# STATEMENT BY
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**THE SUBCOMMITTEE ON THE FEDERAL WORKFORCE, U.S. POSTAL SERVICE AND LABOR POLICY**
**COMMITTEE ON OVERSIGHT AND GOVERNMENT REFORM**
**UNITED STATES HOUSE OF REPRESENTATIVES**

**HEARING ON**
**"THE THRIFT SAVINGS PLAN:  HELPING FEDERAL EMPLOYEES ACHIEVE RETIREMENT SECURITY"**

**JULY 27, 2011**

Chairman Ross, Ranking Member Lynch, and members of the subcommittee**,** on behalf of our nation's 4.6 million federal employees, retirees and survivor annuitants, I appreciate the opportunity to express the views of the National Active and Retired Federal Employees Association (NARFE) on the Thrift Savings Plan (TSP).

We continue to be pleased with the performance of the TSP. We believe that the Federal Retirement Thrift Investment Board (FRTIB) and its staff, have acted as dutiful fiduciaries on behalf of federal workers and retirees.

Indeed, the TSP has been a huge success, with an 85.5-percent voluntary contribution rate by Federal Employees Retirement System (FERS) employees. It is the largest 401(k)-type plan in the country, with more than $289 billion in assets and with an exceptionally low expense ratio, just 25 cents on each $1,000 invested.

In 1986, NARFE worked with key legislators to write the law that created the TSP and FERS. Today, Richard G. Thissen, NARFE's National Treasurer, represents our Association on the Employee Thrift Advisory Committee (ETAC), which meets with the FRTIB executive director and his staff on a regular basis to consider the operations and investment policies of the plan.

NARFE continues to be interested in advancing the program further by allowing federal workers to contribute accumulated and accrued annual or vacation leave and, bonuses, to their TSP accounts in the same manner as  private-sector employees.

The Viability of Defined Contributions Plans

The test of any organization is its performance during a crisis. We believe that FRTIB and its vendor fund managers have continued to perform admirably during the most volatile financial market periods of the recession. Unfortunately, because of events beyond our control, nearly all Americans who participate in a defined-contribution retirement plan – including TSP participants – lost a significant amount of their savings value during the economic downturn, the worst since the Great Depression. While many of us are just now gaining back what we lost, few if any retirement plan participants will take it for granted that their investments in the stock and bond markets will always grow.

Federal workers who are years away from retirement should have plenty of time to make back what they lost – and hopefully gain ground along the way. The same is not true for workers who are at or near retirement. Those employees are in the unenviable position of either retiring with a smaller nest egg than they had hoped for or deferring retirement until some undetermined point in the possibly distant future – after the market sufficiently rebounds.

Employers originally created retirement plans for their workers to ensure that they would not have to work into old age, and also to make room for younger employees to move up the promotion ladder and take their places. As employers have migrated away from "**defined-benefit**" pensions and annuities to "**defined-contribution**" retirement savings plans, the burdens of retirement liabilities and risk have been shifted from employer to employee. While this transition has improved corporate balance sheets and enabled workers to have portable retirement benefits, the original purpose of employer-sponsored retirement programs is diminished when employees are compelled to remain in the workforce until they make up for lost gains.

<u>Preserving the FERS "Three-Legged Stool"</u>

We acknowledge that it is unlikely that a bear market would result in employers going back to defined-benefit pensions and annuities. Fortunately, the retirement security of FERS workers is diversified with the "three-legged stool" consisting of the TSP, a modest defined-benefit annuity (significantly smaller than provided under the Civil Service Retirement System (CSRS), and Social Security benefits. In fact, we believe the FERS defined-benefit annuity has become an increasingly important safety net for FERS workers, particularly given the recent market slump of the country's economic recession.

Unfortunately, the FERS annuity has been threatened by a series of recent deficit-reduction proposals:

- Basing the FERS annuity on the highest five years of salary rather than the highest three years of average salary would reduce the annuity of FERS retirees by an average of $462 over five years, according to the most recent estimate made by the Congressional Budget Office.

- Ending the FERS annuity would mean that, for the first time since 1921, the federal government would not offer a defined-benefit retirement annuity to its employees. The average FERS annuity is $1,050 per month. Absent a FERS annuity, retiring federal employees could lose their health insurance (FEHBP) since coverage is currently linked to receipt of a retirement annuity. Likewise, if a federal worker is no longer eligible to receive an annuity, he or she could no longer elect to provide a modest survivor annuity to a spouse or dependent, even by paying the actuarial cost of that benefit. The average FERS survivor annuity is $375 a month.

In addition, the proposal to require federal workers to contribute an additional 5.5 percent of salary to the Civil Service Retirement and Disability Fund (CSRDF) will significantly reduce the wage earnings available to employees that could otherwise be contributed to their TSP account.

