STATE SOCIAL SECURITY DEPOSITS

HEARING

BEFORE THE

SUBCOMMITTEE ON SOCIAL SECURITY

OF THE

COMMITTEE ON FINANCE
UNITED STATES SENATE

NINETY-SIXTH CONGRESS

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CONTENTS

ADMINISTRATION WITNESSES

Page

Ahart, Gregory J., Director, Human Resources Division, General Accounting Office; accompanied by Michael Zimmerman, Assistant Director Human Resources Division; and Elliott Bushlow, supervisory auditor, Human Resources Division ... 2
Ross, Hon. Stanford G., Commissioner of Social Security ... 20

PUBLIC WITNESSES

Breitenberg, John, representing Hon. James Clark, president, Maryland State Senate, on behalf of the National Conference of State Legislatures ... 51
Franke, Hon, John, chairman, board of commissioners, Johnson County, Kans., and chairman, Labor-Management Policy Steering Committee of the National Association of Counties ... 41
Gallison, Edwin, deputy State treasurer of the State of Vermont, accompanied by Gerald Slay-Baugh, State administrator for the State of Kansas and Chairman, Federal-State Procedures Committee of the Social Security Administration, Purvis Collins, South Carolina, Carl Blechinger, State administrator, California, Fred Henne, executive director, Arkansas Public Employees Retirement System, Alta Moore, State social security administrator, Wisconsin, Kenneth Cook, chief accountant, Division of Pensions, State of New Jersey, Robert R. Kennedy, director, State Retirement System State of Florida ... 68
Krivitz, James A., supervisor, Milwaukee County, Wis ... 50
National Conference of State Legislatures, John Breitenberg, representing Hon. James Clark, president, Maryland State Senate ... 51
National Association of Counties, Hon. John Franke, chairman of the labor-management policy steering committee, and chairman, board of commissioners, Johnson County, Kans ... 41
National Association of State Treasurers, Charles P. Smith, vice president and treasurer, State of Wisconsin ... 90
National Association of Towns and Townships, Russell Barton, executive director ... 45
Smith, Charles P., treasurer, State of Wisconsin, and vice president, National Association of State Treasurers ... 90

COMMUNICATIONS

Brooks, Hon. Jack ... 93
Bumpers, Hon. Dale, a U.S. Senator from the State of Arkansas ... 92
Dalton, Hon. John N., Governor, Commonwealth of Virginia ... 97
Murphy, Joseph N., Jr., executive director, Employee Retirement System of Texas ... 95
National Governors' Association, Gov. Richard A. Snelling, chairman, committee on executive management and fiscal affairs ... 94
National League of Cities ... 96

ADDITIONAL INFORMATION

Press Release announcing this hearing ... 1
Resposes of Commissioner Ross to questions from Senate Subcommittee on Social Security ... 36

STATE SOCIAL SECURITY DEPOSITS

MONDAY, JANUARY 29, 1979

U.S. SENATE,
SUBCOMMITTEE ON SOCIAL SECURITY OF THE
COMMITTEE ON FINANCE,
Washington, D.C.

The subcommittee met, pursuant to notice, at 10:10 a.m. in room 2221, Dirksen Senate Office Building, Hon. Gaylord Nelson (chairman of the subcommittee) presiding.

Present: Senators Nelson, Dole, and Danforth.

[The press release announcing this hearing follows:]

[Press release]

FINANCE SUBCOMMITTEE ON SOCIAL SECURITY SETS HEARING ON STATE DEPOSIT REQUIREMENTS

Senator Gaylord Nelson (D., Wis.), Chairman of the Subcommittee on Social Security of the Finance Committee today announced that a hearing will be held on Monday, January 29, 1979, on the subject of the requirements for deposit by the States of the amounts due to the Social Security Trust Funds as contributions related to the wages of State and local governmental employees who are covered under social security. The hearings will begin at 10 A.M. and will be held in room 2221 Dirksen Senate Office Building.

Senator Nelson noted that the purpose of the hearing is to examine the impact on State and local governments and on the Social Security Trust Funds of a change in regulations concerning the frequency with which States must deposit social security contributions related to the employment of State and local employees. On November 20, 1978, the Department of State and local employees. On November 20, 1978, the Department of Health, Education, and Welfare published final regulations designed to require more frequent deposits. Under past practice, deposits were required by 45 days after the end of each calendar quarter. Under the new regulations, deposits will be required by 15 days after the end of each month except that the deposits related to the third month of each calendar quarter will not be required until 45 days after the end of the quarter. Under a law enacted in 1976 to allow Congress adequate time to examine proposals of this type, the new regulations may not become effective until 18 months after publication in the Federal Register. The new regulations meet this requirement by having an effective date of July 1, 1980. The present hearing should produce the necessary information so that this long-standing issue can be resolved prior to that effective date.

Witnesses.—Senator Nelson stated that Hon. Stanford G. Ross, Commissioner of Social Security, will testify at the hearing on behalf of the Administration. Other organizations scheduled to testify are:

The U.S. General Accounting Office; National Governors Association: National Conference of State Legislatures; National Association of Counties; National League of Cities; and National Conference of State Social Security Administrators.

Written Testimony.—The Chairman stated that the Subcommittee would be pleased to receive written testimony from those persons or organizations who wish to submit statements for the record. Statements submitted for inclusion in the record should be mailed with five (5) copies by Friday, February 16, 1979, to Michael Stern, Staff Director, Committee on Finance, room 2227 Dirksen Senate Office Building, Washington, D.C. 20510.

Senator NELSON. Today's hearing will examine the impact on State and local governments and on the social security trust funds of the proposed change in regulations concerning the frequency with which States must deposit social security contributions related to employment.

Currently, States deposit social security taxes collected from State and municipal workers four times a year, 45 days after the end of each calendar quarter. On November 20, 1978, HEW published final regulations designed to require more frequent deposits. Under the new regulations, deposits will be required within 15 days following the end of the first and second months in a calendar quarter and 45 days following the close of the third month in the quarter. The last deposit would accompany the States' quarterly wage reports.

HEW has argued that the countinuation of quarterly wage deposits would permit the States to retain about $200 million a year in interest income which HEW maintains should go to the social security trust funds. The States maintain the new regulations will impose an undue administrative burden on them.

The social security trust funds clearly need all of the income to which they are entitled. However, the States' concerns must also be considered.

The new regulations become effective July 1, 1980. Today's hearing should produce the necessary information to resolve this longstanding issue prior to that effective date.

Everybody has been notified of the time limitations on testimony. We have a number of witnesses and we must conclude the testimony by 12 noon.

Our first witness this morning is Mr. Gregory Ahart, Director of the Human Resources Division of the General Accounting Office.

Mr. Ahart, your statement will be printed in full in the record. If you wish to summarize it, or extemporize from it, you may do so.

Mr. AHART. Thank you, Mr. Chairman, I would like to introduce my associates. On my left is Mr. Micheal Zimmerman, Assistant Director, Human Resources Division and on my right is Mr. Elliott Bushlow, who is on Mr. Zimmerman's staff.

I do have a prepared statement, Mr. Chairman, which I do not think I will try to read in full, that very briefly summarizes our position if you would accept this statement for the record.

Senator NELSON. It will be printed in full in the record.

Mr. AHART. Also, we have issued a report dated December 18, 1978, which covers this issue which I would offer for the record also.

STATEMENT OF GREGORY J. AHART, DIRECTOR, HUMAN RESOURCES DIVISION, GENERAL ACCOUNTING OFFICE; ACCOMPANIED BY MICHAEL ZIMMERMAN, ASSISTANT DIRECTOR, HUMAN RESOURCES DIVISION; AND ELLIOTT BUSHLOW, SUPERVISORY AUDITOR, HUMAN RESOURCES DIVISION

Mr. AHART. Very briefly, Mr. Chairman, your opening statement outlined the background of the issue involved. Our position with respect to the social security regulations is, yes, they certainly go in the right direction. We see no reason why the States and local governments should have the benefit of the interest income from contributions that are collected from employees, as well as from their own contributions,

to the detriment of the financial stability of the social security trust funds.

We think that the final social security regulations do not go far enough. We would urge that they at least go back to the March 30, 1978, proposal which would have required deposits 15 days after the end of each month in a calendar quarter.

Senator NELSON. Fifteen days?

Mr. AHART. Fifteen days after the end of each month in the calendar quarter as opposed to having it stretch out the last deposit to 45 days after the end of the final month of the quarter.

This would make about a $30 million a year difference in the trust fund earnings in the first year, and that would rise over time as the amount of the contributions increased.

Senator NELSON. Am I correct that the pending HEW proposal would require the deposit of social security contributions within 15 days after the end of each of the first two months of the quarter and 45 days after the end of the third month in the quarter. Is that correct?

Mr. AHART. That is correct, Mr. Chairman.

Senator NELSON. For the month of January, the deposit would be due on the 15th of February; for February the deposit would be due on March 15. The March payment would not be due until the 15th of May?

Mr. AHART. That is correct. This is a stretchout which by delaying the last deposit will cost the trust funds $30 million the first year (1980) and increasing over a period of time to $49 million for 1985.

Senator NELSON. $30 million?

Mr. AHART. $30 million the first year.

Senator NELSON. Is that compound interest?

Mr. AHART. It would be simple interest. We have projected it out over a period of years. The figures are viewed as conservative because they are computed using simple interest as opposed to compound interest.

Senator NELSON. Do you agree with the HEW estimate that, as of now, the States and municipalities are earning about $200 million a year on withheld social security contributions?

Mr. AHART. That is the amount of interest the trust funds would lose if no change were made in the regulations, Mr. Chairman.

Senator NELSON. The projections for the next 5 years would add another $1 billion. That must be on the assumption that the number of municipal and State employees covered by the social security system is not going to change in a 5-year period. Is that the assumption?

Mr. AHART. If you kept the current deposit procedure, which is once every quarter, 45 days after the end of each quarter, the trust funds would lose approximately $1 billion over a 5-year period. It is based on the estimated annual contributions of the State and local governments.

Senator NELSON. All right. Go ahead.

Mr. AHART. As I say, we think the November 1978 regulations do not go far enough. We would like to see them backed up at least to require deposits 15 days after the end of each month in the calendar quarter. Further than that, we have suggested to the Secretary that he reconsider and tighten it up even more to require deposits on a biweekly or semimonthly basis where that is the payroll period in the States and localities concerned.

Biweekly or semimonthly deposits would increase the earnings to the trust funds in the 5-year period, 1890–84, to $73 million more than HEW's original—March—proposal and $267 million more than HEW's final—November—regulations.

Senator NELSON. You are saying—your are recommending—that they pay social security withholding on the same schedule that they pay the income tax withholding.

Mr. AHART. The Federal income tax withholding; yes, sir.

Senator NELSON. On the same schedule, same day. Is that what you are saying?

Mr. AHART. Basically that would be the procedure.

That is a very brief summary of our position, Mr. Chairman. In essence, we support the direction in which the regulations are going. We think that they do not go far enough, and we would urge that they be tightened up even more.

