FEDERAL BENEFITS: ARE WE MEETING EXPECTATIONS?

HEARING

BEFORE THE

SUBCOMMITTEE ON FEDERAL WORKFORCE, POSTAL SERVICE, AND THE DISTRICT OF COLUMBIA

OF THE

COMMITTEE ON OVERSIGHT AND GOVERNMENT REFORM

HOUSE OF REPRESENTATIVES

ONE HUNDRED TENTH CONGRESS

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FEDERAL BENEFITS: ARE WE MEETING EXPECTATIONS?

THURSDAY, AUGUST 2, 2007

HOUSE OF REPRESENTATIVES,
SUBCOMMITTEE ON FEDERAL WORKFORCE, POSTAL SERVICE, AND THE DISTRICT OF COLUMBIA,
COMMITTEE ON OVERSIGHT AND GOVERNMENT REFORM,
Washington, DC.

The subcommittee met, pursuant to notice, at 2:15 p.m. in room 2154, Rayburn House Office Building, Hon. Danny K. Davis (chairman of the subcommittee) presiding.

Present: Representatives Davis of Illinois, Norton, Lynch, and Marchant.

Staff present: Tania Shand, staff director; Caleb Gilchrist, professional staff member; Lori Hayman, counsel; Cecelia Morton, clerk; Ashley Buxton, intern; Mason Alinger, minority deputy legislative director; and Alex Cooper, minority professional staff member.

Mr. DAVIS OF ILLINOIS. The subcommittee will come to order.

Welcome Ranking Member Marchant, members of the subcommittee, hearing witnesses, and all of those in attendance. Welcome to the Subcommittee on the Federal Workforce, Postal Service, and the District of Columbia hearing entitled, "Federal Benefits: Are We Meeting Expectations?"

Hearing no objection, the Chair, ranking member, and subcommittee members will each have 5 minutes to make opening statements, and all Members will have 3 days to submit statements for the record.

We will begin. I expect that our other very distinguished witness will be here momentarily, but we will begin.

Welcome Ranking Member Marchant, members of the subcommittee, hearing witnesses, and all those in attendance. Much like the Federal pay hearing the subcommittee held on Tuesday, today's hearing will get an overview of insurance and retirement benefits available to Federal workers. Future hearings will focus on the existing benefits programs discussed today. However, the Federal Government must keep current in the types of benefits it offers employees, if it is to attract and maintain a quality work force.

The Federal Government's life and health insurance programs were created in the mid-1950's and the early 1960's. The mid-1980's brought us a new retirement system called FERS, and the late 1990's, early 2000's, ushered in paid organ donor leave, long-term care and dental/vision insurance. In some cases the Government shares benefit costs; in others, the employee pays all.

While we examine the administration and operation of existing programs, we must begin discussions on future benefit options for our Federal employees.

Today I will be circulating a draft legislative proposal to Federal employee stakeholders that would provide 8 weeks of paid leave for the birth or adoption of a child and 4 weeks of paid leave for elder care or the serious health condition of a spouse or child. The proposal will also increase the age from 22 to 25 that young adults can receive health insurance benefits under the FEHBP.

I look forward to working with the Office of Personnel Management and employee groups over the recess so this cradle to independence legislation can be introduced in the fall.

On March 14th I introduced H.R. 1518 to allow employees of federally qualified health centers to obtain health coverage under the Federal Employees Health Benefits Program. It is my hope that this legislation draws attention to the fact that health centers across this country are finding it more and more difficult to provide affordable health insurance to their own employees.

I understand that Representatives Tom Davis and Jim Moran have legislative proposals of their own that would benefit Federal employees. I look forward to hearing their recommendations and the recommendations of OPM and the employee groups on how to improve the Federal Government's benefits programs.

[The prepared statement of Hon. Danny K. Davis follows:]

ONE HUNDRED TENTH CONGRESS

Congress of the United States

House of Representatives

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STATEMENT OF CHAIRMAN DANNY K. DAVIS
AT THE
SUBCOMMITTEE ON FEDERAL WORKFORCE, POSTAL SERVICE,
AND THE DISTRICT OF COLUMBIA
HEARING ON
FEDERAL BENEFITS

August 2, 2007

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Thank you.

Mr. DAVIS OF ILLINOIS. I now yield to the ranking member, Mr. Marchant, for his opening statement.

Mr. MARCHANT. Thank you, Mr. Chairman. Thanks for convening this second hearing on the status of the Federal employees pay and benefits.

Earlier this week the subcommittee learned about the Federal Government's basic pay setting policies, as well as its various policies and practices regarding locality pay, cost of living adjustments, and other compensation and incentives.

Today the subcommittee will hear from personnel experts about the Federal employee health and retirement benefits. As I mentioned at Tuesday's hearings, there is a tremendous amount of turnover in the Federal work force today, and these hearings will help the subcommittee get a better sense of what changes, if any, need to be made to the current system.

As we discuss the status of the Federal employees pension and health care, I believe we also must be mindful of the financial impact that changes to Federal employee benefits could have on the Federal budget. I trust the experts will keep this perspective in mind as we discuss any potential changes to improve health and retirement benefits of Federal employees.

I look forward to hearing from all the witnesses today.

Thank you, Mr. Chairman.

Mr. DAVIS OF ILLINOIS. Thank you very much, Mr. Marchant.

Delegate Norton, do you have a statement?

Ms. NORTON. Only a brief statement, Mr. Chairman, which has to begin with gratitude for you for holding these comprehensive hearings on pay, last week on benefits, employee and retirement benefits this week. I don't remember the last time, frankly, that we have had comprehensive hearings on our employee and retirement benefits, and yet what you are doing today could not be more timely.

You say the expectations, are we meeting expectations, we would have to ask of whom. The expectation of employees who, after all, most of whom could retire today? By they way, most of whom could get top dollar in the private sector. Or do we mean new people? Do we mean people coming out of college? Do we mean expectations of people who the private sector is fighting tooth and nail to get?

There is a difference between what is expected of us today and what was expected when I was a kid growing up in this town and a Government job was considered a good job. It was considered a good job in no small part because its benefits were superior to the benefits of the private sector at that time to make up for lower pay. Well, the private sector is still, for many of the employees of the kind who are now employed today, and certainly of the kinds of workers we need to attract, private sector is still a better deal. It is a better deal for wages, it is a better deal for health care, and it is a better deal for benefits.

We have had hearings in prior years, even when we were in the minority, about the shock waves going through the Government with the retirement of the Baby Boom. We had this artificial windfall of some of the most talented people in the United States who chose to come to Government, that came to Government in part because of the era in which they grew up. This was the era of the great movements, the era of Government service. But also because there were so many of them that there were enough of them to go around. But they produced fewer children, Mr. Chairman, and there are not enough to go around now, not if you mean go around to the private sector, which every day of the week is trying to get the best of them to come while we, frankly, are doing too little to get those same workers to come.

Finally, Mr. Chairman, if I may say so, you and I and a number of us on this side have cosponsored a bill for years now just to raise the retirement benefits from 75 percent of what the employee pays to 80 percent, and we have not gotten to first base on that. Meanwhile, the other side spent all the money on tax cuts for the rich and on invading another country, and one wonders if we will get there in time.

If you were to ask me the single most important thing we could do to catch up, I think I would focus on health benefits, because that is where most Americans feel most dubious today. Health benefits go up so quickly compared to compensation in private and public compensation.

On the other hand, Mr. Chairman, for competitive reasons, alone, we need to take an across-the-board serious understanding that we don't have the kinds of funds that we should have, that should be available to us, but looking across the board at what we will have to do just to be a competitive employer in the 21st century, and looking at benefits, it is a very good place to start.

Thank you very much, Mr. Chairman.

Mr. DAVIS OF ILLINOIS. Thank you very much, Delegate Norton. Mr. Lynch.

Mr. LYNCH. Thank you, Mr. Chairman.

I want to associate myself with your opening statement, your remarks, and simply add that our ability to attract dedicated and highly capable employees really will depend on—obviously, we can't compete with the private sector in terms of dollar-for-dollar on salary. While we deal with many of the same subjects here in the Congress and many of our regulatory agencies deal with the same subject matters—technology, biotech, the FDA, different agencies in Government—where on the regulatory side it still requires us to have highly intelligent folks who are willing to work for this Government.

It is frustrating at times when you see how much progress industry has made, especially over the last 50 years, things that we never even dreamed about, and yet basically the Government's side of things is basically the same. We have lost the powdered wigs. That is about it. But we are still operating on a 19th century model.

We have to be able to attract bright, competent, innovative people to help us with the regulatory side of Government, and we need to be able to attract the best and brightest employees who are dedicated.

I think the way we can close the gap in some respects, given the fact that we can't compete on a wage basis or a salary basis, is the benefits that we might be able to employ and to give to our employees. We could be a kinder, gentler Government to our workers and encourage them and appreciate them. That is the way we will bring people onboard, because I think there really is a goodness in the American people to serve their Government. I see it at the VA every day. They are not making as much money, the nurses, the therapists, the docs over at the VA, but they take their reward in large part from the good that they are doing for our servicemen.

You can go across every single agency in our Government and see people doing the same thing, and we need to reward that. I think this is a great hearing, it is a great way to address the inequity sometimes of some of our Federal employees. I am not surprised, Mr. Chairman, that you are the one to bring this to the committee, and I appreciate your doing so.

I yield back the balance of my time.

Mr. DAVIS OF ILLINOIS. Thank you very much, Mr. Lynch.

We will now proceed to our first panel of witnesses and our distinguished colleague will be the first witness, the Honorable James Moran, who was elected to his ninth term in the U.S. House of Representatives after a distinguished career of local public policy decisionmaking. He was elected to the House of Representatives to his ninth term in 2006. He is a member of the Appropriations Committee, where he serves on the Defense and Interior Subcommittee, and one of the outstanding leaders in the House of Representatives, Representative Moran.

STATEMENT OF HON. JAMES MORAN, A REPRESENTATIVE IN CONGRESS FROM THE COMMONWEALTH OF VIRGINIA

Mr. MORAN. Thank you very much for your kind words, Chairman Davis. It is a pleasure to appear before you, ranking member and Congressman Lynch. My good friend, I really appreciate your holding this hearing on the retirement benefits available to Federal employees.

I am proud to represent more than 40,000 Virginians who serve our country as Federal civil servants, as well as 60,000 Federal retirees in my District. Protecting the strength and the integrity of the Federal work force and the quality of life of all beneficiaries is obviously an appropriate priority.

During the past several years we have worked with the Office of Personnel Management, who is well represented here by its Director, Linda Springer. She has been very helpful with us. I want to thank her, as well as the labor organizations who are also represented here today, representing millions of Federal employees and retirees. NARFEA is represented, as well.

What we are doing is introducing legislation that will fix an inequity in the current annuity computations within the Federal retirement system.

About a decade ago Congress amended the Civil Service Retirement System for workers with part-time service. Some part-time employees were switching to full-time work for their last 3 years in order to receive their high three annual average salaries. By doing so, they received the same amount of retirement annuity as those who worked their entire career full time, so they were gaming the retirement system by switching to full time only at the very end of their careers. That forced the Congress to create the current methodology for determining part-time retirement benefits.

Today a part-time salary is assigned by its full-time equivalent salary, and then the benefit is pro-rated by the proportion of a full-time career that a part-time employee actually works. The new law is intended to allow an employee to receive a high three salary during the period of part-time service, therefore encouraging part-time service at the end of a career. This often happens when a senior level workers cuts back on his or her hours. The disproportionate share of these workers appears to be women who leave the Federal service to care for others in their family.

Unfortunately, there are two major problems with the implementation of this new law. First, the law didn't specify that the calculation of full-time equivalent salary would apply to all part-time service before and after the implementation of the law. The result of this omission is the retirement benefits are calculated in two parts: one part based on retirement law for pre-1986 work, and another part based on retirement law for post-1986 work.

It also has another adverse consequence. As a result of these two different annuity calculations, there is a financial disincentive for Federal employees to take part-time work at the end of their careers. Retirement annuity calculations are sometimes hundreds of dollars less because employees have taken part-time work during the late stages of their career, which is a problem for us because we are trying to keep these very experienced people who may not want to work full time but they will lend their expertise, particularly transitioning to younger employees for various responsibilities.

Now, the subcommittee's members' heads are probably spinning over this, because it is difficult to grasp how these annuity calculations occur, but you can imagine what it is like for a retiree. They are told that there are two different calculations. How much did you work pre-1986, post-1986? How much was part-time? How much was full-time? It is an overly complex formula that has led to some serious computational errors.

Federal retirees, though, are starting to get the picture: part-time work hurts your retirement. So my legislation will restore full credit for part-time work for 1986 and clarify how the full-time equivalent pay is to be applied. It will provide a simplified annuity computation in cases involving part-time service for all CSRS employees. In doing so, this proposal will effectively eliminate the adverse effect of part-time service performed late in an employee's career.

This change of the law can help stem the wave of retirement the Federal Government faces imminently. It has been well documented and this subcommittee knows all too well that over the next decade, as the Baby Boom generation nears retirement age, the OPM has shown us that we are going to have a crisis of manpower. Approximately 60 percent of the Government's 1.6 million white collar employees and 90 percent of its Federal executives will be eligible for retirement over the next decade. Since a leading factor that influences the retention of senior personnel is a worker's retirement package, I am optimistic that fixing this part-time inequity can provide some help to address this impending worker shortage.

Over the past several sessions of Congress we have submitted this proposal to change the recommend calculation of not only future retirees but for current retirees that may have suffered a reduction in pension benefits as a result of part-time work.

We would have preferred that the legislation that may ultimately gain favor in this subcommittee contain a retroactive component for the current retirees, but I recognize that such a provision would weaken the bill's chances of success. Applying the annuity calculation retroactively could significantly exacerbate the depth that the CSRS retirement fund already faces. Ultimately, that debt will be passed on to the Federal Employees Retirement System [FERS], as the last CSRS employees retire. At some point Congress is going to have to then either increase taxes or limit benefits.

So, as important as it is to right the inequity of the current part-time calculation, we don't want to add to the burdens of the next generation.

Now, I understand that dropping the retroactive provision may lose some support from the Federal retirees that are experiencing this retirement inequity, but I do think that the only way that this legislation moves forward is with bipartisan cooperation and coordination. The changes that we have offered as an amendment reflect this effort. A perfect bill should not be the downfall of a good one.

Mr. Chairman and ranking member and Ms. Norton and Mr. Lynch, I want to thank you for the opportunity to be heard.

In orchestrating this hearing, I want to thank Ms. Tania Shand, who has reached out to our office. She has ensured that our questions and concerns are answered in a very professional and timely manner.

I do think this proposal will correct a longstanding obstacle to part-time service and help agencies retain qualified Federal employees nearing retirement, so I do ask for your support. It is important. This legislation could affect up to 600,000 current Federal employees, 30 percent of the Federal work force. Now, of course, that figure decreases over time as CSRS employees move over to FERS. It will cost about $18 million over a 5-year period, but it doesn't require any additional appropriations. The funds come to the CSRS financial count through an intergovernmental transfer. Of course, FERS is not impacted.

Now, I am more than happy to answer any questions, but I do think it is important to create this parity between FERS and CSRS.

Mr. Chairman, that concludes my statement.

[The prepared statement of Hon. James P. Moran follows:]

Subcommittee Hearing
Federal Workforce, Postal Service, and the District of Columbia
Written Statement of James P. Moran
August 2, 2007

Introduction

Chairman Davis and Ranking Member Marchant, I want to thank you and the other Members of the Subcommittee for holding this hearing today on the retirement benefits offered to federal employees. I am proud to represent more than 98,000 Virginians who have served our country within the ranks of the federal civil service. Protecting the quality of life of these beneficiaries and ensuring the future strength of the federal retirement system are two of the most important issues to my district. In doing my best to represent these interests, it is imperative that I remain steadfast to maintain the integrity, quality and vitality of the federal workforce. I know that these are interests that the Subcommittee shares.

During the past several years, I have worked with both the Office of Personnel Management (OPM) and labor organizations representing millions of federal employees and retirees to introduce legislation that will fix an inequity in the current retirement system that may affect thousands of future retirees. I believe my proposal will help support the federal government's ability to retain current employees in the face of the oncoming wave of retirement that will hit the federal workforce in less than a decade. H.R. 2780, a fix to the calculation of retirement benefits, is a result of a collective effort, and I look forward to working with this Subcommittee to offer the best policy prescription possible as the federal workforce confronts the challenges of this new century.

State of the Federal Workforce

It has been well documented that over the next ten years, the federal workforce will undergo significant demographic changes that threaten the federal government's strength and effectiveness. As the baby-boom generation, which makes up a disproportionately large part of the overall workforce, nears retirement age, federal agencies will face a crisis in manpower, especially within its senior executives and management ranks. Information from OPM shows that approximately "60 percent of the government's 1.6 million white-collar employees and 90 percent of about 6,000 Federal executives will be eligible for retirement over the next ten years."

This likely wave of retirement threatens to drain the federal workforce of its most experienced and talented employees at a pace that will be difficult to replace with a well-qualified, trained workforce. Congress, in coordination with the Executive Branch, must develop an overall strategy with specific policy solutions so that the potential "brain drain" doesn't threaten the efficient delivery of government services.

One leading factors that influences the retention of senior personnel is the retirement package offered by the federal government. As currently structured, the federal retirement system for some workers actually penalizes employees that wish to extend their careers by working part-time. As the federal workforce faces the prospect of losing an unprecedented number of employees over the next 10 years, many of the anticipated shortages can be met with part-time employees. The obstacle that these potential part-time employees face is the negative impact of part-time employment on their federal pensions.

H.R. 2780 – Part-Time Employment Retirement Computation

I have introduced H.R. 2780 to address the annuity computations of federal employees retiring under the Civil Servant Retirement System (CSRS). I believe that this legislation can serve the dual purpose of correcting a longstanding inequity for retiring federal employees, as well as offering employees nearing retirement the option for continued part-time service without negatively impacting their retirement benefits.

Over 10 years ago, the 100th Congress included a provision in the Consolidated Omnibus Budget Reconciliation Act (COBRA) of 1986 (P.L. 99-272) that amended the civil service retirement law for federal workers with part-time service. Section 15204 prevented part-time employees from being credited with the same number of years of service as those who worked full-time over the same period. Before the law's passage, an individual who had worked part-time for most of his or her career could switch to full-time work the last three years of his or her career and receive the same retirement benefits as someone who worked full-time throughout the same period.

As the Subcommittee knows, federal annuities are calculated by multiplying the average three highest continuous years of salary, times years of service, by an accrual rate. The new methodology determines the proportion of a full-time career that a part-time employee works and scales annuities accordingly. Under the formula, a part-time salary is calculated on a full-time equivalent basis (FTE) for retirement purposes. Thus, a worker's "high-three salary" could occur during a period of part-time service. This often happens when a senior-level worker cuts back on his or her hours. The disproportionate share of these workers appears to be women, who leave the federal service to care for others.

The problem with the new formula is that it has negative consequences for workers hired before 1986. First, it fails to provide the accrued full year of credit for each year of part-time service of workers who, before 1986, had completed part-time service for which they had understood they would receive full-time credit. Second, the formula can have a negative impact on retirees' annuity if the computation of the "high-three salary" occurs during part-time service. Specifically, the formula incorrectly minimizes full-time employment before 1986, which hurts agencies' ability to retain experienced federal workers by offering part-time employment. Finally, this complex formula can lead to computational errors involving annuities with part-time service. There are possibly thousands of civil servants who are eligible under CSRS that may be impacted by the inequity in this law.

My legislative proposal will restore full credit for part-time work performed before 1986, eliminate the adverse effect of part-time service performed late in an employee's career, and provide a simplified annuity computation in cases involving part-time service. Though it is important to eliminate the inequity for future retirees, it is perhaps more important to tear down the artificial barrier to part-time service at the end of an employee's career.

For the past several sessions of Congress, I have submitted this proposal to change the retirement calculation for not only future retirees, but also for current retirees that suffered a reduction in pension benefits as a result of part-time work. One of the main reasons that I introduced legislation years ago was because of federal retirees informing me of this problem.

While I would have strongly preferred that the legislation that may ultimately gain favor in this Subcommittee contain a retroactive component for the current retirees, I understand and recognize that such a provision could weaken the bill's chances of success. There are two concerns that the Subcommittee and OPM have brought to my attention. First, applying the annuity calculation to current retirees would exacerbate the debt that the CSRS retirement fund already faces. Ultimately this debt will be passed on to the Federal Employee Retirement System (FERS) as the last CSRS employees retire, and at some point Congress will either have to increase FERS taxes or limit benefits. Though it is important to right the inequity of the current part-time calculation, I do not wish to add to the burdens of the next generation.

Second, I have been informed that retroactively recalculating federal annuities would set a new precedent within the federal retirement system. I am not adverse to changing precedent, but I understand the reluctance of the Subcommittee to make such changes in light of the difficult financial times facing CSRS and the pressures of our looming national debt.

The Subcommittee and OPM's concerns are legitimate, and I respect their perspective. I understand that dropping the retroactive provision of my proposal may lose me some support of the federal retirees that are experiencing this retirement inequity, but I believe that the only way that this legislation moves forward is with bipartisan cooperation and coordination. I believe that the changes that I have offered in the attached amendment reflect this effort. Ultimately, a perfect bill must not be the downfall of a good one.

Conclusion

Mr. Chairman and Mr. Ranking Member, I want to thank you for this opportunity to be heard. In orchestrating this hearing, the Subcommittee's staff has been tremendously helpful. I would like to particularly thank Ms. Tania Shand, who has been supportive in reaching out to my office and ensuring that our questions and concerns were answered in a professional and timely manner.

I believe that this proposal will correct a long-standing obstacle to part-time service and may help agencies retain qualified federal employees nearing retirement for part-time service. I ask for your support in moving this bill through the Committee on Oversight and Government Reform, and through the House of Representatives.

I look forward to your questions, and I thank you.

Mr. DAVIS OF ILLINOIS. Thank you, Representative Moran.

Let me just ask you, What has been the general reaction, both inside the Congress as well as among the employee groups, to your proposal?

Mr. MORAN. They are very supportive of this proposal because the CSRS retiree that take part-time service at the end of their careers are potentially losing hundreds of dollars per month because of this part-time inequity. You know, over time it is a big deal. It really affects their quality of life, and so there is very strong support among all those organizations and individuals representative of the Federal work force and its retirees.

Mr. DAVIS OF ILLINOIS. Thank you very much.

Let me ask Mr. Marchant if he has questions.

Mr. MARCHANT. Thank you.

The retirees that will be affected by the new plan there will be certain people that have already retired that this will affect their check?

Mr. MORAN. Yes.

Mr. MARCHANT. Is it a large number?

Mr. MORAN. No, not really. We are not going retroactively back to——

Mr. MARCHANT. So everybody would be held harmless that has already retired that is getting their——

Mr. MORAN. That is my understanding. I expect Keith Bumgardner, who has done my staff work here for me, to tell me if I say anything wrong.

Mr. MARCHANT. And, as far as the way it works now just functionally, the last 3 years, is it the amount of time that you work the day? Is it half time? Three-quarter time? Or is it the amount of pay that sets the limit?

Mr. MORAN. It had been the amount of pay, and that is why people were switching who had worked part time throughout their careers, switching to full time for the last 3 years, and then getting as much as people who had worked full time their entire career.

Mr. MARCHANT. Yes.

Mr. MORAN. That is why the Congress fixed it. But then they had two different calculations, and it actually penalized people who went to part time. So we are trying to make it more consistent now, and we have a proportionate calculation now that makes it fair and does it the same way they do it in the other retirement system. Basically, we achieve parity between the two retirement systems.

Mr. MARCHANT. Thank you.

Mr. DAVIS OF ILLINOIS. Mr. Lynch.

Mr. LYNCH. Thank you, Mr. Chairman.

Congressman Moran, I appreciate your bringing this forward. I certainly am supportive of the measure. I realize you have made some compromises here in your own legislation, and I think that is courageous.

I do want to say that, from my own experience, even on my own staff, trying to keep people on part time long enough to train the new employees is critical. My office manager in Boston just retired recently, and I begged her to stay. She worked part time for quite a while training the new people coming in the door, and she had a wealth of experience, having been with Congressman Moakley for about 25 years. I cried when she left, because she was just terrific in bringing in the new people and teaching them the professional standards.

That is happening all across Government. I think your bill, by putting real value on the service, the part-time service of these employees, very experienced, very expertise, at the end of their careers will not only allow them to transition slowly into retirement, but also will benefit us greatly in training new employees.

I am with you on the bill. You might have to explain to me again some of the calculations here at another time. I won't do that on the chairman's time. But I appreciate your good work on this and I yield back the balance of my time.

Mr. MORAN. Thank you so much, Mr. Lynch.

Mr. DAVIS OF ILLINOIS. Thank you, Mr. Lynch, and thank you, Representative Moran for coming.

Mr. MORAN. Thank you, Mr. Chairman.

Mr. DAVIS OF ILLINOIS. We appreciate your testimony.

Mr. MORAN. Thank you.

Mr. DAVIS OF ILLINOIS. I know that Mr. Davis was not able to get here. Without objection, we will enter his statement into the record and he will have opportunity to amplify on it should he desire.

[The prepared statement of Hon. Tom Davis follows:]

Statement of
Ranking Member Tom Davis
House Committee on Government Reform

before the

Subcommittee on the Federal Workforce, Postal Service, and the District of Columbia

August 2, 2007

Good afternoon, Chairman Davis and Members of the Subcommittee, and thank you for holding this hearing today. Given the federal government's active efforts to recruit and retain new federal employees, combined with the pending wave of retirements facing the federal workforce, this is an opportune time for Congress to evaluate the current system of federal health and retirement benefits in order to determine whether the current mix is sufficient to meet employee needs.

I am here today to testify about two legislative proposals I believe would help the federal government recruit and retain the best and the brightest employees our nation has to offer.

The first bill I would like to discuss is H.R. 1110, legislation commonly referred to as "premium conversion." I have sponsored this legislation since the 107th Congress and it has always enjoyed broad bipartisan support, collecting 340 cosponsors last Congress. I re-introduced this legislation in February, and it is currently pending before this Subcommittee.

H.R. 1110 has widespread support for good reason. It would end a discrepancy that exists between active duty federal employees and federal retirees. Under current law, federal employees are allowed to pay for their healthcare costs using pre-tax dollars. When those employees retire, however, those same employees are suddenly forced to begin paying for those same health care expenses using after-tax dollars.

Health care costs in the Federal Employees Health Benefits Program have gone up by over 9 percent a year since 1999. H.R. 1110 would alleviate these increases by saving retirees nearly $800 annually. Here in Washington that might not seem like a lot of money over the course of a year, but to those on a fixed income, it can make a huge difference.

The federal government has a long history of treating our active employees and retirees the same – providing them equal access to health care, for example. Why shouldn't retirees have the same ability to pay their premiums with pre-tax dollars? And why shouldn't our military personnel be able to do the same under their Tricare programs?

This Committee approved this legislation unanimously last Congress and I look forward to working with the Subcommittee Chair this year to make sure this important legislation advances once again. Perhaps this year it won't die once again in the Ways and Means Committee.

The second piece of legislation I would like to discuss is not pending before this Subcommittee, but considering the impact it could have on our ability to recruit and retain new federal employees, I would like to bring it to your attention. The legislation is H.R. 2363, introduced by

Rep. Tim Bishop and myself, entitled the Generating Opportunity by Forgiving Educational Debt for Service Act of 2007, better known as GOFEDS.

GOFEDS seeks to attract and retain employees who have recently completed undergraduate or graduate-level education by allowing them to exclude their student loan repayments from gross income.

The challenges we face – from homeland security to pandemic health crises to energy supplies – will require a committed and talented human capital pool. But more and more, young Americans are opting for employment in the private and non-profit sectors, leaving the federal government hard-pressed to attract the right people to the right jobs.

In a recent report on the need to build expertise in the federal workforce to protect the nation from bioterrorism, the Partnership for Public Service pointed out that bio-defense agencies are finding it increasingly difficult to hire employees with the required scientific and medical expertise. The overall demand for bio-defense talent will continue to rise for the foreseeable future – by as much as 25 percent through 2010 – while the supply of such talent will decline unless we act.

