

Coordination Between the Railroad Retirement and Social Security Systems

by ABRAHAM M. NIESSEN*

PRACTICALLY all retirement plans in this country, particularly those serving persons in the private sector of the economy, are coordinated in some way with the general social security (OASDHI) system. Such coordination may take the form of adjustments in benefit provisions in response to changes in social security law, direct tie-ins between certain benefits of the plan and those payable under social security, or compliance with the "integration" rules of the Internal Revenue Service.

Because the railroad retirement-social security coordination involves so many areas, a study of it by reference to the statutes themselves is cumbersome. This article aims to provide a unified reference to all aspects of this interesting subject and, more specifically, to trace briefly the history of the coordination between the two systems, to delineate the major areas in which it now operates, and to indicate in a general way its effects on the railroad retirement system. The discussion deals primarily with the statutory provisions pertaining to the railroad retirement, disability, and survivor benefits program. Other aspects, such as those involving administrative coordination and Medicare, is touched on only briefly.

HISTORICAL BACKGROUND

Attempts at some measure of coordination between the railroad retirement and social security systems were made as early as 1937. The Railroad Retirement Act enacted on June 24, 1937, contained a provision guaranteeing that monthly benefits under the act were to be at least equal to what social security would have paid on the basis of the railroad service involved. This provision

never became operative, however, because the reference to the Social Security Act was construed to relate to the Social Security Act of 1935 and monthly benefits were never paid under that act.

The legislative history of the Railroad Retirement Act of 1937 indicates that some thought had been given at that time to the propriety of some financial coordination with the social security system. Section 15(d) of the 1937 Act (P. L. 162-75) provided that the actuarial reports of the Railroad Retirement Board "shall also contain an estimate of the reduction in liabilities under title II of the Social Security Act arising as a result of the maintenance of this Act . . ." and this language is still in the statute today. But the law made no provision for any transfers of money as a result of such an estimate. Consequently, and because technically the reference was to the Social Security Act of 1935, no estimate was ever made under this particular provision. All financial interchange determinations to date were made under the authority of section 5(k)(2) of the Railroad Retirement Act, added to the law by the railroad retirement amendments of 1951.

It took, however, more than 15 years before such coordination on a broad scale was made a part of railroad retirement law. The first real phase of coordination with social security came about as a result of the 1946 railroad retirement amendments when the program was expanded to include survivor benefits similar to those payable under the Social Security Act of 1939. For purposes of these benefits, credits under both systems were to be combined and only the agency with jurisdiction over the case was to pay them. Furthermore, the monthly survivor benefits were made subject to the same earnings restrictions as then applied to social security benefits,¹ even though different work clauses applied to retirement benefits. These coordinating provisions are

* Chief Actuary and Director of Research, Railroad Retirement Board. This article is based on a paper presented at the October 1968 meeting of the Conference of Actuaries in Public Practice. The opinions expressed do not necessarily reflect the official views of the Railroad Retirement Board.

¹ These restrictions were in addition to the general prohibition against railroad employment regardless of the amount of earnings in such employment.

still in effect today. (Another form of coordination involved reductions in railroad survivor annuities for the receipt of social security benefits, but this reduction was repealed in 1955.) The 1946 amendments also provided for allocating the cost of the newly instituted survivor benefits between the two systems. The financial interchange provisions enacted in 1951 made this financial coordination obsolete before it actually went into operation.

An attempt at coordinating railroad retirement employee and social security benefits was made in 1951. One provision involved partial reduction of an employee's railroad retirement annuity if he was simultaneously eligible for a social security benefit. The part of the annuity attributable to railroad service before 1937 was to be reduced by the social security benefit amount. This social security offset proved to be highly unpopular, and the whole restriction was repealed in 1954, with the stipulation that all reductions previously made were to be restored to the beneficiaries or their survivors.

