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The Honorable William D. Ford
Chairman, Committee on Post Office and
Civil Service
House of Representatives

The Honorable William V. Roth, Jr.
Chairman, Committee on Governmental
Affairs
United States Senate

Subject: Effect Of Requiring New Federal Employees To Be Temporarily Covered By Both Social Security And Civil Service Retirement (GAO/OCG-83-1)

We have analyzed the potential effects of requiring Federal employees hired on or after January 1, 1984, to be temporarily covered by both social security and the civil service retirement system. This situation is the result of the April 1983 social security amendments (Public Law 98-21) which provided social security coverage for all newly hired Federal employees, including former employees who are rehired after a break in service of 1 year or more.

A new retirement system to supplement social security coverage for these employees is not expected to be in place by the January 1, 1984, effective date. Therefore, under current law until the new system is established, the employees must also participate in the civil service retirement system (CSRS) and pay the required employee contributions to both systems.

Most employees in the civil service system must pay 7 percent of their salary into the retirement fund. Members of Congress pay 8 percent, and congressional staff, law enforcement and firefighter personnel pay 7.5 percent. All employees are also required to pay the 1.3-percent medicare tax. Employees hired after January 1, 1984, will also be required to pay social security taxes of 5.4 percent in 1984 and 5.7 percent in 1985. While both social security and medicare taxes currently apply only to the first $35,700 of annual salary, nearly all new employees will receive salaries below this level. Thus, they will be contributing a total of about 14 percent to these programs.

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By contrast, while employees in the private sector must pay social security taxes, few are required to contribute to their employer-sponsored retirement plans. A 1982 survey by the Bureau of Labor Statistics of plans covering 17 million workers showed that 93 percent were in plans fully paid for by their employer.

For purposes of our analysis, we assumed the new supplemental retirement system will retroactively cover all periods of service by new employees subsequent to January 1, 1984. However, it is difficult to speculate at this time on what the new system will provide or how it will be implemented. For example, it might not require any employee contributions other than social security taxes. Presumably, any contributions employees make to the civil service system during the period of temporary coverage that are greater than the amount required by the new system would be refunded. In any event, it is clear that, if, as is anticipated, the new supplemental retirement system is not established until the end of 1985, employees hired after January 1, 1984, will receive little or no benefits from the civil service system for their retirement contributions. Five years of civilian service is required for vesting under the civil service system, and the only benefits available before 5 years is a survivor annuity payable to the spouse and children of an employee who dies after at least 18 months of service.

The Office of Personnel Management (OPM) estimates that 385,000 employees would be affected by the dual contribution requirement by the end of 1985.

The extra contributions to be required of new employees would place the Government at a competitive disadvantage because of the substantial reduction in take-home pay thus adversely affecting recruitment and retention efforts. Officials in the five departments and agencies we visited told us that the higher retirement contributions would make recruiting more difficult particularly in those occupations where the Government pays special salary rates.

In view of the very limited benefits that employees will derive from temporarily contributing to the civil service system and the problems the increased contributions may cause, we evaluated several alternatives to the current law that could alleviate this situation.

OBJECTIVES, SCOPE, AND METHODOLOGY

Our objectives were to identify personnel management and financial impacts resulting from the requirement for new employees to contribute to both retirement systems and evaluate possible alternatives to that requirement.

At OPM, we obtained data on estimated accessions and pay rates. We obtained the views of responsible officials on the effects of higher retirement contributions on recruiting and retention. We also obtained data on recruiting, retention, and special pays at the Veterans Administration (VA), the National Aeronautics and Space Administration (NASA), and the Departments of the Army, the Navy, and the Air Force. These departments and agencies were selected because they are the largest users of special pay due to current recruiting and retention problems. We also obtained views of responsible officials in those agencies on the effects of the higher retirement contributions on recruiting and retention. At the Bureau of Labor Statistics, Department of Labor, we obtained data on private sector pension plans.