Senator NELSON. We may have some further questions when the hearings are over and we have looked at the testimony. We will submit those in writing.

I assume you will be prepared to respond for the record?

Mr. AHART. We would be happy to.

Senator NELSON. Within the next 2 weeks to the written inquiries?

Mr. AHART. We would be happy to, Mr. Chairman.

Senator NELSON. Thank you very much. We appreciate it.

Mr. AHART. Thank you, Mr. Chairman.

[The prepared statements and study of Mr. Ahart follow:]

STATEMENT OF GREGORY J. AHART, DIRECTOR, HUMAN RESOURCES DIVISION, GENERAL ACCOUNTING OFFICE

Mr. Chairman and Members of the Subcommittee, we are pleased to be here today to discuss the impact on the Social Security trust funds of a change in HEW's regulations regarding the frequency of State deposits of social security contributions.

As you are aware, we reviewed this matter and issued a report to the Congress on December 18, 1978, entitled, "Liberal Deposit Requirements of States' Social Security Contributions Adversely Affected Trust Funds."

I would like at this time to submit a copy of the report for the record, and then summarize the report.

Effective January 1, 1951, the Social Security Act extended social security coverage to State and local government employees. Coverage is through voluntary agreements between the Secretary of HEW and the individual States. The act provides that the regulations of the Secretary of HEW shall be designed to make the deposit requirements imposed on States the same, so far as practicable, as those imposed on private employers.

Each State deposits the combined State and local government social security contributions directly with the Federal Reserve Bank for transfer to the trust funds. As required by HEW, each State deposits contributions and files wage reports of covered employees with HEW within 1 month and 15 days after the end of each calendar quarter. This timeframe was requested by the States and has been in effect since 1959. Before 1959, the States were required to file wage reports and make deposits within 30 days after the end of each calendar quarter.

Contributions paid by workers and their State and local government employers increased from about $865,000 in 1951 to over $10 billion in 1977. These contributions are estimated to increase to about $14.5 billion by 1980.

On March 30, 1978, HEW published in the Federal Register its proposed rulemaking increasing from quarterly to monthly the frequency with which States must deposit social security contributions on wages and salaries paid to covered employees—the so-called 15-15-15 method.

By allowing the States to make quarterly deposits of State and local contributions, HEW lost about $1.1 billion in interest income to the trust funds from 1961 through 1979.

Monthly deposits, 15 days after the end of each month under the proposed rulemaking, and prompt investment could result in additional interest earnings to the trust funds of over $1 billion during the 5-year period 1980-84. Semi-monthly or biweekly deposits could result in additional interest income of over $70 million for the trust funds during the same 5-year period.

HEW received about 3,300 comments on its March proposal, primarily from State officials, local political subdivisions, and governmental organizations. The commenters were overwhelmingly opposed to any changes in the States' deposit procedures.

HEW considered both the oral and written comments and, as a result, made what we consider to be a significant change which required that the States deposit the social security contributions for each of the first 2 months of a calendar quarter by the 15th day after each month. However, the contributions for the third month of the quarter will not be due until 1 month and 15 days after the end of that month—the so-called 15-15-15 method. These changes were published in the Federal Register on November 20, 1978, and are to become effective July 1, 1980.

The States' primary objection to more frequent deposits is loss of interest earned from investing contributions remitted to States by State agencies and local governments and the loss of cash flow.

However, there will not be a total loss of interest. In a July 5, 1978, letter to you, Mr. Chairman, the Secretary of HEW pointed out that States and local governments could still earn, under the March 30, 1978, proposed monthly depository procedure, a minimum of $50 million annually from prudent short-term investment of withheld contributions before depositing them with the Federal Reserve Bank. We believe that HEW deposit regulations which allow States to earn interest on funds which should be deposited in and earning interest for the trust funds are detrimental to the financial stability of the trust funds cannot be rationally justified, and should be changed. These funds are contributions in support of the Social Security System and should not be diverted for other purposes

States and local governments also indicated that administrative problems such as collecting and depositing funds, reporting, and documenting States' liabilities would result if more frequent deposits are required. These matters are discussed in detail in our report and we see no insurmountable problems that could not be reasonably worked out. Further, the 18-month implementation delay provided by Public Law 94-202, should be sufficient to deal with such problems.

On November 1, 1978, before the revised proposal was approved by HEW, we met with HEW officials and informed them that we could find no logical or valid justification for delaying the last monthly deposit. We pointed out, among other things, that

If the third monthly deposit were required, any monetary adjustments could be made when the quarterly report is filed. Also, by delaying the last deposit, States would be sending in two deposits on the same day.

Delaying the third monthly deposit in a quarter could allow States to retain the funds as long as 2½ months.

The HEW Secretary previously stated that the States and local governments could still earn under the originally proposed monthly depository procedures a minimum of $50 million annually from prudent short-term investments, which should fully compensate the States for administrative costs.

HEW is considering an annual reporting system, which, if adopted, would require less administrative reporting by the States. This would seem to negate the argument that the States need more time to receive, account for, and transmit payment.

By delaying the last deposit, HEW is placing itself in the same position it did in 1959 when it was estimated that the extra 15 days was costing the trust funds $0.5 million annually in interest income. We estimate that for 1977, the additional 15 days at the end of each quarter resulted in a loss of investment income of about $31 million to the trust funds. HEW apparently is saying that if it knew 20 years ago what it knows today, it might have acted differently and more quickly. What we are trying to prevent is a recurrence of the same situation.

Additionally, we estimate that for the 5 years from July 1, 1980 to June 30, 1985, the trust funds would earn $204.2 million less in interest income under the 15-15-45 requirements than under the March 1978 (15-15-15) proposal and $280.8 million less under the 15-15-45 requirements than under a semi-monthly deposit schedule. Social Security actuaries believe that these estimated 5-year losses should be considered as conservative, due to our using simple interest instead of compound interest.

HEW's original proposal to increase the frequency of deposits to a monthly basis was a step in the right direction. However, if these contributions were required to be deposited biweekly or semi-monthly, obviously additional interest would be earned.

We believe that the November 20, 1978, regulations calling for the 15-15-45 deposit requirements are not in the best interest of the trust funds since they do not maximize interest earnings to the trust funds. Since these regulations will not become effective until July 1, 1980, we recommended in our December 17, 1978, report that the Secretary of HEW reconsider his decision to implement the 15-15-45 requirements and urged that semi-monthly or biweekly deposits be required. However, at a minimum the HEW original proposal (15-15-15) would be a better alternative than the 15-15-45 requirements.

Mr. Chairman, that concludes our statement. We will be happy to answer your questions.

Report to the Congress

LIBERAL DEPOSIT REQUIREMENTS OF STATES' SOCIAL SECURITY CONTRIBUTIONS ADVERSELY AFFECTED TRUST FUNDS

Thd Social Security Administration could have earned about $1.1 billion in interest for the years 1961 through 1979 is States had been required to make more frequent deposits of Social Security contributions. If requirements were not changed, the trust funds would lose an additional $1 billion for the years 1980 through 1984 and significant amounts each year thereafter.

New regulations were published in the Federal Register on November 20, 1978, but under law are not effective until July 1, 1980. These regulations will partially correct the problem, but they are still too liberal and will not maximize interest income to the trust funds.

Comptroller General of the United States,
Washington, D.C.

B-164031(4)

To the President of the Senate and the Speaker of the House of Representatives

This report points out (1) how the Social Security trust funds were affected in the past by State depository requirements and (2) the effects of the Health, Education, and Welfare Department's decision to require more frequent deposits of Social Security contributions.

During the review, we found that the Social Security trust funds have lost interest income due to special treatment given to States, and we found that the latest requirements on the frequency of State deposits are less desirable than an earlier proposal.

We are sending copies of this report to the Director, Office of Management and Budget; the Secretary of Health, Education, and Welfare; the Secretary of the Treasury; and the Commissioner of the Social Security Administration.

Elmer B. Staats,
Comptroller General of the United States.

Digest

If quarterly deposit requirements to the Social Security trust funds were continued, an additional $1 billion in interest would be lost from 1980 through 1984. The funds could have earned about $1.1 billion in additional interest from 1961 through 1979 had the States been required to deposit contributions more frequently—monthly instead of quarterly—thus making the funds available for earlier investment. (See p. 4.)

In March 1978 the Department of Health, Education, and Welfare published in the Federal Register a proposal to require these deposits to be made on a monthly basis, but in November 1978 it decided to modify the proposal to require less frequent deposits. GAO could find no logical or valid justification for the modification, which will result in the trust funds earning an estimated $30 million less in interest income the first year than could have been earned under their March proposal, and a total of several hundred million dollars less in 5 years. (See pp. 16 to 20.)

The Social Security Act requires that regulations be designed to make the deposit requirements imposed on States the same, so far as practicable, as those imposed on private employers. In earlier discussions with HEW officials, GAO suggested

that, where applicable, HEW should consider requiring States to deposit contributions more often than monthly—semimonthly or biweekly. This would increase interest earnings to the trust funds and more closely aline frequency of deposits by States with that of the Internal Revenue Service regulations, which generally require private employers to deposit Federal income and social security taxes weekly, biweekly, or monthly. Based on semimonthly or biweekly deposits, an estimated additional $73 million in interest earnings could be earned over the amount from monthly deposits during the same 5-year period, 1980–84. (See pp. 4 to 8).

The States' principal objections to increasing the frequency of deposits are loss of interest earnings or cash flow and administrative problems and additional costs. GAO believes social security contributions should be deposited in and earning interest for the trust funds, and were not intended to provide States with interest earnings or cash flow. In addition, the Secretary of HEW stated that, under its March 1978 proposal, the States could still earn about $50 million annually from prudent short-term investment of contributions prior to deposit with the U.S. Treasury. States and local governments indicated that administrative problems such as collecting and depositing funds, reporting, documenting States' liabilities, etc., would result if more frequent deposits are required. (See pp. 9 to 15.)

GAO recognizes that some problems will occur but believes that the 18-month implementation delay provided by law should be sufficient to deal with such problems.

New regulations were published in the Federal Register on Nobember 20, 1978. These regulations call for deposits within 15 days of the end of each of the first 2 months of a calendar quarter, and within a month and 15 days of the end of the third month of the calendar quarter. (See p. 16.)

In commenting on the draft of this report, HEW stated:

"In arriving at the depository schedule contained in the new regulations, the Department was concerned about its responsibility to protect the interest of the Trust Funds. At the same time, it had to consider the concerns expressed by State Social Security Administrators, numerous local governments, governors, and many Members of Congress. The process agreed upon protects the trust fund interests; at the same time it is a reasonable accommodation to the States' concerns about administrative costs and problems in collecting and transmitting more frequent deposits."

HEW's response to GAO's draft report did not comment on (1) GAO's arguments regarding the revised proposal or (2) the significant amounts of interest income which will be lost under the revised proposal. Therefore, GAO still believes that the regulations as published in the Federal Register are not in the best interest of the trust funds since they do not maximize interest earnings to the trust funds. GAO further believes that financial assistance to States should be specifically legislated and not provided at the expense of the trust funds. (See p. 22.)