Many of the important coordination provisions that exist today were put into the law by the 1951 legislation. These amendments included (1) the provision for transferring to the social security system the railroad credits of individuals who die or retire before the completion of 10 years of railroad service; (2) the restoration of a social security "minimum guarantee" for railroad retirement benefits; and (3) the establishment of a broad financial interchange between the systems.

The 1951 amendments also added annuities for wives and dependent husbands (spouses' annuities). Furthermore, the wives' annuities were made subject to a maximum derived from the social security law and to a reduction for receipt of certain social security benefits. The maximum provision still stands today (through in a different form), but the reduction for other benefits was repealed in late 1965.

The evolution of coordination with social security progressed further to include a partial dependence of the railroad retirement tax rates on those in effect for OASDI benefits (1959), an automatic linkage between the limits on taxable and creditable earnings (1965), partial offsets for receipt of OASDI benefits (1966 and 1968), and benefit increases geared to OASDI benefit increases (1968). All of these coordinating provisions are in effect today.

Present Coordinating Provisions

The following discussion deals only with those coordinating provisions that have a major impact on the operations or the financing of the railroad retirement system. The situation is viewed in the context of railroad retirement and social security laws in effect on March 1, 1968.²

Transfer of credits.—When a railroad employee dies or retires after completing less than 10 years of railroad service, his railroad retirement credits are transferred to the social security system and are treated as regular social security credits. In such cases, the Railroad Retirement Board pays no benefits other than a possible residual amount—essentially a refund of the railroad retirement taxes that are in excess of specified benefits paid to an individual and his family.

Railroad retirement credits are also transferred to the social security system for purposes of survivor benefits in certain cases involving deceased individuals who had completed 10 or more years of railroad service. When such an individual has no current connection with the railroad industry at the time he dies or retires, though he and his wife may have been receiving railroad retirement annuities, the survivor benefits are paid by the Social Security Administration rather than by the Railroad Retirement Board. When the Board has jurisdiction over a case involving survivor benefits, the transfer of credits occurs in reverse order—that is, the social security credits are transferred to the railroad retirement system and only the Board pays the benefits.

There is no specific provision for reimbursing one system or the other for the service credits transferred to it. Proper payment for accepting and using such credits is made, however, under the general financial interchange arrangement discussed below.

Survivor benefits.—In addition to being based on combined credits under both systems, the railroad survivor benefits are further coordinated with social security in that (a) the insured-status requirements under the Railroad Retirement Act are nearly the same as those under the Social

² For a summary of provisions in the law, see Orlo Nichols, "The Railroad Retirement Amendments of 1968," *Social Security Bulletin*, June 1968.

Security Act (they can be no less favorable), (b) the amounts of monthly benefits are in most cases computed according to social security formulas (with a 10-percent increment), (c) the earnings restrictions for employment other than railroad work are exactly the same as for social security benefits, and (d) the definitions of family relationships are generally the same as in the Social Security Act.

The fact that benefits to survivors of railroad workers are paid by only one of the two agencies has very important cost implications for the railroad retirement system. If dual survivor benefits had been permitted, the benefit reimbursements under the financial interchange would have been considerably smaller and, consequently, a corresponding increase in the tax rates required to maintain the railroad retirement system would have been necessary.

Spouses' annuities.—A spouse's annuity under the Railroad Retirement Act can be as high as 110 percent of the maximum wife's benefit payable under the Social Security Act. This provision, together with the absence of reductions for the receipt of other benefits, makes wives' benefits under the Railroad Retirement Act much higher than corresponding social security benefits in most cases.

Social security minimum.—Coordination with the social security system in the area of benefit amounts takes the form of an overall guarantee that the total of monthly benefits payable to a family under the Railroad Retirement Act cannot be less than 110 percent of the benefits, or the additional benefits plus 10 percent of the total benefits, that would have been paid under the Social Security Act on the basis of the railroad service involved. This provision currently affects about 10 percent of the retirement benefits, some 65 percent of the aged widows' benefits, and practically 100 percent of the other monthly survivor benefits.