The GOFEDS Act would improve the effectiveness of the existing loan repayment program as a recruitment tool and in turn improve federal programs. While current law allows federal agencies to repay student loans on behalf of employees, up to $10,000 a year with a $60,000 cap, the incentive is taxed. Nonprofits and educational institutions offer loan repayments which, in contrast, are not counted as taxable income for the recipient. H.R. 2263 simply puts the federal government on par with nonprofits by excluding loan repayment from the employees' taxable income.

I look forward to working with this Subcommittee and other interested Members of Congress on these important initiatives so that we can better meet the federal government's workforce challenges, which are so critical to the success of the federal government's core missions, today and in the future.

Again thank you for holding this hearing, Mr. Chairman. I would be happy to answer any questions you might have.

Mr. DAVIS OF ILLINOIS. We will now proceed to our second panel: The Honorable Linda Springer, the Honorable Patrick McFarland, and Mr. Gregory Long.

I will proceed with the introduction of our witnesses.

The Honorable Linda Springer is the eighth Director of the U.S. Office of Personnel Management. She was unanimously confirmed by the U.S. Senate in June 2005. As OPM Director, Ms. Springer is responsible for the Federal Government's human resource planning benefit programs, services, and policies for the 1.8 million employee civilian work force worldwide. We thank you again, Ms. Springer.

The Honorable Patrick McFarland has been the Inspector General of the Office of Personnel Management since August 1990. He provides leadership that is independent, nonpartisan, and objective in the pursuit of waste, fraud, and abuse, and mismanagement in programs administered by the OPM. Welcome, Mr. McFarland.

Mr. Gregory Long is the Director of the Federal Retirement Thrift Investment Board. Before joining the TSP, Mr. Long spent 7 years with CityStreet, where he served as Director of Marketing for the American Bar Association Retirement Funds. In that position, he oversaw all marketing, sales, and product development activities for a program that provides 401(k) services to over 4,000 law firms nationwide. Thank you very much, Mr. Long. We appreciate your coming.

It is the custom of this committee that all witnesses be sworn.

[Witnesses sworn.]

Mr. DAVIS OF ILLINOIS. The record will show that the witnesses answered in the affirmative.

We thank you all for coming and we will begin, Ms. Springer, with you.

STATEMENTS OF LINDA SPRINGER, DIRECTOR, OFFICE OF PERSONNEL MANAGEMENT; PATRICK MCFARLAND, INSPECTOR GENERAL, OFFICE OF PERSONNEL MANAGEMENT, ACCOMPANIED BY TIMOTHY WATKINS, OFFICE OF THE OFFICE OF THE INSPECTOR GENERAL, DEPARTMENT OF HEALTH AND HUMAN SERVICES; JILL HENDERSON, OFFICE OF PERSONNEL MANAGEMENT GROUP CHIEF OVERSEEING AUDITS OF PHARMACY BENEFIT MANAGERS; AMY PARKER, OFFICE OF THE INSPECTOR GENERAL SPECIAL AGENT ON MEDCO INVESTIGATION; AND GREGORY LONG, EXECUTIVE DIRECTOR, FEDERAL RETIREMENT THRIFT INVESTMENT BOARD

STATEMENT OF LINDA SPRINGER

Ms. SPRINGER. Thank you, Mr. Chairman. Good afternoon to you and members of the subcommittee. Thank you for inviting me back again for the second time this week to discuss, in this case, Federal employee benefits.

The Federal Government has long been recognized as a leader in employee-sponsored benefits, and that helps us to maintain a competitive advantage, both when we are recruiting and retaining top talent to work for our country.

The Office of Personnel Management has primary responsibility with respect to these programs, and, with respect to your topic today, we can report that, based on the most recent Federal Human Capital Survey, we are largely meeting expectations with respect to benefits. In a variety of categories, ratings have increased, ratings of employee satisfaction.

This has been recognized in the private sector, as well. The Gallup Organization has done surveys as recently as last fall that indicate that one of the attractors of the work force to Federal employment is our benefit programs.

Just to put the size of these in perspective, let me comment that we run the world's largest single employer-sponsored health insurance program. We run a retirement system that has nearly three-quarters of a trillion dollars in assets. And we have paid out benefits from our major programs totaling about $92 billion, over $91 billion just in 1 year. So these are major, major programs.

The description of our activities with respect to each of these programs is in my written statement, so I will just touch on a few highlights and then spend more time with our legislative initiatives.

With respect to retirement, as you have heard, the SERS plan is the older of the two plans. There are about 650,000 employees covered by SERS, and over 2 million covered by the FERS plan. With the impending retirement wave, it is important that OPM be able to service all of these retirees and new retirees with the most accuracy and timeliness as we can so, as you know, we have been working on a retirement systems modernization project that will transform our processing from a paper-based system that relies on 150,000 file drawers of paper records that could start in this room and end to end go all the way up I–95 to Baltimore and come back to this room again. So converting from that type of system to a cutting-edge, state-of-the-art system will help to ensure that we can give Federal employees the type of service they deserve when it comes to their retirement.

We are on target to roll that out in February 2008, and we appreciate the support, particularly of this subcommittee, as we move forward in that effort.

Our life insurance program, again, the Nation's largest group life insurance program, covers over 4 million Federal employees and many of their family members. In fiscal year 2006, approximately 90,000 claims were paid under our life insurance program, and $2.3 billion dispersed.

Health insurance benefits—the Federal program, again, the largest single employer-sponsored health insurance program in the world. We have over 284 plan choices from approximately 130 private sector plans. We negotiate with each of those programs and provide those plan choices across the country. They feature the full range of options—HMOs, high deductible plans, fee-for-service plans. Those choices and that commitment to choice is a hallmark of the Federal program.

One of the very, very important features is the fact that employees are able to carry that coverage into retirement, and, unlike many of their counterparts in the private sector, they retain the full subsidy. That is something we look at. We look at competitors. I can tell you that the private sector has backed off in many cases from maintaining that subsidy level from the employer into retirement, but we have continued that, so, in effect, we have improved our position by continuing it, whereas other employers have backed away from it.

We have done a good job, we believe, in maintaining premium rates. For this year that we are in, 2007, those rates only went up by 1.8 percent, the lowest increase in 11 years. We saw, over the past 5 years, rate increases that were lower than the average for the industry. There are some who would say that is because we released reserves. The level of reserves is determined by the insurers, and they are the ones that came to us. In effect, that represented an overpayment by employees, and so it is entirely fair to give that back in the way of a smaller premium increase.

We are doing a lot in the way of making medical records accessible to the advanced health information technology that will allow for better care. We have also worked to have our carriers, our health plans, provide information about quality of the providers, as well as cost, through Web sites, and that is something we are continuing to do.

In 2006 we published new regulations to allow OPM's Office of the Inspector General the right to audit provider contracts, including prescription benefits management companies. I know you are going to be hearing a report from Inspector General McFarland about their success, which has been substantial. That helps us to maintain a rate of over 99 percent accuracy in the payment of the Federal health plan benefit payments. We appreciate the work of the Inspector General.

Our Federal long-term care program was authorized in 2000 by the Congress, and we, again, have the largest group insurance program of its type in the country.

Last year, as you know, we added dental and vision. We currently have 400,000 enrollments in the dental program and more than 300,000 in vision. Those enrollments are indicative of the interest people have in maintaining good care before bad things happen. By those regular checkups, they are able to forestall things that otherwise might progress to a more serious stage, so it is very important to have participation.

The one area that I believe we have a shortcoming in our health program is short-term disability. People today in our programs have to cobble together a combination of sick leave, other paid leave, and donated leave to support times when they are too sick or hurt to work for longer periods of time. That includes maternity.

I know there is a great deal of interest by Members in dealing with this and addressing it, and that is something that we all share. What the right answer for that is is something we look forward to working with you on, but we acknowledge and believe candidly that it is something that needs to be dealt with because it is an important area. And programs exist. There is no need to have to cobble something together.

Our legislative proposal, our most important one that I will highlight is the part-time reemployment proposal. I am happy to hear Mr. Lynch mention the experience he had with retaining the services of a very valued employee. This proposal, along with the one that we have successfully worked on with Congressman Moran, would allow us to address the need for part-time service of our employees. In this case, the one you heard was about keeping people before they retire. In this case this would allow us to bring back annuitants without a penalty to them so that they could work, be paid for their work, still get their annuity—which, by the way, is not double dipping. It is two different streams of service—but would allow us to have their services to train new employees. That is valued service, as Mr. Lynch has indicated.

So that is our major one. There are other improvements that we have suggested and that I would be happy to answer any questions on.

Thank you, Mr. Chairman.

[The prepared statement of Ms. Springer follows:]

Statement of
The Honorable Linda M. Springer
Director
U.S. Office of Personnel Management

before the

Subcommittee on Federal Workforce, Postal Service,
and the District of Columbia

on

"Federal Benefits: Are We Meeting Expectations?"

August 2, 2007

Good afternoon, Mr. Chairman and Members of the Subcommittee.

Thank you for inviting me today to discuss Federal employee benefits. The Federal Government has long been a recognized leader in employer-sponsored benefits, which helps to make sure we have a competitive advantage in recruiting and retaining top talent to work for our country. The U.S. Office of Personnel Management (OPM) has primary responsibility with respect to these benefit programs, a responsibility we take very seriously. With respect to your hearing topic today, the results of OPM's recent Federal Benefits Survey indicate that we are largely meeting expectations with respect to our benefit programs. In fact, the 2006 survey shows that employee satisfaction with regards to benefits has increased since 2004. Ratings increased on average by 3 percent on importance, 4 percent on meeting employee/family needs, 5 percent on value, and 7 percent on competitiveness. The Thrift Savings Plan (TSP), retirement annuity, retirement health benefits, and employee health benefits consistently receive high ratings in all of these dimensions. While we are pleased with these results, we know we need to continue our efforts to make sure we offer a full range of benefits that effectively meet the needs of all of our employees and retirees and their families. This is critical if we are to maintain an effective Federal civilian workforce, and it is the primary reason the Administration has put forth new legislative proposals for your subcommittee's consideration during this current session of Congress.

Retirement

The Federal Government's benefit programs started with the Civil Service Retirement System (CSRS) in 1920. CSRS is a defined benefit plan which still covers about three out of ten active Federal employees. In 1983, Congress enacted a three-tier system to better meet the needs of today's workplace. This program consists of a defined benefit tier (the Federal Employees' Retirement System, or FERS), a defined contribution tier (the TSP, the Federal Government's 401(k) equivalent), and Social Security.

There are about 650,000 employees covered by CSRS, and over 2 million under FERS. The Civil Service Retirement and Disability Fund, from which both CSRS and FERS benefits are paid, has approximately $700 billion in assets. Last year, over $57 billion was paid to retirees and survivors. CSRS benefits were paid to almost 1.6 million retirees and over 600,000 survivors. And FERS benefits were being paid to about 230,000 retirees and over 22,000 survivors.

In administering these systems, we work closely with other agencies that are involved in benefit administration. We have a particularly close relationship with the Federal Retirement Thrift Investment Board. Although the Thrift Board is an independent entity, our formal and informal cooperation with them on matters of both policy and operations helps to ensure that we both are able to fulfill our interdependent obligations.

As you know, we are also currently working on our Retirement Systems Modernization (RSM) project. This is our strategic initiative to better serve our customers by transforming our retirement processing from a paper-based system to an automated electronic system, which will help ensure retiring Federal employees get their correct annuity payments in a timely manner. I would like to take this opportunity to express our appreciation for the support the House, and specifically this subcommittee, has demonstrated with respect to RSM. We believe this project is now well-positioned to be rolled out to agencies beginning in February, 2008.

Insurance

Beginning in 1954 with Federal Employees' Group Life Insurance (FEGLI), and in 1960 with the Federal Employees Health Benefits Program (FEHBP), we offer a broad array of insurance and related benefits.

Life Insurance

The FEGLI program is the Nation's largest group life insurance program, covering over 4 million Federal employees and retirees, and many of their family members. OPM contracts with the Office of Federal Employees' Group Life Insurance (OFEGLI), which is a private entity that processes and pays claims under the FEGLI Program. FEGLI provides group term life insurance which includes basic life insurance coverage and three optional choices. In most cases, new Federal employees are automatically covered by basic life insurance. The cost of basic insurance is shared between enrollees and the Federal Government. While age does not affect the cost of basic insurance, the enrollee pays the full cost of optional insurance, and age does affect its cost.

In FY 2006, approximately 90,000 claims were paid and $2.3 billion disbursed in FEGLI benefits. Our goal is to maintain program stability and continue to ensure OFEGLI provides excellent customer service.

Health Benefits

The Federal Employees Health Benefits Program (FEHBP) is the largest employer-sponsored health insurance program in the world. OPM administers the program by contracting with private sector health plans, and this program structure allows us to offer quality healthcare choices at an affordable price. This year, FEHBP offers 284 plan choices including national fee-for-service plans, HMOs, High Deductible Health Plans and Consumer-Driven Health Plans. Retirees are also able to carry coverage into retirement at the same level and with the same premium paid as employees, unlike their counterparts in the private sector.

We emphasize flexibility and consumer choice as very important features of a competitive health benefits program. We have been able to negotiate a comprehensive level of benefits while keeping premium rates down. Premiums for 2007 increased by an average of only 1.8 percent. Approximately 63 percent of enrollees saw no increase in their premiums, with another 15 percent seeing an increase of less than 5 percent. In the past five years, rate increases have been lower than the industry average, with the last three years being remarkably lower.

The Medicare Modernization Act of 2003 allowed a subsidy for employers who elect to continue providing prescription drug coverage to their retirees. The potential use of the subsidy was evaluated by the Federal Government, and it was determined there was no good rationale for the Federal Government to pay itself to continue providing prescription drug coverage to Federal retirees, especially since OPM has no plans to discontinue this coverage. The law does not require employers to apply for the subsidy, not does it require those who receive the subsidy to use it to offset future premiums. The fact is the subsidy could be used by employers for other business purposes or even to increase a company's bottom line.

OPM is also playing a key leadership role in fulfilling the President's vision of making medical records easily accessible to consumers through the adoption of advanced health information technologies. We have also taken a lead in promoting healthcare price and quality transparency to help patients better control their medical expenses. Last year we worked with FEHBP carriers to post the costs of some common medical procedures on their websites so consumers could view them in making their health plan choices. Over 30 FEHBP carriers were selected for their best practices in price transparency. Many more carriers subsequently made price and quality transparency information available to their members on their websites. Federal enrollees can now find information on healthcare transparency information prominently posted on our website, as well.

And transparency goes beyond price and quality. In 2006, we published new regulations to allow OPM's Inspector General's office the right to audit provider contracts, including Prescription Benefits Management companies. We believe this has helped our FEHBP carriers in their negotiations for the best possible contract terms and prices as well as allowed for greater oversight of those organizations now responsible for managing almost one quarter of the total benefits paid under the Program through their contracts with FEHBP carriers.

Federal Long Term Care Insurance Program

In 2000, the Long-Term Care Security Act authorized OPM to offer a voluntary long term care insurance program to Federal employees and retirees. OPM contracted with Long Term Care Partners, LLC (a jointly held subsidiary of John Hancock and MetLife) to administer the Federal Long Term Care Insurance Program (FLTCIP) program. Through negotiations, OPM has used its buying power to get very competitive premiums and coverage which we believe to be among the most comprehensive available. Enrollment has increase to over 215,000 to make the program the largest group insurance program of its type in the country.

The initial contract will reach the end of its seven-year term in 2008. The Act required us to issue a letter to Congress with our recommendation on whether the program should be continued. In June, we sent our recommendation to Congress that the program be continued. We look forward to reviewing the Congressional response to our recommendation. As we move forward we will look to improve contract terms by September 2008 and seek contemporary and innovative ways to manage future benefits and rate stability.

Flexible Spending Account Program (FSAFEDS)

Since 2003, the Federal Government has offered FSAFEDS which is the Flexible Spending Account (FSA) program for Federal employees. The program is offered under section 125 of the Internal Revenue Code, the same arrangement that governs analogous private sector plans. It is a voluntary program which allows employees to use pre-tax funds to pay for a wide range of common, out-of-pocket health and dependent care expenses. OPM contracts with SHPS, one of the largest FSA administrators in the country, to serve as the program administrator. OPM provides oversight of many aspects of the program, including customer service issues, program management and contract performance.

Current enrollment includes more than 200,000 in health care accounts and more than 30,000 enrollments in dependent care accounts. We are working to promote the advantages of this program to all Federal employees and to promote dependent care accounts, especially to lower income employees. And, we are assessing the SHPS contract terms and performance to determine if there are ways to improve the program beyond what it is today.

Federal Employees Dental and Vision Insurance Program (FEDVIP)

The latest addition to our insurance offerings is dental and vision benefits coverage. The Federal Employees Dental and Vision Insurance Program (FEDVIP) became effective in December 2006 as a voluntary, enrollee-pay-all supplemental dental and vision benefits program for Federal employees and retirees.

OPM has contracted with seven dental carriers and three vision benefit plans. Now in its first year of operation, enrollment in the program far exceeded pre-operational projections. There are currently more than 400,000 enrollments in the dental program and more than 300,000 enrollments in the vision program. As we move forward, we will be using our purchasing power to keep premiums down and allow the FEDVIP to remain an attractive supplemental benefit for Federal employees and retirees.

Short Term Disability Insurance

There is one additional benefit program, short term disability insurance, that we are now considering. That proposal would be designed to close the gap for employees who may have short-term disability needs, such as maternity leave, but are unable to do more than patch together various forms of annual, sick, advance, or donated leave to fulfill those needs, as the current Federal benefits package requires.

The Part-Time Reemployment proposal

You have heard me on any number of prior occasions make reference to the retirement tsunami, and it is essential that we make preparation for the changes we are facing in our workforce. Toward that end, earlier this year, I submitted to Speaker Pelosi a legislative proposal which would authorize Federal agencies to reemploy retired Federal employees on a limited basis without offset of annuity from salary. While they would receive both salary and annuity payments, they would not be considered employees for the purposes of retirement, would earn no additional retirement benefits based on the service, and would have all insurance premiums paid from their annuity payments. They may be reemployed under temporary appointments on either a part-time or full-time basis to meet agency needs. The proposal is carefully drafted to make such reemployment both attractive to annuitants and easy for agencies to use, and to avoid possibilities for significant abuses.

The Retirement Improvements Act

I would also ask that you take action on another legislative proposal submitted to Speaker Pelosi earlier this year, the "Federal Retirement Improvements Act of 2007". The draft bill would 1) endorse the long-standing policy that states that receipt of military retired pay bars civilian retirement service credit for all military service; 2) improve the provisions for computing CSRS annuities involving part-time service; 3) clarify the use of service as a cadet at a U.S. military academy for civilian retirement purposes; and 4) authorize Federal employees to invest bonuses in the Thrift Savings Plan.

While the third aspect of the proposal dealing with service credit for U.S. military academy service is being considered in connection with the FY2008 Defense Authorization bill, each of the elements of the proposal would be useful. I am particularly concerned that the delay in enacting the provisions dealing with computing CSRS annuities involving part-time service will result in the permanent loss of CSRS employees who would wish to continue their career on a part-time basis, but who are unwilling to do so because of the double reduction in their annuity if they do. This anomaly needs to be eliminated.

FEHB Improvements

For the FEHB Program, the Administration has proposed legislation to allow the Service Benefit Plan (BCBS) and Indemnity Benefit Plan to offer more than two levels of benefits since current law does not permit it. This would effectively allow these plans to offer a high deductible health plan. We are also seeking an expansion of our contracting authority to allow us to contract directly with other types of health plans such as regional PPOs, and high deductible health plans.

Conclusion

We are proud of the package of benefits we offer to Federal employees, and of the manner in which we administer them. We believe that they represent an appropriate package that has proved to be influential in both the recruitment and retention of an effective workforce. Nevertheless, I strongly urge that action be quickly taken on the proposals we have submitted to you.

In conclusion, Mr. Chairman, thank you for inviting me back today to continue our discussions on issues important to our Federal workforce and their families. I will be glad to answer any questions you or other Members of the subcommittee may have.

Mr. DAVIS OF ILLINOIS. Thank you very much for that, Ms. Springer.

Mr. McFarland.

STATEMENT OF PATRICK MCFARLAND

Mr. MCFARLAND. Mr. Chairman, members of the subcommittee, thank you for the opportunity to appear before you today to discuss OPM's Office of the Inspector General audit and investigative efforts in helping to safeguard the benefits of the Federal Government employees and retirees in waste, fraud, and abuse.

If I may, immediately behind me is Timothy Watkins. We partnered with HHS OIG in developing the corporate integrity agreement that I will talk about. To your right, Jill Henderson is the organization's group chief who oversees the audits of the PBMs. And Amy Parker is a special agent on the Medco investigation.

The U.S. Office of Personnel Management administers benefits from its trust funds for all Federal employees and retirees participating in the Civil Service Retirement System and Federal Employees Retirement System, Federal Employees Health Benefits Program, and the Federal Employees Group Life Insurance Program. These programs cover over 8 million current and retired Federal civilian employees, including eligible family members, and disperse approximately $91 billion annually from the program trust funds.

The majority of our auditing and enforcement activities are spent in protecting these trust funds, particularly the Federal Employees Health Benefits Program. Since fiscal year 1997, these activities have produced over $306 million in judicially ordered recoveries, and over $1 billion in recommended recoveries through our audits of the participating FEHBP health plans.

Today I want to inform you of one of our recently concluded investigations. We participated in an 8-year investigation of Medco Health Solutions, Inc., Medco, the largest pharmacy benefit manager in the United States. This was a joint investigation with the U.S. Attorney's Office for the Eastern District of Pennsylvania, as well as the Offices of Inspector General at the Department of Health and Human Services and the Department of Defense.

The investigation was initiated after a former Medco employee filed a qui tam lawsuit alleging that Medco defrauded the FEHBP and other health programs. At that time, Medco contracted with the FEHBP to provide mail order prescription drugs to Federal employees, retirees, and their eligible family members insured under the Blue Cross/Blue Shield Association Federal employees program and other FEHBP plans.

The joint investigation concluded that Medco falsely reported their turn-around work performance agreement under the FEHBP carrier contracts. They dispensed prescriptions without properly performing drug utilization reviews that protect the patient. They falsified paper or electronic records relating to the dispensing process. They improperly used pharmacy technicians and other non-pharmacist personnel to perform functions which legally must be performed by a pharmacist or under a pharmacist's direct supervision. They billed the Government for prescriptions that were never filled or ordered. They mailed prescriptions to patients with less than the number of pills prescribed but charged for the full amount.

They made false statements to patients that their mail order prescriptions had not been received when, in fact, the prescription had been received and then canceled in order to appear to meet contractually required turn-around times. They favored Merck drugs over the other manufacturer's drugs in switching programs, even when the Merck drugs were more expensive. And they made false statements to the United States during the investigation of Medco's illegal conduct.

During the investigation, Medco and the U.S. Government agreed to a permanent injunction against several practices. This consent decree, which did not resolve the issue of restitution and monetary damages, was entered into in April 2004. In October 2006, the Federal Government and Medco entered into a settlement agreement to resolve alleged false claims acts violations totaling $155 million. Of this amount, $137 million related directly to the FEHBP. The remainder involved other Federal programs, including Medicare.

As a result of the settlement, the FEHBP trust fund received $97 million in restitution. In addition, $40 million in multiple damages associated with the false claims were returned to the U.S. Treasury. This amount represents the largest single recovery by our office.

Because of the growing importance of drug benefits to the health of FEHBP enrollees and the financial integrity of the trust fund, we pursued additional oversight. Due to the substantial impact Medco and other PBMs could have on the FEHBP, we partnered with the HHS OIG in having Medco sign a corporate integrity agreement, referred to as a CIA. The HHS OIG, with our assistance, is monitoring the corporate integrity agreement with Medco. We felt this was the best and most efficient way to protect the FEHBP, in part because the outstanding program the HHS OIG has developed to implement and monitor corporate integrity agreements.

This is not the first PBM that our office has investigated for allegedly defrauding the FEHBP. Our office, in coordination with the HHS OIG and the U.S. Attorney's Office for the Eastern District of Pennsylvania, conducted a 6-year joint investigation of the PBM AdvancePCS that administered prescription drug benefits for some of the FEHBP plans and Medicare plus choice organizations. This case was resolved in September 2005 with a civil settlement in which AdvancePCS paid $137 million to the Federal Government. Of this amount, $54 million was returned to the FEHBP trust funds.

Mr. Chairman, this statement described a detail of two of our longest and most-complex health care fraud cases that not only affected the health and well-being of Federal employees, retirees, and their families, but also allowed the FEHBP to recover $151 million. We continue to investigate a great number of complex FEHBP health care fraud cases and involve billions of dollars.

The efforts of our investigators and auditors are critical in preventing waste, fraud, and abuse within OPM programs. For example, results of our past PBM audits have highlighted that much remains to be done to improve oversight and controls regarding PBMs participating in the FEHBP. In this regard, we are working with OPM to identify methods to ensure that the FEHBP derives the safest and best possible pharmaceutical services at a fair price.

We feel very strongly that our rigorous, ongoing oversight of organizations participating in the FEHBP provides a sentinel effect that helps reduce erroneous and fraudulent payments in the $32 billion a year Federal health program.

A special note is the positive and cooperative relationship between our office and OPM leadership in pursuit of trust fund integrity.

I would be glad to answer any questions that you have.

[The prepared statement of Mr. McFarland follows:]

Statement of the Honorable
Patrick E. McFarland
Inspector General
U.S. Office of Personnel Management

before the

Subcommittee on Federal Workforce, Postal Service,
and the District of Columbia

on

"Federal Benefits: Are We Meeting Expectations?"

August 2, 2007

Good afternoon, Mr. Chairman and Members of the Subcommittee. Thank you for the opportunity to appear before you today to discuss OPM's Office of the Inspector General's audit and investigative efforts in helping to safeguard the benefits of Federal Government employees and retirees from waste, fraud, and abuse.

The U.S. Office of Personnel Management administers benefits from its trust funds for all Federal employees and retirees participating in the Civil Service Retirement System, the Federal Employees Retirement System, the Federal Employees Health Benefits Program, and the Federal Employees Group Life Insurance Program.

These programs cover over eight million current and retired federal civilian employees, including eligible family members, and disburse approximately $91 billion annually from the program trust funds. The majority of our auditing and enforcement activities are spent in protecting these trust funds, particularly the Federal Employees Health Benefits Program (FEHBP). Since fiscal year 1997, these activities have produced over $306 million in judicially ordered recoveries and over $1 billion in recommended recoveries through our audits of the participating FEHBP health plans.

Today, I want to inform you of one of our recently concluded investigations. We participated in an eight-year investigation of Medco Health Solutions, Inc. (Medco), the largest pharmacy benefit manager (PBM) in the United States. This was a joint investigation with the U.S. Attorney's Office for the Eastern District of Pennsylvania, as well as the Offices of Inspector General at the Department of Health and Human Services (HHS OIG) and the Department of Defense.

The investigation was initiated after a former Medco employee filed a *qui tam* law suit alleging that Medco defrauded the FEHBP and other health programs. At that time Medco contracted with the FEHBP to provide mail order prescription drug benefits to Federal employees, retirees, and their eligible family members insured under the

BlueCross BlueShield Association's Federal Employees Program (FEP) and other FEHBP plans.

The joint investigation concluded that Medco:

- falsely reported their turnaround work performance agreement under the FEHBP carrier contracts;
- dispensed prescriptions without properly performing drug utilization reviews that protect the patient;
- falsified paper or electronic records relating to the dispensing process;
- improperly used pharmacy technicians and other non-pharmacist personnel to perform functions which legally must be performed by a pharmacist or under a pharmacist's direct supervision;
- billed the government for prescriptions that were never filled or ordered;
- mailed prescriptions to patients with less than the number of pills prescribed, but charged for the full amount;
- made false statements to patients that their mail order prescriptions had not been received, when in fact the prescription had been received and then cancelled in order to appear to meet contractually required turnaround times;
- favored Merck drugs over the other manufacturer's drugs in switching programs, even when the Merck drugs were more expensive; and,
- made false statements to the United States during the investigation of Medco's illegal conduct.

During the investigation, Medco and the United States Government agreed to a permanent injunction against several practices. This consent decree, which did not resolve the issue of restitution and monetary damages, was entered into on April 26, 2004.