Since these regulations will not become effective until July 1, 1980, the Secretary, HEW, should reconsider his decision to require deposits less frequently than monthly. GAO urges semimonthly or biweekly deposits to substantially increase interest earnings to the trust funds. However, at a minimum, the HEW original (monthly) proposal would be a viable alternative.

To carry out this change in frequency of deposits, the Secretary, HEW, should consider the feasibility of requiring State and local governments to make their deposits together with their withheld income tax deposits. (See pp. 21 and 22.)

CHAPTER 1

INTRODUCTION

Effective January 1, 1951, the Social Security Act, as amended (42 U.S.C. 418), extended social security coverage to State and local government employees. Coverage is through voluntary agreements between the Secretary of Health, Education, and Welfare (HEW) and the individual States to avoid the constitutional question of Federal authority to impose social security taxes on State and local government employers. The States, in turn, generally have agreements with local governments and are responsible for depositing and reporting social security contributions (employees' and employers' shares) by State agencies and local governments within State boundaries. All 50 States, Puerto Rico, the Virgin Islands, and about 50 interstate instrumentalities (treated as States for coverage purposes) have made agreements with the Secretary of HEW for social security coverage.

About 9.4 million (73.8 percent) of State and local government employees are currently covered by the program and represent about 10.3 percent of covered workers. Contributions paid by workers and their State and local government employers increased from about $865,000 in 1951—the first year the States participated—to about $825 million in 1961, about $4 billion in 1971, and over $10 billion in 1977.

Each State deposits the combined State and local government social security contributions directly with the Federal Reserve bank for transfer to the trust funds. As required by HEW, each State files wage reports of covered employees with HEW within 1 month and 15 days after the end of each calendar quarter. This time frame was requested by the States and has been in effect since 1959. Before 1959 the States were required to file wage reports and make deposits within 30 days after the end of each calendar quarter.

PURPOSE AND SCOPE OF REVIEW

On March 30, 1978, HEW published in the Federal Register its proposal to increase the frequency by which States must deposit social security contributions. We evaluated the issues surrounding the frequency of State deposits and the reasonableness of HEW's proposal.

Our work was performed in Arkansas, Louisiana, Maryland, New Jersey, and Texas and at Social Security Administration (SSA) headquarters in Baltimore, Md.

We reviewed the legislative history of certain sections of the Social Security Act, as amended, interviewed SSA and State and local government officials, and reviewed and analyzed necessary agency records

FINANCING THE SOCIAL SECURITY SYSTEM

The Federal Old-Age and Survivors Insurance Trust Fund, the Federal Disability Insurance Trust Fund, and the Federal Hospital Insurance Trust Fund (hereafter referred to as trust funds) were established as separate accounts in the Treasury on January 1, 1940, August 1, 1956, and July 30, 1965, respectively.

Program funds are accounted for and administered separately. The major sources of receipts of all of these trust funds are paid by (1) workers and their employers, (2) individuals with self-employment income, and (3) workers employed by State and local governments and their employers.

In general, an individual's contributions are computed on annual wages or self-employment income, or both. In 1977 the maximum amount payable by an employee was 5.85 percent of $16,500 ($965.25) while the maximum amount payable by a self-employed individual was 7.90 percent of $16,500 ($1,303.50).

In recent years the financial stability of the trust funds has been seriously impaired. In fiscal year 1977 receipts to the trust funds totaled $96.5 billion while disbursements totaled about $100.3 billion. This reflected a continued drain on the assets of the trust funds. In December 1977 the Congress enacted the Social Security Amendments of 1977 (Public Law 95–216) in an attempt to maintain the trust funds on a sound financial basis and to strengthen both the short- and long-range financial stability of these funds. One of the major provisions of Public Law 95–216 increased the social security tax rate and contribution base for both employees and employers. For example, the tax rate will increase from 5.85 percent for 1977 to 7.15 percent through 1989. After 1989 the rate will be 7.65 percent. The contribution base will increase from $16.500 for 1977 to $29,700 for 1981. For 1982 and later years, the changes in the contribution base will be indexed to the changes in average earnings in covered employment

The Board of Trustees of the trust funds is composed of the Secretaries of Treasury, Labor, and HEW. The SSA Commissioner serves as Secretary of the Board of Trustees.[1] The 1978 Trustees report dated May 15, 1978, reflects the enactment of the Social Security Amendments of 1977. The report indictates hat the near-term financing seems adequate, and for the last decade of this century the year-by-year income should be considerably more than expenditures. However, after the first decade of the next century income should be considerably less than expenditures; the Federal Disability Insurance Trust Fund may be depleted in 2021 and the Federal Old-Age and Survivors Insurance Trust Fund in 2029.

The Federal Hospital Insurance Trust Fund, according to the Trustees, is adequately financed over the next 7 years; however, the tax rates scheduled for

[1] Section 5 of Public Law 95–292, approved June 13, 1978, transfers this responsibility from the SSA Commissioner to the Administrator of the Health Care Financing Administration for the Federal Hospital Insurance Trust Fund.

the mid-1980s are not adequate. As a result, the Federal Hospital Insurance Trust Fund is expected to be depleted about 1990, rather than 1987, as was estimated in 1977.

The improved financial outlook for the old-age survivors and disability insurance programs developed because the 1977 amendments decreased future expenditures and increased future income. The hospital insurance program, however, was left in approximately the same financial position that it would have been in if the amendments had not been enacted.

Chapter 2

THE SOCIAL SECURITY TRUST FUNDS HAVE LOST INVESTMENT INCOME

The Social Security trust funds could have earned about $1.1 billion in additional interest income from 1961 through 1979—19 years. The loss of this interest resulted from allowing States to make less-frequent deposits of social security contributions than HEW could have required. If States had made deposits monthly instead of quarterly the moneys would have been available for earlier investment to earn additional interest. If quarterly deposit requirements were continued, over $1 billion would be lost from 1980 through 1984—5 years—as shown below.[1]

[In millions]

Year:	*Amount*
1980	$180.4
1981	216.7
1982	237.9
1983	255.9
1984	275.2
Total	1,166.1

The amount of interest lost increases each year and will continue to increase as the contribution rate and contribution base increase.

MORE FREQUENT STATE DEPOSITS NEEDED

The Social Security Act, as amended, provides for social security coverage to State and local government employees. To accomplish this, the act further provides that:

The HEW Secretary shall enter into an agreement with the State to extend the program to State and local government employees.

The agreement requires the State to pay State and local government social security contributions to the Secretary of the Treasury at such time as the HEW Secretary may prescribe by regulations.

The regulations of the HEW Secretary shall be designed to make the requirements imposed on States the same, so far as practicable, as those imposed on private employers.

The Secretary of the Treasury, as managing trustee, shall invest contributions not currently needed for withdrawals in obligations of the United States or in obligations guaranteed by the United States.

The 1951 Federal regulations required the States to report on wages and salaries paid to covered employees and to deposit both the employers' and employees' contributions within 30 days after the end of each calendar quarter. In 1959 the States petitioned HEW for additional time and were granted an extra 15 days after the end of each calendar quarter for reporting and depositing contributions. These requirements are still in effect.

The Internal Revenue Service (IRS) requires private employers to follow a depository schedule based on accumulated withheld income and social security taxes. The social security amounts are then transferred to the trust funds.

The State and local governments are subject to the IRS depository schedule only for withheld income taxes, since the States remit social security contributions directly to the U.S. Treasury. Generally, the current IRS deposit rules for accumulated withheld income and social security taxes are:

Deposit at end of month after end of the quarter if the total undeposited taxes are less than $200.

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[1] New regulations increasing the frequency of deposits were published in the Federal Register on Nov. 20, 1978, and are discussed in chapters 4 and 5.

Deposit within 15 days after the end of month if taxes are $200 to less than $2,000.

Deposit within 3 banking days after the quarter-monthly period in which a payday occurred (7th, 15th, 22d, and last day of the month) if taxes are $2,000 or more.

Since 1951 IRS has made several changes requiring deposits to be made monthly, semimonthly, biweekly, or weekly. However, HEW has made no changes from 1959—when States were given 15 additional days to make deposits, from 30 days after the end of each calendar quarter to 1 month and 15 days after the end of each calendar quarter—to November 1978.

EFFORTS TO INCREASE FREQUENCY OF STATE DEPOSITS

Monthly State deposits of contributions were considered by HEW in 1969. However, HEW decided that it was not the proper time to propose more frequent deposits. HEW believed that monthly or semimonthly deposits would eventually be required if the trust funds could reasonably be expected to earn additional interest income in excess of $20 million annually through more frequent deposits. The effort to require more frequent deposits was apparently not vigorously pursued at that time, although States' contributions for 1969 were about $3 billion.

Again in 1974, HEW considered initiating procedures for increasing the frequency of deposits by the States from quarterly to monthly. The States opposed HEW's position because they used contributions for investments or cash flow. Some States indicated that they would have administrative and legal problems if they were required to make more frequent deposits. No changes were made at that time.

During these times HEW considered having the State and local governments make their deposits to IRS together with their Federal withholding tax deposits; but, apparently because of legal problems which would have required changes in the Social Security Act and in some State laws, this change in procedure was not pursued.

The Subcommittee on Social Security of the House Committee on Ways and Means looked into these problems in late 1975 by using a questionnaire prepared in conjunction with SSA and States. The questionnaire was designed to secure data from States and to assume, for purposes of computation and analysis, the establishment of a monthly depository procedure. The Subcommittee requested SSA to summarize States' responses to the questions. The SSA Report summarized the data but did not attempt to evaluate facts or draw conclusions.

In February 1978 we became aware of HEW's proposal to change its regulations requiring that deposits be made 15 days after the end of each month, and we discussed this matter with SSA officials. Although we had not looked into this matter in detail, it appeared to us that if it was reasonable for the States to deposit contributions 15 days after the end of each month, then it was just as reasonable for those States where employees were paid semimonthly or biweekly to deposit contributions 15 days after each semimonthly or biweekly payday. We pointed out that:

Over half of the State and local government employees are currently being paid more often than monthly—generally semimonthly or biweekly.

Some States require State agencies and local governments to remit social security contributions to them more often than quarterly (semimonthly, biweekly, or monthly). The semimonthly or biweekly submissions are more stringent than the monthly deposits proposed by SSA.

Deposits after each semimonthly or biweekly payday would increase interest earnings to the trust funds.

We also stated that if HEW was going to change its regulations to require monthly deposits and decide at a later date to change them again (to more frequently than monthly), it would be better to make the entire change at one time. A subsequent effort to change the regulations would be subject to the 18-month waiting period required in Public Law 94-202. (See p. 15.) SSA officials acknowledged that our suggestion for requiring deposits more frequently than monthly was valid and could be implemented. However, they were reluctant to request more stringent deposit requirements because the States had been told that the HEW proposal would require deposits no more frequently than monthly.