The cost implications of this minimum provision are considerable since the benefits paid under this provision are usually higher than they would have been under regular railroad retirement formulas. Furthermore, this special minimum necessitates substantial additional benefit outlays whenever the social security benefit program is

liberalized. Similarly, the cost of spouses' annuities also rises when the social security earnings base or its benefits are increased.

Earnings base and tax rates.—The linkage between the earnings bases of the two systems was instituted by the Railroad Retirement Amendments of 1965. They provide specifically that the monthly limit on taxable and creditable earnings for railroad retirement are to be equal to one-twelfth of the annual limit under the social security program. Thus, when the social security earnings base went up to \$7,800 per year as a result of the 1967 amendments, the railroad retirement monthly limit automatically went up from \$550 to \$650.

The permanent linkage between the railroad retirement earnings base and that of social security is of great importance to the railroad retirement system. Any substantial increase in the social security earnings base results in a greater portion of railroad earnings becoming subject to taxation for purposes of the railroad retirement program. The additional income derived from such increases in the proportion of taxable railroad earnings is a major factor in partially offsetting the additional benefit costs created by liberalizations in the social security law.

The railroad retirement tax rates are also permanently linked (since 1959) to those in effect for earnings covered by social security. The railroad retirement rate of tax on employees and employers alike (exclusive of the employers' taxes for the support of the railroad supplemental annuity program) consists of three parts: (1) the basic rate, currently 7¼ percent, (2) the number of percentage points by which the combined rate for OASI and DI exceeds 2.75, (3) a percentage equal to the rate in effect for support of the hospital insurance program. Thus, whenever the social security contribution rates change, the railroad retirement tax rates increase or decrease by the same number of percentage points.

Social security offsets.—Direct offsets for social security benefits have been in effect since November 1966. Under present law, the offset is limited to the approximate amount of the combined increases received by the individual in his social security benefits as a result of the 1965 and 1967 amendments to the Social Security Act. An offset

cannot, however, exceed the specific amount of the scheduled dollar increase provided for by the 1968 railroad retirement amendments.³ The rationale behind the offset provision is to avoid preferential treatment of railroad retirement beneficiaries who are also entitled to social security benefits (dual beneficiaries). Without such offsets, the dual beneficiaries would receive increases from both systems totaling considerably more than the single increase given to nondual beneficiaries by the railroad retirement system. Another reason for maintaining the social security offset is that it significantly reduces the cost of the recent general increases in railroad retirement benefits.

The financial interchange.—The financial interchange is by far the most important aspect of the coordination of the railroad retirement and social security systems. The purpose of the interchange is to put the social security trust funds (old-age and survivors insurance, disability insurance, and hospital insurance) in the same position they would have been in if railroad service had been covered under the Social Security Act since 1937.⁴ Financial interchange determinations are made jointly by the two agencies every year and involve the following steps:

1. Determination of the amount of contributions each social security trust fund would have received with respect to railroad employment.
2. Determination of the amount of additional benefits that would have been paid out from each fund on the basis of railroad employment.
3. The difference between the amounts in step 1 and step 2 (with appropriate adjustment for interest and administrative costs) is the net amount that is transferred either to the railroad retirement account or to the appropriate social security trust fund, depending on whether the difference is positive or negative.

Determination of the benefits that would have

³ For more detailed information on this point, see the report of the House Committee on Interstate and Foreign Commerce on H.R. 14563, 90th Congress, or the report of the Senate Committee on Labor and Public Welfare on S. 2839, 90th Congress.

⁴ The interchange with the hospital insurance trust fund merely involves a transfer of the hospital insurance taxes collected by the Board with adjustments for the difference between an annual and monthly earnings base and for administrative expenses.

been paid with respect to railroad employment is made on the basis of a continuous 1-percent sample of railroad retirement beneficiaries and includes adjustments for certain differences between railroad retirement and social security law. Gross benefit reimbursements are first computed under applicable social security law on the basis of railroad and social security credits combined. This amount is then reduced by the actual total of social security benefits that were paid to railroad retirement beneficiaries during the period under consideration. The remainder is the amount of additional social security benefits that would have been paid from the trust funds.