Medco Consent Decree

Medco agreed to implement the following practices:

- Disclose to prescribers and patients the minimum or actual cost savings for health plans and the difference in co-payments made by patients;
- Disclose to prescribers and patients Medco's financial incentives for certain drug switches;

- Disclose to prescribers material differences in side effects between prescribed drugs and proposed drugs;

- Reimburse patients for out-of-pocket costs for drug switch-related health care costs and notify patients and prescribers that such reimbursement is available;

- Obtain express, verifiable authorization from the prescriber for all drug switches;

- Inform patients that they may decline the drug switch and receive the initially prescribed drug;

- Monitor the effects of drug switches on the health of patients; and,

- Adopt the American Pharmacists Association code of ethics and principles of practice for pharmaceutical care for employees at its mail order and call centers.

In October 2006, the Federal Government and Medco entered into a settlement agreement, to resolve alleged False Claims Act violations totaling $155 million. Of this amount, $137.5 million related directly to the FEHBP. The remainder involved other federal programs, including Medicare. As a result of the settlement, the FEHBP trust fund received $97 million in restitution. In addition, $40.5 million in multiple damages associated with the false claims were returned to the U.S. Treasury. This amount represents the largest single recovery by our office.

Because of the growing importance of drug benefits to the health of FEHBP enrollees and the financial integrity of the trust fund, we pursued additional oversight. Due to the substantial impact Medco and other PBMs could have on the FEHBP, we partnered with the HHS OIG in having Medco sign a corporate integrity agreement. The HHS OIG, with our assistance, is monitoring the corporate integrity agreement with Medco. We felt this was the best and most efficient way to protect the FEHBP, in part because of the outstanding program the HHS OIG has developed to implement and monitor corporate integrity agreements.

Medco Corporate Integrity Agreement

The terms of the agreement require Medco to:

- Hire a compliance officer/appoint a compliance committee;

- Develop written standards and policies;

- Implement a comprehensive employee training program;

- Review claims submitted to federal health care programs;

- Establish a confidential disclosure program;

- Restrict employment of persons found ineligible to participate in Federal programs; and,

- Submit detailed reports to the Offices of the Inspector General at OPM and HHS, as a means of assisting them in monitoring its compliance with the corporate integrity agreement.

This is not the first PBM that our office has investigated for allegedly defrauding the FEHBP. Our office, in coordination with the HHS OIG and the U.S. Attorney's Office for the Eastern District of Pennsylvania, conducted a six-year joint investigation of the PBM AdvancePCS that administered prescription drug benefits for some FEHBP plans and Medicare Plus Choice organizations. This case was resolved in September 2005 with a civil settlement in which AdvancePCS paid $137.5 million to the Federal Government, $54.6 million of this amount was returned to the FEHBP trust fund.

The AdvancePCS civil settlement resolved False Claims Act and Public Contract Anti-Kickback Act violations arising from:

- Reimbursements and rebates by pharmaceutical manufacturers to AdvancePCS as improper rewards for favorable treatment of the manufacturers' drugs in AdvancePCS' contracts with the FEHBP and Medicare; and,

- Payments made by AdvancePCS to health insurance plans that contracted with federally-funded health care plans to ensure that it was selected or retained as the PBM for the plans.

AdvancePCS also agreed to a consent order that required them, for the five years following the settlement, to provide significant information to its client health plans, plan participants, doctors and pharmacists regarding its business practices. AdvancePCS was also required to disclose to health plans information about the payments it receives from pharmaceutical manufacturers that are in addition to rebates. Further, AdvancePCS agreed that it will not engage in drug switching that results in the health plan or plan participant paying more for a drug than the cost of the drug that the doctor originally prescribed.

Mr. Chairman this statement described in detail two of our longest and most complex health care fraud cases that not only affected the health and well being of Federal employees, retirees, and their families, but also allowed the FEHBP to recover $151.6 million. We continue to investigate a great number of complex FEHBP health care fraud cases and involve billions of dollars.

The efforts of our investigators and auditors are critical in preventing waste, fraud and abuse within OPM programs. For example, results of our past PBM audits have highlighted that much remains to be done to improve oversight and controls regarding

PBMs participating in the FEHBP. In this regard, we are working with OPM to identify methods to ensure that the FEHBP derives the safest and best possible pharmaceutical services at a fair price.

In addition, we intend to conduct more frequent audits of PBMs. For example, we will be on-site at Medco next month to begin compliance audits covering Medco's contracts with several participating FEHBP carriers. Our future audit activity will also involve detailed analysis of the 2008 FEP Pharmacy contracts recently awarded by the BlueCross BlueShield Association. Of critical importance is developing an understanding of the pricing models of both contracts and preparing a corresponding audit plan.

To further enhance our audit effort, we have begun to work with Medco to receive routine downloads of prescription drug claims data. This effort will eventually be expanded to other PBMs that participate in the FEHBP. With this information we will be able to verify contract charges, quickly determine potential program exposure in prescription drug related fraud cases and ultimately, develop analytical techniques to identify erroneous payments and potential fraud.

We feel very strongly that our rigorous, ongoing oversight of organizations participating in the FEHBP provides a sentinel effect that helps reduce erroneous and fraudulent payments in this $32.5 billion a year Federal health program. A special note is the positive and cooperative relationship between our office and OPM leadership in pursuit of trust fund integrity.

I would be glad to answer any questions you or the other Subcommittee Members may have regarding my statement.

Mr. DAVIS OF ILLINOIS. Thank you very much, Mr. McFarland. Mr. Long.

STATEMENT OF GREGORY LONG

Mr. LONG. Good afternoon, Chairman Davis, members of the subcommittee. My name is Greg Long. I am the executive director of the Federal Retirement Thrift Investment Board, and I am also the managing fiduciary of the Thrift Savings Plan. I welcome this opportunity to summarize my statement.

The TSP is a voluntary savings and investment plan that allows Federal and Postal employees and members of the Uniformed Services to accumulate savings for their retirement. It currently has approximately 3.8 million individual accounts, and the Thrift Savings Fund has now grown to over $224 billion in assets.

Participants may invest in any or all five of the core investment funds and the five lifecycle funds. TSP administrative expenses are borne by the participants, not the taxpayers.

The FERS participation rate stands at 85.8 percent. For CSRS employees it is about 69 percent. For the Uniformed Services, after only 5 years of availability, now stands at 25.6 percent.

The TSP is administered by the Federal Retirement Thrift Investment Board, which was established as an independent Federal agency. There are approximately 70 employees of that agency. With input from the executive director, the statutory Employee Thrift Advisory Council, Board staff, the five board members establish the policies under which the TSP operates.

First, it provides that all moneys in the Thrift Savings Fund are held in trust. The executive director and the board members are required to act prudently and solely in the interest of TSP participants and their beneficiaries. This fiduciary responsibility gives the board members and the agency a unique status within Government.

FERSA also requires the Secretary of Labor to establish a program of fiduciary compliance audits, and it mandates that the Board contract with the private accounting firm to conduct an annual audit, and it also authorizes the 15 member Employee Thrift Advisory Council. The Council includes representatives of the major Federal and Postal unions, other employee organizations, and the Uniformed Services.

The agency has always enjoyed an extraordinarily cooperative relationship with the Office of Personnel Management. By law, OPM has statutory responsibility for the overall retirement education for the Federal work force and the training of retirement counselors at the Federal employing agencies.

The Board is the entity that ensures the efficient delivery of benefits and services to plan participants. They are located in the executive branch, but are not part of the administration.

The TSP is a participant-directed plan. Each participant decides how to invest the funds in his or her accounts. The TSP funds now include Treasury securities, corporate bonds, the entire U.S. stock market, and stocks of developed countries in Europe, Australia, and the Far East.

In August 2005 the TSP introduced lifecycle funds, the L Funds, which are invested in various combinations of the five statutory funds. Participants benefit from having professionally designed asset allocation models that are appropriate for their particular investment horizon. We are pleased with the reception of the L Funds. As of June, over 515,000 TSP participants have invested more than $21 billion in the L-funds.

The Board contracts with Barclays Global Investors [BGI], to manage the F, the C, the S, and I Fund assets. BGI is the largest investment manager of index funds in the United States, with almost $2 trillion in assets under management.

Although we invite proposals from all qualified providers, only those asset management companies capable of efficiently handling our very large cash-flows could satisfy the minimum qualifications required. We know that there are many excellent vendors who would like to perform services for the TSP but are unable to satisfy the extraordinary demands which an operation of our size requires. In this regard, Mr. Chairman, you and others have expressed interest on behalf of smaller companies. We appreciate that interest and do all that we can to fashion our RFPs to achieve the broadest possible competition, consistent with the fiduciary's duty to act solely in the interest of participants.

By law, TSP investment policies must provide for both prudent investments and low administrative cost. From the beginning of each fund's existence through December 31, 2006, the G, the F, the C, S, and I funds have provided compound annual returns net of expenses of 6.6 percent, 7.3 percent, 11.9 percent, 10 percent, and 9 percent, respectively.

For calendar year 2006, the net plan administrative expenses were 0.03 percent. What this means is that the 2006 net investment return to participants was reduced by approximately $0.30 for every $1,000 of account balance. These costs compare very favorably with the typical private sector 401(k) plan.

Many improvements made by Congress during the plan's 20 year history have kept pace with the best features of 401(k) plans offered by private sector employers; however, neither participant expectations nor the Congress stand still. When Congress passed the Pension Protection Act last August, we carefully examined it for potential TSP improvements. The Board members recently voted to seek statutory authority to institute automatic enrollment and to make default investments in an age-appropriate L Fund.

Both of these changes, which private sector plans are encouraged to make under the Pension Protection Act, will improve the TSP. Our own survey of TSP participants, which found that only 3 percent of respondents were dissatisfied, nevertheless found strong support for these two changes. We hope that the Congress will favorably consider these proposals.

The Board members further decided at the June meeting to more carefully examine the possibility of establishing a Roth feature for the TSP and to revisit this issue within 2 years.

The Board also continues to pursue administrative program enhancements, including improvements that guard against the constant threat of computer fraud.

Early this year we replaced our four-digit PIN number with an eight-character alpha-numeric password for the TSP Web site.

Later this year we will replace our current Social Security number identifier with a computer-generated account number.

In closing, Mr. Chairman, I would like to thank you and the members of this subcommittee for your interest in the TSP and all benefits provided to Federal employees. Since coming to the agency last year, I have gained an enormous appreciation for how well this program meets the needs of employees, and I remain committed to moving forward, together with the Congress, the administration, the Council, OPM, the employing agencies, and others to continue to meet the evolving needs of Federal employees.

That concludes my comments.

[The prepared statement of Mr. Long follows:]

STATEMENT BY GREGORY T. LONG
EXECUTIVE DIRECTOR
FEDERAL RETIREMENT THRIFT INVESTMENT BOARD
BEFORE THE
HOUSE SUBCOMMITTEE ON THE FEDERAL WORKFORCE, POSTAL SERVICE, AND THE DISTRICT OF COLUMBIA

AUGUST 2, 2007

Good afternoon Chairman Davis and Members of the Subcommittee. My name is Greg Long. I am the Executive Director of the Federal Retirement Thrift Investment Board and, as such, the managing fiduciary of the Thrift Savings Plan, or TSP. I welcome this opportunity to appear before the Subcommittee.

You have invited my testimony as part of a comprehensive look at Federal employee pay and benefits. The TSP is a voluntary savings and investment plan that allows Federal and Postal employees (and, since 2002, members of the uniformed services) to accumulate savings for their retirement. It was created by the Congress in the Federal Employees' Retirement System Act of 1986 (FERSA). It offers employees of the Federal Government savings and tax benefits similar to those offered by many private corporations under 401(k) retirement plans. The TSP currently has approximately 3.8 million individual accounts, and the Thrift Savings Fund has grown to $224 billion. Each month, participants add more than $1.6 billion in new contributions. Participants may invest in any or all of five core investment funds and five lifecycle funds; transfer their monies among the funds; borrow from their accounts; transfer money into their accounts from other eligible employee plans or individual retirement accounts; and receive distributions under several withdrawal options. TSP administrative expenses are borne by the participants, not by the taxpayers.

The Government-wide Federal Employees' Retirement System (FERS) employee participation rate is 85.8 percent. TSP participation by Civil Service Retirement System (CSRS) employees is currently about 69 percent. Additionally, after only five years, more than half a million members or 25.6 percent of the uniformed services now have TSP accounts.

PLAN STRUCTURE

Employees who are covered by FERS, CSRS, or members of the uniformed services contribute via payroll allotment to the TSP. The maximum amounts they may contribute are prescribed by law. These limits are currently $15,500 annually for most employees, and $20,500 annually for those age 50 and over.

FERS employees receive an automatic contribution to their TSP accounts, paid by their employing agency, which is equal to one percent of their basic pay each pay period. Their employing agency also matches the first five percent of basic pay contributed -- dollar-for-dollar on the first three percent and fifty cents on the dollar for the next two percent. CSRS employees and members of the uniformed services receive the same tax benefits as FERS employees, but generally receive no automatic or matching contributions from their agencies. (A pilot program of matching contributions for uniformed services members authorized by the Congress is currently underway in the Department of the Army.)

GOVERNANCE AND ADMINISTRATION

The TSP is administered by the Federal Retirement Thrift Investment Board, which was established as an independent Federal agency. There are approximately 70 employees of the Board. Governance is carried out by six individuals who serve as fiduciaries of the Plan. Five are part-time presidential appointees (one recommended by the House, one recommended by the Senate) who serve four-year terms as Board Members. The sixth is a full-time Executive Director. The latter is selected by the Board members and serves an indefinite term. Each of these persons is required by FERSA to have "substantial experience, training, and expertise in the management of financial investments and pension benefit plans." 5 U.S.C. §§ 8472(d), 8474(a)(2). With input from the Executive Director, the statutory Employee Thrift Advisory Council, and Board staff, the five Board members establish the policies under which the TSP operates.

The Executive Director carries out the policies established by the Board members and otherwise acts as the full-time chief executive officer of the agency. The Board members, the Executive Director and the senior staff convene monthly meetings open to the public to establish and assess policies, practices, and performance.

FERSA provides that all monies in the Thrift Savings Fund are held in trust for the benefit of the participants and their beneficiaries. As fiduciaries, the Executive Director and the Board members are required to act prudently and solely in the interest of TSP participants and their beneficiaries. This fiduciary responsibility gives the Board members and the Agency a unique status among Government agencies.

Congress wisely established this fiduciary structure because it recognized that all Plan funds belong to the participants, not the Government, and thus must be managed independent of political or social considerations.

In keeping with the intent of Congress that the Plan be administered in accordance with fiduciary standards derived from those applicable to private sector employee benefit plans -- as distinct from the usual administration of an executive branch agency -- Congress exempted the Board from the annual appropriations process and the legislative and budget clearance processes of the Office of Management and Budget. The testimony I am presenting today was not subject to clearance by the OMB.

The Plan's independence is critical to ensure the fiduciary accountability envisioned by FERSA. So long as the Plan is managed by the six fiduciaries named in FERSA (the members of the

Board and the Executive Director) in accordance with the statute's strict fiduciary standards, Federal employees and members of the uniformed services can be confident that their retirement savings will not be subject to political or other priorities which might otherwise be imposed.

FERSA protects the Thrift Savings Fund through more than just the independent fiduciary governance by the Board members and the Executive Director. Additional safeguards to protect TSP participants include FERSA provisions relating to (1) the role of the Secretary of Labor in establishing a program of fiduciary compliance audits; (2) the requirement that a private accounting firm conduct an annual audit of the TSP on the basis of generally accepted accounting principles; and (3) the participation of the 15-member Employee Thrift Advisory Council, which includes representatives of the major Federal and Postal unions, other employee organizations, and the uniformed services.

The TSP has benefited greatly from hundreds of audits conducted by the Department of Labor over the past twenty years. These audits, which have covered every aspect of the TSP, are reported to the Congress annually under the Inspector General Act of 1978, as amended.

The independent accounting firm has conducted annual reviews as required. The result has been twenty unqualified audit opinions.

The Advisory Council meets with the Executive Director and advises on investment policy and the administration of the TSP. These meetings are very helpful in providing the Executive Director with insights into employee needs, attitudes, and reactions to the various TSP benefits and investments.

The TSP also benefits from the cooperation of every agency and service in the Federal establishment. Although the Board is independent, successful administration of the TSP is highly dependent upon coordination with all Federal agencies and the uniformed services, which have direct responsibilities under FERSA for the administration of the TSP.

RELATIONSHIP WITH THE OFFICE OF PERSONNEL MANAGEMENT

Since its earliest days, the Agency has enjoyed an extraordinarily cooperative relationship with the Office of Personnel Management. OPM is the authority for the Administration with regard to pay and benefits in the Executive Branch. It is OPM that has statutory responsibility for the overall retirement education of the Federal workforce and the training of retirement counselors at Federal employing agencies. OPM is comparable to private sector "plan sponsors," the employers who offer benefit plans to employees. As such, OPM, in conjunction with the Administration and the Congress, looks at the overall level of benefits necessary to attract and retain a qualified workforce to conduct the public's business. In this regard, I note that OPM annually surveys employees to determine attitudes about the importance, adequacy, value, and competitiveness of the various benefit programs. I am pleased that the attitudes toward the TSP reported in those survey results are quite positive.

As an independent establishment, the Board is comparable to a private sector "plan administrator," which is the entity that ensures the efficient delivery of benefits and services to plan participants. We are located in the Executive Branch, but operate with extraordinary independence. We are not part of the Administration, and we carry out our activities solely in the interest of participants and beneficiaries.

One might anticipate friction from the different but closely related roles of the Board and OPM. However, our experience has been just the opposite. We are grateful for the many courtesies extended by OPM, and know that the Plan and its participants have benefited from this excellent relationship.

PLAN SERVICES AND BENEFITS

Employees and service members who participate in the TSP are served primarily by the personnel, payroll, and other administrative employees in their own agencies. The agencies are responsible for distributing TSP materials, providing employee counseling, and accurately and timely transmitting participant and employer contributions and necessary records to the TSP record keeper.

Additionally, the Board has contracted with private firms for TSP record keeping, call center and data center services. TSP record keeping services are currently provided by SI International, a contractor located in Fairfax, Virginia. In addition, SI maintains one of the TSP call centers which is located in Clintwood, Virginia. A second TSP call center is operated by InfoSpherix, Inc., in Cumberland, Maryland. Participants with questions may call the ThriftLine, our toll-free number, which routes calls to participant service representatives at one of these sites. Further, to support continuity of TSP operations, we maintain one primary data center and one back-up data center.

Actively employed participants may borrow a portion of their own contributions and earnings from their accounts according to rules established by the Executive Director and regulations of the Internal Revenue Service. Participants repay the loans, with interest, and the money is reinvested in their TSP accounts. A $50 fee is charged to cover the costs of loan processing. During 2006, the TSP issued more than 240,000 loans to participants.

The other major benefit program is the TSP withdrawal program. Participants may withdraw funds from their TSP accounts before separation after reaching age 59½ or in cases of financial hardship. Upon separation, a participant may:

- withdraw his or her account balance in a single payment (and have the TSP transfer all or part of the payment to an Individual Retirement Account (IRA) or other eligible retirement plan);
- withdraw his or her account balance in a series of monthly payments (and, in certain cases, have the TSP transfer all or part of each payment to an IRA or other eligible retirement plan);
- receive a life annuity; or
- keep his or her account in the TSP, subject to certain limits.

Participants may also elect a combination of these withdrawal options. During 2006, more than 850,000 withdrawal payments were issued to participants.

COMMUNICATIONS

The Board maintains its communication program on a number of levels within the Federal establishment in order to achieve employee understanding of the investment choices, benefits, and the administration of the program. This is especially important given the voluntary nature of the Plan and the participants' degree of individual control over investments and benefits.

The communication effort is initiated through the issuance of a "new account letter" to each new participant after the employing agency establishes his or her account. Employing agencies distribute program information, including the *Summary of the Thrift Savings Plan*, which provides a comprehensive description of the Plan, as well as booklets describing the loan and withdrawal program for employees to review at the time they are examining those benefits. Investment information is provided by the TSP Fund Sheets and the *Managing Your Account* leaflet which discusses operations. Copies of these publications are also available on our Web site at www.tsp.gov or through the ThriftLine. We have also designed pamphlets to support specific campaigns to increase TSP participation. An example would be the leaflets provided to the uniformed services to include with their retirement materials.

In addition, we issue materials related to specific events. For example, the *TSP Highlights* is a newsletter issued with the quarterly participant statement. Copies of the newsletters, which address topical items and convey rates of return, are provided on the TSP Web site. Participants can also use the Web site to obtain their daily balances, request contribution allocations and interfund transfers or, in some cases, loans and withdrawals, and use various calculators as convenient planning tools.

The ThriftLine, the Board's toll-free automated voice response system, also provides both general plan and account-specific information and allows participants to perform some transactions via the phone as well as speak to a representative.

In connection with the new lifecycle funds we introduced in 2005, we revised all of our communications materials and now feature the benefits of the asset allocation approach used in "Life" funds as discussed below. We also issued a DVD explaining the L Funds to all participants.

Because of the importance of the agencies and services in administering the TSP for their employees and members, the Board conducts quarterly interagency meetings. These have proven to be an effective means of communicating program and systems requirements to Federal agency administrative personnel. These meetings also allow the TSP to hear and address representatives' concerns and to incorporate their suggestions in the establishment of TSP policies and operations. We also issue TSP Bulletins regularly to inform agency personnel and payroll specialists of current operating procedures.

INVESTMENT FUNDS

The TSP is a participant-directed plan. This means that each participant decides how the funds in his or her account are invested.

As initially prescribed by FERSA, participants could invest in three types of securities -- U.S. Treasury obligations, common stocks, and fixed income securities -- which differ considerably from one another in their investment characteristics. In 1996, on the Board's recommendation, Congress authorized two additional investment funds, which allow further diversification and potentially attractive long-term returns. The Small Capitalization Index Investment Fund and the International Stock Index Investment Fund were first offered in May 2001.

The Government Securities Investment (G) Fund is invested in short-term nonmarketable U.S. Treasury securities guaranteed by the full faith and credit of the U.S. Government. 5 U.S.C. § 8438(b)(1)(A), (e). There is no possibility of loss of principal from default by the U.S. Government and thus no credit risk. These securities are similar to those issued to the Social Security trust funds and to other Federal trust funds. See 42 U.S.C. § 401(d) (Social Security trust funds); 5 U.S.C. § 8348(d) (Civil Service Retirement and Disability Fund).

The Fixed Income Index Investment (F) Fund, which by law must be invested in fixed income securities, is invested in a bond index fund, chosen by the Board to be the Lehman Brothers U.S. Aggregate (LBA) index. The LBA index represents a large and diversified group of investment grade securities in the major sectors of the U.S. bond markets: U.S. Government, corporate, and mortgage-related securities.

The Common Stock Index Investment (C) Fund must be invested in a portfolio designed to replicate the performance of an index that includes common stocks, the aggregate market value of which is a reasonably complete representation of the U.S. equity markets. The Board chose the Standard & Poor's 500 (S&P 500) stock index in fulfillment of that requirement. The S&P 500 index consists of 500 stocks representing approximately 73 percent of the market value of the United States stock markets. The objective of the C Fund is to match the performance of that index.

The Small Capitalization Stock Index Investment (S) Fund must be invested in a portfolio designed to replicate the performance of an index that includes common stocks, the aggregate market value of which represents the U.S. equity markets, excluding the stocks that are held in the C Fund. The Board chose the Dow Jones Wilshire 4500 Completion index, which tracks the performance of the non-S&P 500 stocks in the U.S. stock market. The objective of the S Fund is to match the performance of the Wilshire 4500 index. The Wilshire 4500 index represents the remaining 27 percent of the market capitalization of the U.S. stock market. Thus, the S Fund and the C Fund combined cover virtually the entire U.S. stock market.

The International Stock Index Investment (I) Fund must be invested in a portfolio designed to track the performance of an index that includes common stocks, the aggregate market value of which represents the international equity markets, excluding the U.S. equity markets. The Board chose the Morgan Stanley EAFE

(Europe, Australasia, Far East) index, which tracks the overall performance of the major companies and industries in the European, Australian, and Asian stock markets. The objective of the I Fund is to match the performance of the EAFE index. The EAFE index was designed by Morgan Stanley Capital International (MSCI) to provide broad coverage of the stock markets in the 21 countries represented in the index.

In August 2005, the TSP introduced Lifecycle Funds. The Lifecycle Funds are invested in various combinations of the five statutory funds. Participants benefit from having professionally designed asset allocation models available to optimize their investment performance by providing portfolios that are appropriate for their particular investment horizon. This is known in the financial world as investing on the "efficient frontier." We are very pleased with the reception of the L Funds by participants. As of the end of June, over 515,000 TSP participants have invested more than $21 billion of their retirement savings in the L Funds.

One likely concern associated with a Federal agency's investing in equities is the potential for the Government to influence corporate governance questions and other issues submitted to stockholder votes. FERSA wisely provides that the voting rights associated with the ownership of securities by the Thrift Savings Fund may not be exercised by the Board, other Government agencies, the Executive Director, a Federal employee, Member of Congress, former Federal employees, or former Members of Congress. 5 U.S.C. § 8438(f). Barclays Global Investors (BGI), the manager of the C, S, and I Fund assets, has a fiduciary responsibility to vote company proxies solely in the interest of its funds' investors.

The fund assets held by the F, C, S, and I Funds are invested in passively managed indexed funds; that is, they are invested in portfolios of assets in such a way as to reproduce market index returns. The philosophy of indexing is that, over the long term, it is difficult to improve upon the average return of the market. The investment management fees and trading costs incurred from passive management through indexing generally are substantially lower than those associated with active management. Passively managed index funds also preclude the possibility that political or other considerations might influence the selection of securities.

The manager of the assets held by the F, C, S, and I Funds has been selected through competitive bidding processes. Proposals from prospective asset managers were evaluated on objective criteria that included ability to track the relevant index, low trading costs, fiduciary record, experience, and fees.

The Board has contracts with BGI to manage the F, C, S, and I Fund assets. BGI is the largest investment manager of index funds in the United States, which had over $1.99 trillion in total assets under management as of May 31, 2007.

Although we have invited proposals from all qualified providers, only those asset management companies capable of efficiently handling our very large cash flows could satisfy the minimum qualifications required. We know that there are many excellent vendors who would like to perform services for the TSP, but who are unable to demonstrate that they can satisfy the extraordinary demands which an operation of our size requires. In this regard, Mr. Chairman, you and others have expressed an interest on behalf of smaller companies. We appreciate that interest and do all that we can properly do in fashioning our requests for proposals to achieve the broadest possible competition consistent with the needs of the fund and the fiduciaries' duty to act solely in the interest of the participants.

The centralized management of TSP investments was carefully considered in FERSA by Congress. The Congress clearly expected the fiduciaries to use the size of the Plan for the benefit of its participants. According to the Joint Explanatory Statement of the Committee of Conference on the TSP enabling legislation, Congress designed the plan to preserve "the economic advantage of this group's purchasing power derived from its large size...." H.R. Rep. No. 99-606, at 137-38, reprinted in 1986 U.S.C.C.A.N.

1508, 1520-21.

INVESTMENT RETURNS

By law, TSP investment policies must provide for both prudent investments and low administrative costs. From the beginning of the G Fund's existence (April 1987) and the beginning of the F and C Funds' existence (January 1988) through December 31, 2006, the G, F, and C Funds have provided compound annual returns net of expenses of 6.57 percent, 7.25 percent, and 11.86 percent, respectively. The related BGI funds closely tracked their respective market indexes throughout this period. Since the S and I Funds were introduced in May 2001, they have produced compound annual returns of 10.04 percent and 9.69 percent, respectively.

For calendar year 2006, the net Plan administrative expenses were .03 percent. This means that the 2006 net investment return to participants was reduced by approximately $.30 for each $1,000 of account balance. The expense ratio would be approximately .01 percent higher in the absence of account forfeitures and loan fees, which offset expenses. These costs compare very favorably with typical private sector 401(k) service provider charges.

FUTURE IMPROVEMENTS

I believe that the Thrift Savings Plan has effectively and efficiently realized the numerous objectives Congress thoughtfully established for it twenty years ago. Further, I believe that the many improvements made by the Congress during the Plan's twenty year history have kept pace with the best features of 401(k) plans offered by private sector employers. Earlier, I noted that the annual OPM benefits survey reported positive views of the TSP by respondents. Our own survey last year showed a high level of satisfaction, with only 3 percent of participants providing an unfavorable assessment of the TSP.