While employees currently make contributions from their salary to the CSRDF, most large private-sector employers historically have not required their workers to make any contribution toward their defined-benefit pensions. According to the U.S. Department of Labor, private-sector workers put in $1 for every $109 their employers contributed to their defined-benefits plans in 2008, the latest year for which statistics were available.

Taken together – and compounded by the  two-year federal pay freeze enacted in December 2010 that will permanently lower future retirement annuities – these proposals send the wrong signal to the federal employees whose jobs are to protect us and drive America's progress. The American people have come to expect that federal meat inspectors will ensure the safety of the food our families eat and federal nuclear regulators will prevent the next nuclear disaster from happening on U.S. soil. However, the cumulative affect of proposals to substantially reduce the earned compensation of federal workers could severely undermine the government's ability to attract and retain the best American employees.

What's more, for some FERS workers, the Social Security leg of retirement is eroded by the so-called Windfall Elimination Provision or WEP. The WEP unfairly and arbitrarily reduces the Social Security benefits of certain FERS and CSRS employees who paid Social Security payroll taxes just long enough to qualify for benefits at age 62. Repeal or reform of the WEP would shore up the retirement security of more than 950,000 federal, state and local government retirees. NARFE supports H.R. 1332, legislation introduced by your colleagues, Howard "Buck" McKeon (R-CA) and Howard Berman (D-CA), which would repeal the WEP and the related Government Pension Offset or GPO.

TSP Improvements

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. We have supported adding new features to the TSP that have succeeded when offered in private retirement savings plans and when they are consistent with the program's investment philosophy.

With the help of this committee, and through the advocacy of NARFE and our colleagues in the federal/postal community, several TSP improvements were included in the Tobacco Regulatory legislation signed into law by President Obama on June 22, 2009, as P.L. 111-31. Collectively, those improvements are referred to as the Thrift Savings Plan Enhancement Act of 2009.

For example, the new law automatically enrolls newly-hired federal employees in the TSP and makes them eligible to receive an immediate matching contribution from their employing agency. We believe this is the most important enhancement added to the program since it was created. Indeed, 97 percent of newly hired federal employees are voluntarily putting their own wages in their TSP accounts and the government, as an employer, is matching these contributions as a result of this new feature. Now, more federal workers will be better prepared for their retirement.

NARFE supported authorizing the FRTIB to add a "Roth" option to the TSP, which will allow participants to make after-tax contributions to the plan and withdraw their earnings tax-free upon retirement. A growing percentage of private 401(k) plans have a Roth option, and it could be a viable alternative for individuals whose income taxes are likely to be higher in retirement than they were when they were working. We are pleased that the FRTIB plans to implement use of the TSP Roth option in the second quarter of 2012.

In addition, the new law addresses the retirement security of the surviving spouses of workers and retirees by granting them the same rights over their inherited accounts as any other TSP participant. Prior to the enactment of P.L. 111-31, a spouse married to a TSP participant who passed away was required to either transfer their inherited account to an individual retirement account (IRA) or take the benefit as a cash withdrawal, which is subject to federal income taxes. Today there are 4,834 spousal accounts, and this number will only grow over time. NARFE is grateful to our friends on this committee for extending full ownership of TSP accounts to surviving spouses.

I would also like to acknowledge my colleague, Dick Strombotne, for leading this effort for more than six years on spousal account rights. Mr. Strombotne is also a long-time NARFE Maryland Federation and chapter officer.

"Self-Directed" Option

Beyond these improvements, the only change in the TSP Enhancement Act that gives us pause is the authority granted to the Thrift Board to allow participants to invest their account in mutual funds outside the investment funds currently offered by the plan. While some TSP participants might enjoy this "self-directed" option, the administrative costs incurred by funds beyond TSP are typically much higher than our program. That is because the more than 4.5 million federal workers and military personnel who participate in the TSP create a large economy of scale, which achieves administrative savings unheard of in other employer-sponsored retirement savings plans. Indeed, TSP's index plans are large, well-diversified portfolios of securities that have reduced risk to investors and have a proven performance, over the long term. The same cannot be said for many funds outside of the TSP. For that reason, NARFE is concerned that such a self-directed option could result in federal workers taking on too much risk in which they could put all their eggs in one perilous basket.

When the TSP Enhancement Act became law, some said that the self-directed option was added to the legislation to placate interest in offering single-sector industry or commodity funds or socially responsible investment funds in the TSP. As part of their fiduciary duty, the Thrift Board has advised against adding such funds because they conflict with the diversified index fund strategy of the program, which has minimized risk, created retirement security for participants and beneficiaries and insulated the federal government from being accused of manipulating the stock market through the TSP. NARFE agrees with this position, and we hope that future fund selection will not be driven by the politics of outside self-interested funds. Do not tie the hands of the fiduciaries in delivering the best TSP to participants and beneficiaries that money can buy. Instead, we urge Congress and the Thrift Board to work together and to base fund decisions on carefully crafted, objective financial analysis and not on politics. Most of all, Congress and the Thrift Board must act in the best interests of federal civilian workers and military personnel who put their hard-earned dollars in the TSP.

