, which was established by Public law 94-566.

AGENCY COMMENTS

The Civil Service Commission, overseer of the severance pay program for most Federal civilian employees, agreed that severance pay and unemployment insurance were designed for different purposes. Severance pay compensates severed workers for loss of seniority and disruption of their lives, and unemployment insurance partially replaces wages over periods of unemployment. CSC further noted that these different purposes are often overlooked, resulting in criticism that Federal employees receive dual benefits to meet their loss of wages until they find new jobs.

CSC did not believe that it was the intent of the Congress to include severance pay in the unemployment insurance reduction provisions of Public Law 94-566. It felt that if the Congress intent had been to end the concurrent receipt of severance pay and unemployment insurance, it would have specifically mentioned severance pay and would not have restricted action to only severance benefits paid at periodic intervals, which is the least common method of payment.

CSC concluded that since the Department of Labor has the primary role in administering the unemployment insurance program for Federal employees, its interpretation of Public Law 94-566 will have a significant impact on the administration of the program.

The Department of Labor agreed with us that the Unemployment Compensation Amendments of 1976 (Public Law 94-566) needs to be clarified.

Labor also emphasized that for unemployment insurance purposes, the Congress intended that Federal civilian and military personnel be treated the same as their private sector counterparts. Consequently, regulations for severed Federal personnel pertaining to the concurrent receipt of severance pay and unemployment insurance are determined by individual State law.



MANPOWER,
RESERVE AFFAIRS
AND LOGISTICS

ASSISTANT SECRETARY OF DEFENSE
WASHINGTON, D. C. 20301

1 SEP 1978

Mr. H. L. Krieger
Director, Federal Personnel and
Compensation Division
United States 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 July 17, 1978 on "The Federal Government's Severance Pay Programs Need Reform" (OSD Case 4953) (GAO Code 963077).

The essential recommendation of the subject report is that all Federal severance programs be reconstituted on a uniform basis, since all have the same purpose. Specifically, various aspects of the severance pay programs of the uniformed services are recommended for revision in a manner that would make them more compatible with civilian severance pay programs. Various inconsistencies in military severance pay authorities are cited to support this view.

The Department of Defense opposes such a recommendation.

The Department of Defense intends to submit legislation to the next session of Congress which restructures, where appropriate, the military compensation system. It is anticipated that the legislation will address many of the items cited in the report. Examples of these are: authorizing severance pay for enlisted personnel and establishing common standards for eligibility and amounts of severance pay for the armed forces. However, as the report itself points out (p. 18), severance pay must be in a systemic balance with the retirement system. Precisely how the military retirement system should be restructured has not yet been decided by the President. Until that has been done, the Department of Defense considers it inappropriate to endorse any specific severance pay revision.

Thank you for the opportunity to comment on this draft report.

Sincerely,

ROBERT B. PIRIE, JR.

Principal Deputy Assistant Secretary
of Defense (MRA&L)

Enclosure

DETAILED COMMENTS

The Department of Defense believes that it would be premature for the Congress to enact changes to the military severance pay system pending consideration of the proposed military compensation legislation. We oppose this enactment for two reasons: first, we see no evidence of any compelling urgency for such a change, and second, we believe the rationale for such a change to be faulty.

With respect to the first point, the subject report has shown no evidence to indicate that reform of military severance pay is an issue that requires immediate attention. Is there a major savings to the taxpayer to be expected from such a change? Are the members of the armed forces so upset about the alleged inequities of the current system that their performance is adversely affected? Is the Congress demanding action? The report is silent on these issues. Thus, we question the urgency to change the military severance pay system prior to consideration of full compensation revision.

With respect to the second point, we believe that the use of the same term to describe dissimilar content and conditions of service can be more than a semantic trap. Of course, military and civilian severance pay systems are different. The question raised in the report is: should they be? The answer given is "no". The Department of Defense disagrees with this judgment for a number of reasons, most of them related to conditions of service. Major among these reasons are:

- o A military career is necessarily foreshortened for a number of accepted reasons whereas a civilian career extends until normal old age retirement is reached.

- o Military personnel are subject to military discipline as codified in the Uniform Code of Military Justice, which is a stricter code than that applicable to the vast majority of Federal civilians. In practical terms, this means that the military equivalent of a civilian removal "for cause" could be a court martial and that a military and civilian "unsatisfactory performance" rating mean quite different things.