I further note, however, that neither participant expectations, nor the Congress, stand still. Last August, Congress approved and the President signed into law the Pension Protection Act (PPA) which authorized certain new benefits and encouraged private sector plans to adopt design changes intended to increase voluntary participation and improve investments. After carefully examining this new law and making those appropriate changes which we could on our own authority, the Board voted at its June 19, 2007, meeting to seek statutory authority to institute automatic enrollment and to make default investments in an age-appropriate L Fund. Both of these changes, which private sector plans are encouraged to make under the PPA, will improve the TSP. They were widely supported by participants in the survey noted above. We hope that the Congress will favorably consider these proposals.

The Board further decided at its June meeting to more carefully examine the possibility of establishing a Roth feature for the TSP and to revisit that issue in two years. A Roth

401(k) feature could first be implemented by private plans in 2006, with expiration scheduled for 2010. The PPA made it permanent. While our initial review found that some participants might benefit from a Roth feature, it is still not clear whether it would generate enough support to justify its expense. In those few 401(k) plans offering a Roth feature, participant utilization remains in the low single digits. Moreover, a Roth feature would add significant complexity to the TSP. We strongly believe that more experience and information is needed on this matter.

We are also aware of interest expressed by various individual members of Congress and interest groups in establishing new TSP investment funds or in removing certain companies from the existing TSP funds. Congressional proposals have included a REIT fund, a precious metals fund, and a corporate responsibility fund. On the divestment side, proposals to exclude companies doing business in Darfur, the Iran energy sector, or those marketing tobacco products, have also found congressional sponsorship.

There are many good products or meritorious causes that some in Congress support for many legitimate reasons. However, in determining TSP investment policy, the Congress directed the Board fiduciaries to make their decisions solely in the interest of TSP participants. With the assistance of our investment consultant, Ennis Knupp + Associates, the Board last year conducted a comprehensive review and determined that we should not add any additional investments to the TSP at this time. We will, of course, continue to monitor industry best practices and products in this regard in the future.

In addition to these legislative matters, the Board continues to pursue administrative program enhancements. Most notably, we continue to implement more sophisticated security protections to guard against the constant threat of computer fraud. Early this year we replaced our 4 digit PIN with an eight character alpha-numeric password for the TSP Web site. Later this year we will replace our current Social Security number identifier with a computer generated account number. (The latter may generate some participant complaints during implementation, but we consider it to be essential to protect participants and the Plan.)

In addition to our own security enhancements, we need to continuously remind participants that they need to keep their personal information secure. Last December, a number of individuals were victimized by thieves who, using "keylogging" techniques, were able to "eavesdrop" and steal personal information from some participants' personal computers. These thieves then used that information to initiate TSP withdrawals.

We quickly recognized the problem and took action. I would like to thank the U.S. Secret Service for its investigation of this matter, and, also, thank various financial institutions who made affected participants whole. I hope this incident, which we reported to participants on our Web site, has helped them better appreciate the need for constant vigilance.

We also continue to improve the TSP Web site at www.tsp.gov. Most recently, we have instituted a search engine to help visitors more easily navigate and locate precisely the information they seek. We plan to send a new annual statement to all participants beginning early next year, and we are examining other potential improvements suggested during my first meeting with our Employee Thrift Advisory Council.

In closing, Mr. Chairman, I would like to thank you and the members of the Subcommittee for your interest in the TSP and all of the benefits provided to Federal employees. We understand the key role which these benefits serve in attracting and retaining an outstanding workforce capable of performing the many important services which the American public deserves. Since leaving the private sector and coming to the Agency last year, I have gained an appreciation of how well this program, designed by the Congress, meets the needs of employees. As I noted earlier, this does not mean that we can rest on our laurels. Rather, I remain committed to moving forward together -- the Board, the Congress, the Administration, the Employee Thrift Advisory Council, the Office of Personnel Management, the employing agencies and others -- to continue to meet the evolving retirement savings needs of Federal employees and members of the uniformed services.

Mr. DAVIS OF ILLINOIS. Thank you very much, Mr. Long.

We will proceed directly to questions.

Director Springer, I will begin with you. The President's fiscal year 2008 budget proposed the Blue Cross/Blue Shield and the Indemnity Benefit Plan be allowed to offer health savings accounts in the FEHBP. As you know, the Federal employee and retiree organizations that will testify later this afternoon are concerned that further expansion of HSAs could increase premiums for comprehensive plans, since relatively healthy enrollees with higher incomes could be siphoned off into these HSAs.

Given the fact that these employee groups have expressed concerns, could you tell us why the administration continues to support this proposal, since relatively few employees have joined the HSAs?

Ms. SPRINGER. Yes, Mr. Chairman. We do have, as you mention, a few options of that type today, but none are associated with the Blue Cross and Blue Shield system. The Blues represent over half of our membership in the Federal health plan, so there is a very strong brand identity. I think that my expectation would be that we would see minimal enrollment in those types of plans today until it is available through the Blue Cross/Blue Shield system, because the first level of decisionmaking is to associate yourself with the brand.

But adding it and allowing that capability for the Blue Cross and Blue Shield system we think is important because we think that a plan of our type, the largest offered in the world by a single employer, should have a full range of choice, and we think that only offering it in those very limited circumstances where it is available today doesn't provide that full range of choice.

Ultimately, we will deal with the experience, but we think that the population across the system of the Blues, all of the three options that will be available will still be substantial in all three.

Mr. DAVIS OF ILLINOIS. Thank you very much.

As you know, OPM's Inspector General found that Medco Health Solutions engaged in fraud in the FEHBP. However, OPM has decided not to bar Medco from the program. Could you explain?

Ms. SPRINGER. Yes. Medco actually is under contract, I believe, or will be directly with the Blue Cross and Blue Shield, not with us directly. Now, indirectly that means some services will be provided by them to people who are enrolled in the Blue Cross/Blue Shield system, but we have not directly contracted with Medco.

I visited with Inspector General McFarland and I learned that Blue Cross/Blue Shield had engaged in that contract with them, because I had the same concern that I think you are expressing. There are a number of safeguards in place. The senior management team has changed at Medco. There are a variety of things that I have been told will give them enough comfort to have engaged in it, that contract, but we will be keeping a very watchful eye on it through the work of the Inspector General.

Mr. DAVIS OF ILLINOIS. Let me ask what changes would you recommend to improve the Federal Employees Health Benefits Program, and what concerns do you have, if any, about the effects of increased enrollment and potential adverse selection issues for high-deductible health plans and health savings accounts?

Ms. SPRINGER. Well, the first part of your question as far as changes, the thing that I really and truly believe that we need to look at at the top of the list is the short-term disability benefit, to include maternity. As I say, that is not a benefit that we provide today. We have found that companies of 200 employees or more 80 percent of the time offer a short-term disability program. We do not, and I think it is disgraceful.

That would be my No. 1 issue to attack.

With respect to the participation issue, again, with high-deductible plans I think that there are circumstances where that works and is appropriate. I think there are other people where that is not a good option. But I think that it is important to offer it so that we are state-of-the-art. A plan like ours should offer the full range of choice.

Mr. DAVIS OF ILLINOIS. Is it true that employees pay all of the disability benefit's costs?

Ms. SPRINGER. We have not transmitted a proposal to the Congress yet about that. We are still trying to craft the right proposal to send to you. I know that there are several proposals here. There is interest. We would like to work together with you.

Balancing cost with the benefit is obviously a concern, and one thing we can offer for sure, though, is our negotiating power in getting a good rate, and certainly the tax benefit that comes with a pre-tax contribution of payment, even if it is employee pay all.

Mr. DAVIS OF ILLINOIS. As a sort of a side question, I have introduced legislation to allow community health centers to participate in the FEHBP. Are you familiar with these centers?

Ms. SPRINGER. I have become familiar with your proposal and learned a little bit about the centers just by reading the testimony that was submitted on it.

Mr. DAVIS OF ILLINOIS. And as of now you don't have any concerns about that?

Ms. SPRINGER. Well, I don't want to speak for the administration. Because it has just come to our attention, we would have to review that, and we will do that.

Mr. DAVIS OF ILLINOIS. Thank you very much.

I will go to Mr. Marchant.

Mr. MARCHANT. Thank you.

Ms. Springer, you stated earlier that the increase in the premium was 1.8 this year, but that was as a result of an overpayment from the previous year?

Ms. SPRINGER. That was a contributing factor, but not the only factor. There are a number of things that have helped us to control costs in the plan, but that was a factor. It would have been higher had that not been the case.

Mr. MARCHANT. What would have been the rate of increase without that overpayment?

Ms. SPRINGER. It would have been a little over 6 percent increase, which still would have been pretty favorable increase.

Mr. MARCHANT. Yes. Explain to me the issue about the $3,000 exclude on the health premiums for public safety officers.

Ms. SPRINGER. I am going to need a little help on that, if I may.

Mr. MARCHANT. OK.

Ms. SPRINGER. May I have someone get back to you on that, Mr. Marchant?

Mr. MARCHANT. Absolutely.

Ms. SPRINGER. I don't want to give you an incomplete answer, and I need a little help with that.

Mr. MARCHANT. You have answered the other question, what would your top priority be. You have answered that with the disability.

Ms. SPRINGER. I answered that, yes, with respect to just the health plan, which I think that was the way that was raised. Certainly nothing is a higher priority to us than the reemployed annuitant proposal that we have that would allow us to have the benefit of the knowledge and experience of annuitants who want to come back and help train that next generation.

I know that there has been overwhelming support for this. Polls show over 80 percent of employees want it. The Chief Human Capital Officers representing the hiring agencies want it. There was a little bit of question about do these people take the place of new employees. Well, when you are facing a shortage of 600,000 potential positions turning over due to retirement, as Congressman Moran said, this is just a drop in the bucket in filling that, and it actually helps these new people to come in and learn from the masters, and then they go on and the new people are remaining. So that and the short-term disability.

Mr. MARCHANT. And the last question I will ask you is: with the greater number of veterans that are leaving the service today and, in many instances, the probability of a lot of those injured veterans coming into the Federal work force, have you contemplated the fact that many of them will be disabled? And do you feel like there are an adequate number of jobs that will be available to a disabled vet in the Federal system?

Ms. SPRINGER. We do believe there will be. Right now veterans make up a quarter, about 450,000 members, of the Federal work force, and some agencies obviously have greater participation than others, and we encourage all of them. One of the things we do is highlight veterans' preference and work with our agencies. But with respect to disabled veterans particularly, we have established over the past 2 years programs onsite at Walter Reed, at Brook Army Medical Center, and we will be starting one at Fort Collins at the three medical facilities there for the Armed Services to counsel them on jobs in the Federal Government, on writing resumes, on interviewing.

We have people that we staff onsite. I have been to Brook Army Medical Center. I have been to the Center for the Intrepid to visit those wounded warriors. They are terrific people, and we want them.

Yesterday I just filmed a video to be played for the Navy. We want these people. There is a place for them, whether disabled or not, and we are very happy to have them. We have indicated by our presence onsite at the hospitals.

Mr. MARCHANT. Thank you very much.

Mr. DAVIS OF ILLINOIS. Thank you very much, Mr. Marchant.

We will go to Ms. Norton.

Ms. NORTON. Ms. Springer, I am looking for ways that might be considered more realistic to try to encourage the adjustment of benefits so that somebody will want to come work for the Federal Government, so we will be competitive. Even with FEHBP, you have 250,000 or so people who don't subscribe to this plan because they can't afford it. Those are people who work for the Federal Government and giving up a plan that some of us see as decent because we can afford it, and only because we can afford it.

The 72 percent that the Federal Government now pays on average, when was that percentage set?

Ms. SPRINGER. I don't know when that was set. I could get back to you. I don't know exactly when the 72 percent——

Ms. NORTON. Well, I think the reason that you can't think about when it was set is because it was so long ago.

Ms. SPRINGER. I just don't happen to know. That is all.

Ms. NORTON. No, it is not that you don't happen to know. I didn't expect you to come up with it off the top of your head. Somebody ought to know. I don't know when the FEHBP was, in fact, established, but it strikes me that—and I don't know the date, myself—but it strikes me that the Government has rested on its laurels on 72 percent and said just take that, premiums will go up, and be satisfied with it.

So you don't intend to recommend any increase in the Government share of FEHBP, do you?

Ms. SPRINGER. We do not. I could tell you why, but we do not.

Ms. NORTON. That being the case, it is certainly not because you consider it adequate or competitive——

Ms. SPRINGER. We do.

Ms. NORTON [continuing]. With employees of the caliber we have.

Let me go on. One way to make up for that, it seems to me, would have been for OPM to have asked for the subsidy for Medicare Part D. It would have had the effect of reducing the premiums somewhat overall and, of course, of helping to keep up with the hugely growing prices of drugs in the first place, but the Federal Government has chosen not to participate, and therefore to have an effect, at least, on premiums which, as you have just testified, you do not intend to increase as to the Government's portion.

Don't you think that if you are not going to increase the share you have to look at other lower-cost ways such as participating in Medicare Part D to try to stay competitive with the kind of private sector employers who want the same people that we want?

Ms. SPRINGER. You have raised, I think, four questions in there. One is about our participation and the affordability; one about the Medicare subsidy; one about would we raise the subsidy, the 72 percent, and increases——

Ms. NORTON. No, you said you wouldn't.

Ms. SPRINGER [continuing]. And increases in price.

Ms. NORTON. You said you wouldn't.

Ms. SPRINGER. I just want to elaborate, if I may, a little on that so you have the complete answer.

With respect to participation, 85 percent of the people who are eligible do participate. Another 4 percent have spouses in the FEHBP through whom they get their coverage. Another 9 percent have coverage elsewhere, probably from a prior employer. So there is really only 2 percent who are not covered one way or the other, but 90 percent almost are covered through the FEHBP. So participation is high.

With respect to the competitiveness of the plan, we believe that it is competitive. We believe when we look at other employers what we see is that they are backing off from their subsidy, in many cases, and so in effect that means by us staying at 72 percent——

Ms. NORTON. On the contrary, Ms. Springer.

Ms. SPRINGER [continuing]. We are staying——

Ms. NORTON. Ms. Springer, that is true. I am thinking about employees of the kind we need.

Ms. SPRINGER. Yes.

Ms. NORTON. You have many, many Fortune 500 employers who pay for 100 percent.

Ms. SPRINGER. I do not know of many who pay 100 percent. I know in the experience we have looked at that, particularly in retirement, that they are decreasing the share of the employer.

Ms. NORTON. I am not talking about retirement. That is bad enough. I understand the difference in retirement and I understand what we do. I am thinking about the fact that the Government, in fact, understood that it wasn't always able, given the level of employee we have, to be competitive in benefits, to be competitive in wages, but it would do things like thrift savings, for example, which is the kind of thing you think about, well, maybe the pay isn't as good, but there is the Thrift Savings Account.

Or, again, I am focusing on health benefits. To name a benefit that if it were, in fact, changed, this without going from 72 percent to the 80 percent that people like me want, might, nevertheless, have at least a marginal effect, particularly on keeping certain employees who are already here, such as the benefit that some employers have again of the caliber of the Federal Government that would say a kid doesn't age out at 22 but, say, ages out at 26, so that one of the most troublesome age groups still remains covered because you are covered by your FEHBP plan.

What I am trying to get at is if there is not something around the edges, if we keep at increases like, hey, you can have your own vision and dental plan if you pay for it 100 percent; hey, how about a long-term plan, which you actually market even when not all employers will need it. How about a long-term plan if you pay for it?

I mean, if anything, you are devolving benefits to the point that you can have anything you want to as a group if you pay for it as a group, and you have not thought about even around the margins of how you might, in fact, if you can't, in fact, raise the level of benefits forthrightly.

Ms. SPRINGER. Well, nothing comes without a cost. There is a price tag to all those things, and ultimately the decision will have to be made where we put what is the right level amount of cost and what is the right place to invest. You must be seeing something different than we do, but we do not see that this is a barrier to retaining or hiring people. People see this in our surveys as a competitive advantage. The satisfaction level with benefits has gone up in our most recent survey compared to the last one.

All I can say is we think that it is still positioned properly.

Ms. NORTON. I will go. I just want to say I think this is the most short-sighted notion of your competitive position relative to particularly the kinds of people you are going to have to recruit to become workers in the future.

Mr. DAVIS OF ILLINOIS. Thank you very much. We will return.

[Recess.]

Mr. DAVIS OF ILLINOIS. Thank you all very much. The subcommittee will return to order.

We will try and finish up with this panel. Let me thank all of you for continuing to have been here and for being here. We always say that this is the week that we try to get as many things done as we possibly can, and everybody is racing, hopefully, for a recess that we still don't know when it is going to take place, but we suspect that it will be some time before next week.

Let me just ask, Mr. McFarland, due to the complexity of the prescription benefit managers, that is the PBM contracts, what challenges and obstacles have you encountered in performing your audits, and what are your recommendations for eliminating these obstacles?

Mr. MCFARLAND. Mr. Chairman, let me mention five points here, and then I will mention what we think we can do to help resolve this.

First of all, your point is well taken. Auditing these PBM contracts has proven to be a great challenge. In addition to the normal delays in requesting data from the carriers, both PBMs we have audited, Medco and CareMark, were reluctant to provide the claims and administrative data necessary to perform the audits.

Overall, our PBM audits revealed that the major issue was not contract compliance, but rather the weaknesses found within the contracts, themselves.

Some of the specifics that we have encountered are the five that I mentioned. First, the PBMs contract directly with the insurance carriers and not with OPM; therefore, OPM has limited control over the terms of these contracts, especially related to pricing and fees. Carriers pay PBMs based on a negotiated rate which may have no relationship to the actual price paid for the drugs; therefore, we could not determine accurately the amount of profit made on Federal business, nor can we determine if a price is fair and reasonable.

Contracts are complex, and the specific pricing terms are difficult to understand. OPM should require full disclosure from the PBM regarding pricing terms, including rebates generated from the Federal business.

Each FEHBP carrier negotiates the terms, pricing methods, rebates, administrative fees, etc., of its contract with the PBM; therefore, there is no consistency among these contracts.

Finally, little incentive for the carriers to negotiate the best price for the pharmacy services, since OPM reimburses them for all costs charged by the PBMs.

Now, as far as the potential solutions, I speak in the singular, but for the great majority of my comments I am referring to a cooperative venture with the program office at OPM and our office. To that end, the first suggestion would be the possibility of changing the language in the Federal employees health benefits acquisition regulations to include large providers as subcontractors.

Second, to assess the benefits and risks—and I emphasize the risk—of carving out pharmacy benefits and having OPM contract directly with the PBMs for these services and benefits.

Finally, reimburse PBMs based on the actual cost of the drugs dispensed.

The OIG has identified many areas that require change in the current contract language and/or areas that require greater oversight. We are still currently analyzing the contracts and the process of administering pharmacy benefits through the FEHBP. At the conclusion of this process, we will provide our findings and recommendations to OPM and work with the appropriate contracting officials to strengthen the controls and oversight regarding FEHBP's pharmacy benefits.

Those are the solutions that we are working toward in concert with OPM.

Mr. DAVIS OF ILLINOIS. Thank you very much.

Let me ask you, Mr. Long, what is the average percent of pay contributed by TSP participants? Has it been going up or down? And how do the contributions of younger and lower-paid employees compare with others in the program?

Mr. LONG. Mr. Chairman, we did some homework on this a few months back and we prepared a report that is available on our Web site. It is called the Participant Behavior and Demographics Report, in which we took a look at activity from 2000 through 2005. To specifically answer your question, the rate of salary deferral among FERS employees stands at 8.6 percent at the end of 2005.

Over the last 5 years I am very pleased to say that has been steadily increasing. Specifically, the younger and lower-paid employees, the challenge there is, first, to get them participating in the plan, and then, second, to get them participating at higher rates. We have seen over the years that participation among most age groups is fairly stable, but we have seen some slight increases of participation among the younger and lower-paid. We are very pleased to see that. They are contributing at a lower rate than the more highly paid and older employees. They are at about 6.4 percent of pay.

Mr. DAVIS OF ILLINOIS. And let me ask you, what are your views on adding socially responsible investment funds to the TSP?

Mr. LONG. This is an issue which has received a bit of press lately, and it is one that I have been doing a bit of homework on since I joined the Board about a year and a half ago. I gather that over the years there have been many proposals to divest in certain types of securities that are considered bad or over-invest in certain types of securities that are considered good.

The congressional designers of the TSP 20 years ago clearly came out and said that social and political considerations should not be used in the TSP. Certainly, we shouldn't be using participant money to further those goals. That is a position which I agree with and the Board agrees with.

What we can't do is there is no particular social or political goal that everybody is going to agree with, so you would end up with a hodgepodge of multiple different goals, and that would really cause significant problems, especially when we work in a passive management index. Our funds are designed to cover broad segments, and in this case you would be trying to pluck out certain securities that create significant problems, as well as cost.

Finally, I would say that the promise that was made to TSP participants was that when you invest your money the fiduciaries will invest it only for your best interest without consideration of social or political goals, and that would change the game.

Mr. DAVIS OF ILLINOIS. Thank you all so very much. We again appreciate your patience and your willingness to stay while we go through our machinations, but it is all a part of the process. Thank you, indeed. We appreciate it.

I wonder if we could actually go to panel four. I know that Ms. Kelley has to catch a plane, and if we could accommodate her we would like to do that, so if we could go to panel four.

While we are exchanging, I will just go ahead and introduce the panelists.

Colleen Kelley is the president of the National Treasury Employees Union, the Nation's largest independent Federal sector union, representing employees in 31 different Government agencies. As the union's top elected official, she leads the NTEU's efforts to achieve the dignity and respect Federal employees deserve. Ms. Kelley represents the NTEU before Federal agencies, in the media, and testifies before Congress on issues of importance to NTEU members and Federal employees.

J. David Cox is the national secretary-treasurer of the American Federation of Government Employees. He was elected during the union's 37th convention in August 2006.

Ms. Margaret Baptiste of Mount Pleasant, SC, is the first woman to be elected national president of the National Association of Retired Federal Employees and the first spouse of a Federal retiree to hold the position. Mrs. Baptiste is the former president of the South Carolina National Association of Retired Federal Employees Federation.

Thank you all so much for being here.

It is the custom of this committee to swear in witnesses.

[Witnesses sworn.]

Mr. DAVIS OF ILLINOIS. The record will reflect that each of the witnesses answered in the affirmative.

Of course, you know our procedure. Your entire statement will be included into the record. If you would summarize in 5 minutes, the green clock means that you start. When it begins to get yellow you are down to 1 minute. Of course, red means that you are to cease.

Thank you all very much. We will begin with you, Ms. Kelley.

STATEMENTS OF COLLEEN KELLEY, NATIONAL PRESIDENT, NATIONAL TREASURY EMPLOYEES UNION; J. DAVID COX, NATIONAL SECRETARY-TREASURER, AMERICAN FEDERATION OF GOVERNMENT EMPLOYEES; AND MARGARET BAPTISTE, PRESIDENT, NATIONAL ACTIVE AND RETIRED FEDERAL EMPLOYEES ASSOCIATION

STATEMENT OF COLLEEN KELLEY

Ms. KELLEY. Thank you very much, Chairman Davis, Ranking Member Marchant. I appreciate the opportunity to speak with you today about Federal employee benefit and retirement programs.

The question you asked, are we meeting expectations, is a relevant and an important one for all Federal employees. It is difficult to say that we are meeting expectations when every day Federal employees are asked to do more with less and face an often hostile administration that does not seem to value the work done by Federal employees every day.

We appreciate those Members of Congress like yourself, Mr. Chairman, who put substantial time and effort into improving working conditions for Federal employees. NTEU is actively working on a number of these proposals.

First, increasing the coverage for dependents in FEHBP to age 25. Thank you very much for your draft legislation, Mr. Chairman. Young adults are the fastest-growing age group among the uninsured, and while the current law does provide health insurance until age 22, 22 year olds are seldom in a position to obtain health insurance themselves. Several States have enacted legislation to avert this health crisis. Because young adults are healthier than older adults, it is possible that adding more of them to a pool of health care participants may even lower the average cost for group insurance. NTEU looks forward to working with you to have your proposal enacted into law.

Paid parental leave, NTEU has long been an advocate for parental leave and was instrumental in the successful passage of the Family and Medical Leave Act of 1993. Since that time, it has become clear that many who would take advantage of time off to care for a baby have not because they were unable to forego their income. A benefit that you cannot take advantage of is not much of a benefit.

Most industrialized nations already provide paid family leave. Mr. Chairman, we will do all we can to help enact your draft legislation in making this a reality.

We have been fortunate in the 110th Congress to have many issues advanced by NTEU that were introduced as legislation, and in most cases with bipartisan support. These include: Premium conversion to allow Federal and military retirees to use pre-tax dollars to pay for their health insurance premiums; recapture credit, allowing individuals who return to the Government service after receiving a refund of their retirement contributions to recapture credit for the service covered by that refund; annuity and part-time service, correcting the glitch in the 1986 law that changed that financial management that Congressman Moran spoke to. NTEU is supportive of that change, but we are concerned about the elimination of the retroactivity clause, and we will work with this committee and with Mr. Moran on that issue.

Pension offset and windfall elimination, changing the Social Security provisions that prevent Federal retirees from receiving the full Social Security benefits to which they are entitled; cost of health insurance, where there has been some discussion today already. NTEU continues to be very concerned about the escalating cost of health insurance for Federal employees, and we ask for your help in persuading the Office of Personnel Management to pursue two items that could lower health benefit premiums for Federal workers.

First, which was talked about earlier, the Medicare drug subsidy. If OPM had applied for the drug subsidy to which it is entitled under Medicare, it would have lowered the average 2006 FEHBP premium by 2.6 percent. We need a legislative measure to require OPM to apply for that subsidy.

Second, negotiating the drug prices. OPM negotiates with carriers for the best overall health care package, but the carriers negotiate for the best drug prices. We would like to see OPM negotiate for the drug prices, trying to bring those costs down.

In addition, we are working to achieve the passage of H.R. 1256 introduced by Congressmen Hoyer and Wolf, which would increase the level of Government contributions under FEHBP from 72 percent to 80 percent. Federal employees are paying a constantly increasing share of their paycheck for health insurance premiums for their families, often at the same time watching their coverage decline.

Since 2001, FEHBP premiums have risen by 50 percent. Had the OPM not dipped into the reserve funds for the current year, Federal participants would have realized increases, as we heard from Director Springer, of over 6 percent. Making FEHBP premiums more affordable is a priority for NTEU.

Finally, Mr. Chairman, in regard to the Federal Retirement Thrift Savings Plan, Congress established TSP investment policy by passing the Federal Employees Retirement System Act, which wisely left the management of the fund to the Thrift Investment Board, the only group that has a fiduciary responsibility to the fund's investors. They take it seriously, and that fund is a great success. We believe that they should take the lead in deciding on new investments in the future.

Thank you very much. I would be happy to answer any questions.

[The prepared statement of Ms. Kelley follows:]

NTEU
The National Treasury Employees Union

Statement of

Colleen M. Kelley

National President

National Treasury Employees Union

Subcommittee on Federal Workforce, Postal Service and the District of Columbia

Oversight and Government Reform Committee
United States House of Representatives

on

Federal Benefits: Are We Meeting Expectations?

August 2, 2007

Chairman Davis, Ranking Member Marchant, and distinguished Members of the Subcommittee, thank you for the opportunity to speak with you today about federal employee benefit and retirement programs. The question you ask, "Are we meeting expectations?" is a relevant and important question for the approximately 150,000 federal employees in 30 federal agencies and departments who are represented by the National Treasury Employees Union (NTEU), as it is for the Government in general. My name is Colleen Kelley and I am the National President of NTEU.

It's difficult to say that we are meeting expectations when every day federal employees are asked to do more with less and face an often hostile administration that does not seem to value the work that federal employees do. We appreciate those Members of Congress who put substantial time and effort into making the way easier for federal employees. There are some issues before this Congress that NTEU is actively working on and I would like to share some of them with you. First, I would like to address FEHBP, the Federal Employees Health Benefits Plan.

