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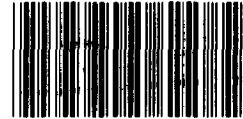
UNITED STATES GENERAL ACCOUNTING OFFICE
WASHINGTON, D.C. 20548

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STATEMENT OF
HARRY S. HAVENS
ASSISTANT COMPTROLLER GENERAL
BEFORE THE
HOUSE POST OFFICE AND CIVIL SERVICE COMMITTEE

ON

BUDGET REDUCTION PROPOSALS AFFECTING
FEDERAL COMPENSATION PROGRAMS



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Mr. Chairman and Members of the Committee:

We are pleased to be here today to provide our views on various proposals being considered which would change Federal compensation programs. Our work has covered several items under consideration including the Federal pay reform plan, cost-of-living adjustments for Federal retirees, and "dual compensation" for Federal employees who serve in the National Guard or Reserve. I will briefly discuss each of these as well as mention some other areas in which our work has shown that cost savings could be accomplished.

FEDERAL PAY REFORM

The Federal Salary Reform Act of 1962 established the principle that salary rates for Federal white collar employees under the General Schedule should be comparable with salaries for the same level of work in private enterprise. The comparability

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principle was adopted to assure equity for the Federal employee with his or her equals throughout the national economy; to enable the Government to compete fairly for qualified personnel; and to provide a factual standard for setting Federal salaries.

Since 1972, we have made a number of studies of the pay comparability processes. Our work has shown that numerous refinements in the processes were needed and, in many cases, our recommendations were adopted. Through this work, we have become convinced that comparability is a sound and equitable policy to follow in establishing Federal pay levels. We can see no better way to assure employees and the taxpayers that compensation levels are sound than to pay Federal employees amounts comparable to what their counterparts outside the Government are receiving.

I believe it is very important in considering the pay reform proposals to recognize the several refinements that have already been made and the significant savings that were achieved. For example, in 1973, a new technique for relating private sector pay rates to General Schedule pay rates was adopted. In 1976, changes were made to the composition of the pay survey, the weighting process, and the development of the payline. And, in 1977, the scope of the pay survey was expanded. These refinements resulted in savings to the Government of about \$3.7 billion a year.

While these refinements have been made, other legislative and administrative actions over the years have actually been

counterproductive to the achievement of pay comparability for Federal employees.

Reducing or delaying annual comparability adjustments, along with salary ceilings for Federal executives, have "saved" the Federal Government at least \$6.9 billion since 1975, but not without a significant accompanying "cost" in morale and basic fairness to Federal employees. In this connection, we believe the routine reduction or denial of pay adjustments for Federal executives is one of the most severe problems impacting on the effective operation of Government programs. In several reports we have cited recruitment and retention problems, creation of an environment in which there is little incentive for top Federal executives to seek positions of greater authority and responsibility, and the retirement of top officials as soon as eligible. We believe the need for meaningful pay adjustments for this group is both clear and compelling.

The Administration's pay reform proposal includes many provisions which we have reported on in the past. Several of these we have supported as appropriate refinements to the comparability principle. Administration estimates for the pay reform bill indicate that about \$3.7 billion in payroll savings could be effected in fiscal year 1982 with greater savings in later years. These estimates assume that the reforms would result in a 4.8 percent raise for the General Schedule this October as compared to 13.5 percent or higher that would be produced by the current system.

While we believe that some of the changes included in the proposal need to be made, we do not believe the proposal, in its entirety, should be enacted at this time.

In a 1975 report, we recommended that a policy which allows for adjusting not only pay but also benefits to achieve total compensation comparability be developed. We continue to support such a concept. However, we believe that certain features of the plan developed by the Office of Personnel Management for implementing a total compensation comparability system need to be modified or substantiated before an accurate total compensation system can be achieved. As we noted in our December 1980 report on developing and implementing a total compensation comparability system for Federal employees, all significant benefits must be included in such a system, assumptions used must be justified, and differences in benefits by major employee groups and by locality must be appropriately considered.

Given these complexities, we believe an evolutionary approach to implementing total compensation comparability may be more appropriate. One possible approach would be to initially implement a total compensation comparability system in which pay and benefits are measured and adjusted separately. In this way, Federal pay would not be directly affected by possibly imprecise benefits comparisons. Under such an approach, changes would not be made to the Federal benefits package unless there were indications that the package was clearly higher or lower than benefits in the non-Federal sector.