Aside from these basic differences in conditions of service, the Department of Defense would like to make clear that there is no "vesting" of military retired pay at any time. The report confuses conditional entitlement to retired pay with vesting. A retired member is still a member of a uniformed service, subject to the Uniform Code of Military Justice at all times (including the possibility of recall, court martial, and reduction of retired pay), and his estate has no automatic rights to his retired pay in the event of his death. All of these conditions are at odds with the generally accepted definition of the term "vesting".

Finally, as a general point, the Department of Defense sees no advantage to be gained from further "civilianization" of the armed forces. The basic mission of the armed forces is to be prepared to exercise armed force, and the imperatives stemming from that mission necessarily are different from the practices of civilian employment.

On the issue of the clarification of the intent of the Unemployment Compensation Amendments of 1976 (Pub. L. 94-566), the Department of Defense defers to the Civil Service Commission.



UNITED STATES CIVIL SERVICE COMMISSION

WASHINGTON, D.C. 20415

SEP 20 1978

Mr. H. L. Krieger
Director, Federal Personnel
and Compensation Division
United States General Accounting
Office
Washington, D.C. 20548

Dear Mr. Krieger:

We have reviewed your draft of a proposed GAO report, "The Federal Government's Severance Pay Programs Need Reform." We have confined our comments to Chapter 4 of your draft report which is the chapter relevant to the Federal civilian sector. While we agree with respect to unemployment benefits that treatment should be uniform for Federal civilian, military and private sectors, we do not agree about the need to seek an interpretation from Congress on the provision in question.

The basic purpose behind severance pay is, and should be, different than the purpose behind unemployment compensation. Severance pay is intended as compensation for the loss of seniority and other benefits earned in an employee's previous job, and for the disruption to his or her life. Unemployment compensation partially replaces wages over periods of unemployment. These different purposes, however, are often overlooked, with the resulting criticism that Federal employees receive dual benefits to meet their loss of wages until they find another job. Part of this criticism may result from the method of paying severance pay to Federal civilians. The Federal civilian sector pays the severance pay benefit in regular biweekly payments which, in effect, continue the employee's regular salary payments. On the other hand, the military and most of private industry pay the severance pay benefit in a lump sum. Many private sector employees working for an employer with a severance pay plan receive both severance pay and unemployment compensation upon separation, where the separation is through no fault of the employee.

With respect to your question regarding the interpretation of Public Law 94-566 on the concurrent receipt of severance pay and unemployment compensation, we see no evidence that it was the intent of Congress to cover Federal civilian severance pay under the offset provision in question. We have reviewed both the language of the offset provision

as it is stated in the law and the reports of the Congressional committees on the legislation. The only specific references in both the law and the committee reports are to retirement, annuity and pension payments. The phrase in question, "other similar periodic payments," appears to have been included as a means to cover retirement or annuity type benefits which are identified by other terms.


We believe, in the absence of legislative history to the contrary, that the wording in question can be interpreted on its face. In that connection, we can only assume Congress was aware at the time it was considering this amendment that most severance pay is disbursed in a lump sum in all sectors except the Federal civilian sector. If Congress' intent had been to end the concurrent receipt of severance pay and unemployment compensation, we feel that they would have directly referred to it and would not have restricted their action to only severance benefits paid at periodic intervals, which is the least common method of payment. In the absence of any reference to other than retirement type benefits and the fact that Congress should have been aware of the implications of its actions, we see no reason or need to reopen the question of Congressional intent.

We do realize, however, that the Department of Labor has the primary role in the administration of the unemployment compensation program with regard to Federal employees. Its interpretation of the amendment in question will have a significant impact on the administration of the program. Therefore, it may be necessary to seek a clarifying amendment if the Department of Labor has substantive questions on the intent of the phrase in question.

We believe that dual entitlement to severance pay and unemployment benefits should be uniform, not only between military and civilian personnel, but between Federal and private industry employees. If an amendment is sought, this view should be emphasized and the potential inequities of the inclusion of severance pay as a "periodic payment" pointed out.

We appreciate the opportunity to comment on your draft report.

Sincerely yours,


Raymond Jacobson
Executive Director

U.S. DEPARTMENT OF LABOR
OFFICE OF THE SECRETARY
OFFICE OF SPECIAL INVESTIGATIONS
WASHINGTON, D.C. 20210



SEP 5 1978

Mr. Gregory J. Ahart
Director
Human Resources Division
U. S. General Accounting Office
Washington, D.C. 20548

Dear Mr. Ahart:

This responds to your July 17, 1978, invitation to the Secretary of Labor for comments on the Draft Comptroller General's Report to the Congress entitled "The Federal Government's Severance Pay Programs Need Reform." According to your letter,

"We believe that severance pay for all Federal personnel, military and civilian, should be based on like criteria, be equitable to all recipients, and not be confused with the intents of other income protection problems."