- **Increase coverage for dependents in FEHBP to age 25**: Young adults are the fastest-growing age group among the uninsured. While the current law provides health insurance until age 22, 22 year-olds are seldom in a position to obtain health insurance themselves. Several states have enacted new legislation to avert this health crisis. Utah recently changed its law so that a dependent may not age-out of health care coverage until their 26th birthday, regardless of whether they are enrolled in school. New Jersey provides coverage for dependents until their 30th birthday. Further, because young adults are healthier than older adults, it may be possible that adding more young adults to a pool of health care participants may even lower the average costs for group insurance. NTEU would like to see this change in FEHBP, and we appreciate your interest in this proposal.

- **Increasing the Government contribution to the Federal Employees Health Benefits Plan (FEHBP)**: H. R. 1256, introduced by Congressmen Hoyer and Wolf, will increase the level of Government contributions under FEHBP from 72 percent to 80 percent. Federal employees are paying a constantly increasing share of their paycheck for health care premiums for their families, often at the same time their coverage has declined. Unlike the private sector, or even state and local government employees, whose employers pay a greater share of the premium cost, the federal government's share continues to remain at 72 percent. For 2007, health insurance premiums increased an average of 2.3 percent, but since 2001, FEBHP premiums have risen by 50 percent. Had the Office of Personnel Management (OPM) not dipped into reserve funds for the current year, federal participants would have realized premium increases of nearly 7 percent. There are many federal employees who have left FEHBP, and in some cases the federal government, because they could not afford the health care premiums for their families. The importance of ensuring that the federal government continues to employ the best and brightest that our country has to offer cannot be underestimated in these difficult times. One way of doing that is to provide more affordable health care premiums to federal employees.

- **Medicare Drug Subsidy**: It is NTEU's position that OPM should apply for the drug subsidy to which it is entitled under the Medicare Prescription Drug, Improvement, and Modernization Act of 2003 (Pub.L. 108-173). According to GAO, if OPM had applied for the subsidy, it would have lowered the average 2006 FEHBP premium by 2.6 percent. Some of the individual health plans that serve a high number of retirees could have realized a slowdown in premium growth by as much as 3.5 to 4 percent. These savings could have been passed on to keep the enrollee portion of the premium down. According to the National Association of Active and Retired Federal Employees (NARFE), the agency could have left more than $1 billion on the table by forgoing the subsidy. NTEU would support legislative measures to require OPM to apply for the subsidy.

- **Negotiating Drug Prices**: We would like to see a thorough investigation into the issue of drug price negotiations. It is our understanding that OPM negotiates with carriers for the best overall health care package, but the carriers negotiate individually for the best drug prices. We would be happy to work with your committee to reopen the drug pricing discussion, perhaps find a creative way to bring down premiums.

- **Vision and dental care**: We were very pleased when vision and dental care was added to the benefits available to federal employees. We would like to see more federal employees take advantage of this benefit, but, sadly, some cannot afford to pay the entire premium amount. We would like to see legislation that would provide a government contribution to the vision and dental care benefit.

- **Premium conversion**: NTEU would like to see passage of H. R. 1110, sponsored by Rep. Tom Davis, and S. 773, introduced by Senator Warner this year. Both bills enjoy widespread bipartisan support. The bill would allow federal and military retirees to use pre-tax dollars to pay for their health insurance premiums, as active federal workers already do. Since October 2000, OPM has allowed active federal employees to use pre-tax dollars to pay these premiums. However, legislation is needed to treat federal and military retirees the same as active workers. During the past six years, cost of living adjustments have ranged from 1.3 to 3.5 percent for retirees, yet health care premiums have risen by more than 50 percent. Passage of this legislation will help relieve the expense federal retirees are absorbing to pay for their health care costs.

Administration Proposals

We appreciate Congress's help in defeating two administration proposals that would have seriously affected the integrity of the FEHBP. One such proposal was to expand the use of Health Savings Accounts (HSAs). Businesses have been promoting the benefits of HSAs and it's easy to see why. HSAs can shift some costs to employees, lowering costs for employers. However, HSAs require a significant amount of luck by the employee. If you keep yourself healthy, you may realize some savings, but if catastrophe strikes and you haven't adequately funded your HSA, you may have to pay significant additional health expenses out of pocket before reaching your annual cap. This is not mentioned clearly in OPM's materials on HSAs, by the way. In addition, if healthier workers choose HSAs, then the health plans will be left with an older, sicker pool of people (See GAO report, GAO-06-1133T). The increased exposure to risk is not in the best interests of federal employees.

The other Administration proposal I would like to mention is one that was buried in the budget submission, referred to as a "technical change". It was not technical. It was unconscionable. The proposal to reduce the federal subsidy for the FEHBP program for retirees with between five and ten years of service would hinder efforts to recruit the very group we are trying to attract. With unprecedented retirements looming in these next few years, the Government will need mid-career professionals. The federal subsidy for health insurance is a benefit that can be touted to this group. NTEU is opposed to reducing this subsidy.

Other Benefits

There are other significant initiatives in Congress right now that NTEU is pursuing.

- **Parental Leave**: NTEU has long been an advocate for parental leave, and was instrumental in the successful passage of the Family and Medical Leave Act of 1993. When it was passed, it was viewed as an important step in helping Americans balance family needs and work needs. Since that time, it has become clear that many who would take advantage of time off to care for a baby have not because they were unable to forgo their income. A benefit that you cannot take advantage of is not much of a benefit. It is time for the Federal Government to step up and make family leave real, not a mirage that few can afford to use. This is an opportunity to provide Federal workers with a benefit that not only helps them, but helps society in general, by offering a chance for a mother and father to bond with his or her child.

  Most industrialized nations already provide paid family leave. Some 128 countries now provide paid leave. The average amount of paid leave is 16 weeks. We applaud the efforts of Congresswomen Maloney and Woolsey and Senator Stevens for the introduction in this Congress of bills to create paid family leave. Most especially, Mr. Chairman, we would like to thank you for working with NTEU to make paid parental leave a reality.

- **Recapture credit**: Congressman Moran's bill, H. R. 2533, (introduced with Reps. Wolf, Wynn, Norton and Van Hollen) will allow individuals who return to Government service after receiving a refund of retirement contributions to recapture credit for the service covered by that refund by repaying the amount that was received, with interest. As mentioned above, there is a need to attract older workers.

- **Annuities and part-time service**: NTEU would also like to thank Congressman Moran for introducing H. R. 2780 which will correct a glitch in a 1986 law that changed the formula calculation for retirement annuities for individuals with part-time service. Thousands of civil servants who are eligible under the Civil Service Retirement System (CSRS) and have worked part-time in their careers are in jeopardy of losing credit for the years they worked full-time. I have long supported correcting this problem which affects employees who choose to work part-time, often because of family obligations or illness.

- **Pension Offset and Windfall Elimination**: Other provisions that NTEU would like to see passed in this Congress are changes in the Government Pension Offset (GPO) and the Windfall Elimination Provision (WEP), Social Security provisions that prevent federal retirees from receiving the full Social Security benefits to which they are entitled. Legislation this year has been introduced by Rep. Howard Berman (H. R. 82), Sen. Feinstein (S. 206), and Sen. Mikulski, (S. 1254). We thank them for their untiring efforts to overcome this inequity.

- **TSP Changes**: As you know, NTEU is a member of the Employee Thrift Advisory Council (ETAC) at the Thrift Investment Board. We endorse the legislative proposal that the Thrift Board is pursuing that will authorize automatic enrollment of all newly hired federal employees and to change the Thrift Savings Plan (TSP) default fund for new enrollees from the G Fund to the L Fund. The statistics kept by the Board have been very helpful in fine-tuning the TSP for the benefit of all employees.

Incentives

I will just mention two more incentives that NTEU would like to see used more frequently for federal workers: student loan repayments, and telework enhancement. Senator Stevens has introduced S. 1000, a bill that will force the establishment of a telework policy at every Executive agency, with reporting requirements. Telework is the wave of the future, and perhaps with passage of this bill, the reluctance seen on the part of many agencies within the Government will be diminished.

We have been talking about student loan repayment for a long time, but still very few people seem to know that this incentive exists. As our federal workforce retires out, we must be smarter in our recruitment to replace them. The authority to repay federally insured loans is one agencies should be persuaded to use. Sadly, these programs often lack sufficient funding. I would like to ask you, Mr. Chairman, to help us find a way to persuade agencies to use the tools we already have to keep our workforce at a sufficient level to carry on our nation's work. I would be happy to answer any questions that you have.

Mr. DAVIS OF ILLINOIS. Thank you very much.
We will go to Mr. Cox.

STATEMENT OF J. DAVID COX

Mr. COX. Thank you, Mr. Chairman and members of the subcommittee, for the opportunity to testify today.

Federal employee benefits need to be considered in the context of overall compensation. The shortcomings in Federal salaries make it increasingly difficult for Federal employees to afford the cost of fully participating in all the benefit programs made available to them through OPM. The list of benefits available for Federal employees sounds impressive. The new list of new benefits sounds pretty impressive, too, until you realize the new benefits are all employee pays all.

But this approach is just the logical conclusion of the attitude OPM currently has toward all Federal employee benefits. This attitude is that benefits should be made available to Federal employees for purchase; that is, they should not be paid for by the employer. They seem to think that at most the employer should negotiate a group discount. This has been the case with long-term care insurance, as well as the newest benefits for vision and dental insurance.

AFT strongly opposes OPM's approach. Until major national health care reform is enacted, we believe that it is our employers' responsibility to finance coverage generously enough so that every Federal employee and retiree and all their dependents have comprehensive and affordable coverage. This means financing at the rate of at least 80 percent so that even the lowest-rated Federal employees can afford coverage for themselves and their families.

We also believe that dental and vision coverage are fundamental components of health care, and it is a disgrace that Federal Government has carved out these two categories of coverage into separate employee-pays-all plans.

Comprehensive dental and vision belong in a standard benefits package that should be required offering in the Federal Employees Health Benefits Program and should be subsidized at the same rate as other health care services.

In 2000, OPM initiated long-term care insurance as a first employee-pays-all benefit, or pseudo-benefit. Then came the Bush administration, and this time the employee-pays-all insurance idea was applied to health care benefits previously considered part of a comprehensive package and subsidized at the same rate as other health care services. Although the plans that provide vision and dental benefits have not yet dropped this coverage, enrollees are bracing for this eventuality, as coverage of these services is not included in the statutory requirements for benefits.

AFGE opposes the carve-out of dental and vision coverage in the strongest possible terms. Both dental and vision care are fundamental to good health and to the ability to function in any work environment. Earlier this year, we became aware of not only a tragic consequence that happened of lack of access to dental care, but also how closely dental illness is linked to other illnesses. In March, a 12 year old boy from Prince George's County, MD, died from an infection that started in an abscessed tooth. The infection spread to the boy's brain and, for the want of dental care, a completely preventable death was not prevented.

Corrected vision and healthy gums are not cosmetic electives. This is not about tinted contact lenses or bleached teeth; this is about health care.

AFG urges Congress to add language to Chapter 89 of Title 5 to make vision and dental coverage mandatory categories for the Federal employee health benefit plans. OPM has carried out the Bush administration's health care policy by shifting costs to enrollees and trying to persuade them to replace traditional insurance with health savings accounts. In addition, the administration has each year included in its budget proposals policies that would require employees to pay more or receive less. Worse, it has promoted carving out benefits currently subsidized by the Government and offering them on an employee-pays-all basis.

None of these policies is consistent with an effort to recruit the next generation of Federal employees or to maintain morale and commitment among those on board. AFG urges Congress to resist the administration's efforts to undo a generation's progress and establish the Federal Government as a fair employer and provide decent benefits sufficient to provide economic security to its employees and retirees.

This concludes my statement. I would be glad to take any questions, sir.

Mr. DAVIS OF ILLINOIS. Thank you very much, Mr. Cox.

Ms. Baptiste.

STATEMENT OF MARGARET BAPTISTE

Ms. BAPTISTE. Mr. Chairman, I am pleased to present NARFE's views on the Federal retirement benefit programs which are so crucial to the economic and health care security of our Federal employee, retiree, and survivor members. Our primary legislative objective is to preserve the retirement and insurance benefits we earn as part of the total compensation packages of careers in Federal service.

Clearly, it is essential that Federal service attract and retain the highest caliber employees as new challenges put new pressures on the Federal budget, yet it also is imperative that the Federal Government continue to honor its commitments to its workers and retirees. Among those commitments is the Federal Employees Health Benefits Program, a program cited by many policy experts as a model group health insurance plan.

I cannot pass up this opportunity to thank Congressman Tom Davis and the majority of the members of this subcommittee for the introduction and support of H.R. 1110, the NARFE-backed bill to extend to retirees the tax benefit of premium conversion which executive and legislative branch employees have had for several years. This clarification of the tax code would be a modest step in making annuitants' FEHBP premiums more affordable.

I hope that by working together we can move this legislation out of the Ways and Means Committee toward enactment in this Congress.

The Office of Personnel Management does a good job of negotiating premiums for the FEHBP, but we are concerned that a $1 billion payment which could be used to lower costs is left on the table. The 2003 Medicare law provided all employers, including to Government, a subsidy if they provide drug coverage as generous as Medicare. Unfortunately, the administration has decided to forego this payment on behalf of FEHBP enrollees.

A recent GAO report found that premium growth in one of the largest FEHBP plans, with many older enrollees, could have been 3.5 to 4 percent lower in 2006 had the payment been accessed, and it could have reduced overall FEHBP premiums for the year by more than 2 percent. We cannot understand why the administration failed to apply for this subsidy, to which they did not originally object.

In addition, NARFE is concerned that offering health savings accounts could undermine the FEHBP. GAO data has strengthened our belief that healthier, wealthier enrollees tend to be attracted to HSAs because, as low health care users, they can be rewarded with unspent balances at the end of each year. Less-health enrollees avoid them and are more likely to stay in traditional, comprehensive plans, forcing these plans to raise premiums, cut benefits, or both.

So far, HSAs have had minimal effect on comprehensive plans because few have joined them. The administration's 2008 budget could jump start enrollment in HSAs if Blue Cross/Blue Shield is allowed to offer them in the FEHBP. Their brand loyalty and marketing resources could significantly increase HSE enrollment if they offered such an option in the FEHBP, and if an additional indemnity HSA also should be added, as the administration has suggested.

NARFE opposes any further expansion of HSAs. HSAs are a solution in search of a problem. Prescription drugs, the greatest cost driver in FEHBP, are a problem in search of a solution.

FEHBP plans should be allowed to buy prescription drugs for enrollees at the discounts provided through the Federal supply schedule. This was considered as a pilot project, but the pharmaceutical industry refused to participate. New congressional support for allowing Medicare to directly negotiate drug prices makes it time to revisit this proposal.

Retirement income security is a critical part of our compensation package, and an integral part of retirement income planning is the option to select a survivor annuity. Survivor annuities go a long way in providing peace of mind to the loved ones of Federal retirees. I know because I am a survivor annuitant. When my husband elected a survivor annuity, the most he could provide was 55 percent in exchange for an 8.5 percent reduction in his own retirement.

NARFE believes a Federal employee should be able to elect a higher survivor amount if they pay the additional actuarial cost. To make this a reality, we ask you to support a budget neutral proposal allowing retiring employees to elect additional amounts in 5 percent increments up to a maximum 75 percent.

Unfortunately, certain CSRS retirees who work part time toward the end of their careers do not receive the full amount of the annuity they earned because of the application of a 1986 law. Current interpretation discourages many from working part time at the end of their careers and can result in annuities being reduced by 20 percent. President Bush's 2008 budget proposed using full-time equivalent salary to calculate the annuities of future retirees who work part time, but current retirees are left out of this plan. For that reason, NARFE had supported Representative Jim Moran's bill, H.R. 2780, but we were disappointed to hear from him today that retirees will be excluded from the part-time remedy in his amended bill.

On the other hand, we are pleased that retirees are being sought by agencies that want to re-hire them. We believe retirees interested in returning to Government service should receive the full salary of the job without any offset of their annuity. NARFE supports OPM's proposal to allow agencies to reemploy Federal retirees on a limited, part-time basis without this offset.

Mr. Chairman, we are pleased with the performance of the Federal Thrift Savings Plan and its management. We support a proposal to allow Federal workers to contribute bonuses into their TSP accounts and are pleased OPM also supports this.

Thank you for your support of Federal employee benefits and retirement programs as an investment in the Federal Government's most valuable asset, its human capital.

We stand ready to work with you and the administration to ensure that our retirement programs remain competitive, innovative, and a model for others.

Thank you.

[The prepared statement of Ms. Baptiste follows:]

STATEMENT BY
MARGARET L. BAPTISTE
PRESIDENT
NATIONAL ACTIVE AND RETIRED FEDERAL EMPLOYEES ASSOCIATION

TO THE SUBCOMMITTEE ON THE FEDERAL WORKFORCE, POSTAL SERVICE AND THE DISTRICT OF COLUMBIA
COMMITTEE ON OVERSIGHT AND GOVERNMENT REFORM
U.S. HOUSE OF REPRESENTATIVES

HEARING ON
FEDERAL EMPLOYEES BENEFITS AND RETIREMENT PROGRAMS

AUGUST 2, 2007

Mr. Chairman, on behalf of our nation's 4.6 million federal employees, retirees and survivors, I appreciate the opportunity to express the views of the National Active and Retired Federal Employees Association (NARFE) on federal employee benefits and retirement programs.

Our first priority in any discussion on this subject is the preservation of the earned economic and health security of federal workers, retirees and survivors. With your help, Mr. Chairman, and the dedication of many members of this committee from both sides of the aisle, the government has been held to its obligations to employees and retirees for over a decade.

The compensation we receive, both as employees and retirees, is an investment in a system that makes federal service attractive as a career for millions of Americans. The retirement and insurance coverage promised employees when they first come to work for our government are critical in attracting and retaining the brightest and the best to public service.

Today's challenges, both at home and abroad, continue to require the highest caliber of employees, making it essential that the government honor their commitment as the retirement of 77 million baby boomers places tremendous pressure on the federal budget. Fortunately, federal retirement will not be directly affected by the boom in the senior population, because the federal retirement population is a function of the size of the federal workforce, not the general population, and employee and government contributions are designed to ensure that the Civil Service Retirement and Disability Fund will run an indefinite surplus.

While federal retirement is not part of the problem, it could become part of a broad entitlement reform solution. In fact, during the budget crises of the 1980s and early 1990s, federal retirees and survivors lost $50 billion in deferred, reduced and canceled cost-of-living adjustments (COLAs) while 40 million Social Security beneficiaries never missed a dime's worth of COLAs. Federal employees and retirees have always been willing to make sacrifices, but let us not again repeat the mistakes of the past. Instead, let us ensure that the government honors its commitments to its own employees.

Federal Employees Health Benefits Program

One of those commitments is the Federal Employees Health Benefits Program (FEHBP). For almost 50 years, the FEHBP has minimized costs and provided a wide choice of comprehensive health insurance plans to nearly nine million federal employees, retirees and their families. Many health care policy experts cite the FEHBP as the best group health insurance plan in America today and believe it should serve as a model for others.

Indeed, NARFE has long held that, even in years of double digit rate hikes, the Office of Personnel Management (OPM) -- on behalf of the government as an employer -- does a better job negotiating premium increases than any other employer. But we can't say that everything is being done to contain premium growth when a $1 billion payment, which could be used to lower worker and annuitant premium costs, is left on the table.

The Medicare Modernization Act of 2003 (MMA) provides that all employers, including the government, who provide drug coverage to their retirees age 65 and older, at least as generous as the new Medicare Part D prescription drug plan, are eligible to receive a subsidy of 28 percent of the cost per enrollee for drug coverage. Unfortunately, the Administration has decided to forgo this payment on behalf of FEHBP enrollees.

In response, Senator Daniel Akaka asked the Government Accountability Office (GAO) to determine how FEHBP premiums would have been affected had the OPM applied for this subsidy.

In their January 2007 report (GAO-07-141), GAO found that premium growth in one of the largest FEHBP plans with a high share of older enrollees could have been 3.5 to 4 percent lower in 2006 had the payment been accessed. Additionally, the payment would have lowered the growth in premiums across all FEHBP plans for 2006 by more than 2 percentage points on average, from 6.4 percent to about 4 percent. GAO also wrote that, "Absent the drug subsidy, FEHBP premiums in the future would likely be more sensitive to drug cost increases than would be premiums of other large plans [state and local government and private employers] that receive the retiree drug subsidy for Medicare beneficiaries." The report said that prescription drug costs accounted for 34 percent of the increase in total expenditures per enrollee for the five largest FEHBP plans – the single largest cost driver -- between 2003 and 2005.

Federal workers, retirees and survivor annuitants, who often struggle to pay their increasing premiums, cannot understand why the federal government has failed to do what so many other employers have done to reduce this burden, especially when state and local governments don't think twice about accepting the payment.

The Administration's Objections

OPM has cited two reasons for the Administration's decision to forgo the payment.

First, they have said they did not need to take advantage of the payment since they have no plans to significantly change the drug coverage of federal annuitants age 65 and older. It is fair to say that other public and private employers who had no intention of reducing or ending their retiree drug benefits decided to apply for the payment anyway. Certainly, the Centers for Medicare and Medicaid Services (CMS) do not withhold the payment based on what they think an employer's behavior will be in response to the Medicare drug benefit and the employer payment. Stockholders and employees would be understandably furious if their company did not avail themselves of anything that could contain health care costs without sacrificing coverage.

Second, OPM claims that they do not believe it is appropriate for the federal government to be paying itself for this purpose. Nonetheless, what they do not say is payments to OPM, unlike other employers, would not result in a spending "outlay" under federal budget rules, since they remain within the government. Such "intragovernmental transfers" are not unusual. In fact, the federal government pays itself for the future retirement obligations when federal agencies make contributions from their appropriated salary and expense accounts to the on-budget retirement trust fund on behalf of their employees.

We also wonder why the Administration chose not to object to the payment much earlier. NARFE announced on June 17, 2003 that we would oppose the version of the Medicare Prescription Drug bill that was about to go to the House floor because of concerns that employers, including the federal government, might dump retiree drug coverage in response to the creation of a Medicare drug benefit. Then-Ways and Means Committee Chairman Bill Thomas and Health Subcommittee Chairwoman Nancy Johnson responded by clarifying in the House-passed legislation that the federal government, as an employer, would be eligible for the payment. Their change not only survived the legislative process; it was enhanced when state and local governments also were made eligible for the payment.

At no point during the consideration of MMA did the Administration oppose including the federal government among the eligible employers. Indeed, OPM and CMS staff met in 2004 to discuss how OPM would receive the employer subsidy and made arrangements to ensure that payments to OPM would be considered an intragovernmental transfer. That is why OPM's announcement in the 2005 FEHBP "call letter" that the Office would not apply for the payment came as a surprise and disappointment to us.

OPM has also said that the payment is unnecessary since FEHBP is already "heavily subsidized."

NARFE objects to this characterization because it implies that something federal employees and retirees earn is really welfare. The "government contribution," which is the statutory term used to describe the FEHBP employer premium share, is no different from any other form of earned compensation, like wages and retirement benefits. Moreover, we would think that the government would want to exercise the option of lowering the worker share of health premiums to attract a talented and skilled workforce, particularly as we respond to the human capital shortage precipitated by a growing wave of retirements.

NARFE is also concerned that the Administration's decision to forgo the payment further stacks the deck against federal workers whose jobs are considered for contracting out to the private sector. Contracting-out decisions are based on an assessment of the cost of having the government continue to perform a specific function against moving that work to the private sector. For that reason, private contractors who use the Medicare employer payment to lower their health insurance costs have an advantage in such competitions over federal agencies, who, by Administration policy, are barred from doing the same.

Health Savings Accounts

In addition, our Association has been concerned for over 12 years that offering the combination of Health Savings Accounts and High Deductible Health Plans (HSA/HDHP) could undermine the best group health care system in the country. The controversial option has more potential for separating healthy from sick enrollees than any other form of health insurance. Indeed, healthier enrollees tend to be attracted to HSAs and other consumer-driven financing schemes because, as low health care users, they can be rewarded with unspent balances or credits at the end of each year.

Less healthy enrollees avoid HSAs and consumer-driven plans because they could pay thousands of dollars in out-of-pocket costs. As a result, higher volume health care users are more likely to stay in traditional comprehensive plans. This phenomenon, called "adverse selection," forces traditional insurance plan carriers to raise premiums, cut benefits or both. NARFE concerns about HSAs were confirmed by a January 2006 GAO report (GAO-06-271), which found that HSAs tended to attract younger and wealthier FEHBP enrollees.

In addition, the nonpartisan Employee Benefit Research Institute (EBRI) reported in December 2005 that individuals with HSAs are "significantly more likely to spend a larger share of their income on out-of-pocket health care expenses than those in comprehensive plans," and that they were "significantly more likely to avoid, skip or delay health care because of costs than those with more comprehensive health insurance."

In 2006, only 0.2 percent of FEHBP participants were enrolled in an HSA or similar plan. If HSA enrollment continues to be low, the controversial options will have minimal effect on comprehensive plans. However, without precautions against HSA-inspired "risk selection," the new plans could result in higher premiums and lower benefits for enrollees in the FEHBP's comprehensive plans if large numbers of healthier enrollees migrate to HSAs.

The Administration's FY 2008 budget would give lackluster enrollment in HSAs a jump start by allowing Blue Cross/Blue Shield (BC/BS) to offer the controversial option in FEHBP.

The federal law which authorizes the FEHBP stipulates that one government-wide "Service Benefit Plan" offers two levels of benefits. BC/BS is the Service Benefit Plan. The budget recommends that the FEHBP law be amended to allow the Service Benefit Plan to offer three, instead of two, benefit levels which would enable BC/BS to offer a government-wide HSA/HDHP.

BC/BS's current health plans are the largest and most popular in the FEHBP. The insurance carrier's brand loyalty and considerable marketing resources could significantly increase HSA enrollment in FEHBP if they decided, and were allowed, to offer such an option.

What is new about this recycled proposal is that, in addition to BC/BS, the Administration says that the "Indemnity Benefit Plan" should provide HSAs as a system-wide option.

Despite being named in the law which authorizes FEHBP, the Indemnity Plan has not been available since Aetna left the program in 1990. The entry of a second large insurance carrier with an HSA option available to most enrollees could also boost participation in HSAs.

NARFE opposes further expansion of HSAs because they could increase premiums for comprehensive plans since relatively healthy enrollees with higher incomes could be siphoned off into HSAs.

Lowering FEHBP Prescription Drug Costs

While HSAs have been a solution in search of a problem, prescription drugs, as the single largest cost driver in FEHBP, are a real problem in search of solution. Pharmaceutical Benefit Managers (PBM) hired by most FEHBP plans have helped to contain costs, but their leverage to negotiate drug discounts from manufacturers is limited by their enrollment size. In other words, the potential buying power of nine million enrollees is fragmented into 284 separate plans offered by FEHBP. That's why FEHBP plans should finally be allowed to buy prescription drugs for their enrollees at the discount mandated by the Federal Supply Schedule (FSS).

OPM proposed in 2000 that the Special Agents Mutual Benefit Association (SAMBA), an employee organization FEHBP plan, be permitted to buy drugs off the Federal Supply Schedule for their participants as part of a two year demonstration program to determine if the arrangement was feasible for other FEHBP carriers. The agency cancelled the pilot project not long after it was announced, due to the pharmaceutical industry's refusal to participate. Drug companies argued they did not have to provide SAMBA drugs at the Federal Supply Schedule discount because, unlike Department of Defense and the Department of Veterans Affairs, the employee organization plan, while part of FEHBP, was not a government agency.

Given substantial congressional support for allowing Medicare to directly negotiate drug prices, it is time for this committee to revisit using the same leverage to make such coverage less expensive in the FEHBP.

Federal Retirement Annuity

Income security, along with health care coverage, is a critical part of the earned compensation of retired federal workers, and an integral part of retirement income planning is the option to elect a survivor annuity for one's spouse or certain other dependents. Survivor annuities have been providing peace of mind to the loved ones of federal retirees for decades. I know, because I am a survivor annuitant. When my husband, a Civil Service Retirement System (CSRS) employee, elected to provide a survivor annuity, the most he could provide for me was a survivor benefit which equaled 55 percent of his base annuity amount and accepting a reduction of about 8.5 percent in his own annuity. Under the Federal Employee Retirement System (FERS), retiring workers pay a flat 10 percent of earned annuity for a survivor annuity of no more than 50 percent of the unreduced amount.