The interchange has been a major factor in the financing of the railroad retirement program, and it is expected that under this arrangement funds will flow in the direction of the railroad retirement account for many years to come. Eventually, however, the flow of funds will be reversed, and transfers will be made from the railroad retirement account to the social security trust funds. Although the total amount received to date under the financial interchange is considerable from the point of view of the railroad retirement system, it is small in relation to the magnitude of the financial operations under the social security program.

Administrative Coordination

Implementing the coordination of the railroad retirement and social security systems requires close administrative cooperation between the two agencies in several areas. This cooperation stems either from certain statutory provisions or from agreements on specific matters. Examples of this administrative coordination are: (1) Joint activities in the area of the financial interchange; (2) use of social security information to police the work clauses of the Railroad Retirement Act and to compute social security offsets in railroad retirement benefits or benefits payable under the social security minimum guarantee; (3) use of railroad retirement records to determine eligibility and compute benefits based in whole or in part on railroad service and for certain other purposes; (4) review by the Social Security Administration of certain disability freeze determinations made

by the Railroad Retirement Board; (5) extensive utilization of the Board's facilities in administering Medicare; and (6) expansion of the Social Security Administration health insurance statistical program to include data on the experience of railroad retirement beneficiaries under Medicare.

CONCLUSION

Coordination of the two systems has progressed to a point where it affects practically all of the operations of the railroad retirement system. The

outstanding features of this coordination are that it is not unilateral and that it has been achieved without impairing the independence of the railroad program. The success of the coordinating efforts has prompted inquiries concerning its possible adoption with respect to certain other retirement benefits.⁵ Whether or not there are such developments, this coordination has provided a significant chapter in the story of social insurance in the United States.

⁵ For an example of such an inquiry, see appendix H of the report, *Social Security and Federal Employment* (submitted to Committee of Ways and Means, U.S. Congress, House of Representatives, March 13, 1965).

Notes and Brief Reports

Health Insurance for the Aged: Participating Independent Laboratories*

Health insurance for the aged (Medicare) under the Social Security Act provides coverage of and reimbursement for diagnostic laboratory tests performed in an independent laboratory for persons enrolled in the supplementary medical insurance program (SMI). Diagnostic laboratory services furnished by an independent laboratory are covered under medical insurance if the laboratory is an independent clinical laboratory that is approved to participate in the Medicare program. Covered services of approved independent laboratories are reimbursed at 80 percent of their reasonable charges after the patient has incurred sufficient services to meet the SMI deductible of \$50.

This note defines participating (approved) independent laboratories and presents data on their number, location, and characteristics as of the end of November 1967.

* Prepared by Wayne Callahan and David Allen, Division of Health Insurance Studies, Office of Research and Statistics.

WHAT IS AN INDEPENDENT CLINICAL LABORATORY

An independent laboratory is one that is independent both of the attending or consulting physician's office and of a hospital that meets the conditions for coverage in the program. A laboratory operating under the direction of a physician primarily for the performance of diagnostic laboratory services for other physicians is considered to be an independent laboratory. The laboratory maintained by a physician for performing diagnostic tests in connection with his own practice is not considered to be an independent laboratory.

A clinical laboratory is a laboratory where microbiological, serological, chemical, hematological, biophysical, cytological, immunohematological, or pathological examinations are performed on materials derived from the human body, to provide information for the diagnosis, prevention, or treatment of a disease or assessment of a medical condition.¹

In order to participate in the Medicare program, a laboratory must be approved by the

¹ See section at end of note for specific definitions of the categories of diagnostic laboratory tests that are covered when they are performed by approved independent clinical laboratories.