The draft report discusses the reasons why these objectives are not currently being met and makes recommendations for remedial congressional action.

The report describes legislative history indicating that Congress did not intend for severance pay and unemployment insurance to be considered duplicate payments. However, the report points out that, despite that intent,

- (1) Unemployment insurance is either reduced or eliminated by reason of severance pay in 16 States;
- (2) Different treatment of unemployment insurance arises because some persons receive severance pay at regular pay period intervals while others are paid in lump-sum (those paid at regular intervals are likely to incur greater over-all reductions in benefits); and
- (3) Public Law 94-566 appears to require reduction of unemployment benefits by severance pay, effective after March 31, 1980.

Under the Federal program of unemployment insurance for ex-servicemen (UCX) and Federal employees (UCFE), States must provide the same treatment for those workers as they provide for all other unemployed workers. Accordingly, the impact of severance pay on UI varies from State to State. Presumably, this is accepted and recognized by the report, since it contains no recommendation that Congress require all States to treat UCX and UCFE claimants differently from other claimants.

We recommend that the report contain at least a brief description of the UCFE and UCX programs and their requirements for "equal treatment" so that readers will understand that these programs represent one reason why not all severance pay recipients are treated alike nationwide for UI purposes. We would think it desirable to point out in the report that in creating UCFE and UCX, Congress chose to have these claimants treated the same as other claimants under the State law.

The report calls for Congressional clarification of Public Law 94-566 as to whether the required reduction of unemployment benefits by "a governmental or other pension, retirement or retired pay, annuity, or any other similar periodic payment which is based on the previous work of such individual" applies to severance pay. The report also points out that if Section 3304(a)(15) of the Federal Unemployment Tax Act, (quoted in part above) is intended to apply to severance pay, then Congress be made aware of the inequities that will arise if severance pay is provided some individuals at periodic intervals and other individuals in lump-sum.

We support these two recommendations. Please advise us if additional comments or clarification of the above comments would be helpful to you.

Sincerely,



R. C. DeMARCO
Director

FEDERAL CIVILIAN AND UNIFORMED SERVICES SEVERANCE PAY PROGRAMS

CIVILIAN

Title 5

Are all employees covered? Yes.

Who qualifies? Employees with 12 months of continuous service who are involuntarily separated through no fault of their own.

How is pay computed? Severance pay consists of 2 items: (1) a basic allowance of 1 week's basic pay for each year of service for the first 10 years and 2 weeks' basic pay for each additional year and (2) an age adjustment allowance computed at 10 percent of the basic allowance for each year over age 40.

Method of payment. Severance is paid at regular pay-period intervals at the same basic rate of pay.

Maximum pay allowable. 52 weeks' pay during an employee's lifetime.

Limitations. No severance pay if the employee is (1) entitled to an immediate Federal annuity, (2) receiving disability compensation, (3) declining a comparable Federal job with his agency in the same commuting area, (4) reemployed by the U.S. Government, or (5) entitled to receive other severance pay from the Government.

UNIFORMED SERVICES

(1) Separation for Nonpromotion

(Regular Officers)

	<u>Army/Air Force</u>	<u>Navy/Marine Corps</u>	<u>Coast Guard</u>	<u>NOAA</u>	<u>Public Health Service</u>
Are all members covered?	No. Officers only.	No. Officers only.	No. Officers only.	Yes. All officers.	Yes. All officers.
Who qualifies?	Grades 0-2 thru 0-4 who twice fail selection for promotion.	a/Grades 0-2 or 0-3 who twice fail selection for promotion.	Grades 0-2 or 0-3 who twice fail selection for promotion.	Grades 0-2 or 0-3 who twice fail selection for promotion.	Grades 0-2 or 0-3 who twice fail selection for promotion.
How is pay computed?	Years of service, but not more than 12 x 2 months' basic pay, not to exceed the lesser of 2 years' basic pay or \$15,000.	2 months' basic pay x years of service, not to exceed 2 years' basic pay or \$15,000.	Years of service, but not more than 12 x 2 months' basic pay.	2 months' basic pay not to exceed 2 years' basic pay.	0-2s: 6 months' basic pay and allowances. 0-3s: 1 year's basic pay and allowances.
Method of payment.	Lump sum.	Lump sum.	Lump sum.	Lump sum.	Lump sum.
Maximum pay allowable.	2 years' basic pay or \$15,000, whichever is lesser.	2 years' basic pay or \$15,000, whichever is lesser.	2 years' basic pay.	2 years' basic pay.	0-2s: 6 months' basic pay and allowances. 0-3s: 1 year's basic pay and allowances.
Limitations.	No severance pay if eligible for retirement.	Severance pay is deducted from the retirement pay of members who qualify for retirement benefits.	Severance pay is deducted from any retirement benefits to which the member becomes eligible.		

a/Officers in grade 0-1 found not to be professionally qualified for promotion are severed with pay computed on the basis of 2 months' basic pay multiplied by years of creditable service, not to exceed 1 year's basic pay.