The shortcoming in this arrangement is that federal employees do not have the flexibility to elect a higher percentage amount for their survivors. That's why NARFE supports a budget neutral proposal to provide retiring CSRS and FERS employees the option of electing, and paying the full actuarial cost of, additional survivor annuity amounts in 5 percent increments up to a maximum 75 percent of the employee annuity.

Assuming that the government employer would not take on any additional costs, the OPM has estimated that it would cost the retiring employee an additional 1.5 percent of earned annuity for each 5 percent increment in the survivor annuity.

We urge this subcommittee to consider amending the current "one size fits all" maximum allowable survivor benefit so that retiring workers can elect an amount which best suits their own family needs, without incurring additional costs to the retirement system.

Part-Time Inequity

Unfortunately, certain CSRS retirees who worked part-time toward the end of their careers do not receive the full amount of the annuity they earned because current application of a 1986 budget law has unfairly reduced it. The present interpretation of this statute discourages many federal employees from working part-time in the later years of their careers.

Federal annuities are calculated by multiplying the average three highest continuous years of salary, times years of service, by an accrual rate. As a result of the application of Section 15204 of the Consolidated Omnibus Budget Reconciliation Act of 1986 (COBRA) (P.L. 99-272), the annuities of many federal employees who worked part time in the final years of their careers are substantially lower than they should be. This reduction occurs when actual part-time wages received -- instead of the full-time equivalency of those earnings -- are used in the calculation to determine the employee's average highest three years of salary. The inequity does not affect employees who began working for the federal government after April 7, 1986, or who have no part-time service after that date.

I offer an example: Susan, employed by the Department of Defense as an Afghan Persian and Pashtu language expert, worked part-time during the last three years of her career before retiring in 1990 after 30 years of service. Like most workers, Susan reached her highest salary level (about $40,000 a year for a full-time worker as a GS-13 in 1988, 1989 and 1990) toward the end of her federal service. However, because her full-time equivalent salary was not used, Susan's annuity is significantly lower than another GS-13 colleague with fewer years of federal service who did not work part-time in the final years on the job.

We believe that thousands of federal employees who chose to make the transition to retirement by working part-time were needlessly penalized. Indeed, in some cases, annuities are 20 percent less than what they otherwise would be with proper calculation.

President Bush's fiscal year (FY) 2008 budget recognized this inequity and proposed using full-time equivalent salary to calculate the annuities of future retirees who work part-time towards the end of their service. We agree with the Administration's recognition that allowing employees to work part-time is a proven and successful management tool, particularly for workers near retirement who remain on the job and continue to contribute their skills, talents and experience. Unfortunately, the Administration's proposal falls short. It would leave in place the inequity for current retirees whose annuities have been lowered as a result of the interpretation of the 1986 budget law.

For that reason, NARFE supports Rep. Jim Moran's bill -- H.R. 2780 -- which applies the President's proposal to correct the annuities of affected current as well as future retirees. Fairness dictates this inclusion.

H.R. 2780 would alleviate any potential administrative complication, putting the burden on annuitants to identify themselves as eligible for the correction rather than directing OPM to seek them out. Upon enactment, annuitants would have 18 months to apply to OPM for a prospective recalculation of their annuity under the clarified law. H.R. 2780 would require that the newly calculated amount become effective only for annuity payments made **after** the annuitant applied to OPM for eligible application of the corrected law.

NARFE agrees that removing the obstacle that prevents current federal workers from working part-time is particularly important to retaining skilled staff. Still, we feel any correction to this inequity must be extended to those unfairly penalized by the misapplication of this law. Who wants a job with an employer that treats their workers and retirees unfairly?

Reemploying Annuitants

While NARFE is disappointed by the Administration's reluctance to fix the part-time inequity for current retirees, we are pleased that their contributions to our nation are being recognized by federal agencies who rehire them because their skills and talents are needed back in the workforce.

We believe that federal retirees who are interested in returning to government service ought to be able to receive the full salary of their new job without any offset as the result of the retirement annuity they earned through their prior federal service.

NARFE's retired members count among our rank agency managers and line supervisors, security specialists, computer programmers, air traffic controllers and law enforcement personnel with special skills and experience. During the next 10 years, 60 percent of the federal workforce will be eligible to retire. Retirements have already created workforce shortages and deprived some agencies of employees with critical and specialized skills. Some feel compelled to return to federal service, particularly when they know their talents could be used to respond to a national emergency. For those capable and willing to give more in answer to this call, laws, regulations and the manner in which they are applied must not be an impediment to accessing their talents.

For that reason, we support OPM's proposal to allow federal agencies to reemploy federal retirees on a limited, part-time basis without offset of annuity from salary. This plan is a welcomed expansion of existing reemployment authority.

We commend OPM, and Members of Congress who are supporting this proposal, for your interest in enabling annuitants to return to federal service where and when needed, and we look forward to working with you.

Thrift Savings Plan

Mr. Chairman, we continue to be pleased with the performance of the federal Thrift Savings Plan and its management by the Federal Retirement Thrift Investment Board (FRTIB) and its staff, which has acted as a dutiful fiduciary on behalf of federal workers and retirees.

NARFE worked with key legislators to write the law that created TSP and FERS in 1986 and we are also members of the Employee Thrift Advisory Committee which meets with the FRTIB executive director and his staff on a regular basis to consider the operations and investment policies of the plan.

For several years, we have worked with Congress and the FRTIB on legislation to conform TSP regulations to Internal Revenue Service rules on other qualified retirement savings plans such as 401(k)s.

As an improvement to TSP, NARFE supports a proposal to allow federal workers to contribute bonuses into their tax-deferred accounts, and we were pleased when OPM announced their support for this enhancement. We acknowledge that bonus investments would not be exempt from IRS retirement contribution limits, and would not be eligible for any government/employer matching contributions otherwise available to Federal Employee Retirement System (FERS) workers. For instance, if such a proposal became law this year, TSP participants already making the maximum contribution ($15,500 for workers 49 years old and younger, and $20,500 for those 50 and older) would not be able to deposit a bonus in their account. However, allowing the deposit of bonuses for civilian participants would be helpful for those who contribute under the current limits.

Conclusion

In sum, NARFE applauds your support of federal employee benefits and retirement programs as an investment in the federal government's most valuable asset – its human capital. We support improvements to our earned compensation so long as they are genuine enhancements, contain costs without sacrificing quality and, most of all, do no harm. And while we represent both current federal employees and retirees, NARFE wants to ensure that the dedication of those who have already spent decades in public service are not forgotten and that the entire federal family is treated equitably. We stand ready to work with this panel, others in Congress and the Administration, and to find the ways and means to ensure that federal benefit and retirement programs remain competitive, innovative and a model for other employers to follow.

Mr. DAVIS OF ILLINOIS. Thank you very much.

Mr. Marchant, I will go to you first.

Mr. MARCHANT. Thank you very much for your testimony. I am on a learning curve on this subject, so I have a few questions.

I come from a Texas system. I spent 18 years in the this legislature, and actually served on the Pensions Board and the Pensions Committee, so I am still trying to digest and understand the Federal system.

We do have a 25 year old provision in our insurance, and that is why I am not on Federal insurance. I am a retiree from Texas and my family and I are still on the Texas insurance as a retiree, mainly because I have two kids under the age of 25.

Have you been able to get an actuarial study done? I know that when the kids go out at age 22 and 23 that their insurance is cheaper. Have you been able to get some kind of a study or anything in your hands that will show that there might even be a premium lowering?

Ms. KELLEY. Actually, I am aware of a study that OPM did, but I would call it kind of a back-of-the-envelope calculation. It was a three-page report, and I think it would be very helpful and beneficial if there were a better look taken, a closer look, to see what the actual numbers would be, and also to make sure that all of the costs and benefits are considered in the calculation. I do not think that has been done to date.

Mr. MARCHANT. Yes. It may be a missed opportunity to broaden the pool and at least stabilize the premium.

Ms. KELLEY. I agree.

Mr. MARCHANT. The other aspect of it, I have opted to do a deferred retirement so that if I pass away my wife gets the retirement, but ours is a substantial decrease. It is about a 30 to 40 percent decrease with 100 percent replacement, so, Mr. Chairman, I am wide open to that idea. I think that we should explore it and I think it should be the prerogative of the retiree. Again, it would have to be actuarially sound, but I do know States that are funding their benefits out of an independent pool, not out of the budget, the operating budget, are doing that, and it is actuarially sound. So I would be a proponent of that.

Those are the two thoughts I had, Mr. Chairman. Thank you very much.

Mr. DAVIS OF ILLINOIS. Thank you very much.

Let me ask each one of you: do you have any recommendations or how would you improve the prescription drug benefit in the FEHBP?

Ms. KELLEY. Well, actually a number of us have mentioned the drug subsidy. I mean, from a cost perspective that is the complain that I hear all the time from enrollees in the plan. There just seems to be such a missed opportunity here that I don't understand why OPM has not taken advantage of, you know, with the opportunity with the Medicare subsidy. I would hope they would just take it because it is the right thing to do, but absent that, again, I would hope that some legislation is passed that directs them to do it and requires them to do it. It is costing Federal employees money that they shouldn't have to pay.

Mr. COX. Mr. Chairman, as I shared with you, I worked for the Veterans Administration for 23 years. I believe AFGE has raised the issue on numerous occasions. Why can't Federal employees, their health insurance, bargain with the VA and those other entities that go out to the drug manufacturers and try to get the better prices? I mean, VA does very well with its drug buying, and I believe if you put that pool of several million Federal employees and retirees in that, that you certainly would have a much larger buying power and could certainly have a cost savings with that.

Mr. DAVIS OF ILLINOIS. Ms. Baptiste.

Ms. BAPTISTE. Well, as I said in my statement, Mr. Chairman, we believe strongly that the subsidy should have been taken, and I agree with Ms. Kelley on that. We also believe that the FEHBP plan should be allowed to buy prescription drugs at the discounts provided through the Federal supply schedule.

Mr. DAVIS OF ILLINOIS. How important would you say that vision and dental coverage are? Both of those I think have always been stepchildren, quite frankly, of health care delivery. We have reached the point where dental, vision, or mental health services have had the kind of attention that I think they have needed. Just the dental vision, how important do you think that is?

Mr. COX. Mr. Chairman, I would not be able to see you without my glasses on. I would not be able to read this paper. Vision is very, very important to all of us. Think what it would be like to not be able to see.

Dental, again, that is part of a healthy person. Your teeth are in your head that is next to your brain. You do not want infections in your teeth.

It is a shame that the Federal Government has not, again, with the many Federal employees and the retirees, had a program that required all of the participants in the Federal Employees Health Benefits Program, all the companies to offer dental and vision and to cover, like at 80 percent, to do that for them. That is how you have healthy people. It will save money in the long run because you keep people well and you prevent things.

I think of this 12 year old boy. That is a tragedy that should have never occurred in a country as great as this.

Ms. KELLEY. I think the numbers of enrollment for the first year in the vision and dental speak volumes to how important this is. Even with employees having to pay 100 percent of the cost, there were 700,000 Federal employees who signed up when it was first made available.

NTEU supported the introduction of a vision and dental plan for Federal employees, but we had also supported that it be done with some Government contribution, even if starting out it wasn't the full FEHBP contribution, some contribution, and we had hoped right up to the last minute that would happen.

Even in the end, when it was clear there would be no contribution by the Government, NTEU still supported these plans because we believed that they were important to Federal employees and that they would be taken advantage of. Like I said, I think for a first year enrollment that those numbers were higher than I expected, but they would have been much, much higher had there been any kind of contribution by the Government so that others who could not afford to pay the whole premium could do so.

Mr. DAVIS OF ILLINOIS. Ms. Baptiste, do you have any comment on that?

Ms. BAPTISTE. I agree with Ms. Kelley. It would put up the cost of enrollment a very considerable amount, but teeth and vision are important, and it is a subject that needs working on.

Mr. DAVIS OF ILLINOIS. Let me ask each of you, Ms. Kelley, are you familiar with community health centers?

Ms. KELLEY. I am not, Mr. Chairman.

Mr. DAVIS OF ILLINOIS. Mr. Cox, are you familiar with them?

Mr. COX. No, sir.

Mr. DAVIS OF ILLINOIS. Ms. Baptiste, are you familiar with community health centers?

Ms. BAPTISTE. No.

Mr. DAVIS OF ILLINOIS. Well, let me thank you all so very much in terms of, again, your patience and willingness to be here and to share your testimony with us. We appreciate it. Thank you very much.

Mr. COX. Thank you, Mr. Chairman.

Ms. KELLEY. Thank you.

Ms. BAPTISTE. Thank you very much, Mr. Chairman.

Mr. DAVIS OF ILLINOIS. The first shall be last, and the last shall be first, but in this one we will say that the third shall be last.

While our panel is assembling, let me just introduce them. Our panel consists of Ms. Hinda Chaikind, who is a Specialist in Health Care Financing at the Congressional Research Service [CRS], covering Federal employee health benefits, Medicare advantage, Medicare reform, Medicare spending, retiree health insurance, and other private health insurance issues. Prior to joining CRS, she was with the Department of Health and Human Services in the Office of the Assistant Secretary for Management and Budget, responsible for budgetary, legislative, and regulatory activity in the Medicare program.

Thank you so very much for being with us.

Ms. CHAIKIND. Thank you.

Mr. DAVIS OF ILLINOIS. Mr. Patrick Purcell is a Specialist in Income Security at the Congressional Research Service. He specializes in policy issues related to the Civil Service Retirement System, the Federal Employees Retirement System, the Thrift Savings Plan, individual retirement accounts, and 401(k) plans. He has previously worked at the Urban Institute, the Congressional Budget Office, and the Department of Health and Human Services.

Thank you both for being here.

It is our custom to swear in witnesses.

[Witnesses sworn.]

Mr. DAVIS OF ILLINOIS. Thank you very much. The record will show that each of the witnesses answered in the affirmative.

Of course, each of you know the drill with this, and so if you would summarize your statement, we will put the whole statement in the record, of course. Then we will have some questions after 5 minutes.

STATEMENTS OF HINDA CHAIKIND, SPECIALIST IN SOCIAL LEGISLATION, DOMESTIC SOCIAL POLICY DIVISION, CONGRESSIONAL RESEARCH SERVICE; AND PATRICK PURCELL, SPECIALIST IN INCOME SECURITY, DOMESTIC SOCIAL POLICY DIVISION, CONGRESSIONAL RESEARCH SERVICE

STATEMENT OF HINDA CHAIKIND

Ms. CHAIKIND. Mr. Chairman and members of the subcommittee, my name is Hinda Chaikind and I am a Specialist in health care Financing with Congressional Research Service. Thank you for inviting me to speak to you today about the Federal Employees Health Benefits Program and the Federal Employees Dental and Vision Insurance Program.

The Federal Employees Health Benefits [FEHB], Program covers about 8 million current full-time and part-time workers, Members of Congress, annuitants, and their families. Eligible family members include a spouse, unmarried dependent children under the age of 22, and continued coverage for qualified disabled children 22 years and older.

As Director Springer stated, in total there are about 300 different plan choices, including nationally available fee-for-service plans, locally available plans such as HMOs, as well as choices offered by plans for standard option, high option, and, since 2003, high-deductible health insurance plan options combined with a tax advantaged account.

Beneficiaries can use their tax advantaged accounts to cover qualified medical expenses. As a practical matter, depending on where an enrollee resides, his or her choice of plans is limited to about five to fifteen plans. Also, since July 2002, FEHB-eligible active employees can place their own pre-tax wages into a health care flexible spending account to cover qualified medical expenses.

Participation in FEHB is voluntary, and enrollees may change plans during designated annual open season periods. Special enrollment periods are also allowed for new employees and for those with a qualifying special circumstances such as marriage. Pre-existing condition exclusions are not allowed.

The Government's share of premiums is set at 72 percent of the weighted average premium of all plans in the program, not to exceed 75 percent of any given plan's premium. It is calculated separately for self only and for family coverage.

Part-time workers pay a larger share of their premiums, depending on the number of hours that they work. Annuitants and active employees pay the same premium amounts, although active employees have the option of paying premiums on a pre-tax basis.

Premiums in 2007, compared to the prior year, remain the same for about 63 percent of enrollees, and another 15 percent of enrollees had a premium increase of less than 5 percent. That said, while these overall increases are small, some plans did have large increases.

Although there is no core standard benefit package required for fee plans, OPM may prescribe reasonable minimum standards for health benefits. All plans cover broad categories of services, including basic hospital, surgical, physician, and emergency care. Plans are required to cover certain special benefits, including prescription drugs, mental health care with parity of coverage for mental health and general medical care coverage, child immunizations, and limits on an enrollee's total out-of-pocket costs for the year.

Plans must also include certain cost containment provisions, such as offering a preferred provider organization network and a fee-for-service plan.

Despite the wide range of plan choices, more than one-half of all individuals enrolled in a fee plan choose one of the Blue Cross and Blue Shield plans, and even those enrolled in other plans tend to remain in their plan from year to year.

Comparing the access and employer contributions for the benefits of Federal workers to those offered in the private sector provides some insight into how these benefits measure up. According to the Department of Labor's March 2006, National Compensation Survey, 71 percent of private sector workers have access to health benefit plans and 67 percent have access to prescription drug coverage. Access to health insurance in the private sector increases for firms with more than 100 workers, those who employ white collar workers, full-time workers, union workers, and those with average wages of $15 per hour or higher.

Private sector employers contributed an average of 82 percent of the health insurance premium for self only coverage, and an average of 70 percent of the premium for family coverage.

On average, 46 percent of private sector employees have access to dental care, and 29 percent have access to vision care. As required by statute, OPM created the Federal Employees Dental and Vision Insurance Program [FEDVIP], available since December 2006. Employees who are eligible to enroll in a fee program, whether or not they are actually enrolled, may also enroll in FEDVIP. Enrollees are responsibility for 100 percent of the FEDVIP premium. There are three nationally available vision plans, four nationally available dental plans, and another three dental plans that are only available regionally.

FEDVIP enrollment occurs during annual open season, as well as special election periods, and individuals may choose a self only, self plus one, or family plan. This set of options differs from the fee plans, which allows for two choices, self only or family plan.

Premiums vary by plan, by whether enrollment includes other family members, and residency. Unlike the fee plans, individuals enrolled in a nationwide FEDVIP plan, dental plan, pay different premiums depending on where they live. Active employees must pay FEDVIP premiums on a pre-tax basis. While there are no preexisting condition exclusions for this coverage, there are waiting periods for orthodontia, and switching to a new plan may require a new waiting period.

Finally, turning to current issues, Congress is considering legislation that encompasses a wide range of changes to the fee program, including but not limited to: Allowing Federal, civilian, and military retirees to pay health insurance premiums on a pre-tax basis; expanding the program to cover individuals who are not Federal employees, such as employees of small private businesses or, as the chairman has mentioned, employees of federally qualified health centers; expanding required benefits to include additional services such as hearing aids; increasing the level of Government contributions; eliminating the time limit on the continuation coverage for employees who leave Federal service; and requiring plans to establish and maintain electronic individual personal health records.

Other issues facing the program include maintaining the integrity of the risk pool eliminating fraud and abuse, and containing cost.

This concludes my statement. I would be happy to answer any questions that the members of the subcommittee might have.

[The prepared statement of Ms. Chaikind follows:]

United States House of Representative
Committee on Oversight and Government Reform
Subcommittee on the Federal Workforce, Postal Service, and the District of Columbia

Federal Benefits: Health, Dental and Vision Benefits

August 2, 2007

Statement of Hinda Chaikind
Specialist in Social Legislation
Domestic Social Policy Division
Congressional Research Service

Mr. Chairman and members of the subcommittee, my name is Hinda Chaikind and I am a specialist in health care financing with the Congressional Research Service. Thank you for inviting me to speak to you today about the Federal Employees Health Benefits program and the Federal Employees Dental and Vision Insurance Program.

FEHB Background

The federal government is the largest employer in the United States, and the Federal Employees Health Benefits (FEHB) program is the largest employer-sponsored health insurance program. FEHB covers about 8 million current workers, Members of Congress, annuitants, and their families. FEHB offers enrollees a choice of five fee-for-service plans available government-wide and another five plans available to employees of certain small federal agencies (such as the Foreign Service). In total, there are about 300 different plan choices, including all regionally available options, as well as choices offered by plans for standard option, high option, and high-deductible plans. As a practical matter, depending on where an enrollee resides, his or her choice of plans is limited to about five to 15 different plans. Plan details for all FEHB plans are available on the website of the Office of Personnel Management (OPM) — [http://www.opm.gov]. Beginning this year, those eligible for FEHB (whether or not they are actually enrolled) may also enroll in the Federal Employee Dental and Vision Insurance Program (FEDVIP), which provides supplemental dental and vision insurance.

Participation in FEHB is voluntary, and enrollees may change plans during designated annual "open season" periods. Special enrollment periods are also allowed for new employees and for those with a qualifying special circumstance, such as marriage. Contracts must offer enrollees and their family members temporary extension of coverage with an option to convert to a non-group contract, without requiring evidence of good health, for certain qualified employees who lose coverage because of a change in work or family status. Enrollees are not subject to pre-existing condition exclusions.

The government's share of premiums is set at 72% of the weighted average premium of all plans in the program, not to exceed 75% of any given plan's premium. The percentage of premiums paid by the government is calculated separately for individual and family coverage, but each uses the same formula. Individuals may enroll in an individual plan or a family plan, which covers 2 or more family members. Generally, premiums for family plans are more than double the premium for an individual plan. Part-time workers pay a larger share of their premium, depending on the numbers of hours that they work. Annuitants and active employees pay the same premium amounts, although active employees have the option of paying premiums on a pre-tax basis. Premiums in 2007, when compared to 2006, remained the same for about 63% of enrollees, and another 15% of enrollees had a premium increase of less than 5%. The average premium increase was 1.8%, with the enrollee's share increased by about 2.3% and the government's share increased by about 1.6 %. While overall, the increases are small, some plans have large premium increases. Furthermore, premium increases do not take into account any changes in benefits or cost-sharing in a particular plan from year to year.

Although there is no core or standard benefit package required for FEHB plans, OPM may prescribe reasonable minimum standards for health benefit plans. All plans cover broad categories of services, including basic hospital, surgical, physician, and emergency care. Plans are required to cover certain special benefits including prescription drugs (which may have separate deductibles and coinsurance); mental health care with parity of coverage for mental health and general medical care coverage; child immunizations; and limits on an enrollee's total out-of-pocket costs for a year, called the catastrophic limit. Generally, once an enrollee's covered out-of-pocket expenditures reach the catastrophic limit, the plan pays 100% of covered medical expenses for the remainder of the year. Plans must also include certain cost-containment provisions, such as offering preferred provider organization (PPO) networks in fee-for-service plans and hospital pre-admission certification.

<u>FEHB Plans</u>

FEHB statutes specify three types of participating plans:

- The **government-wide plan** is the fee-for-service plan that pays providers directly for services (this slot has always been filled by Blue Cross and Blue Shield).
- **Employee organization plans** are fee-for-service plans, such as the American Postal Workers Union (APWU) plan. All persons eligible to enroll in FEHB may choose an employee organization plan, subject to small annual membership dues.
- **Comprehensive medical plans** include the HMOs. Availability of these plans varies, depending on where the individual resides.

Deductibles, copayments, and coinsurance amounts vary across plans. Many plans offer two or more options with different premiums and levels of coverage. Even within individual plans, enrollees are offered a lower deductible and coinsurance amount if they choose to use services, such as a physician or hospital provider, in the plan's network. Additionally, when selecting out-of-network providers, beneficiaries may also be subject to balance billing amounts. Examining the premiums, deductibles, copayment and coinsurance amounts for physician office visits in the Blue Cross and Blue Shield (BCBS) plans provides an example of this variation. For 2007, BCBS offers both a *Standard* plan (its more generous plan) and a *Basic* plan. Under the *Standard* BCBS plan, in 2007, enrollees pay a monthly premium of $124.15 for individual coverage and $290.98 for family coverage, a slight decline from 2006 premium amounts. The 2007 calendar year deductible is $250 per person with a maximum family deductible of $500. Enrollees receiving services from a "preferred" provider are responsible for a $15 copayment for a physician office visit with no requirement to first meet the deductible.

For an office visit with a participating physician, enrollees are responsible for 25% of the plan's allowed amount, after meeting the deductible. For an office visit with a non-participating physician, enrollees are responsible for 25% of the allowed amount, after meeting the deductible, plus all of the difference between the allowed amount and the physician's actual charge.

Under the *Basic* plan, in 2007, enrollees will pay the same monthly premium amount as in 2006, $82.32 for individual coverage and $192.82 for family coverage. There is no calender-year deductible. Enrollees pay a $20 copayment for an office visit to a preferred primary care provider and a $30 copayment for an office visit to a preferred specialist. The *Basic* plan operates similarly to an HMO, in that enrollees may use only preferred providers to receive benefits, except in special circumstances such as emergency care.

High-Deductible Plans Combined with Tax-Advantaged Accounts

In 2003, FEHB began offering high-deductible plans coupled with tax-advantaged accounts that could be used to pay for qualified medical expenses. These plans are believed to help control costs by exposing enrollees to more risk for their health care expenditures. FEHB first offered this arrangement by combining a consumer-driven health plan (CDHP) with a Health Reimbursement Arrangement (HRA). In 2005, FEHB expanded this option to include a high-deductible health plan (HDHP) with either a Health Savings Account (HSA) or an HRA. Currently, both the employee organization plans and the comprehensive medical plans offer CDHPs and HDHPs. While CDHPs and HDHPs are both high-deductible plans, there are major differences between them, which are described below.

Consumer-Driven Health Plans -- For 2007, those choosing APWU's CHDP plan are provided with an HRA (referred to as a Personal Care Account, or PCA, in the APWU plan), which the plan funds in the amount of $1,200 for individuals and $2,400 for families. PCA funds are not taxable. Unused balances of a PCA may be carried over, with a limit of $5,000 for individuals and $10,000 for families, but balances are forfeited when an enrollee leaves the plan.

In APWU's CDHP, all eligible health care expenses (except in-network preventive care) are paid first from the PCA. Eligible expenses include basic medical, surgical, hospital, prescription drug and other services covered under the high-deductible plan, as well as dental and vision services (with a limit of up to $400 per year for self and $800 for family). Once the enrollee has spent the amount contributed by the plan to the PCA (i.e., $1,200 or $2,400), enrollees must pay the "member responsibility." This member responsibility ($600 for individuals and $1,200 for families) is similar to a deductible, except that it is not for first-dollar coverage. Members who have built up the balances in their PCA over time may use any excess funds to meet their member responsibility.[1] Once the deductible has been satisfied, the high-deductible plan starts covering services,

[1] For example, for individual coverage, if the PCA balance is $2,000, the individual could use $1,200 from the fund to pay for services and another $600 from the fund to meet the member responsibility. The enrollee would then qualify for coverage under the high-deductible health care plan while still retaining a PCA balance of $200.

with copayments and coinsurance amounts similar to those found in traditional health plans. The 2007 monthly premium for APWU's CDHP is $88.60 for self and $199.33 for family coverage, the same as in 2006. While enrollees may use either in- or out-of-network providers, the PCA funds will go further for in-network providers. For example, amounts over the plan allowance for out-of-network services do not count toward reducing the member responsibility.

In 2007, in addition to APWU's nationally available CDHP, two other plans, AETNA and Humana, also offer a CDHP. Although widely available, neither of these plans is nationally available. While these three plans are similar in many ways, there are some significant differences, including (1) the amount the plans place in the HRA, (2) the carryover amount, (3) rules for when the plan begins to cover medical expenses, (4) the catastrophic limit amount, and (5) availability. For example, AETNA's Medical Fund (similar to the PCA) is funded by the plan in the amount of $1,000 for individuals and $2,000 for families with a carryover limit of $4,000 for self and $8,000 for families.

High-Deductible Plans with an HSA or HRA – Since 2005, FEHB has offered several HDHP plans paired with either an HSA[2] or HRA, available both nationally and regionally for 2007. FEHB's HRAs coupled with the HDHP are similar to HRAs offered with CDHPs, in that they (1) cannot exclude FEHB-eligible individuals, (2) can only be used for medical expenses, (3) are not subject to tax, (4) are funded solely by the plan, (5) do not earn interest, and (6) are forfeited when an enrollee leaves the plan. However, FEHB's HRAs connected with HDHPs have no limits on carryover amounts, unlike the HRAs connected with CDHPs.