We support the bill's provision for a locality pay system for white-collar employees similar to that for blue-collar workers. Salaries for comparable jobs often vary substantially from one geographic area to another. Setting Federal white-collar pay on a locality basis would lessen situations in which the Federal Government overpays in some areas and is unable to effectively recruit and retain employees in others. It would also obviate the need for separate cost-of-living allowances in non-foreign areas.

While details of the locality pay plan have not been finalized, one plan that OPM is considering would survey pay in each of approximately 150 geographic areas; however, under the proposed total compensation comparability system, only a nationwide measurement of benefits would be obtained. Since indications are that private sector benefits can vary significantly from area to area, the use of local pay but national (instead of local) benefits in a total comparability analysis and adjustment could result in serious inequities to Federal employees in some localities and undue enrichment to employees in other areas. We have recommended that OPM analyze local benefits and, if they are found to differ materially by locality, we believe that OPM should be required to take local benefits into account when assessing and adjusting Federal compensation.

We would at this time oppose the pay reform bill's proposal to establish the Federal compensation standard at 94 percent of average non-Federal compensation (including benefits). This

standard was proposed, according to the Administration, to recognize aspects of Federal employment, such as job security, promotion potential, and portability of benefits, which make it more attractive than many comparably-paid jobs in the private sector.

We believe that it is both inequitable and inappropriate to adjust Federal compensation upward or downward without first substantiating that differences do, in fact, exist, attaching a value to each of those differences, and assessing the implications of making such adjustments. OMB officials have told us that there is no way to adequately and analytically assess the value of such factors and that they see the setting of the value as a judgment which should be made by the President with input from the Congress. We cannot accept this rationale as a basis for adjusting Federal compensation. It is inconsistent with the comparability principle. Moreover, even if these factors are legitimate, they would be partially or totally offset by the fact that the process includes a 6-month time lag in determining the needed pay adjustments.

We support the proposed inclusion of State and local governments in the Federal white- and blue-collar pay surveys as an appropriate refinement to the comparability principle. This would broaden the comparability processes to include all major segments of the non-Federal sector. I should point out, however, that no savings in payroll costs have been attributed to this change. It is not known at this time what effect the inclusion of State and local governments would have on Federal pay rates.

The pay reform bill includes changes to certain features of the blue-collar pay system that we fully support and, in fact, have recommended. These features cause Federal blue-collar pay to exceed private sector rates, reducing confidence in the Government's pay-setting policies and increasing outlays for pay and benefits.

In summary, we believe that the comparability principle is sound and the Federal Government should strive to continually improve the process. However, because there are several aspects of the pay reform legislation which we do not believe are ready for implementation or maybe should not be implemented at all, we cannot support full enactment of the legislation at this time.

CHANGES IN THE FEDERAL ANNUITY COST-OF-LIVING ADJUSTMENT

We support the Administration's proposal to provide annual cost-of-living adjustments to Federal retirees instead of the current practice of adjusting annuities biannually. We have advocated this since 1976.

Adopting a policy of annual adjustments would bring the system more in line with practices found in non-Federal retirement programs, social security, and other Federal income security programs.

DUAL PAY FOR RESERVISTS

Present law entitles Federal employees who are on annual active duty for training with the National Guard or military reserve to receive the full amount of both their civil service

and military pay while on active duty status for up to 15 days. It also entitles them to administrative leave, full retirement credit for both military and civil service, and accrual of annual and sick leave during their active duty status.

GAO has generally favored eliminating or amending certain laws which provide dual compensation to Federal employees. Limiting the total compensation of these employees to only their regular salary would save an estimated \$52 million a year. Unless there is some evidence which will show that elimination of this dual compensation will severely affect the recruitment and maintenance of an adequate reserve force, we would favor elimination of this particular practice.

OTHER POSSIBLE COST
SAVING MEASURES

Over the years, our work has shown several areas in which Federal compensation programs need to be changed and savings achieved. Many of the changes we have recommended have been adopted, but other recommendations are still open. I would like to briefly mention some of them.

Recognizing Full Federal
Retirement Costs

Civil service retirement costs are understated because they are calculated on a "static" basis--no consideration is given to the effect of future general pay increases and annuity cost-of-living adjustments on ultimate benefit payments. The static cost of benefits is currently estimated to be 13.73 percent of pay, about equal to contributions made by agencies and employees. The estimated dynamic cost of the system, however--including

factors for pay and annuity cost-of-living increases--is 36.81 percent of pay. On this basis, the cost to the Government for benefits which accrued during FY 1980 was \$15.1 billion--\$11.6 billion more than the \$3.5 billion agencies contributed to the retirement fund.

