

**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.