To determine financial impacts in fiscal years 1984 and 1985, we estimated the contributions to CSRS for the new employees. We also analyzed social security and CSRS programs to identify potential benefits for these employees during the 2-year period.

This report focuses on CSRS as it covers most Federal employees. However, some Federal employees are covered under other retirement systems, and they will also have to temporarily contribute to social security and their retirement system. These systems include the Foreign Service, the Central Intelligence Agency, the District of Columbia, and the Federal Reserve Board.

FINANCIAL IMPACT

We estimate that contributions to the civil service retirement trust fund for individuals having dual coverage will be as follows:

Fiscal year	Employee contributions	Employing agency contributions	Total
1984	$ 82,040,000	$ 82,040,000	$164,080,000
1985	387,520,000	387,520,000	775,040,000
Total	$469,560,000	$469,560,000	$939,120,000

The above estimates are based on 178,000 accessions in 1984 with a related payroll of $1,172,000,000 and a total of 385,000 accessions at the end of 1985 with a payroll of $5,536,000,000.

Any changes to the contribution requirements would reduce these receipts accordingly.

POTENTIAL CSRS BENEFITS FOR NEW EMPLOYEES

We reviewed the eligibility requirements of CSRS to estimate the potential benefits that could be paid to the affected employees during the 2 years of temporary coverage. We found that most of the 385,000 new or rehired employees will receive no CSRS benefits. Although these employees will have contributed about $470 million to CSRS, OPM estimates that disability or death benefits will be paid in 750 instances. OPM estimates such benefit payments will be $500,000 in 1984 and $2,900,000 in 1985. (As previously indicated, we would assume that any employee contributions to CSRS during the 2-year period that were greater than the contributions eventually required by the new supplemental retirement system would be refunded to the employees.)

None of the newly hired employees would have the necessary 5 years of service to be eligible for civil service disability benefits. However, on the basis of its mortality rate estimates, OPM estimates that, during the 2-year period, civil service death benefits would be paid in about 100 instances to survivors of newly hired employees.

Rehired employees could be eligible for civil service disability benefits and their survivors for death benefits, but the precise number of instances cannot be estimated because data is lacking on their prior Federal service. However, if all rehired employees had 5 years of prior Federal civilian service, OPM estimates that 450 individuals could receive disability benefits and there could be 200 instances of death benefits during the 2-year period.

Prior employment covered by social security and current Federal employment would be considered in determining whether these employees or their survivors were eligible for social security benefits. Lacking data on prior employment, a precise estimate of the number of instances where such benefits would be paid cannot be made.

A comparison of the disability and death benefit eligibility requirements and benefit provisions of these systems is shown in the enclosure.

PROBLEMS IN RECRUITING AND RETAINING QUALIFIED PERSONNEL

The requirement for new employees to contribute to two retirement systems could make it more difficult to recruit and retain qualified individuals for the Federal service, particularly those in special pay categories because the dual contributions will cause a substantial reduction in employees' take-home pay.

The Government over the years has experienced difficulty in recruiting and retaining people in particular occupations because of the difficulty in competing with the private sector. Consequently, the Government has the authority to pay salaries over and above the normal amounts when vacancies occur and when adjustments to salaries are needed to make them competitive with the private sector. These adjusted salaries are referred to as special pay rates. In 1982, agencies were paying about $93 million annually in supplements over and above regular rates to about 34,300 employees.

The following examples of occupations with recruitment and/or retention problems are based upon situations in Federal agencies. In our opinion, they are illustrative of the problems which could result if the requirement for contributions to both systems is not eliminated.

Clerks and secretaries

Clerical and secretarial positions in certain geographic areas are designated for special pay rates. For example, the Air Force in Los Angeles has been paying special rates to individuals in these occupations. The reason for the pay differential, according to the Air Force, is to alleviate the recruiting and turnover problems caused by industry recruiting these individuals at more than the regular Government salary rates. Requiring employees to contribute to two systems could aggravate an already serious turnover problem according to the Air Force.