PROPOSED REGULATION TO INCREASE FREQUENCY OF DEPOSITS

On March 30, 1978, HEW published in the Federal Register its proposed rulemaking increasing from quarterly (1 month and 15 days after the end of each calendar quarter) to monthly (15 days after the end of each month) the frequency

with which States must deposit social security contributions on wages and salaries paid to covered employees. Reporting by States is to remain on a quarterly basis—1 month and 15 days after the end of each calendar quarter.

Monthly deposits, 15 days after the end of the month under the proposed rulemaking, and prompt investment could result in additional interest earnings to the trust funds of over $1 billion during the 5-year period 1980-84. (See p. 4.)

Semimonthly or biweekly deposits could result in an additional $73 million of interest income for the trust funds during the same 5-year period:

[In millions]

Year:	*Amount*
1980	$11.3
1981	13.6
1982	14.9
1983	16.0
1984	17.2
Total	73.0

The additional interest income which can be earned by requiring deposits more frequently than monthly increases each year; this additional interest income will continue to increase as the contribution rate and contribution base increase.

However, several bills [1] have been introduced in the 95th Congress to permit States and local governments to continue making social security deposits on a calendar-quarter basis. Any of these bills, if enacted, would prevent the trust funds from earning the additional interest income.

Chapter 3

STATE AND LOCAL GOVERNMENT OBJECTIONS TO MORE FREQUENT DEPOSITS

We visited five States and a selected number of local governments to evaluate their views on the proposed regulations, published in the Federal Register on March 30, 1978, requiring monthly deposits of social security contributions. The States and local governments visited expressed strong opposition to the proposed regulations. The principal objections were: (1) loss of interest earnings or cash flow and (2) additional administrative costs and problems.

LOSS OF INTEREST EARNINGS OR CASH FLOW

The States' primary objection to more frequent deposits is loss of interest earned from investing contributions remitted to States by State agencies and local governments and the loss of cash flow from using these contributions from the time the employees are paid and their deductions are retained by the State until deposits are made with the Treasury Department.

SSA's report on the results of the Subcommittee on Social Security of the House Committee on Ways and Means questionnaire showed that, for those responding, an estimated $45 million was earned by the States in 1974 on social security contributions and that, if monthly deposits were required, these States would lose about $30 million, resulting in a net investment income of about $15 million. We noted, however, that estimates were not always comparable. For example, one State's estimated interest income resulted from investing State employees' shares only, while another State's estimated interest income included both the State and local employees' shares. The estimated amounts of interest income reported for the five States visited ranged from about $184,000 to $6,067,000 and totaled about $10,100,000 for 1974.

It is important to note, however, that the interest earnings on the employer and employee social security contributions held by the States and local governments are derived from funds that should be deposited in and earning interest income for the trust funds. These contributions were not intended to provide the States with interest earnings or cash flow.

Most of the State and local governments visited were required to make, and were making, deposits of withheld income taxes to IRS within 3 banking days after each quarter-monthly period in which a payday occurred (7th, 15th, 22d, and last day of the month). Thus, a State which pays its employees semimonthly or biweekly and withholds $2,000 or more remits withheld Federal income taxes to IRS semimonthly or biweekly (3 banking days after the quarter-monthly period

[1] H.R. 1300, Jan. 4, 1977; S. 1967, Aug. 1, 1977; and H.R. 11117, Feb. 23, 1978.

in which the payday occurred), but that State is not required to remit to a Federal Reserve bank the social security contributions it deducts from the pay of these same employees until 1 month and 15 days after the end of each calendar quarter. Under HEW's proposed regulations States would be required to make deposits within 15 days after the end of each month during the calendar quarter.

In a July 5, 1978, letter to Senator Gaylord Nelson, the HEW Secretary pointed out that States and local governments could still earn, under the proposed monthly depository procedures, a minimum of $50 million annually from prudent short-term investment of withheld contributions before depositing them with the U.S. Treasury.

We noted that, of the five States visited, two are investing in U.S. securities. It was not possible to specifically identify these investments as coming from trust fund moneys because the sources of States' invested funds are not always identified. However, it seems reasonable to assume that some of these investments are being made with trust fund moneys or with moneys which are available because of cash flow furnished by trust fund moneys. Thus, it appears that the Treasury may be paying interest to States on moneys which should be deposited in and earning interest for the trust funds. We believe that HEW deposit regulations which allow States to earn interest on investments by using funds which should be deposited in and earning interest for the trust funds are not only detrimental to the financial stability of these trust funds but cannot be rationally justified and should be changed.

ADMINISTRATIVE PROBLEMS AND ADDITIONAL COSTS

The States' other objections to more frequent deposits are the administrative problems and the related additional costs. Their concerns were conveyed:

In responses to the 1975 questionnaire of the Subcommittee on Social Security of the House Committee on Ways and Means,

In meetings with HEW/SSA officials,

During our visits to the State and local governments, and

In subsequent letters to us.

These concerns are discussed below.

Collecting and depositing funds and reporting

With regard to the timeliness of collecting and depositing funds and the frequency of reporting, three of the five States require State agencies and local governments to remit social decurity contributions to them more often than quarterly (semimonthly, biweekly, and monthly).[1] In these instances, the funds are already deposited with the States and the additional administrative work, other than reconciling contributons to the entities' quarterly reports, has already been accomplished.

Other States, however, require social securtiy deposits from State agencies and local governments on a quarterly basis. Since social security contributions are based on the same payroll records as withheld income taxes, it would seem reasonable that State agencies and local governments could remit social secuirty contributions to States in the same timely manner as withheld income taxes are remitted to IRS. Most State agencies and local governments visited were required and were making these deposits to IRS within 3 banking days after each quarter-monthly period. This time frame should allow States sufficient time to remit these contributions to HEW on a "payday" basis.

Monthly reporting is another issue raised by the States. Some States feel that a wage report is required to be forwarded along with each deposit of social security taxes, no matter how frequently. When States and local governments make semimonthly, biweekly, or monthly deposits of Federal income taxes, only one report to IRS is required and that report is not due until 1 month after the end of each calendar quarter. Similarly, if as stated under the HEW proposed rulemaking, States and local governments were required to make monthly deposits of social security contributions, no additional wage reports would be required—only one report to HEW would be required, and that report would not be due until 1 month and 15 days after the end of each calendar quarter.

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[1] The summary report responses to questionnaires sent to States prepared by SSA regarding the dates payments are due in State Social Security agencies from other State agencies and political subdivisions stated that "in 17 States some or all of the contributions are paid to the State social security agency more than once each quarter (primarily each pay date or monthly). * * * In two States, it was indicated that only the employees' shares for State agencies are paid more frequently * * *."

Documentation to support States' liabilities

Another administrative matter which concerned the States was the documentation required to support payment of contributions by both local government agencies and the States. Examples of required documentation included vouchers, warrants, certification statements, wage statements, payroll information or records, etc.

Payments to the State by local governments would be based on payrolls at the local levels, which should provide sufficient documentation to support the employees' and the employers' shares if the local agency is responsible for both. As such, the State, having received both the employers' and employees' shares, should be able to forward these amounts to Treasury for deposit to the trust funds. However, some States also pay the employer's share of some non-State or local employees, such as teachers, librarians, and Boards of Education. One of the States visited contended that it has no knowledge of its employer liability on behalf of these individuals until it receives a quarterly report from each entity; the State would only pay the employer cost based upon evidence of an established liability.

We believe that the evidence required by the States is a matter for them to determine; however, as we understand it, the amount transmitted by local governments and other State agencies representing the employees' shares would be about one-half of the total liability. Accordingly, this would seem to be reasonable evidence to indicate the States' liability, keeping in mind that the exact liability is not determined until 1 month and 15 days after the final month ending the calendar quarter and that any minor adjustments can be made at that time. If, however, under the above-described procedure the State would require additional evidence to support its liability, it could request a certified statement from the reporting agencies or a copy of the payroll. We see no insurmountable problems in this matter that could not be reasonably worked out.

Other areas of concern

The following are some of the other statements made during our visits to the States and local governments:

The workload would increase because of additional deposits, reconciliations, and adjustments.

There would be no major problems in more frequent deposits to the States if no additional reporting was required.

More checks would have to be issued if the frequency of deposits were increased.

15 days is not sufficient time because some entities are unable to meet the present deadline.

Additional personnel and space would be needed to handle the increase in workload.

Some of the above items would increase administrative costs. However, we noted that three of the five States we visited charge each State agency and local government within the State a fee for each person covered under the social security program; these fees were sufficient to recover all (in two States) and part (in one State) of the administrative costs of operating the social security program.

We did not study the reasonableness of the 15-day time frame for depositing monthly contributions. Although 15 days seems to be a reasonable amount of time to make deposits to the trust funds, the exact number of days should be determined by HEW after consulting with the States. If all State and local government employees are paid twice a month on the 15th and 30th of the month, the interim deposits (if semimonthly) could be required by the 30th and the following 15th, respectively, if the 15-day time frame is decided upon. However, if all State and local employees are paid twice a month and paid on many different days, so that some employees were being paid on every working day of the month, HEW could consider requiring the interim deposits of that State to follow the IRS quarter-monthly rule or perhaps a "half-monthly" rule.

As mentioned previously (see p. 10), administrative problems were examined in 1975 by the Subcommittee on Social Security of the House Committee on Ways and Means by using a questionnaire prepared in conjunction with HEW and the States. In response to a question regarding administrative changes States believed were needed to implement a monthly deposit procedure, the study pointed out that most States indicated additional employees would be needed. The study further added that some States indicated it was difficult to provide precise information. We believe that some of the responses indicating substantial increases in personnel and related costs could have been based on the States' misunderstanding in 1975 that the frequency of reporting requirements to HEW would be increased; i.e., each time a deposit was made, a report would be required from

45-083—79——2

the local governments and from the State. This possible misunderstanding was discussed in our comments on the notice of proposed rulemaking dated June 9, 1978, where we suggested that clarification was needed. (See app. I.)

In the July 5, 1978, letter to Senator Gaylord Nelson, the HEW Secretary stated there could be some minor increases in administrative costs. In view of the minimum $50 million interest earnings the States could still realize annually under the monthly deposit procedure, the Secretary stated that the total cost of administration by the States should continue to be more than fully compensated. As a point of reference, the Secretary stated that the cost of IRS administration of the contribution colleciting and reporting functions required of the States under the proposed regulation would be less than $2 million annually. Our review did not include an evaluation of the reasonableness of the $2 million figure used by the HEW Secretary. The Secretary further stated that he could see no reason for a reduction in the present level of accuracy in reporting contributions by the States (another issue raised by the States) since reporting contributions, including reconciliation of accounts, will continue on a quarterly basis—exactly as presently done.

We agree that the States would have to perform additional work in collecting and reporting funds and in issuing more checks, reconciling checks to the quarterly reports, and maintaining appropriate records—particularly in States with large numbers of reporting entities. We recognize that in a situation involving all 50 States, about 60 interstate instrumentalities, and over 60,000 local governments that problems will arise due to a lack of uniformity or exceptions to the norm.