UNIFORMED SERVICES

(2) Separation for Unsatisfactory Performance

(Regular Officers)

	<u>Army/Air Force</u>	<u>Navy/Marine Corps</u>	<u>Coast Guard</u>	<u>NOAA</u>	<u>Public Health Service</u>
Are all members covered?	No. Officers only.	No. Officers only.	No. Officers only.	Yes. All officers.	Yes. All officers.
Who qualifies?	Officers whose performance is sub-standard.	Officers whose performance is unsatisfactory.	Officers whose performance falls below standards and officers separated in the interest of national security.	0-2s or 0-3s whose performance is below expected levels and officers separated for the best interest of the service.	Officers originally appointed to grade 0-3 or above who are unsatisfactory at the end of the first 3 years of service.
How is pay computed?	Years of service, but not more than 12 x 1 month's basic pay.	2 months' basic pay x years of service, not to exceed 2 years' basic pay or \$15,000, whichever is lesser.	Years of eligible service, but not more than 12 x 1 month's basic pay.	2 months' basic pay for each year of service, not to exceed 2 years' basic pay.	6 months' pay and allowances.
Method of payment.	Lump sum.	Lump sum.	Lump sum.	Lump sum.	Lump sum.
Maximum pay allowable.	1 year's basic pay.	2 years' basic pay or \$15,000, whichever is lesser.	1 year's basic pay.	2 years' basic pay.	6 months' pay and allowances.
Limitations.	No severance pay if eligible for retirement.	Severance pay is deducted from the retirement pay of members who qualify for retirement benefits.	No severance pay if eligible for retirement.		

UNIFORMED SERVICES

(3) Reserve Readjustment Pay

	Army/Air Force	Navy/ Marine Corps	Coast Guard	NOAA	Public Health Service
Are all members covered?	Yes. Officers and enlisted.	Same as Army-Air Force	Same as Army-Air Force	No Reserve Readjustment Program	No Reserve Readjustment Program
Who qualifies? (3 groups)	(1) Members involuntarily released from active duty after 5 continuous years of service.	Same as Army-Air Force	Same as Army-Air Force	No Reserve Readjustment Program	No Reserve Readjustment Program
How is pay computed?	Years of service, but not more than 18 x 2 months' basic pay.				
Method of payment.	Lump sum.				
Maximum pay allowable.	2 years' basic pay or \$15,000, whichever is lesser.				
Limitations.	No readjustment pay if member elects to receive another severance pay. If receiving VA compensation, 75% of readjustment pay is deducted from that compensation. If member later becomes eligible for retirement based on 20 years of active service, 75% of readjustment pay is deducted from the retired pay.				
Who qualifies?	(2) OR; members released for unsatisfactory performance after 5 continuous years of service.				
How is pay computed?	1/2 month's basic pay x years of service, but not more than 18.				
Method of payment.	Lump sum.				
Maximum pay allowable.	2 years' basic pay or \$15,000, whichever is lesser.				
Limitations.	Same as limitation under (1).				
Who qualifies?	(3) OR; members released from active duty without their consent before their active service contract expires (contract cancellation).				
How is pay computed?	Unexpired service x 1 month's basic pay, special pay and allowances.				
Method of payment.	Lump sum.				
Maximum pay allowable.	5 months' pay and allowances.				
Limitations.	No readjustment pay if eligible for retired pay or severance pay under another law.				

UNIFORMED SERVICES

(4) Disability Severance Pay

(Regular and Reserve)

	<u>Army/Air Force</u>	<u>Navy/ Marine Corps</u>	<u>Coast Guard</u>	<u>NOAA</u>	<u>Public Health Service</u>
Are all members covered?	Yes. Officers and enlisted.	Same as Army-Air Force	Same as Army Air Force	Same as Army Air Force	Same as Army-Air Force
Who qualifies?	Members qualify for disability severance if (A) they have not completed 20 years or more of active service, (B) their disability is permanent, and (C) the percentage of disability is less than 30 percent (with some qualifications).	Same as Army-Air Force	Same as Army Air Force	Same as Army Air Force	Same as Army-Air Force
How is pay computed?	2 months' basic pay x years of eligible service, but not more than 12.				
Method of payment.	Lump sum.				
Maximum pay allowable.	2 years' basic pay.				
Limitations.	--Disability severance pay is deducted from any compensation for the same disability to which the member becomes entitled from VA. --Members with 20 or more years of service may not receive disability severance pay.				