According to an OPM representative responsible for managing the special pay program as well as several agency officials, it is not unusual for individuals at the lower grade levels to change jobs for as little as a $5 to $10 increase in their paychecks. The contribution to the two retirement systems would cost an additional $22 every payday for individuals at the current GS-3 entry level. And, for entry level GS-5s and GS-7s, the additional cost each payday would be $28 and $34, respectively. Since lower salary differentials than these may influence the decision to leave an existing job, it is likely that reductions of the foregoing magnitude will increase future recruitment and retention problems and possibly cause the payment of special pay rates to even more employees.

Engineers

NASA, the Army, the Navy, and the Air Force all recruit engineers with special pay rates. NASA recruits many engineers while they are still in school under what is known as the co-op program. For example, an individual could attend school for two semesters, then work a semester, repeating the cycle until graduation. According to NASA, this program not only helps instill a sense of loyalty to NASA but helps the co-ops pay for their tuition and books when they return to college. Normally hired at a GS-3 level, the co-ops' contributions to the two retirement systems will be $51 of their $410 biweekly salary (about $29 to civil service retirement and $22 to social security). The potential effect on NASA's permanent engineering staff is illustrated by the following. At any one time, NASA has about 1,000 co-ops of whom about 60 percent continue through graduation and become permanent employees. If the program were to suffer, NASA would have to be more successful in its recruiting of engineering graduates. However, one reason NASA relies on this program is its need to supplement its recruiting of engineering school graduates. NASA questions the likelihood of as many quality individuals applying for the co-op program in light of this retirement contribution, particularly in an improving economy.

The Army Corps of Engineers also anticipates that the double contribution for a retirement program will have an adverse effect on recruiting of new graduates who, in the past, have already found Federal employees' benefits to be less attractive than those offered by many private organizations.

Physicians

VA has had a difficult time recruiting enough physicians to fill its needs. To help meet its demand, VA pays physicians an amount over and above their basic salary. For example, physicians hired by VA can be paid a basic salary of $50,000 and a supplement of $25,000. The entire $75,000 is a special salary rate and is included in the employee's salary base for civil service retirement purposes. Consequently, the contribution to both systems will be about $7,200 -- about $2,000 more than the amount paid by employees hired before January 1, 1984. According to VA, this will likely make it more difficult to recruit and retain new physicians.

ALTERNATIVES TO DUAL CONTRIBUTIONS

We evaluated several alternatives which would alleviate adverse impacts on recruiting and retention which could result from the requirement for greater retirement contributions.

These alternatives were:

1. Provide a temporary tax credit to Federal employees covered by the social security system for the amount of their contribution to the CSRS.

2. Provide no CSRS coverage; therefore, no contributions to CSRS would be required.

3. Provide temporary CSRS coverage without requiring employee contributions but with a 100-percent social security offset against any civil service benefits received.

4. Voluntary temporary participation in CSRS by new employees.

Under each of these alternatives, employees' service credits would be transferred to the new supplemental system when it is established.

The alternatives are discussed in more detail below along with the advantages and disadvantages of each one.

Tax credit

One way to alleviate the impact of greater retirement contributions would be to provide the new employees an income tax credit for their CSRS contributions during the 2-year period. Bills have been introduced in the House of Representatives (H.R. 3371) and the Senate (S. 1522) to permit such credits. However, timing of the tax credit could be a disadvantage, inasmuch as the employees may not benefit from the credit until the following year when they file their tax returns.

This alternative would continue full employee and employer contributions to the civil service trust fund. Employees would have greater disability and death benefits than those hired prior to 1984 because of the dual coverage but would have contributed less. Since the proposed bills do not change the refund provisions of CSRS, employees could receive not only the tax credit but also a refund of their contributions if they later left Government service.