For example, not all States and local governments pay their employees on the same frequency or on the same day. Thus, one should not expect a State or local government to remit deposits semimonthly or biweekly if it pays its employees monthly.

Another example is where a State pays some or all of the contribution for a State or local employee or elected official. It may not be possible to determine the exact State liability on a semimonthly, biweekly, or monthly basis. In these instances, exceptions to the general depositing requirements should be allowed by HEW.

Public Law 94-202 provides that any changes pertaining to frequency of deposits may not become effective until 18 months after the date of HEW's final publication of the rulemaking in the Federal Register. The purpose of Public Law 94-202 is to assure that States would be given ample lead time to implement any changes and would also give the Congress an opportunity to review any changes which the HEW Secretary might propose. We believe the States and local governments should be able to effectively and efficiently implement the change in the frequency of deposits within 18 months.

CHAPTER 4

HEW'S MODIFICATION TO PROPOSED REGULATIONS

In chapter 2 we discussed HEW's (1) efforts to increase the frequency of deposits and (2) proposed regulations to increase the frequency of deposits published in the Federal Register on March 30, 1978. In chapter 3, we discussed the State and local governments' objections to more frequent deposits.

HEW ACTIONS ON COMMENTS ON PROPOSED REGULATIONS

HEW received about 3,300 comments, primarily from State officials, local political subdivisions, and governmental organizations. The commenters were overwhelmingly opposed to any changes in the States' deposit procedures. Reasons given included those discussed in chapter 3. HEW officials also met with members of the National Conference of State Social Security Administrators, who opposed any plan for more frequent deposits under which the States would remain liable for the contributions due.

HEW considered both the oral and written comments on the proposal to require States to deposit 15 days after the end of each month and, as a result, made a significant change. HEW then proposed to retain the requirement that the States deposit the social security contributions for each of the first 2 months of a calendar quarter by the 15th day after each month. For example, the contributions for the months of January and February will be due February 15 and March 15, respectively. However, the contributions for the third month of the quarter (March) will not be due until 1 month and 15 days after the end of that month—May 15. These changes were published in the Federal Register on November 20, 1978, and are to become effective July 1, 1980.

The following are excerpts from some of the documents, which explain HEW's rationale for the modifications to the March 1978 published proposal and discuss the issues raised.

States need time to receive, account for, and transmit payment from the employing entities. HEW believes however, that a 15-15-45 day depositing requirement strikes a reasonable balance in (1) allowing the States time to receive moneys from their local governments, (2) making the treatment of government and private employers more equitable, and (3) increasing the interest income to the social security trust funds.

HEW is considering an annual reporting system; if it is adopted, the 45-day deposit schedule will still accommodate the States, which will continue to reconcile their payment quarterly.

One commenter indicated that it would be "* * * just as practical to require deposits to be made 15 days after the end of the pay period as it is to be made 15 days after the end of the month as currently proposed." This proposal does not take into account the States' need to accumulate the necessary information and funds from the local governments.

HEW believes there are many advantages to the 15-15-45 method which were not present in the methods previously published or suggested in response to those proposals:

(1) The States will have more use of the social security contributions than under the 15-15-15 day requirement and will be able to use these moneys to defray any administrative expenses.

(2) The States will also have more control of their liability under the agreement since they will have time each quarter to reconcile their total liability.

(3) This method causes less change in existing State procedures and facilitates the accommodation of State processes.

(4) The social security trust funds will receive more money than they currently do under quarterly payments, and the flow will be more predictable and steady than at present.

(5) The Secretary will be fulfilling his statutory responsibility to make requirements for States and private employers as similar as possible.

Additionally, in a September 26, 1978, letter to Senator Gaylord Nelson, the acting Commissioner of Social Security stated that the new proposed depository schedule for the States (15-15-45) is designed to fulfill HEW's trust fund obligation and to meet two basic concerns:

Elimination of additional administrative complexity.

Assurance that the States have sufficient use of the contributions to pay the administrative costs involved in handling reports and moneys for the employees of the States and their localities.

The letter also stated that the 15-15-45 proposal will reduce the amount of interest earnings to the trust funds by about $30 million annually. It does, however, provide opportunities for earnings in at least that amount by the States through judicious short-term investment, thus more than compensating them for costs attributable to administering the program.

HEW'S MODIFICATION WILL RESULT IN ADDITIONAL LOSS OF INTEREST INCOME

On November 1, 1978, before the revised proposal was approved by HEW, we met with HEW officials and informed them that (1) we could find no logical or valid justification for delaying the last monthly deposit from HEW's initial proposal and (2) a biweekly or semimonthly deposit requirement appeared to us to be just as valid as when we initially discussed it in February 1978. We pointed out, among other things, that:

If the third monthly deposit (15-15-15) were required on April 15, July 15, etc., any monetary adjustments could be made when the quarterly report is filed on May 15, August 15, etc., since the current reconciliation quarterly form includes a line for adjustments. Also, by delaying the last deposit in the proposed 15-15-45 method, States would be sending in two deposits on the same day. For example, the payment for the third month (March) of the first quarter would be due on May 15, and the deposit for the first month (April) of the second quarter would also be due on May 15. If the 15-15-15 method were retained and the third deposit for the first quarter were made on April 15, any adjustments needed for the first quarter could be made when the May 15 first deposit of the second quarter is made.

Delaying the third monthly deposit in a quarter would allow States which pay their employees on March 1 and June 1, etc., to retain the funds until May 15 and August 15, etc.—about 2½ months.

The HEW Secretary previously stated in his letter of July 5, 1978 (see p. 10), that the States and local governments could still earn under the proposed (15-15-15) monthly depository procedures a minimum of $50 million annually from prudent short-term investments, which should fully compensate the States for administrative costs. We see no need for the trust funds to lose an additional $30 million in interest income in the first year. (See annual and cumulative effects on p. 20.)

In 1959, when the States were granted the additional 15 days at the end of each quarter to send in their contributions, it was estimated that the extra 15 days was costing the trust funds $0.5 million annually in interest income and that perhaps, to offset the loss of income, monthly deposits should be required. We estimate that for 1977 the additional 15 days at the end of each quarter resulted in a loss of investment income of about $31 million to the trust funds. It seems to us that, by delaying the last deposit under the 15-15-45 proposal, HEW is placing itself in the same position it did in 1959, which will result in a significant loss of investment income to the trust funds over the years.

If annual reporting is adopted, there would be less administrative reporting by the States, which would seem to negate the argument that the States need more time to receive, account for, and transmit payment.

The following table shows the estimated additional amounts of interest income which could be earned if deposits were made (1) semimonthly, (2) monthly (as originally proposed by HEW), and (3) under HEW's revised published regulations. Although July 1, 1980, is the earliest the change can become effective, the table shows (for illustrative purposes) the effect on a calendar-year basis. The amounts were based on estimated calendar year State and local government contributions using simple interest.

ESTIMATED ADDITIONAL INTEREST INCOME THAT COULD BE EARNED BY THE TRUST FUNDS OVER PRESENT DEPOSITORY METHOD

[In millions]

Calendar year	Deposit requirements: Semi-monthly	HEW original proposal (15-15-15)	HEW revised regulations (15-15-45)	Differences: Semi-monthly/ 15-15-15	15-15-15/ 15-15-45	Semi-monthly/ 15-15-45
1980	$191.7	$180.4	$150.3	$11.3	$30.1	$41.4
1981	230.3	216.7	180.5	13.6	36.2	49.8
1982	252.8	237.9	198.2	14.9	39.7	54.6
1983	271.9	255.9	213.2	16.0	42.7	58.7
1984	292.4	275.2	229.3	17.2	45.9	63.1
Total, 1980-84	1,239.1	1,166.1	971.5	73.0	194.6	267.6
1985	314.3	295.8	246.5	18.5	49.3	67.8
Total, 1980-85	1,553.4	1,461.9	1,218.0	91.5	243.9	335.4
Total 5 yr (July 1, 1980 to June 30, 1985)[1]	1,300.4	1,223.8	1,109.6	76.6	204.2	280.8

[1] Estimated by including ½ of the amounts for both 1980 and 1985.

As shown above, for 1980 the trust funds would earn $30.1 million less in interest income under the 15-15-45 requirements than under the 15-15-15 proposal and $41.4 million less under the 15-15-45 requirements as compared with a semimonthly deposit schedule. Comparable amounts for 1985 would be $49.3 million and $67.8 million, respectively. It should be noted that these annual differences will continue to increase after 1985 as the contribution rate and contribution base increase.

For the 5 years from July 1, 1980, to June 30, 1985, the trust funds would earn $204.2 million less in interest income under the 15-15-45 requirements than under the 15-15-15 proposal and $280.8 million less under the 15-15-45 requirements than under a semimonthly deposit schedule.

Chapter 5

CONCLUSIONS AND RECOMMENDATIONS

CONCLUSIONS

The States' and local governments' objections to more frequent deposits are (1) the loss of investment income because the social security contributions would no longer be in their possession for a longer period of time and (2) the administrative problems and additional costs of more frequent deposits. We believe that these social security contributions should earn investment income for the trust funds; we see no valid reason for the continued extended retention of these social security contributions by the State and local governments. With respect to the administrative problems and related costs, we believe that these problems can be reasonably worked out within the time frame provided by Public Law 94-202.

It cannot be overlooked that the Social Security trust funds could have earned about $1.1 billion additional interest from 1961 to 1979 if monthly deposits were required. The loss of this interest income resulted from HEW permitting the States to continue to make quarterly deposits of social security contributions rather than requiring more frequent deposits, as required of private employers who generally must deposit social security taxes to IRS weekly, semimonthly, biweekly, or monthly. Increasing the frequency of deposits and relating such deposits for social security contributions to the payday will increase interest earnings for the trust funds. Accordingly, the frequency of deposits should be increased.

We believe HEW's original proposal to increase the frequency of deposits to a monthly basis was a step in the right direction and would result in the trust funds earning additional interest income of over $1 billion from 1980-84. However, if these contributions were required to be deposited biweekly or semimonthly, an additional $73 million could be earned during the same time period.

In a draft of this report submitted for comment on November 14, 1978, we stated that we do not agree with the then-revised proposal to delay the final quarterly deposits. We could find no logical or valid justification for such a delay which, in the next several years, would result in the trust funds earning several hundred million dollars less in investment income than could be earned if deposits were required monthly (as originally proposed by HEW) or semimonthly. (See p. 20.)

Moreover, in view of the continued increase in contributions in future years which should result from increases in both the tax rate and contribution base, the potential for additional investment income by requiring deposits more frequently than monthly will be even greater, and the change to more frequent deposits would seem to be more justified.

Accordingly, we suggested in the draft report that the Secretary, Health, Education, and Welfare expedite issuing the revised regulations and strongly consider semimonthly or biweekly deposits to substantially increase interest earnings to the trust funds. We suggested that once the frequency was decided, the number of days to make such deposits should be determined after consultation with the States. We also suggested that to carry out this change in frequency of deposits, the Secretary should consider the feasibility of requiring State and local governments to make their deposits with their withheld income tax deposits if this deposit procedure (1) would reduce administrative problems and costs at State and local levels and (2) could be arranged with IRS and State and local governments, provided any required changes in the Social Security Act and State laws can be made. (See p. 6.)