PROPOSED CHANGES TO THE PRESENT
MILITARY NONDISABILITY SEPARATION SYSTEM

-Voluntary Separations-

	<u>Present System</u>	<u>Interagency Committee</u>	<u>DOD Retirement Study Group</u>	<u>President's Commission on Military Compensation</u>
Minimum service requirement for benefits	N/A	10 years.	10 years.	5 years.
Eligible members	N/A	Officers and enlisted.	Officers and enlisted.	Officers and enlisted.
Benefits	None	Choice between: (1) deferred annuity at age 60 (2-1/2 percent x years of service x basic pay), or (2) lump-sum payment (5 percent x years of service x final annual basic pay).	Deferred annuity at age 60 (2-1/2 percent x years of service x basic pay).	For members who complete 5 years of service, a deferred compensation trust fund would be established. Government contributions would be made according to the following schedule:

<u>Year of service</u>	<u>Percentage basic pay</u>
6 to 10	20
11 to 20	25
21 to 25	15
26 to 30	5

At the completion of 10 years of service, the amount would be vested to the member. On leaving active duty, the balance of the account would be distributed according to one of the following options:
 (1) Leave in account and withdraw at later point.
 (2) Convert to monthly annuity for no less than 2 years.
 (3) Convert to annual payments for no less than 2 years.
 - plus -
 For members with 10 or more years of service, an old-age annuity (patterned after the Federal civil service retirement system) plan would be provided.

PROPOSED CHANGES TO THE PRESENT
MILITARY NONDISABILITY SEPARATION SYSTEM

-Involuntary Separations-

	<u>Present System</u>	<u>Interagency Committee</u>	<u>DOD Retirement Study Group</u>	<u>President's Commission on Military Compensation</u>										
Minimum service requirement for benefits	No minimum requirement for: --Navy and Marine Corps officers failing promotion to grades 0-3 or 0-4. --Army and Air Force officers failing promotion to grades 0-3 through 0-5.	5 years	5 years	5 years										
Eligible members	Officers only.	Officers and enlisted.	Officers and enlisted.	Officers and enlisted										
Benefits	Severance pay for nonpromotion computed at 2 months' basic pay x years of service, not to exceed 12 years or \$15,000, whichever is lesser.	Readjustment pay computed at 5 percent x years of service x final annual basic pay - plus - For members with 10 or more years of service, an equity payment consisting of either (1) a deferred annuity at age 60 based on 2-1/2 percent x years of service x basic pay, or (2) a lump-sum payment equal to 5 percent x years of service x final annual basic pay.	Readjustment pay computed at 5 percent x years of service x final annual basic pay. - plus - An equity payment consisting of either (1) a deferred annuity at age 60 based on 2-1/2 percent x years of service x basic pay, or (2) a lump-sum payment equal to 5 percent x years of service x final annual basic pay.	Severance pay computed at one-quarter of a month of basic pay for each year of service up to 10 years and one-half of a month of basic pay for each year of service from 11 to 30 not to exceed 1 year's basic pay. - plus - For members who complete 5 years of service, the establishment of a deferred compensation trust fund. Government contributions would be made according to the following schedule: <table border="1" style="margin-left: 20px;"> <thead> <tr> <th>Years of service</th> <th>Percentage of basic pay</th> </tr> </thead> <tbody> <tr> <td>6 to 10</td> <td>20</td> </tr> <tr> <td>11 to 20</td> <td>25</td> </tr> <tr> <td>21 to 25</td> <td>15</td> </tr> <tr> <td>26 to 30</td> <td>5</td> </tr> </tbody> </table> At the completion of 10 years of service, the amount would be vested to the member. On leaving active duty, the balance of the account would be distributed according to one of the following options: (1) Leave in account and withdraw at later point. (2) Convert to monthly annuity for no less than 2 years. (3) Convert to annual payments for no less than 2 years. - plus - For members with 10 or more years of service, an old-age annuity (patterned after the Federal civil service retirement system) plan would be provided.	Years of service	Percentage of basic pay	6 to 10	20	11 to 20	25	21 to 25	15	26 to 30	5
Years of service	Percentage of basic pay													
6 to 10	20													
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