No CSRS coverage

Under this alternative, the social security program would provide disability and survivor benefit coverage for new employees but, depending on individual circumstances, benefits could be greater or less than CSRS benefits. No employee or employer contributions to CSRS would be required.

This alternative avoids any duplicated benefits and the potential administrative burden of refunding employee contributions if a noncontributory supplemental plan is later established or the contribution rate under the new plan is lower.

Recruiting may be more difficult than under other alternatives because of the uncertainty about the level of future retirement benefits. Also, this alternative would generally provide less disability and death benefits, especially for rehired employees who might otherwise qualify for civil service benefits because of prior Federal service but who may not have sufficient service to qualify for social security benefits.

Social security offset

This alternative would provide employees coverage under both systems, but civil service benefits would be reduced by the amount of any benefits received from social security. While employee contributions to CSRS would not be required, agencies would continue to make CSRS contributions which would be used to finance CSRS benefits for these employees.

The alternative assures disability and death benefit coverage comparable to coverage provided employees hired before 1984 but creates some administrative burden in computing the social security offset. It does, however, avoid the potential administrative burden of refunding employee contributions if a noncontributory supplemental plan is later established or the contribution rate under the new plan is lower.

Voluntary participation

While all new employees would have social security coverage, this alternative would permit those employees who desired greater coverage to participate in CSRS. Participating employees and their agencies would each be required to contribute 7 percent of pay to CSRS.

This alternative would give participating employees more coverage than that provided employees hired prior to 1984.

While it would give the individual the responsibility for determining the adequacy of coverage, it would be very costly for the limited additional coverage most employees would receive.

CONCLUSION

Although current law requires all new employees as of January 1, 1984, to contribute to dual retirement systems, it seems likely that only a very small number of those employees would receive any benefits from the civil service system before the supplemental system is established. This being the case, requiring them to temporarily contribute to both systems appears to be an inequity. The dual contribution will reduce employees' take-home pay if the situation is not remedied by the Congress. We believe the Federal Government could experience difficulties in recruiting and/or retaining quality individuals particularly in those occupations where the individuals receive special pay rates because the Government has difficulty in competing with private industry. In some cases, special pay rates might have to be increased or paid to even more employees if the dual contribution requirement is not changed.

Resolution of this problem prior to January 1, 1984, would relieve new employees from the burden of contributing to both social security and the CSRS.

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Copies of this report are being sent to the Director, Office of Management and Budget; Director, OPM; and other interested parties.

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Enclosure

COMPARISON OF ELIGIBILITY REQUIREMENTS AND DISABILITY AND SURVIVOR BENEFITS

Civil service	Social security
Disability benefits	
Employees must have completed 5 years of creditable civilian service and, because of a disease or injury, cannot provide useful and efficient service in positions at their current grade in the same agency and commuting area.	An individual must be unable to engage in any substantial gainful activity by reason of any physical or mental impairment which can be expected to result in death or last more than 12 months. The individual also must have at least 20 quarters of coverage in the last 40 quarters unless disabled prior to age 31, in which case, fewer quarters are required.
Benefit is equal to the larger of amounts derived from the general retirement benefit formula or a guaranteed minimum which is generally 40 percent of the high-3 year average pay.	Benefit is equal to the worker's basic benefit computed as though the worker had attained age 62.
Death benefits	
The deceased employee must have completed 18 months of creditable civilian service.	The deceased employee must have at least 6 quarters of coverage during the last 13 quarters.
Spouse's benefit is equal to 55 percent of the deceased employee's earned annuity or a guaranteed minimum. Generally, the minimum would be 55 percent of 40 percent of high-3 year average pay. A children's benefit is also payable.	If spouse is caring for an eligible child, the spouse's benefit is generally equal to 75 percent of the deceased employee's basic benefit. The child is also entitled to the same benefit as the spouse. Also a lump-sum benefit of $255 is payable.