New regulations were published in the Federal Register on November 20, 1978. These regulations call for deposits within 15 days of the end of each of the first 2 months of a calendar quarter, and within a month and 15 days of the end of the third month of the calendar quarter (15-15-45).

In commenting on the draft of this report, HEW stated:

"In arriving at the depository schedule contained in the new regulations, the Department was concerned about its responsibility to protect the interest of the Trust Funds. At the same time, it had to consider the concerns expressed by State Social Security Administrators, numerous local governments, governors, and many Members of Congress. The process agreed upon protects the trust fund interests; at the same time it is a reasonable accommodation to the States' concerns about administrative costs and problems in collecting and transmitting more frequent deposits."

HEW's response to our draft report did not comment on (1) our arguments regarding the revised proposal or (2) the significant amounts of interest income which will be lost under the revised proposal. Therefore, we still believe that the regulations as published in the Federal Register are not in the best interest of the trust funds since they do not maximize interest earnings to the trust funds. We further believe that financial assistance to States should be specifically legislated and not provided at the expense of the trust funds.

RECOMMENDATION TO THE HEW SECRETARY

Since the revised regulations will not become effective until July 1, 1980, we recommend that the Secretary, HEW, reconsider his decision to implement the 15–15–45 requirements and urge that semimonthly or biweekly deposits be required. However, at a minimum, the HEW original proposal (15–15–15) would be a viable alternative.

APPENDIX I

U.S. GENERAL ACCOUNTING OFFICE,
Washington, D.C., June 9, 1978.

Mr. DONALD I. WORTMAN,
Acting Commissioner of Social Security,
Department of Health, Education, and Welfare.

Dear Mr. WORTMAN: We have reviewed your "Notice of Proposed Rulemaking," Federal Register, Volume 43, Number 62, Thursday, March 30, 1978, concerning more frequent deposits of social security contributions by the States. We agree that more frequent deposits will result in increased interest earnings to the Social Security Trust Funds and be more consistent with the requirement placed on employers in the private sector who generally must make deposits more often than the States.

Because of the preferential treatment afforded the States under current regulations, the Social Security Trust Funds will have lost at least $1 billion in investment income until such changes can become effective in 1980.

While we agree that your proposal to increase the frequency of deposits is a step in the right direction, we have reservations as to whether this proposed change goes far enough to maximize interest earnings to the trust funds. Furthermore, we believe the phasing in options of your proposal are not a viable means for implementing more frequent deposits and the frequency of reporting may not be clearly understood by the States and should be clarified. Our comments on these matters follow.

FREQUENCY OF DEPOSITS OF STATE, LOCAL, AND EMPLOYEES' SHARE OF SOCIAL SECURITY CONTRIBUTIONS

Section 218(e) of the Social Security Act, as amended, provides " * * * that the State will pay to the Secretary of the Treasury, at such time or times as the Secretary of Health, Education, and Welfare may by regulations prescribe, * * *." (Emphasis supplied.) This requirement is included in contracts between the Secretary and the States.

Your proposal under section 218 will increase the frequency with which States and interstate instrumentalities must deposit social security contributions on wages and salaries paid to covered employees from quarterly (15th day of the second month after the end of the calendar quarter) to monthly (15 days after the end of each month). The present quarterly deposit requirement for States results in a substantial loss of interest earnings to the Social Security Trust Funds, and is inequitable to employers in the private sector who generally must deposit Federal income and social security taxes weekly, biweekly, or monthly.

Section 218(i) of the act provides that the same deposit requirements should be imposed on the States, so far as practicable, as is imposed on employers of the private sector. The Internal Revenue Service (IRS) requires private employers to follow a depository schedule based on accumulated social security taxes and withheld income taxes. Generally, the current deposit rules for accumulated social security taxes and withheld income taxes are as follows:

Deposit at end of month after end of the quarter if the total undeposited taxes are less than $200.

Deposit within 15 days after end of month if taxes are $200 to less than $2,000.

Deposit within 3 banking days after the quarter-monthly period ends (end of first, second, or third week) if taxes are $2,000 or more.

State and local government employers are subject to this schedule for withheld income taxes only since social security contributions are remitted to the Social Security Administration (SSA). In our visits to a limited number of State and local governments, we noted that these governments generally deposited withheld income taxes in accordance with the IRS deposit rules. Thus, governments having biweekly payrolls were making deposits of withheld income taxes biweekly.

Your proposal to increase the frequency of the deposits will result in substantial interest earnings to the Social Security Trust Funds. However, we believe that in accordance with the provisions of the law, it is just as practical to require deposits to be made 15 days after the end of the pay period as it is to be made 15 days after the end of the month as currently proposed. In this connection, we noted that:

(1) Over half of the State and local employees are currently being paid more often than monthly;

(2) Many States already require State agencies and local governments to remit social security contributions to them more often than quarterly (biweekly or monthly); and

(3) State and local governments are remitting withheld income taxes in accordance with the IRS depository schedule.

In effect, a State which pays its employees biweekly remits the Federal income taxes it withholds to the IRS biweekly, but is not required to remit to SSA the social security contributions it deducts from the pay of these same employees until the 15th day of the second month after the end of the calendar quarter.

Because the States make less frequent deposits than private sector employers, the Social Security Trust Funds have lost a potential for about $1 billion interest earnings since the States were brought under the social security program in 1951. Deposits by the States rose from about $26 million in 1952 to over $10 billion in calendar year 1977. Based on present wages, salaries, and interest and inflation rates, interest earnings are substantial and should become more substantial in future years. For example, assuming your monthly deposit proposal becomes effective January 1, 1980, additional trust funds interest earnings will total about $856 million (at simple interest rates) for the 4 calendar years 1980–83. These interest earnings would increase an additional $54 million for the same period if deposit requirements were changed to 15 days after the end of the pay period.

PHASING IN OPTIONS

Your proposal sets forth a plan for immediate implementation no less than 18 months after the final rules are published. The 18-month provision was provided by Public Law 94–202, enacted January 2, 1976. In addition, there are five options for phasing in the proposed rules.

In our visits to the State and local governments, we discussed the need for the five options. The State and local governments advised that immediate implementation would be more desirable than the five options for phasing in the proposed rules. The five phase-in options would be more confusing and difficult to implement since these options require quarterly and/or yearly changes in frequency of social security contribution deposits until the rules are fully implemented. We agree with the State and local governments that immediate implementation would be more desirable than a phase-in under any of the five options. In addition, the States would have the 18-month period for planning and dealing with immediate implementation of your proposal on or about January 1, 1980.

FREQUENCY OF REPORTING REQUIREMENTS

The proposed rules appear ambiguous as to the frequency of required reporting by the States on contributions for employees' wages and salaries. It is our understanding that the proposal requires only more frequent deposits, and that the required frequency for reporting will remain quarterly.

Paragraph 404.1255a, (c) of your proposal, pertaining to filing of contribution returns and wage reports for months on or after the effective date of your proposal states.

"Contribution returns (Form OAR–S1) will be sent to the * * * Social Security Administration * * * with respect to each deposit at the same time that the deposit is made. Wage reports, on Form OAR–S3, together with a recapitulation report (Form OAR–S2) shall also be filed with the * * * Social Security Administration."

Since the above paragraph might be interpreted as requiring a report each time a deposit is made, we believe you should advise all States that the current quarterly reporting requirements will remain the same.

We appreciate the opportunity to comment on your "Notice of Proposed Rulemaking" and would like to be advised of any consideration given to our comments. As you are aware, we are currently reviewing the effects of delayed social security contribution deposits by the States under section 218 of the act, and plan to issue a report to the Congress at a later date.

Sincerely yours,

GREGORY J. AHART, *Director.*

APPENDIX II

DEPARTMENT OF HEALTH, EDUCATION, AND WELFARE,
OFFICE OF THE SECRETARY,
Washington, D.C., December 11, 1978.

Mr. GREGORY J. AHART,
Director, Human Resources Division,
U.S. General Accounting Office, Washington, D.C.

DEAR MR. AHART: This responds to your letter asking for our comments on your report, "Trust Funds Adversely Affected By Delayed Payments of Social Security Contributions by the States."

The report recommends that the Secretary expedite the issuing of revised regulations and strongly consider semimonthly or biweekly deposits of social security contributions by the States.

The regulations referred to were issued in final form on November 20. They call for deposits within 15 days of the end of each of the first 2 months of a quarter, and within a month and 15 days of the end of the third month of the quarter. Formerly, States' deposits were required to be made on a quarterly basis.

The matter of increasing the frequency of States' desposits of social security contributions has been thoroughly considered by the Department, including the views expressed by the GAO team.

In March 1978, the Department issued a Notice of Proposed Rulemaking which called for monthly deposits by the States. More than 3,000 respondents registered their concerns about accelerating the depository schedule.

In arriving at the depository schedule contained in the new regulatoins, the Department was concerned about its responsibility to protect the interest of the Trust Funds. At the same time, it had to consider the concerns expressed by State Social Security Administrators, numerous local governments, governors, and many members of Congress. The process agreed upon protects the trust fund interests; at the same time it is a reasonable accommodation to the States' concerns about administrative costs and problems in collecting and transmitting more frequent deposits.

We appreciate the opportunity to comment on this draft report before its publication.

Sincerely yours,

THOMAS D. MORRIS, *Inspector General.*

Senator NELSON. Our next witness is Mr. Stanford G. Ross, Commissioner of Social Security.

Mr. Ross, your primary statement, your statement plus the addendum to it, will be printed in full in the record, and you may present it however you desire. If you can summarize the main points, it would be helpful in terms of our time constraints.

STATEMENT OF HON. STANFORD G. ROSS, COMMISSIONER OF SOCIAL SECURITY

Mr. ROSS. Thank you, Mr. Chairman.

I welcome the opportunity to testify before you today on this subject. Although some concerns have been expressed about the effects of this proposed change on the States, we believe that the considerations supporting the change are clear and convincing.

At issue is the appropriate use of social security contributions withheld from employees' paychecks and matched by their State and local government employers. Should they continue to be used

to generate income for State and local governments, or should they be used for their designated purpose: to finance the social security program?

As you know, the Social Security Act and the Internal Revenue Code provide for contributions on covered wages paid in private employment and for the collection of these taxes by employers. The Department of the Treasury regulations require private employers to deposit their social security contributions weekly, biweekly, monthly, or quarterly, depending on the amount of the employer's payroll; the larger the payroll, the more frequently employers must deposit the contributions.

The Social Security Act requires that, so far as practicable, the same deposit requirements shall apply to States as apply to private employers.

Therefore, what we are doing in these proposed regulations is moving in accordance with that mandate of the social security law.

Under current regulations, States are not required to deposit the contributions for a calendar quarter until 45 days after the end of the quarter. The less stringent requirements for deposits by the States were justified on a number of grounds primarily reflecting a recognition of what the States considered to be administrative problems if payments had to be deposited more frequently.