## NARFE Policy Recommendations for the TSP

Although NARFE is delighted with most of the provisions in the TSP Enhancement Act, we continue to be interested in advancing the program further.

For instance, on September 5, 2009, the Internal Revenue Service issued Revenue Ruling 2009-31, which explained that a 401(k) plan may be amended to require or permit the contribution of the dollar equivalent of unused paid time off annually to a participant's account. Shortly thereafter, NARFE and the National Treasury Employees Union asked the Thrift Board to address whether the new ruling would apply to TSP participants. The Board concluded that federal employees cannot contribute unused annual or sick leave to their TSP accounts unless the Federal Employees Retirement System Act is amended. As a matter of equity, NARFE supported legislation introduced during the 111th Congress by Reps. Stephen Lynch (D-MA) and Jason Chaffetz (R-UT) that would have allowed federal workers to contribute accumulated and accrued annual or vacation leave to their TSP accounts in the same manner as private-sector employees. We urge Reps. Lynch and Chaffetz to reintroduce this bill in the current 112th Congress, and we encourage this subcommittee to approve it.

NARFE also supports a proposal to allow federal workers to contribute bonuses into their tax-deferred accounts. 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 FERS workers. For instance, if such a proposal became law this year, TSP participants already making the maximum contribution ($16,500 for workers 49 years old and younger, and $22,000 for those 50 and older) would not be able to deposit a bonus in their account. Allowing the deposit of bonuses for civilian participants would be helpful for those who contribute under the current limits.

Finally, NARFE supports legislation to authorize the Thrift Board to take legal action to protect the interests of TSP participants and beneficiaries in accordance with its fiduciary responsibilities.

Retirement Savings Education

As our TSP legislative and policy recommendations attest, NARFE wants federal civilian workers and military personnel to have the means to maximize their retirement savings. We made progress towards this goal by the provisions in the TSP Enhancement Act that will automatically enroll new employees into the TSP and provide them with an immediate agency matching contribution.

Still, we can make it easier to save for retirement. A defined-contribution system will not work unless employees do their part. Unfortunately, many Americans cannot afford or are unwilling to accept this responsibility and have little money put away in savings and investments. According to the Employee Benefits Research Institute's 2011 "Retirement Confidence Survey," 56 percent of respondents reported that the total value of their household's savings and investments, excluding the value of their primary home and any defined-benefit plans, is less than $25,000.

We would like to think that a much greater portion of federal workers have saved more money than the general public. Certainly, efforts by the Thrift Board to educate federal employees about the importance of retirement savings have helped. However, we remain concerned that the federal government, as an employer, does not do enough to educate its own workers about how much they need to save now to preserve their quality of life in retirement. Nor do we believe that many workers appreciate that their retirement planning should extend beyond the TSP to other savings vehicles such as Individual Retirement Accounts. Mature and older Americans should be able to live dignified and independent lives. Many will not reach that goal unless our retirement education efforts create a culture of savings. Accordingly, we implore you to promote the establishment of a coordinated effort to educate workers about the need for informed decision making.

TSP G Fund and Default

On May 16, Treasury Secretary Timothy F. Geithner was forced to take extraordinary measures to avoid a government default, including short-term use of the TSP G Fund and the Civil Service Retirement and Disability Fund to manage the U.S. Treasury's cash flow, because Congress failed to increase the statutory debt ceiling. NARFE would prefer that our funds only be used to pay the retirement annuities and TSP benefits earned through a lifetime of public service. However, we also acknowledge that such extraordinary measures ensure that annuities and TSP savings continue to be paid. In fact, once Congress raises the debt limit and the period of debt suspension ends, the Treasury Secretary is required by federal law to "make whole" the retirement funds, with back interest. As we approach the August 2 deadline to pass an increase in the debt limit, many federal employees and annuitants are concerned about how a possible default would affect them. For that reason, we appreciate that the Thrift Board has made it clear that, through the operation of the "make whole" law, a default would have no impact on the G

Fund invested in government securities. Even without action on the debt ceiling, all of the G Fund monies would still be on account with the Treasury, and the interest that would accrue if the G Fund were fully invested would still be credited to the G Fund, according to the FRTIB.

## Conclusion

Chairman Ross and Ranking Member Lynch, we commend you for your interest in ensuring that the Thrift Savings Plan continues to thrive. The TSP is a model employer-sponsored retirement savings program because of the dedication of the Federal Retirement Thrift Investment Board and its staff, and as a result of this committee's support and oversight of the program. The TSP provisions in the Thrift Savings Plan Enhancement Act will only help to perfect the program. We stand ready to work with this panel, others in Congress and the Thrift Board to find the ways and means to ensure that federal civilian workers and military personnel are financially prepared for retirement and that the TSP continues to be innovative and a model for other employers to follow.

I would be happy to answer any questions you may have.