The rules for FEHB HSAs are very different. HSAs are only available to certain individuals: those who are not enrolled in Medicare, not covered by another health plan, not claimed as a dependent on someone else's federal tax return, and those who have not received Veterans Administration health benefits in the past three months. Enrollees may add additional funds to their HSA, as long as the plan's and the enrollee's combined contributions do not exceed the federal limit (for 2007, the limit is $2,850 for self coverage and $5,650 for family coverage). Enrollees over age 55 can make a "catch-up" contribution, in the amount of $800 in 2007. The plan's contribution to the HSA is tax-free, an enrollee's contribution is tax-deductible (an above-the line deduction, not limited to those who itemize), and any interest earned is tax-free. All unused funds, as well any interest, may be carried over each year without limit. In addition to qualified medical expenses, HSA funds may also be used to for non-medical expenses, subject to the income tax and an additional penalty for those under 65. Each month, the plan automatically deposits a portion of the FEHB HDHP premiums into an HSA or HRA. Individuals enrolled in an HDHP who are not eligible for an HSA, as of the first day of the month, have their funds credited to an HRA. Plans place the same amount into an enrollee's HRA as they do into an HSA.

There are also similarities and differences between the CDHP's and HDHP's high-deductible plans. Both may cover preventive services without first meeting a deductible, both operate similarly to traditional health care once the deductible has been met, both

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[2] For more information on HSAs, see CRS Report RL33257, *Health Savings Accounts: Overview of Rules for 2007*, by Bob Lyke.

save beneficiaries money for using in-network services, and both require higher deductibles and catastrophic limits than other FEHB plans. However, the CDHP's high-deductible plan only covers services after both the amount contributed by the plan for the year has been spent and the member responsibility/deductible has been met, while the HDHP begins to cover services once the deductible has been met. There are exceptions in both cases for preventive care. The minimum deductible for the HDHP is specified in law, as is the maximum catastrophic limit, while neither is specified for the CDHP.

Examining GEHA's HDHP provides an example of premiums, deductibles and HSA/HRAs for these types of plans. For 2007, the self coverage monthly premium is $95.20, the deductible is $1,500, the plan will place $90 per month in the HSA/HRA, and those in the HSA may contribute another $1,770 annually (the difference between the amount contributed by the plan and the federal self coverage limit). For family coverage in 2007, the monthly premium is $217.45; the deductible is $3,000; the plan places $180 per month into the HSA/HRA; and those with an HSA may contribute another $3,490 annually (the difference between the amount contributed by the plan and the federal family coverage limit). Enrollees over age 55 may also make "catch-up" contributions. While the premiums for GEHA's HDHP plan did not increase over the 2006 amounts, both the deductible and the amount contributed by the plan to the HSA/HRA increased.

Flexible Spending Accounts and Their Role in FEHB

Active federal employees (not annuitants) may participate in the federal Flexible Spending Accounts (FSA) program, consisting of a Health Care FSA and a Dependent Care FSA.[3] Contributions to an FSA are voluntary, with accounts funded solely by an employee from his or her pre-taxed salary, thereby reducing taxable income. The government does not make any contribution to the FSA. Funds in a Health Care FSA (HCFSA) can be used to pay for qualified medical expenses that are not reimbursed or covered by any other source. Qualified medical expenses include coinsurance amounts, copayments, deductibles, dental care, glasses, hearing aids, as well as certain over-the-counter medical supplies that are not cosmetic in nature. The FSA program provides a complete list of covered and non-covered medical expenses: [http://www.fsafeds.com].

Employees choosing to participate in an HCFSA must contribute at least $250 and no more than $5,000 per year to an account, and the total pledged contribution for the year is available at the start of the year. One significant limitation of the HCFSA is that funds can only be carried over for 2½ months after the end of the plan year (for example, 2007 contributions to the HCFSA may be used to reimburse expenses incurred during calendar year 2007 continuing through March 15, 2008). Unused funds are forfeited. During the annual FEHB open season, employees may voluntarily make an election for an HCFSA amount to be set aside in the upcoming year. Employees eligible for FEHB (even those not currently enrolled) may elect an HCFSA. Under Internal Revenue Code rules, only current employees and not annuitants are eligible to contribute to an HCFSA.

Individuals who are enrolled in either a CDHP or HDHP coupled with an HRA may also enroll in the HCFSA, as long as they are not annuitants. Individuals enrolled in an

[3] For more information on FSAs, see CRS Report RL32656, *Health Care Flexible Spending Accounts*, by Chris L. Peterson and Bob Lyke.

HSA may also enroll in a limited expense HCFSA (LEX HCFSA) that can be used to cover qualified dental and vision care. Individuals have to weigh the pros and cons of the LEX HCFSA coupled with an HSA against a standard HCFSA, choosing the one that best fits their needs, especially if they have a large expense that can only be covered by the standard HCFSA, such as a hearing aid. On the other hand, HSAs funds can be carried over from year to year, and some of the funding in the HSA comes from the plan.

Medicare and FEHB

Most federal employees or annuitants reaching age 65 qualify for Medicare. Federal workers and their employer each pay 1.45% of earnings. Individuals must have the required number of quarters of Medicare-covered employment to be eligible for Medicare Part A, Hospital Insurance (HI). Medicare Part B Supplementary Medicare Insurance (SMI) and Part D prescription drug coverage are voluntary, and qualified individuals choosing to enroll must pay a monthly premium. Generally, individuals who do not enroll in Parts B or D during their initial eligibility period are subject to a penalty. However, for Part B, individuals covered by an FEHB plan either through their own or a spouse's active employment (not annuitant coverage), may wait until either they or their spouse retires to enroll without incurring a delayed enrollment penalty. Upon retirement, individuals must enroll in Part B or be subject to a late enrollment penalty. For Part D, the prescription drug coverage included in FEHB plans is determined to be at least actuarially equivalent to Part D, on average. Therefore, if an individual maintains FEHB coverage and at a later date decides to enroll in Part D, there is no late enrollment penalty. The same rules for late enrollment penalties also apply in the private sector. Annuitants or former spouses may suspend FEHB enrollment to enroll in a Medicare Advantage plan (basically, a Medicare HMO or regional PPO), with the option to re-enroll in FEHB during open season, or sooner, if they involuntarily lose coverage or move out of the Medicare Advantage plan's service area.

Medicare is the primary payer for services provided to Medicare beneficiaries who are retired, even if they have retiree health insurance coverage through their former employer, such as FEHB. However, the rules for secondary coverage are different for Medicare beneficiaries who are working (often referred to as the "working aged") and offered health insurance through their employer. Employer-sponsored group health insurance, including FEHB, is generally the primary payer for individuals covered through their own or a spouse's current employment. Working aged employees have the option of accepting or rejecting the employer's coverage.

Additionally, the FEHB plan is eligible for the special subsidy payment to employers or unions offering qualified retiree prescription drug coverage. Qualified plans are defined as those offering drug benefits at least actuarially equivalent to "standard coverage. " and the prescription drug coverage offered in FEHB plans meets this standard. Subsidy payments are made on behalf of an individual covered under the retiree health plan who is entitled to enroll under a Medicare Part D prescription drug plan or a Medicare Advantage plan with prescription drugs, but elects not to. In 2007, subsidy payments will equal 28% of a retiree's gross drug costs between $265 and $5,350. OPM has opted not to take the subsidy payment. If it did accept the payment, it is unclear whether or not it would reduce the government's share of premiums, enrollee's premiums, or a combination of both. Employers in the private sector may use the subsidy payments as they choose. Subsidy payments to employers and unions are not subject to federal tax.

FEDVIP Background

As required by statute, the Office of Personnel Management (OPM) created the Federal Employees Dental and Vision Insurance Program (FEDVIP), available since December 31, 2006 to federal employees, Members of Congress, annuitants, and dependents. Enrollees are responsible for 100% of the premiums, and OPM does not review disputed claims. Employees who are eligible to enroll in the Federal Employees Health Benefits (FEHB) program, whether or not they are actually enrolled, may enroll in FEDVIP. Annuitants, survivor annuitants, and compensationers (someone receiving monthly compensation from the Department of Labor's Office of Workers' Compensation program) may also enroll in FEDVIP.[4] Eligible family members include a spouse, unmarried dependent children under age 22, and continued coverage for qualified disabled children 22 years or older. Former spouses receiving an apportionment of an annuity, deferred annuitants,[5] and those in FEHB temporary continuation of coverage are not eligible to enroll in FEDVIP.

There are four nationwide dental plans, and three additional dental plans that are only available regionally. The nationwide plans also provide coverage overseas. There are three vision plans, which all provide both nationwide and overseas coverage. Eligible individuals may enroll in a FEDVIP plan during the standard open season for FEHB plans. Coverage began on December 31, 2006. Individuals may change plans during open season each year, or following a qualifying life event. As with FEHB, new employees has 60 days to enroll. FEDVIP enrollment can be done through the Internet at [http://www.BENEFEDS.com], or, for those without Internet access, by calling 1-877-888-FEDS.

Individuals may choose a self-only, self +1, or a family plan. This set of options differs from the FEHB plans, which only allow for two choices: a self-only or a family plan. Individuals who choose to enroll in FEDVIP are not required to enroll in both a dental and a vision plan; they may choose only one type of coverage or both. Individuals are not required to enroll in the dental plan offered by their FEHB plan; for example, an individual whose health insurance is provided by GEHA may enroll in MetLife's dental plan and in FEP BlueVision (Blue Cross/Blue Shield vision plan). However, any coverage for dental and/or vision services provided under the individual's FEHB plan is the primary source of coverage, and the FEDVIP supplemental dental and vision plans pay secondary. Additionally, active workers (not annuitants) may still contribute to a Flexible Spending Account (FSA) to cover any qualified unmet medical expenses, such as dental copayments or deductibles.

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[4] Annuitants must have retired with an immediate annuity; those who have a deferred annuity may not be eligible to enroll in FEDVIP. However, unlike FEHB plans, one does not have to be enrolled in FEDVIP five years before retirement to continue enrollment into retirement.

[5] These are individuals who separate from federal service before they could retire and receive a deferred annuity at age 62. Individuals who retire with at least the minimum retirement age + 10 years of service and postpone receipt of an annuity can enroll in FEDVIP (as well as FEHB), when they begin to receive their annuity.

Premiums vary by plan, by whether the enrollment includes other family members, and by residency (for dental plans only). Unlike nationwide FEHB plans, individuals enrolled in a FEDVIP dental plan pay different premiums depending on where they live in the country or overseas. Active employees must pay FEDVIP premiums on a pre-tax basis (called premium conversion). Pre-tax premiums are not available to annuitants, survivor annuitants, or compensationers.

While there are no preexisting condition exclusions for this coverage, there are waiting periods for orthodontia. Individuals must be in the same plan for the entire waiting period, and switching to a new plan may require beginning the waiting period over again. There are no waiting periods for vision services. The statutes allow for more stringent waiting periods for individuals who do not enroll at their first enrollment opportunity. As these plans are new, it is too soon to know whether or not plans will use this authority. Enrollees pay less out-of-pocket costs if they use in-network services.

Deciding Whether or Not To Enroll in FEDVIP

Several factors are important to consider in deciding whether or not to enroll in FEDVIP, including: 1) coverage of these services in a FEHB plan — more likely for those enrolled in a Health Maintenance Organization (HMO), 2) likelihood of using services covered by the plans, and 3) placing the same dollar amount that would be used toward dental and/or vision benefits premiums in an FSA. Each potential enrollee must weigh these considerations and others against his or her own level of risk aversion, as well as the fact that the individual pays 100% of the premium.

Current coverage in a FEHB plan -- Under the FEDVIP program, coverage provided by an individual's FEHB health plan is primary, and the FEDVIP plans are the secondary payers. However, the nationally available FEHB plans, such as Blue Cross Blue Shield and GEHA, have limited dental and vision coverage. For example, the plans generally do not cover eyeglasses. They may have an arrangement with certain providers for discounted eyewear, but the enrollee would still be responsible for 100% of the discounted cost. In contrast, the FEHB HMO-type plans do offer more comprehensive dental and vision benefits. Some high-deductible plans also provide some coverage. It is important to compare FEHB coverage to determine if also enrolling in FEDVIP is beneficial. For example, M.D. IPA provides for eyeglass frames once every 24 months with copayments, and a $130 retail allowance. This is comparable to the FEDVIP vision coverage, although only one of the factors that needs to be considered.

Likelihood of Using Dental/Vision Services -- While some enrollees know that they will use services, such as the case of an individual who wears glasses or a dependent who will need orthodontics, some services cannot be as easily predicted, such as an individual needing a root canal. Individuals must weigh their expected benefits against the premiums. For example, an individual who wears glasses, has a yearly eye exam, and uses a provider in-network may find that paying the premium will result in lower costs than paying for each of these services separately, even with pre-tax FSA funds for employees. On the other hand, an individual who does not wear glasses may not benefit from vision supplemental insurance. There is not, however, a one-to-one correlation between buying any insurance and the expectation of using the services. There is still a large share of unknown risk that any insurance protects against, so that some individuals who do not anticipate using these services may find themselves needing the services and the coverage provided by these plans.

FEDVIP versus FSA (or Both) -- Both FEDVIP premiums and FSA contributions are pre-tax, so that employees (annuitants may not contribute to an FSA) may decide to enroll in one, none, or both. Enrollees who choose both can use funds in the FSA for any copayments, coinsurance amounts, deductibles, amounts exceeding annual or lifetime maximums, or amounts above the plan's payment for out-of-network services. Some individuals may decide that they prefer to only contribute to an FSA and not enroll in either the dental or vision plan, and instead use their FSA funds to pay for any dental or vision expenditures. While using FSA funds provides the most flexibility, it may be that the dental and vision premiums cover more than the same dollars in the FSA. Individuals who are not sure they will use the services provided under FEDVIP can "wait and see," and if they do not use dental or vision services, they can use the FSA dollars for other qualified medical expenses. Others may choose to enroll only in FEDVIP and minimize their out-of-pocket expenditures by staying in-network. Decisions about FEDVIP and FSA can be revisited every year during open season.

Comparing the FEHB and FEDVIP to Private Sector

Comparing the access and employer contributions for the health benefits of federal workers to those offered in the private sector, provides some insight into how these benefits measure-up. According to the Department of Labor's March 2006 National Compensation Survey, 71% of private sector workers had access to health benefit plans and 67% had access to prescription drug coverage. Access to health insurance in the private sector increases for firms with more than 100 workers, those who employ white-collar workers, full-time workers, union workers, and those with average wages of $15 per hour or higher. Private sector employers contributed an average of 82% of the health insurance premium for individual coverage and an average of 70% of the premium for family coverage. On average, 46% of private sector employees had access to dental care and 29% had access to vision care.

The percentage of employers offering retiree coverage has been declining since the late 1980s. The Henry Kaiser Family Foundation and the Health Research and Educational Trust 2005 Survey on Retiree Health Benefits, found that the percentage of firms with more than 200 workers offering retiree coverage fell by half between 1988 and 2005, from 66% to 33%. Furthermore, between 2004 and 2005, of the 300 firms in their survey with more than 1000 employees, 71% of those companies had increased the share of the premiums paid by the retiree, 34% had increased retiree coinsurance or copayments, 39% indicated that they had increased the amount enrollees pay for prescription drugs through increased drug copayments or coinsurance, and 12% had eliminated subsidized retiree health benefits for their new employees. Employers are also managing their retiree health insurance costs by providing different benefits for current and future retirees. Some employers who offer retiree health insurance to their current retirees will not provide coverage for individuals who retire in the future. Other firms may only provide group access to health insurance for future retirees, requiring them to pay 100% of the premiums. Firms may also use a sliding scale based on factors such as age at retirement, years of service at retirement, or a combination of the two to determine their premium contributions for retirees. According to 2004 Mercer National Survey of Employer-Sponsored Health Plans, 2004 Survey Tables, 28% of pre-Medicare retirees and 30% of Medicare-age retirees of firms offering retiree health based their share of premium contributions on age and years of service. Among large employers (500 or more employees) pre-Medicare retirees are more likely to pay 100% of their health insurance than their Medicare counterparts.

Issues

Finally, turning to current issues, Congress is considering legislation that encompasses a wide-range of changes to the FEHB program, including but not limited too: (1) allowing Federal civilian and military retirees to pay health insurance premiums on a pre-tax basis; (2) expanding the program to cover individuals who are not federal employees, such as employees of small private businesses or employees of Federally-qualified health centers; (3) expanding required benefits to include additional services, such as hearing aids and disease screenings; (4) increasing the level of government contributions; (5) eliminating the time-limit on continuation coverage for employees who leave federal service; and (6) requiring plans to establish and maintain electronic individual personal health records.

Other issues facing the program include maintaining the integrity of the risk pool, containing costs, and eliminating fraud and abuse. HSAs are often associated with attracting the healthiest individuals, altering the composition of the risk pools for other plans because these plans: (1) expose enrollees to more risk for their health care expenditures, at least up to the large deductible amount; and (2) generally have lower premiums than other types of health insurance. For the FEHB program, the structure of the premiums for these plans has worked to try to minimize both of these issues. For example, in the GEHA program, the premium for the HSA plan is set in-between the premiums for the high and the standard plan. Thus, the calculation of the federal contribution is not greatly affected by these plans, and the choice to enroll in one of these plans is not solely driven by lower premiums.

Containing costs, is not a unique problem for FEHB, but rather one that is faced by all employers who offer health insurance to their workers and retirees. Of particular concern to many employers is health insurance for their retired workers, and as discussed above, employer-sponsored retiree health insurance benefits are eroding as employers attempt to control their costs by tightening eligibility requirements and shifting costs to retirees through increased premium contributions, deductibles, and co-payment amounts.

Eliminating fraud and abuse is an effective tool for containing costs. For example, the pharmacy benefit manager Medco Health Solutions settled with the Justice Department to end the probe of allegations that they submitted false claims to the government, solicited and received kickbacks from pharmaceutical manufacturers to favor their drugs, and paid kickbacks to health plans to obtain business. They agreed to pay the United States $155 million and were required to enter into an extensive corporate compliance agreement of the Office of the Inspector general, Department of Health and Human Services and the Inspector General of the Office of Personnel Management.

For enrollees, FEHB's wide range of options allows them to use their own authority to hold down their health insurance costs, and because premiums are based on an average of all plan costs, individual decisions ultimately affect all enrollees. Eligible enrollees must weigh personal factors, such as how much of their wages they are willing to contribute to health insurance and how risk-averse they are to potential out-of-pocket costs. Choosing the best plan for their needs is a difficult task. However, FEHB-eligible individuals may revisit their decision every year during the annual open season. Individuals who find themselves with too much or too little risk, under- or over-coverage, and those whose health status changes, may change plans each year. In the past, however, there has been very little movement from one plan to another each year. More than one-half of all FEHB eligibles are enrolled in a Blue Cross and Blue Shield plan, and similarly those enrolled in other FEHB plans tend to remain in their plan from year to year. Perhaps this will change as more individuals become aware of the newer options.

This concludes my statement. I would be happy to answer any questions that members of the subcommittee might have.

Mr. DAVIS OF ILLINOIS. Thank you very much, Ms. Chaikind.
Mr. Purcell.

STATEMENT OF PATRICK PURCELL

Mr. PURCELL. Mr. Chairman, Ranking Member Marchant, thank you for inviting me to speak with you today about the Federal Employees Retirement System.

Federal employees are eligible for retirement benefits under either the Civil Service Retirement System [CSRS], or the Federal Employees Retirement System [FERS]. Employees hired in 1984 or later are covered by FERS; employees covered before that date are covered by CSRS, unless they switched to FERS in open seasons held in 1987 and 1998.

Today, about three-fourths of Federal employees are covered by FERS. This figure rises each year as employees under the old CSRS retire.

FERS was established under the Federal Employees Retirement System Act of 1986 and it consists of three elements: Social Security, a defined benefit pension called the FERS-based annuity, and the Thrift Savings Plan. Before 1984, Federal employees were not covered by Social Security, they were covered instead by the CSRS, which Congress created in 1920.

Because Social Security needed greater cash contributions to remain solvent, in 1983 Congress required Social Security coverage for all new Federal employees hired in 1984 or later.

Congress recognized that Social Security provided some of the same benefits as CSRS and that covering workers under both plans would require payroll deductions of more than 13 percent of pay. Therefore, Congress directed the development of a new retirement system with Social Security as the base, but also including a defined benefit pension and a savings plan. The result of this was the FERS Act of 1986.

Federal employees are fully vested in the FERS basic annuity after 5 years of service. The minimum retirement age, which was 55 for workers born before 1948, will increase over time to 57 for workers born in 1970 or later. This year a worker with 30 years of service can retire at age 55 and 10 months. Workers with 20 to 29 years of service can retire at 60, and workers with 5 to 19 years of service can retire at 62.

The FERS basic annuity pays a pension equal to 1 percent of the average of the three highest consecutive years of pay, so for a worker retiring at 55 with 30 years of service this annuity is equal to 30 percent of his or her high three pay. FERS also pays a supplement until age 62, which is equal to the amount of the Social Security benefit that the worker earned while employed by the Federal Government. The supplement ends at 62, regardless of whether the employee applies for Social Security at that age.

The legislative history of the FERS Act shows that Congress wished to enroll new employees in Social Security, to provide a benefit that in total was comparable to that under CSRS, and to make the FERS plan similar to retirement plans of large employers in the private sector. Thus, in establishing the FERS, Congress provided Federal employees the opportunity to save for retirement on a tax-deferred basis through the Thrift Savings Plan [TSP].

The thrift plan is similar to 401(k) plans provided by many companies in the private sector. This year employees under age 50 can contribute up to $15,500 to the TSP. Employees 50 and older can contribute an additional $5,000. These contributions are pre-tax, and investment earnings grow tax-free until the money is withdrawn.

The Government contributes an amount equal to 1 percent of pay to the TSP for all employees. In addition, employees covered by FERS receive a 100 percent match on the first 3 percent of pay they contribute and a 50 percent match on the next 2 percent contributed, for a total employer contribution of 5 percent of pay.

Currently, 86 percent of employees covered by the FERS contribute to the TSP, and the Thrift Board has submitted a bill to Congress to make enrollment in the TSP automatic for new Federal employees.

The pension benefits provided to Federal employees compare favorably to those provided in the private sector. Under FERS, employees participate in Social Security. They are covered by defined benefit pension, and they can save pre-tax through the TSP. This combination of benefits has become rare in the private sector.

The Department of Labor reports that only 51 percent of workers in the private sector participated in an employer-sponsored retirement plan of any kind in 2006, and just 20 percent of private sector workers were covered by defined benefit plans that provide a guaranteed retirement income.

The Labor Department estimates that only 12 percent of private sector workers participated in both a defined benefit plan and a 401(k) plan in 2006.

This concludes my statement, and I will be happy to answer any questions.

[The prepared statement of Mr. Purcell follows:]

United States House of Representatives
Committee on Oversight and Government Reform
Subcommittee on the Federal Workforce, Postal Service, and the District of Columbia

"Federal Benefits: Are We Meeting Expectations"

August 2, 2007

Statement of Patrick Purcell
Specialist in Social Legislation
Domestic Social Policy Division
Congressional Research Service

Mr. Chairman and members of the subcommittee, my name is Patrick Purcell and I am a specialist in income security with the Congressional Research Service. Thank you for inviting me to speak to you today about the Federal Employees' Retirement System and the Thrift Savings Plan.

CSRS and FERS

Retirement income for federal employees is provided through the Civil Service Retirement System (CSRS) and the Federal Employees' Retirement System (FERS). Most civilian federal employees who were hired before 1984 are covered by the CSRS, which is a defined benefit pension plan. Employees covered by CSRS do not pay Social Security taxes and are not eligible for Social Security benefits for their period of federal employment. Federal employees first hired in 1984 or later are covered by the FERS. All federal employees who are covered under FERS pay Social Security taxes and are eligible for Social Security benefits. Federal employees enrolled in either CSRS or FERS also may participate in the Thrift Savings Plan (TSP), which is a defined contribution plan. Only employees covered under FERS, however, are eligible for employer matching contributions to the TSP. Because the CSRS has been closed to new entrants for more than 20 years, and now covers less than a quarter of the federal workforce, this testimony focuses on the benefits provided under the Federal Employees' Retirement System.

Origin of the Federal Employees' Retirement System

Prior to enactment of the *Social Security Amendments of 1983* (P.L. 98-21), federal employees were not covered by Social Security. Federal employees were covered instead by the Civil Service Retirement System (CSRS), which was established in 1920. Because the Social Security system needed additional cash contributions to remain solvent, the 1983 Social Security amendments mandated coverage for civilian federal employees hired in 1984 or later.

Congress recognized, however, that Social Security provided some of the same benefits as CSRS. Moreover, enrolling federal workers in both plans would have required payroll deductions equal to more than 13% of employee pay. Consequently, Congress directed the development of a new federal employee retirement system with Social Security as the cornerstone and which would incorporate many features of the retirement programs typical among large employers in the private sector. The result of this effort was the *Federal Employees' Retirement System (FERS) Act of 1986*

(P.L. 99-335). FERS consists of three elements: (1) Social Security, (2) a traditional pension called the FERS basic retirement annuity, and (3) the Thrift Savings Plan.

Eligibility and Benefits under FERS

Two factors determine an employee's eligibility for a FERS retirement annuity: age and years of service. The amount of the worker's retirement annuity is determined by three factors: the number of years of service, the accrual rate at which benefits are earned for each year of service, and the salary base to which the accrual rate is applied.

Retirement Age and Years of Service under FERS

Federal employees are fully vested in the FERS basic retirement annuity after 5 years of service. A current or former federal employee with at least 5 years of service is eligible for a retirement annuity at age 62. A current or former federal employee with at least 20 years of service is eligible for a retirement annuity at age 60. The earliest age at which a worker can retire under FERS was 55 for workers born before 1948. The minimum retirement age under FERS for workers who reach age 55 in 2007 is 55 and 10 months, and it will reach age 57 for those born in 1970 or later. A worker who has reached the minimum retirement age and has completed at least 30 years of service can retire with an immediate, unreduced annuity.

An employee covered by FERS can retire with a *reduced* benefit at the minimum retirement age if he or she has completed at least 10 years of service. The retirement benefit is permanently reduced by 5% multiplied by the difference between 62 and the retiree's age at the time the annuity begins. For example, an employee with at least 10 years of service who retires at 55 would receive a pension benefit that is reduced by 35% below the amount that would be paid to an individual with the same salary and years of service who retired at age 62.

The basic retirement annuity under FERS is determined by multiplying three factors: the *salary base*, the *accrual rate*, and the number of *years of service*. The FERS *salary base* is the average of the employee's highest three consecutive years of base pay.[1] This is often called "high-3" pay.

The *accrual rate* is the pension benefit earned for each year of service, expressed as a percentage of the salary base. Under FERS, workers accrue retirement benefits at the rate of 1% per year. A worker with 30 years of service will have accrued a pension benefit equal to 30% of high-3 pay. For employees in FERS who have at least 20 years of service and who work until at least age 62, the accrual rate is 1.1% for each year of service.

Members of Congress, congressional staff, federal law enforcement officers and firefighters accrue benefits at higher rates than do other federal employees. Under FERS, Members of Congress, congressional staff, law enforcement officers, and firefighters accrue pension benefits at the rate of 1.7% per year for their first 20 years of service and 1.0% per year for years of service after the 20th

[1] This calculation is based on nominal or "current dollars" rather than indexed or "constant dollars."

year. These accrual rates yield a pension equal to 34% of the FERS salary base after 20 years of service and 44% after 30 years of service.

Early Retirement, Social Security and the "FERS Supplement"

Because Social Security retirement benefits cannot begin before age 62, Congress included in FERS a temporary supplemental benefit for workers who retire before age 62. This benefit, the "FERS supplement" is paid to workers who retire at the minimum retirement age or older with at least 30 years of service or at age 60 with at least 20 years of service. The supplement is equal to the estimated Social Security benefit for which the worker will become eligible at age 62, but is based *only* on the portion of Social Security payments that are attributable to the worker's years of federal employment. It is paid only until age 62, regardless of whether the retiree chooses to apply for Social Security at 62.