Senator NELSON. Would you mind? We will ask the State witnesses to comment on that also. As long as you are here as a witness, what complication is caused, additional complication is caused, to the paying unit of Government, State, and municipality, if they paid the same day that they pay withholding tax to IRS?

The argument is that it adds to the complications. My understanding is that they are paying IRS within 3 days after the pay period?

Mr. ROSS. Right, if the withheld income taxes total $2,000 or more.

Senator NELSON. With some exemptions, I guess, depending on the size of the withholding. Is that correct?

Mr. ROSS. That is correct. It is gaged by the size.

Senator NELSON. While you are here, you might address the question, because I am sure it has been asked of you, and the States will be asked the same question.

Why does it create an additional complication, paperwork or problem, to the municipality or State, if, in fact, they were required to pay the social security tax withholding deposit at the same time that the income withholding was paid?

Mr. ROSS. They will have to speak for themselves, but as I understand it——

Senator NELSON. That issue, I assume, was raised in the 3,000 comments you received, so you know their argument. What is your response, is what I am getting at, so I will have it in the record, the testimony on both sides of this question?

Mr. ROSS. Their argument is, in effect, they are in the same position as the IRS. They are really collecting this money as an agent of the Social Security Administration.

The basic problem with that, though, is that they, in effect, use the collection of the money as their mechanism for coming into the agreement with HEW to provide coverage.

So the problem in treating each State like any other employer in requiring remittances is that they voluntarily entered agreements with HEW that put them in a position of being a different kind of employer than the normal employer that is just covered automatically by the law. Unlike private employers, the States are liable for all social security contributions due from each of their subdivisions that participate in social security. The States must collect social security contributions and wage reports from every subdivision. This process naturally takes more time than it takes a private employer to report wages and deposit contributions for just his employees.

That is why, in our regulations, we have recognized to the extent that we feel it is appropriate, their different position from private employers and allow the States somewhat more time.

It is really a question of where you strike the balance on this recognition of the differences between them and a private employer.

GAO, as you just heard, feels that we are too lenient in the way we recognize that difference. We feel, given the concerns that have been expressed, we have hit the balance at the moment.

Senator NELSON. That is not my question. My question is, what additional work burden is placed on the municipality or the State if, in fact, they had to make their deposits within the same timespan as they have to for withholding taxes?

Your response to that is they are in a different posture because of voluntary agreements. I understand that. That is not my question.

The question is, what additional burden does it place on them if, in fact, they made their payments in the same pay period as they do withholding taxes? If, in fact, there is not, you would be better off ordering that and paying them for doing it.

In other words, your present system which you are proposing, according to your statistics, would result in covering their overhead costs, in your judgment amounting to $50 million in income from interest on those deposits, if they are made at the appropriate time.

I am trying to get at the question, what is the additional burden?

Mr. ROSS. I can answer that. The additional burden in terms of the paperwork required to make the deposits at the end of each pay period, I do not think would be much different than the burden now because it would only require some additional deposit forms. The question is when they would have to give the full wage accounting, which is much more of a paperwork burden.

Under the new rules, private employers would do that annually. We have proposed——

Senator NELSON. You mean the old quarterly report will now be made once a year?

Mr. ROSS. Annually for private employers. With respect to the States, we have a proposed notice of rulemaking out which would put the States on annual reporting in 1981.

We are required to give 18 months' leadtime on that.

Senator NELSON. By statute?

Mr. ROSS. By statute.

So that in the interim period, until we can work that out, they will have to do this quarterly so that there is an extra burden, but it is one that we cannot avoid until we can put them on annual reporting also.

Senator NELSON. Did I miss the point? What additional paperwork burden is there if the payments were made at the same time the payment deposit was made for withholding of income taxes?

Mr. ROSS. From the standpoint of social security, none. From the standpoint of the States, collecting from the subdivisions and making the payments is their method of fiscal and accounting control in dealing with their local and municipal units. As I see it, it is really a question of their building their own accumulations of the amounts and their own accounting and fiscal controls into the process of remitting the deposits to us. As compared with the present arrangement whereby the States are responsible for the deposits of their subdivisions, making the deposit schedules the same for income tax and social security tax purposes would mean an increase in paperwork for the States.

Senator NELSON. Apart from that argument, is there any additional paperwork.

Mr. ROSS. Apart from that, no; not that I would see.

Senator NELSON. Go ahead.

Mr. ROSS. Under the final regulation which we published in November, we established the schedule for the States to deposit 15 days after the end of the first month of the calendar quarter, 15 days after the second month, and 45 days after the third month of the quarter.

The deposits that are made 15 days after the end of the month will be done with very simple forms which are already in existence and just report an accumulated amount. The only detailed reporting comes in the quarterly report, which would be the same as it is now.

Therefore, there is relatively little additional paperwork to the scheme under the new regulation. It involves some additional deposit slips, but not a great deal of additional work.

The new requirements have two consequences that are favorable to the social security trust funds. One is by reason of the more current deposits, there is a one-time effect in fiscal year 1980 of additional contribution income of $2.2 billion.

The reason for this, in that first year——

Senator NELSON. How many dollars?

Mr. ROSS. $2.2 billion.

Senator NELSON. From what source?

Mr. ROSS. The reason is the first 2 months which would fall under the following year fall into this year. It is a one-time thing. I am just clarifying the two effects.

The more permanent effect is that the trust funds would receive additional interest income of about $735 million during the period fiscal year 1981 through fiscal year 1984. This is roughly about two-thirds of the maximum that could be realized by the social security trust funds if we followed the full GAO recommendations.

It is only one-sixth less than the amount that would be realized if we followed our originally proposed notice of rulemaking.

Therefore, we are moving substantially in the direction that GAO has recommended. The decision of where to come out in the final regulation was made after careful deliberation and full consultation.

Senator NELSON. Full consultation?

Mr. ROSS. Meaning that we had considered all of these comments. We have had meetings with the State people and others.

We have been working with the States and we believe it is reasonable to expect the States to resolve any remaining administrative problems by July 1980 when the deposit requirements become effective. Moreover, as all parties gain experience with the more frequent deposits, we are confident that the whole process will work well.

I want to stress that the State and local governments should still be able to earn substantial amounts of interest income under the new rule. Assuming a conservative 5-percent interest rate, and assuming that the social security liability on each employee's earnings is invested 5 days after the employee is paid, we estimate that the State and local governments could earn $75 million in fiscal year 1981, even under the new schedule.

Although this is less than the States are currently earning, it is still far more than State administrative costs, including any increases that might result from more frequent deposits.

Senator NELSON. What studies have been made of administrative costs?

Mr. ROSS. We are relying there mainly on the study that came out of the 1976 survey by the House Subcommittee on Social Security which estimated roughly $2.5 million in additional administrative costs in calendar year 1974 if they had to deposit monthly.

Senator NELSON. $2.5 million?

Mr. ROSS. Dollars in additional administrative costs. They estimated their actual administrative costs in 1974 under the present depository system as $4.6 million.

Senator NELSON. For whom?

Mr. ROSS. The States.

Senator NELSON. For all the States?

Mr. ROSS. For all but 10 States and Puerto Rico that did not respond.

Senator NELSON. You are talking about $2.5 million in administrative costs?

Mr. ROSS. I think the $2.5 million is low. That was several years ago.

Senator NELSON. You siad 1970-what?

Mr. ROSS. The survey was taken in 1976 but the data obtained was based on 1974 experience. Even extrapolating that out, I would say you are probably looking at administrative costs in the area of maybe $5 million under the new regulation. There is just no comparison between the amount of interest income that the States can earn and the administrative costs that are involved in this process.

Senator NELSON. Do I understand it to be your position that at the outset—what did you say? Four or five million dollars?

Mr. ROSS. Say roughly $5 million, yes.

Senator NELSON. Then, under your proposed rule change did you say they could earn $75 million in interest income?

Mr. ROSS. They could earn $75 million. It depends on how good money managers they are and what the interest rates are.

Senator NELSON. Let's make it $50 million.

Mr. ROSS. Yes.

Senator NELSON. In any event, what you are saying is that, in your judgment, the administrative costs are $5 million and they will certainly get back at least $50 million interest. Is that what you are saying?

Mr. Ross. Yes, based on prudent money management, current assumptions about interest rates and the economy. The gap is so large that there is no conceivable set of circumstances in what their earnings will not be a substantial multiple of the administrative costs involved.

Senator NELSON. What about the municipalities?

Mr. Ross. I am including them.

Senator NELSON. They are included in that $5 million cost?

Mr. Ross. I believe so. This is based on a 1976 survey by the House Subcommittee on Social Security.

Senator NELSON. You say you base that estimate on what——

NOTE.—The Social Security Administration subsequently informed the subcommittee that the 1976 survey did not include complete information concerning the administrative costs of subdivisions. The $5 million estimate therefore relates only to State costs.

Mr. Ross. Extrapolating from the data that was gathered in connection with the House subcommittee survey. It is hard to get complete and reliable information as shown by the incomplete response to the House subcommittee survey. Perhaps when the State people appear before you, you could ask them what it costs them and what they think they will earn. They are the ones who have this information. We are just guessing based on the limited information we have.

Senator NELSON. I suppose there are any number of ways to make a judgment about that cost, but did the GAO or the Social Security Administration do any studies of its own of what the actual costs would be in a cross-section sampling of municipalities of different sizes and payrolls?

Mr. Ross. We reviewed the data from the 1976 survey and extrapolated from it.

Senator NELSON. Did the House committee make these actual studies, or did they commission someone to make them?

Mr. Ross. No. They did the survey as I understand it, and we summarized the data.

Senator NELSON. It sounds like some of the statistics that I used in my speeches.

Mr. Ross. I wish we had better data, but it is a sensitive issue obviously. You are dealing with a number of States and their own internal relations with the municipalities. It is not an area in which I think it would be sensible for us to try to do anything in depth.

Senator NELSON. Let me ask a question. How many units, how many thousand units, file withholding forms, municipalities? I am talking about public employees.

Mr. Ross. 65,000.

Senator NELSON. When the Paperwork Commission did its study on paperwork—and I have never looked at the background for their figures, but they estimate that the total paperwork in this country required by the Federal Government adds up to $745 million.

They estimated the hours that it took to fill out forms of all kinds. How they did the estimate, I do not know. Then they multiplied the hours by $15 an hour as being what they considered a reasonable cost of managing paperwork. That is an arbitrary figure, of course. But if you have 65,000 units it would not be too hard to do a little study to find out what the size of the municipalities are, how much time it takes to fill out the forms, how much time it takes the States, and make some extrapolations from that.

Anyway, $5 million sounds like a small administrative overhead for 65,000 units to be filing a number of times every year. I do not know.

Mr. Ross. Let us take another look at it and see if we can get a more exact figure.

[More precise information was not available.]

Senator NELSON. That issue is going to be in contention.