Funding retirement costs on a dynamic basis would not affect retirement outlays, but it would require increased contributions from off-budget entities whose employees participate in the retirement system and thus increase revenues.

Altering the Indexing Process for Federal Annuities

In addition to this annual adjustment proposal, we believe that Congress should consider adopting a modified policy of less-than-full inflation indexing for annuities. Although the current policy of providing full increases is a laudable objective aimed at lessening the impact of inflation on Federal employees, it is both inequitable to others who are not similarly treated and it is costly. Historically, it has resulted in Federal retirees receiving far greater percentage increases than active Federal employees. This has encouraged--and continues to encourage--valuable, experienced employees, particularly top officials whose pay rates have been depressed, to retire early. In several reports and in appearances before various congressional committees, we have made several alternatives on how less than full indexing could be implemented.

Standardizing Annuity Reductions for Survivor Benefits

Another change to the cost-of-living adjustment provisions would clarify how increases should be applied to annuities for those retirees who elect survivor benefit coverage. Currently, the law does not specify whether cost-of-living adjustments are to be applied to reduced annuities or unreduced annuities. OPM has elected to apply the increases to the reduced annuities. Because of a mathematical anomaly, this results in a higher cost to the Government and creates monetary inequities between prior and new retirees. New retirees always pay more than earlier retirees for the same survivor coverage.

We believe it would be more equitable to recalculate the annuity reduction each time there is a cost-of-living adjustment. This would insure that past and future retirees pay the same amount for the same survivor benefits. Based on a limited sample, we estimated that this change could result in a savings to the Government of at least \$76.8 million annually. We understand that others have estimated it would save as much as \$200 million a year.

Curtailing Special Early Retirement Programs

The normal civil service retirement age is 55, however, there are several provisions for retirement before that age. Certain types of Federal personnel such as law enforcement and fire fighter personnel, are allowed to retire early under the general presumption that their duties need to be performed by a young and vigorous work force.

We have evaluated the reasonableness, effectiveness, and costs of the special early retirement program and concluded that the need for continuing it was questionable. The employees covered by this policy were not retiring significantly earlier and the cost of covered employees' benefits was considerably greater. Over a 30-year period, the average retirement age of covered employees ranged from only 1 to 3 years less than of those not covered. Furthermore, based on actuarial estimates, the early retirement benefits cost is 61 percent more than the cost of regular retirement benefits.

Unnecessary Voluntary Retirements

Another early retirement program allows employees to volunteer to retire early (age 50 with 20 years service or any age with 25 years) if their agency is undergoing a major reduction-in-force, major reorganization, or major transfer of function. The purpose is to reduce involuntary separations, thereby saving the jobs of younger workers who might be separated but would not be eligible for immediate benefits.

This program is very expensive. Our actuaries estimated that early voluntary retirements would cost \$109 million in 1980. We believe the program, with proper controls, can be workable. However, as presently designed and administered, it is resulting in too many unnecessary retirements. Among our concerns are the following: (1) early retirement authorizations are not restrictive enough to insure a high probability of job savings, (2) agencies turn too quickly to the early

retirement program for solutions to staffing problems, and (3) employees can retire early even though none of the agency's employees are being adversely affected.

Panama Canal Retirement Benefits Cost

As a result of the Panama Canal Treaty, employees of the Panama Canal were granted increased retirement benefits with the intent that all increased costs of these benefits would be paid from Canal revenues. OPM is responsible for calculating the cost of these benefits and charging the Panama Canal Commission accordingly. OPM, however, has based its cost calculations using the static basis which we have explained earlier. Pay increases and increased annuity cost-of-living adjustments will add significantly to the ultimate cost of these increased benefits and result in a "subsidy" of more than \$200 million over a 20-year period if OPM continues to use this method. About \$8 million of this amount is applicable to fiscal year 1982.

We recommended that OPM charge the Panama Canal on the basis of a dynamic cost estimate. This will shift the burden of payment to its appropriate source--the Panama Canal Commission.

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That concludes my statement, Mr. Chairman. My colleagues and I would be happy to answer any questions you may have.