Cost-of-living Adjustments (COLAs)

Cost-of-living adjustments, or COLAs, protect the purchasing power of retirement benefits from being eroded by inflation. COLAs in the Civil Service Retirement System are equal to the change in the Consumer Price Index for Urban Wage and Clerical Workers (CPI-W). As a cost-control measure, when the FERS Act was passed, Congress provided for limited COLAs for the FERS basic retirement annuity. Under FERS, the basic annuity is fully indexed if inflation is under 2% per year and partially indexed if inflation exceeds 2%. If the CPI-W increases by up to 2%, then the FERS monthly benefit amount increases by the same percentage. If the CPI-W increases by 2% to 3%, the FERS annuity increases by 2%. If the CPI-W increases by more than 3%, the FERS annuity increases by the rise in the CPI-W minus one percentage point. As a further restraint on the costs associated with COLAs, FERS provides COLAs only to retirees who are age 62 or older, annuitants of any age who are retired by reason of disability, and to survivor annuitants of any age.

Employer and Employee Contributions toward the FERS Annuity

Federal agencies and their employees prefund the FERS basic retirement annuity through required contributions to the Civil Service Retirement and Disability Fund (CSRDF). By providing a continuous source of budget authority, the trust fund allows benefits to be paid on time, regardless of any delays that Congress may experience in passing its annual appropriations bills. Prefunding pension obligations also requires federal agencies to recognize the full cost of their personnel when requesting annual appropriations from Congress.

Workers covered by FERS are required to contribute 0.8% of pay to the Civil Service Retirement and Disability Fund toward the cost of their future pensions. Federal employees covered by FERS also pay Social Security taxes of 6.2% on salary up to the maximum taxable wage base ($97,500 in 2007). Members of Congress contribute 1.3% of salary to the CSRDF. Members of Congress also pay Social Security taxes. In FY2006, employee contributions to CSRS and FERS totaled $3.7 billion, equal to 4.2% of the total income of the fund.

Federal agencies contribute an amount equal to approximately 11.2% of payroll to the CSRDF, which is part of their annual appropriations from Congress. The CSRDF is required by law to invest all of its assets in U.S. Treasury bonds or other securities backed by the full faith and credit of the United States Government.

The other major sources of revenue to the CSRDF are agency contributions, contributions of the U.S. Postal Service on behalf of its employees, interest on the federal bonds held by the fund, and a transfer from the general revenues of the U.S. Treasury. This transfer is necessary because the costs of the older of the two federal retirement programs, CSRS, are not fully covered by employee and agency contributions. FERS benefits are required by law to be fully funded by the sum of contributions from employees and their employing agencies and interest earned by those contributions.

Total Cost of FERS Benefits

Actuaries calculate the cost of pension programs in terms of "normal cost." The normal cost of a pension plan is the level percentage of payroll that must to be set aside each year to fund the expected pension benefits that will be paid to all members of an employee group and their surviving dependents. Normal cost is based on estimates of attrition and mortality among the workforce, and estimates of future interest rates, salary increases, and inflation-based COLAs for retirees.

The Office of Personnel Management (OPM) has estimated the normal cost of the FERS basic annuity at 12% of payroll. Federal law requires agencies to contribute an amount equal to the normal cost of FERS minus employee contributions to the program, which are equal to 0.8% of payroll. Consequently, the normal cost of the FERS basic annuity to the federal government is equal to 11.2% of payroll. The federal government has three other mandatory costs for employees covered by FERS. Social Security taxes are 6.2% of payroll on both the employee and the employer up to the maximum taxable amount of earnings ($97,500 in 2007). All agencies automatically contribute an amount equal to 1% of employee pay to the TSP. Agencies also make matching contributions to the TSP. The normal cost of FERS to the federal government is therefore at least 18.4% of pay for the average employee. Federal matching payments to the TSP can add up to 4 percentage points to this total, depending on an employee's voluntary contributions.

The Thrift Savings Plan: An Integral Component of FERS

The Thrift Savings Plan (TSP) is a retirement savings plan similar to the "401(k)" plans provided by many employers in the private sector.[2] As of July 2007, the Thrift Savings Plan held more than $225 billion in assets and 3.7 million participants among the federal civilian workforce, the uniformed services, and former employees who continued to hold retirement assets in the TSP.

In 2007, federal employees under age 50 can contribute up to $15,500 to the TSP.[3] Employees age 50 and older can contribute an additional $5,000. For all federal workers covered by FERS, the

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[2] "401(k)" refers to the section of the Internal Revenue Code that authorizes deferral of income taxes on contributions to retirement savings plans.

[3] The annual limit on contributions is set in law at §402(g) of the Internal Revenue Code.

agency at which they are employed contributes an amount equal to 1% of the employee's base pay to the TSP, whether or not the employee chooses to contribute anything to the plan. In addition to the employing agency's automatic contribution of 1% of pay, employers covered by FERS receive dollar-for-dollar employer matching contributions on the first 3% of pay that they contribute and a 50% match on the next 2% they contribute, for a maximum employer contribution of 5% of pay.[4] Contributions to the TSP are made on a pre-tax basis, and the contributions and investment earnings are free from income taxes until the money is withdrawn from the account. All TSP participants are immediately vested in their contributions to the plan, all federal matching contributions, and any growth in the value of their investment from interest, dividends, and capital gains. They are fully vested in the 1% agency automatic contributions to the TSP after three years (two years for congressional employees and executive branch political appointees).

Federal employees are eligible to contribute to the Thrift Savings Plan immediately upon being hired, and they may transfer funds from an individual retirement account (IRA) or another employer's 401(k) plan into the TSP. Of the 3.7 million individuals with TSP accounts, approximately 2.9 million are currently contributing to the plan. Among current federal employees covered by FERS, 86% of those eligible to contribute in the Thrift Plan do so. In terms of both assets and number of participants, the Thrift Savings Plan is the largest employer-sponsored retirement savings plan in the United States.

The Thrift Savings Plan is administered by an independent government agency, the Federal Retirement Thrift Investment Board, which is charged in statute with operating the Thrift Plan prudently and *solely in the interest of the participants and their beneficiaries*.[5] The assets of the TSP are maintained in the Thrift Savings Fund, which invests the assets in accordance with participant instructions in five investment funds authorized by Congress to be included in the plan. TSP accounts are individually owned by the participants in the TSP in the same way that 401(k) accounts are owned by workers in the private sector.

Investment Options

As provided for in statute, TSP participants are offered five investment funds. Participants may allocate their contributions among any or all of the five investment funds, and they may reallocate their account balance among the five funds. One fund invests exclusively in U.S. government securities and the other four funds invest in private-sector stocks and bonds. The four funds that invest in private-sector securities are all index funds. These funds purchase securities in the same proportion as they are represented in an index of stocks or bonds, rather than through the decisions of an investment manager. Index funds have lower administrative costs than actively-managed funds, and because they purchase securities in the same proportion as they are represented in an index, there is little or no opportunity for the purchase of securities by the fund to be influenced by third parties who might benefit from having the fund invest in particular companies or sectors of the economy. In its annual report for 2006, the plan reported administrative costs of $81 million and

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[4] The formula for agency matching contributions is specified in law at (5 U.S.C. § 8432(c)).

[5] See 5 U.S.C. § 8472(h).

assets of $206 billion. Thus, the administrative expenses of the Thrift Plan were about 40 cents for each $1,000 invested.

The Thrift Board has contracted with Barclays Global Investors to manage the index funds in which TSP assets are invested. The five funds in the Thrift Plan are:

- the *Government Securities Investment Fund*, (the "G Fund"). The G fund invests only in U.S. Treasury Securities and other securities backed by the full faith and credit of the United States.
- the *Fixed Income Investment Fund*, (the "F Fund"). The F fund invests in a bond index fund that tracks the performance of the Shearson Lehman Brothers Aggregate (SLBA) bond index, consisting of government bonds, corporate bonds, and mortgage-backed securities.
- the *Common Stock Index Investment Fund* (the "C Fund"). The C fund invests in stocks of the corporations that are represented in the *Standard and Poor's 500* index in the same proportion as they are represented in that index.
- the *Small Capitalization Stock Index Investment Fund* (the "S Fund"). The S fund invests in the stocks of small and medium-sized companies incorporated in the United States. Stocks in this fund are held in the same proportion as they are represented in the *Wilshire 4500* index.
- the *International Stock Index Investment Fund* (the "I Fund"). The I fund invests in the stocks of foreign corporations represented in the Morgan Stanley Capital Investment EAFE (Europe, Australia-Asia, Far East) index.

In 2005, the TSP added five new "lifecycle" funds, which invest in the five authorized TSP funds in allocations that are based on the employee's expected date of retirement. These "L" funds include an income fund and four funds that allocate investments based on expected retirement dates of 2010, 2020, 2030, and 2040. By allocating assets based on expected date of retirement, the worker's assets are gradually moved from higher-returning but more volatile investments when they are young to lower-returning but more stable investments as they approach retirement age.

Participant Loans

Participants may borrow from their accounts. There are two types of Plan loans: general purpose and residential. General purpose loans can be obtained for any purpose, with a repayment period from 1 to 5 years. Residential loans can be obtained for the purpose of purchasing a primary residence, with a repayment period from 1 to 15 years. Participant loans may only be taken from participant contributions and attributable earnings. The minimum loan amount is $1,000. The interest rate for loans is the "G Fund" interest rate at the time the loan agreement is issued by the Plan's record keeper. The rate is fixed at this level for the life of each loan. Interest earned on loans is allocated to the participant account upon repayment. Participants whose loans are in default have until the end of the following calendar quarter to pay the overdue amount. If not repaid by that time, the loan plus accrued interest is treated as a taxable distribution to the plan participant, which may be subject to the 10% penalty on retirement plan distributions made before age 59½.

Benefit Payments

After leaving service, participants may elect benefit withdrawals in the form of a partial withdrawal or a full withdrawal as a single payment, a series of payments, or a life annuity. Participants may choose to combine any two, or all three, of the available withdrawal options. The Board has contracted with the Metropolitan Life Insurance Company to provide annuity products to Thrift Plan participants. The contract to issue Thrift Plan annuities is open to competitive bids every three to five years.

Communication and Education

The Thrift Board communicates with plan participants to help them better understand the investment choices, benefits, and administration of the TSP. Employing agencies distribute information, including the *Summary of the Thrift Savings Plan for Federal Employees*, which provides a comprehensive description of the Plan, as well as booklets describing the loan program, withdrawal programs, and annuity options under the plan. The Thrift Board also issues a quarterly newsletter, *TSP Highlights,* and quarterly participant statements. Participants also can obtain their account balances from the TSP web site, request contribution allocations and interfund transfers or, in some cases, loans and withdrawals. The web site also provides various calculators that can be used as retirement planning tools. TSP Bulletins are issued regularly to inform agency personnel and payroll specialists of current operating procedures. The ThriftLine, the Board's toll-free automated voice response system, also provides both general plan and account-specific information.

The Federal Retirement Thrift Investment Board

The Federal Retirement Thrift Investment Board was established by the FERS Act of 1986.[6] The Board is responsible for developing the investment policies of the Thrift Plan and overseeing the management of the plan, which is under the day-to-day direction of an Executive Director appointed by the Board. Three of the five members of the Board — including the Chairman — are appointed by the President. The President chooses a fourth member of the Board in consultation with the Speaker of the House and the House Minority Leader and a fifth member in consultation with the Majority and Minority Leaders of the Senate. Members of the Board serve 4-year terms and all nominations are subject to Senate confirmation. The law requires that all nominees to the Board must be individuals with "substantial experience and expertise in the management of financial investments and pension benefit plans."[7]

The authorizing legislation that established the Thrift Board defines the Board's authority and responsibilities, and provides for substantial independence of the Board from political pressures.

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[6] See 5 U.S.C. § 8472.

[7] See 5 U.S.C. § 8472(d).

Authority

The Thrift Board has the authority to:

- Appoint the Executive Director of the Thrift Plan;
- Remove the Executive Director for cause;
- Establish investment policies for the Thrift Plan;
- Instruct the Director to take whatever actions the Board deems appropriate to carry out the policies it establishes;
- Submit to the Congress legislative proposals relating to its responsibilities under federal law.

Independence

Members of the Board are nominated by the President and confirmed by the Senate, but once confirmed they cannot be removed from their 4-year terms without good cause. The selection and nomination process are designed to assure that Members of the Board are individuals who are supported by the President and Congress. They serve in times of good behavior, rather than at the pleasure of the President or Congress, assuring that they can carry out the responsibilities of their positions without risk of removal from office. The Federal Retirement Thrift Investment Board receives no appropriations from Congress. Administrative expenses are paid through agency-automatic contributions forfeited by employees who leave federal service before they have vested and charges against participant accounts.

Responsibility

The law requires that the members of the Board shall discharge their responsibilities solely in the interest of participants and beneficiaries. In practice, this means that the investment policies and management practices of the fund are evaluated by the Board exclusively in reference to the efficient and prudent management of the Fund's assets. This exclusive responsibility serves to further insulate the Board from pressures to adopt investment policies or management practices that might not be in the long-term interest of preserving and increasing the security and investment performance of the Fund's assets.

Oversight

To assure that the Members of the Thrift Board remain aware of the interests and concerns of Thrift Plan participants and beneficiaries, the authorizing legislation established the Employee Thrift Advisory Council. This 14-member council is appointed by the Chairman of the Thrift Board and must include representatives of federal employee and Postal Service labor organizations, managerial employees, supervisory employees, female employees, senior executives, and annuitants.

All fiduciaries of the plan, including members of the Thrift Board are required by law to be bonded.[8] The Secretary of Labor is authorized by law to investigate any suspected breach of duty by a fiduciary of the plan. The financial statements of the Thrift Board are audited regularly by an independent accounting firm. Congressional oversight of the Thrift Plan is performed by the House Committee on Oversight and Government Reform and the Senate Committee on Homeland Security and Governmental Affairs.

Legislation in the 110th Congress

TSP. The Federal Thrift Retirement Investment estimates that 86% of employees covered by FERS voluntarily contribute to the TSP. This is a high participation rate compared to private-sector 401(k) plans, in which participation rates of 70% to 75% are the norm. To boost participation rates, a growing number of employers in the private sector are adopting a policy of automatically enrolling new employees in their company 401(k) plan, with the option that those who wish to do so can drop out of the plan. The Thrift Board recently transmitted to Congress proposed legislation that would allow for automatic enrollment of new federal employees in the TSP. The contributions of those so enrolled would be diversified among the TSP's various investment funds.

FERS. Federal employees contribute 0.8% of pay to the Civil Service Retirement and Disability Fund toward their FERS basic annuity. They become vested in this benefit after five years of service. Employees who leave the federal government and who leave their contributions in the CSRDF retain credit for their service and if they later are re-employed by the federal government, this prior period of federal service counts toward both the establishment of eligibility for a FERS annuity and in the computation of the annuity. Departing employees who withdraw their contributions forfeit their credit toward a FERS annuity. If they are later re-employed by the federal government, they are not permitted to re-deposit into the CSRDF the amounts that they had previously withdrawn. **H.R. 2533**, introduced by Representative Moran, would allow federal employees who were formerly employed by the federal government and who withdrew their contributions to the FERS basic retirement annuity upon their separation from service to redeposit those contributions, plus interest, to regain credit toward the FERS basic retirement annuity that they earned during their prior period of federal employment

CSRS. Federal employees with permanent appointments earn credit toward a retirement annuity under either CSRS or FERS whether they work full-time or part-time. Under FERS, the amount of the annuity is based on the pay applicable to the position in which the individual is employed and the computation of the retirement annuity is simply prorated for actual hours worked. Under regulations adopted by the Office of Personnel Management, however, the retirement annuities of workers covered by CSRS whose career includes a period of part-time work may be reduced not only through the pro-rating for reduced hours of work but also through the computation of the individual's high-three average pay. **H.R. 2780**, also introduced by Representative Moran, would change the computation of CSRS annuities for workers whose careers include a period of part-time work so that the annuity is prorated for hours worked and the average pay used in the

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[8] A "fiduciary" is a person in a position of trust or confidence with regard to the property of another. A "bond" is form of insurance against the potential malfeasance of a plan fiduciary.

computation of the annuity is the pay applicable to the position in which the individual is employed. This would conform the computation of CSRS annuities for part-time workers to the process currently applied under FERS. H.R. 2780 also would allow CSRS retirees who worked part-time to apply for a re-computation of their annuity.

Conclusion

The pension benefits provided to federal employees compare favorably to those available to most workers in the private sector. Federal employees covered by the Federal Employees' Retirement System participate in Social Security, as do almost all employees in the private sector. However, federal employees also are covered by a defined benefit pension and they can participate in a tax-deferred retirement savings plan, a combination of benefits that is now relatively rare among employees in the private sector.

According to data collected by the Department of Labor, only 20% of workers in the private sector participated in a defined benefit plan in 2006 (See **Table 1**). The participation rate was 33% at establishments with 100 or more workers and just 9% at establishments with fewer than 100 workers. The Labor Department estimates that 43% of workers in the private sector participated in a 401(k)-type plan in 2006. The participation rate was 54% at establishments with 100 or more workers and 33% at establishments with fewer than 100 workers. While federal employees have the opportunity to participate in both a defined benefit pension plan and the TSP, only 15% of private-sector workers had both types of plan available to them in 2006, and just 12% of private-sector employees participated in both types of plan in 2006.

The FERS basic annuity is adjusted by a full or partial COLA every year for retirees age 62 and older. Private-sector pension plans typically do not provide automatic COLAs. According to the Bureau of Labor Statistics, only 7% of employees in private establishments who participate in a defined benefit pension plans were covered by plans that provide automatic post-retirement cost-of-living adjustments.

This concludes my testimony and I would be happy to answer any questions that members of the subcommittee might have.

Table 1. Percentage of Private-sector Employees Participating in Employer-Sponsored Retirement Plans in 2006

	Type of Retirement Plan		
	All Types	Defined Benefit	Defined Contribution
Establishment Size			
1 to 99 workers	37	9	33
100 or more workers	67	33	54
Work Schedule			
Full-time workers	60	23	51
Part-time workers	21	8	16
All workers	51	20	43

Notes: Some workers are in both types of plan, so the percentage with DB plan plus the percentage with DC plans will not add to the percentage with any type of plan. Data represent 105 million workers employed in the private sector in 2006.
Source: U.S. Department of Labor, National Compensation Survey.

Mr. DAVIS OF ILLINOIS. Thank you both very much.

Ms. Chaikind, let me try to make sure that I understand the comparison between what Federal employees basically qualify for in terms of health benefits and those in the private sector.

It seemed to me that you are saying that basically Federal employees compare rather favorably——

Ms. CHAIKIND. That is correct.

Mr. DAVIS OF ILLINOIS [continuing]. To what they could expect in the private sector.

Ms. CHAIKIND. In terms of access to plans, yes. I mean, that is all that I was talking about. There was access to plans. All Federal workers who are considered either full time or part time do have access to a health benefit plan.

In the private sector, that access varies. As I said, it increases as firm size increases, as pay increases, as full time increases, so there are more barriers, I would say, in the private sector for any given individual to have access to health insurance than there are in the Federal work force.

Mr. DAVIS OF ILLINOIS. Do you have any value comparisons in terms of the values of what they qualify for?

Ms. CHAIKIND. I don't have that, but I think that is something that I could get back to you with, if you would like me to.

Mr. DAVIS OF ILLINOIS. I would appreciate it.

Mr. Purcell, your testimony suggests that when it comes to retiree benefits, that Federal employees similarly compare rather favorably to what exists in the private sector; is that accurate?

Mr. PURCELL. I think that is an accurate characterization. And the reason for that is that in the private sector, since the early 1980's there has been a strong trend away from the traditional defined benefit pension in favor of the 401(k) plan. What that means is if you looked at the statistics in 1980 you would have seen about the same percentage of workers in the private sector in a plan as are in a plan today, about half. But in 1980, virtually all of them would have been in a traditional pension. Today, only one worker in five in the private sector is participating in a traditional pension, and a number of those, perhaps as many as a quarter, have been frozen in one respect or another, meaning either no new benefits are accruing or new workers are not allowed into the plan.

If you isolate on, say, the 500 largest companies in the S&P or Fortune 500, you will still see a majority, roughly two-thirds, that offer a defined benefit pension, but it is still a minority that offer both a DB plan and a tax-favored savings plan, which Federal employees are able to participate in.

Mr. DAVIS OF ILLINOIS. Let me ask both of you, do you have any idea why there is sort of a common perception? I mean, when you talk to people, there seems to be a tendency to believe that the private sector does a better job in both these arenas than the public sector.

Mr. PURCELL. I can't answer for sure why that perception might exist, but, as one of the earlier witnesses said today, the difference in pay is very easy for people to measure. The difference in benefits is more complicated, particularly with younger workers. As the Director of the TSP mentioned today, they have lower participation rates and lower contribution rates. They are going up, which is a good thing. But it is very difficult to get younger workers, in particular, to focus on the importance of saving for retirement or to understand the value of the defined benefit pension.

I think when people are comparing between the private sector and the public sector they have a much clearer idea about differences in pay than they do differences, particularly in retirement benefits. I can't really speak about the health insurance aspect because that is not my area.

Mr. DAVIS OF ILLINOIS. Let me just ask about the health insurance.

Ms. CHAIKIND. Well, I am going to draw from some of my other experience in health insurance and say that many people in both the private and the public sector are concerned about health insurance coverage as employers, whether they are private sector employers or other, are reducing benefits, increasing co-insurance, increasing co-payments. So I am not sure that this is an issue that is of concern only to Federal Employees Health Benefits Program, but it is also an issue of any employer-sponsored health benefit plan.

Mr. DAVIS OF ILLINOIS. Have you seen much movement in the vision/dental coverage arena in terms of trends that might be evolving or developing?

Ms. CHAIKIND. In terms of trends, as I mentioned in my statement, other private sector employees do have lower access than Federal employees have lower access, but what I cannot speak to is whether or not those employees have to pay 100 percent just like Federal employees have to pay.

Mr. DAVIS OF ILLINOIS. Thank you. Thank you both very much. Mr. Marchant.

Mr. MARCHANT. Thank you, Mr. Chairman.

Part-time employees have the same ability to access the health insurance, so if you are brought on at 20 hours, you have the same waiting period and you can enter the program and you have exactly the same access, no pre-existing?

Ms. CHAIKIND. Everything is the same except the premium. Part-time employees will pay a larger share, and it is pro-rated based on the number of hours that they work.

Mr. MARCHANT. But the access is available and they can get it, so there is a great amount of value, as opposed to the corporate world now. Most corporations are moving to a part-time status so that they are not required by law to offer insurance at any price.

Ms. CHAIKIND. Yes, that is correct. In the Federal Employees Health Benefits Program, employees are given the same access. As I said, they just have to pay a larger share of the premium, and they also are able to pay the premiums on a pre-tax basis, just as the full-time workers are.

Mr. DAVIS OF ILLINOIS. Mr. Chairman, that is a great thing to be offered. In the private world right now, in the corporate world, it is almost unheard of for a part-time worker to be even offered the plan.

Is there any document, Mr. Purcell, that you know of that a Federal worker is shown when they take their job that says, Here is your cash compensation and here is the value of your benefits package, its equivalency, so that a person can say, OK, if I have to work for this company and I pay this, or I go to work for the Federal Government and pay this, same cash amount? Is that made available?

Mr. PURCELL. For new Federal employees they would receive information as part of their orientation that will explain the pension benefit that is provided. The Thrift Board puts out numerous publications that are very easy to read. They don't go into eight pages of fine print, but they have charts and show here is what you will accumulate if you start saving at this age or this age. So I believe that the Federal Government is doing a pretty good job right now of informing new employees what retirement benefits they have available to them. How that is done in the private sector I am not sure.

I would say that more companies in the private sector, about a quarter of the, say, Fortune 500, have gone to automatic enrollment in 401(k) plans, and I think most observers expect that trend to continue, and that is going to get a lot more people into 401(k) savings plans at an earlier age, just as it would if it was adopted by the thrift plan.

Mr. MARCHANT. So the ability to enter a defined benefit plan is a plus.

Mr. PURCELL. The interest thing is in a defined benefit plan, the traditional pension, as a worker you don't do anything. You are on the payroll, you are in the plan. You may not even be aware of it. That is one reason I was saying before it is difficult for workers to compare retirement benefits because they are not quite sure of the value of those benefits.

In a defined contribution plan, since you are getting sort of a quarterly statement of how much is in your account, it is much easier to see how you are doing.

The inertia in the past has been that newer workers and lower-paid workers were reluctant to give up take-home pay to put money into either the thrift plan for the Government or the 401(k) plan in the private sector. With automatic enrollment, the default is at 6 months or whatever the start date is, a certain percentage is going to be put into your account.

Now, of course, you have to offer them the option to say I don't want to do that, but studies, real-world experiments in companies, have shown once people are automatically enrolled, 90 percent, 95 percent of them stay in.

Mr. MARCHANT. Well, just from a pure PR standpoint, the Federal Government I don't think does as good a job as they could do informing the potential employee out there that they can join a company, get automatic coverage on the health care and their family—at a price, but get it—get in a pension system that has a definable benefit, and then have a structure that surrounds it that is not contingent on a board of directors annuitizing their pension plan and freezing them in it.

Mr. PURCELL. It is one of those things where I think the appreciation of the health and retirement benefits that Federal employees receive often doesn't dawn on them until they have been in the Federal Government a number of years. I mean, I talk to a lot of Federal employees about retirement issues. Many of them are not aware at all that they are covered by a traditional pension in addition to the Thrift Savings Plan.

Mr. MARCHANT. The one thing that I don't know, Mr. Chairman, if this dogs you or not, but sometimes on Sunday afternoon I am driving back from my ranch back home getting ready to come back here and I listen to these financial gurus, you know, and they harp on the fact that I don't pay any Social Security tax, and then I get these chain e-mails. Was there ever a time that we did not pay Social Security tax? Where does that come from?

Mr. PURCELL. A long time ago. Prior to 1984 Members of Congress, like every other Federal employee, were in the Civil Service Retirement System, and that system was actually created before Social Security.

Mr. MARCHANT. OK.

Mr. PURCELL. When the 1983 Social Security Amendments were passed, part of those amendments said from now on all new employees are going to be in Social Security and all Members of Congress will be in Social Security. All Members of Congress pay Social Security taxes. I have seen the e-mail. I have seen it many, many times. And we do have a report about retirement benefits for Members of Congress that explains very clearly that they pay the same Social Security taxes as every other citizen of the United States except, of course, there are some State workers who don't.

Mr. MARCHANT. Right.

Mr. PURCELL. And Texas I think is one of them.

Mr. MARCHANT. Yes, it is, and they want to double dip.

Thanks for your information. I appreciate your testimony.

Mr. DAVIS OF ILLINOIS. And that the retirement is not nearly as lucrative as some believe.

Mr. MARCHANT. It is probably not going to be the many millions of dollars that the e-mail says.

Mr. DAVIS OF ILLINOIS. Well, you know, the public has this perception that it is just a fat cat pension that you get. I do a television show every week, and I have some callers who just call in and want to know, what are you going to do with your pension? And I am saying, My wife would probably like to know what I am going to get as a pension.

I have just one additional question, Mr. Purcell. What is the average age at which Federal employees retire, and what is their average monthly pension?

Mr. PURCELL. The average age has been very stable for many years, right around 61. Currently, the retirees under the Civil Service Retirement System get an average pension of about $2,500 a month, which will work out to $30,000 a year. And under the FERS the average pension is about $900. Now, the reason that number is so much lower, there are two reasons. One is the FERS pension is smaller because those workers are also covered by Social Security, so their combined benefit is bigger. Second, the retirees under CSRS still have a higher average career length. FERS is still, as a pension system, fairly young, so the FERS retirees don't have as long a career as the CSRS retirees.

Mr. DAVIS OF ILLINOIS. Well thank you very much. I think that is about what the average Member of Congress who retires will get. I understand it is about $35,000 a year.

Let me thank you all very much for your patience and your diligence. We really appreciate the fact that you stayed.

Mr. Marchant, unless you have some additional questions, comments?

[No response.]

Mr. DAVIS OF ILLINOIS. We thank you very much. This hearing is adjourned. We thank our staff who have also done due diligence and got a lot of late evening work.

[Whereupon, at 5:30 p.m., the subcommittee was adjourned.]