Mr. Ross. The exact amount may be in contention, but I would be surprised if the general proposition that the interest income that will be earned is substantially greater than any conceivable administrative burden could be in contention.

Senator NELSON. All right. Go ahead.

Mr. Ross. Actually, on this point I would say that one reason that we would like to move as rapidly as the law permits us to put the States on annual reporting, the same as the private employers, is that we estimate we could save the States 1.4 million pages of forms containing 36 million items of wage data each year.

Senator NELSON. How many pages?

Mr. Ross. 1.4 million pages of forms SSA-3963 containing 36 million items of wage data each year would no longer be required.

When we can get this effective in 1981, the whole paperwork burden involved in the administration of this with the States can go down dramatically.

Senator NELSON. You know what the Paperwork Commission said about savings, when after years of resistance by the Social Security Administration and under pressure from business people and up here on the Hill, they finally went from the quarterly report to the annual report. The Paperwork Commission estimated that that saved a pile of paper 10,500 feet high, or 2 miles of paperwork, that was being sent into Washington that really was not necessary to ship in at all.

We are interested in the reduction of paperwork; so are the municipalities and the States.

Mr. Ross. Let me just conclude by saying that ultimately what we see is involved here is a question of judgment. On the one hand, we know the maximum that we could require. We know where we are at, and we have heard from the States and we have weighed their arguments. What is involved in the final regulation is our judgment of where you take proper recognition of the State concerns.

We feel we have done that. We feel that we can work with them to make the new rules work effectively and well, and we think it is fair to all of the parties so that, despite the criticism by GAO that we should go further, and despite the criticism by the States that we should do nothing, we feel that we have made a proper judgment at this time.

We have reviewed it, and we are comfortable with it.

Senator NELSON. You are proposing that they go to the annual report on the form 941?

Mr. Ross. That will help.

Senator NELSON. Why did you not propose that at the time when you proposed it for the private employers, just out of curiosity? That went into effect January 1 of this year, did it not, or was that last year?

Mr. Ross. That went into effect January 1 of last year. We are on annual reporting now.

Senator NELSON. You have a 1½-year lag time required by statute for you to change?

Mr. ROSS. Right.

Senator NELSON. I know you were not the Administrator at the time.

Mr. ROSS. No; I was not at that time.

Upon checking it was learned that the administration did propose annual reporting for the States as well as for private employers on December 31, 1974. At that time the Departments of Treasury and HEW submitted a joint report to Congress containing recommendations on an annual reporting system. The report specifically recommended against retaining a quarterly reporting system for the States. However, when the Congress enacted annual reporting legislation in 1976, it provided for the 18-month delay before any change in reporting requirements could become effective for the States.

I would hope that the States would recognize the paperwork savings and the other benefits of annual reporting and that they would find this congenial from their standpoint also.

But it is not quite the same as dealing with the private sector.

Senator NELSON. Have you attempted to do a computation of the amount of paperwork burdern, the difference in the paperwork burden between what is done now under the current practice and what would be done under the proposed rule change plus under the proposed change from quarterly to annual reporting on form 941?

Mr. ROSS. Yes.

Senator NELSON. Is it less paperwork, clearly, or more?

Mr. ROSS. When you get to 1981 when the annual reporting regulations will be effective, it will clearly be less. From July 1980 until 1981 there will be slightly more, based on these fairly short forms that would be filed eight times a year where they are not now filed. It is not a very large additional paperwork burden and will just be interim until annual reporting comes in and would outweigh on the downside, if you will, the increase that is temporarily there on the upside during this interim.

Senator NELSON. Senator Danforth?

Senator DANFORTH. Has any analysis been done as to whether this would accelerate States from opting out of social security?

Mr. ROSS. We have studied that. Our judgment is that it will not—that basically the protections afforded by social security are a good deal and that the change will not accelerate terminations of coverage. This will not substantially change the leave in the balance of considerations for such an important decision as withdrawing from social security coverage.

Senator DANFORTH. There has been a gradual or a rapid acceleration over the past few years, has there not?

Mr. ROSS. I do not know whether I would call it a rapid acceleration.

Senator DANFORTH. Moderate?

Mr. ROSS. A rapid acceleration of considering it, I will say that. People are very much into considering it and the impetus on the other side for universal coverage has caused a reaction to take a look at whether their own claims and relationships with social security are sound. I think it is an area where there is a lot of ferment.

I do not think that we see that much activity in coming out. In fact, a number of highly publicized cases of jurisdictions expressing an interest in withdrawing from social security have quietly disappeared.

Senator DANFORTH. Now, it is my understanding that when it is said in 1980 that the administration's budget has a deficit of about $29 billion, built into that is the fact that if we move to monthly remittances, the effect of that would be in fiscal year 1980, for one-time only, there would be 14 months included in the fiscal year, and that the value of that is about $2.2 billion.

And that, therefore, what you might count as an accounting change has the effect of a kind of a windfall in the 1980 budget. Without the 14 months, the deficit would be more like $31 billion. Is that correct?

Mr. ROSS. That is right.

Senator DANFORTH. There is some complaint about this, is that right? Is it a controversial matter?

Mr. ROSS. I would say that that is a controversial matter. The reactions to our notice of proposed rulemaking were numerous and strenuous.

The basic State position was that no change should be made. On the other hand, GAO feels that we have not gone far enough in protecting the interest of the trust funds. We feel that we have taken seriously the State complaints. We have tried to weigh the burdens that we are putting on them. We are willing to work with the States to try to ameliorate their problems.

We think we have hit the balance for the moment in our regulation.

Senator DANFORTH. Is the main complaint the loss of the float, so to speak, or is the main complaint additional administrative burden?

Mr. ROSS. The main public complaint is additional administrative burden. I think that there is a concern over the loss of income.

Senator DANFORTH. Is the main gain, as far as the Social Security Administration is concerned, additional revenue?

Mr. ROSS. Yes.

Senator DANFORTH. Has any thought been given toward keeping the same system with respect to the time of remittances but charging interest, computing interest?

Mr. ROSS. We did consider that, but that would involve probably a larger administrative burden for both the States and the Federal Government. If you went that way, you would then need to worry about fiscal controls and audits to make sure that they had our money and we were entitled to some interest on that and that it was the right amount. It would be a far more cumbersome process, and also one that I think people could have very serious doubts about, allowing different units of government to manage one another's money.

I think we would have had difficulty conceptually carrying that out, even if we could have worked out the mechanical problems.

Senator DANFORTH. It would seem to me to be reasonably easy administratively.

Mr. ROSS. But you would also have to have controls and audits to make sure that we got the right amount, if they were investing our money.

Senator DANFORTH. It is not investing. You would have a fixed amount you would charge them.

Mr. ROSS. Yes; but on what number? And you would have to let it vary from time to time, I suppose, as interest rates vary. You

would not want them caught in a bind with the rate that they would be paying us greater than the rate that they could earn and similarly, we would not want to give them a rate so favorable that there was too big of a gap. You would have a lot of adjusting to do.

Senator DANFORTH. I would think you could just set a figure, say at a pretty low rate of interest, and charge it.

Mr. ROSS. It gets to be a question of how much you think they should earn by holding the Federal Government's money. It is much better, I believe, to do it this way. When it is remitted, it is our money. Up until that point, it is their money. It is much cleaner.

Senator DANFORTH. Thank you.

Senator NELSON. Thank you.

Thank you very much. We undoubtedly will have additional questions to submit in writing to you between now and the close of the hearing record, 2 weeks from now. Your statement and the additional materials submitted will be printed in full in the record.

Thank you very much.

Mr. ROSS. Thank you.

[The prepared statement of Mr. Ross and addendum and responses to questions of Senator Nelson follow:]

STATEMENT BY STANFORD G. ROSS, COMMISSIONER OF SOCIAL SECURITY

Mr. Chairman and members of the subcommittee: I welcome the opportunity to testify before you today on the change in regulations that will increase the frequency with which States and interstate instrumentalities deposit social security contributions. Although some concerns have been expressed about the effects of this change on the States, the Administration believes that the considerations supporting this change are clear and convincing.

At issue is the appropriate use of social security contributions withheld from employees' paychecks and matched by their State and local government employers. Should they continue to be used to generate income for State and local governments or should they be used for their designated purpose: To finance the social security program?

As you know, the Social Security Act and the Internal Revenue Code provide for contributions on covered wages paid in private employment and for the collection of these taxes by employers. The Department of the Treasury regulations require private employers to deposit their social security contributions weekly, biweekly, monthly, or quarterly, depending on the amount of the employer's payroll; the larger the payroll, the more frequently employers must deposit the contributions. The Social Security Act requires that, so far as practicable, the same deposit requirements shall apply to States as apply to private employers.

Under current regulations, States are not required to deposit the contributions for a calendar quarter until 45 days after the end of the quarter. The less stringent requirements for deposits by the States were justified on a number of grounds primarily reflecting a recognition of what the States considered to be administrative problems if payments had to be deposited more frequently.

Treasury transfers amounts equal to the private employer and employee taxes to the social security trust funds on a daily basis—in effect, as FICA tax liabilities are incurred. Amounts equal to FICA taxes with regard to State and local employment are not credited to the trust funds until they are actually paid by the States, and the trust funds do not begin to earn interest on these amounts until then—up to 4 months after the liability has been incurred. Instead, these amounts are used by the States or political subdivisions for short-term investments that earn significant amounts of interest.

We have estimated that since 1961, if the States had deposited social security contributions monthly, the social security trust funds could have earned about $1.1 billion in additional interest. With the increases in the earnings base, the tax rate, and expanding payrolls, these losses have been increasing in recent years, and would increase even more in the future under the current deposit schedule.

45-083—79——3

Under the new regulation, published in the Federal Resgiter on November 20, 1978, the States will be required to deposit contributions more frequently, effective July 1, 1980. The new schedule calls for the States to deposit social security contributions 15 days after the end of the first month of the calendar quarter, 15 days after the second month, and 45 days after the third month of the quarter.

The new deposit requiremnets will mean that the trust funds will receive additional contribution income of about $2.2 billion in fiscal year 1980. The reason for this is that the States, in the first year, will be paying contributions for 2 months which, under the present schedule, would not be paid until the following year.

Further, the trust funds will recieve additional interest income of about $735 million during the period fiscal year 1980 through fiscal year 1984.

The decision to change the frequency of deposits by the States was made after careful deliberation and full consultation. In 1974 SSA informed the States that a change in the deopsit schedule was under consideration. In 1975 members of the National Conference of State Social Security Administrators and SSA representatives met with members of the House Ways and Means Subcommittee on Social Security to discuss the concerns of the States. At the Subcommittee's request, a questionnaire was developed jointly by SSA and State representatives and sent to all States. 40 States responded. Some States indicated in their responses that they would have some administrative difficulties, but the information provided indicates to SSA that the method of accelerated deposits proposed in the final regulation would be feasible.

A Notice of Proposed Rulemaking (NPRM) was published in the Federal Register in March 1978. The NPRM would have required the States to deposit social security contributions 15 days after the end of every month. We received a number of adverse comments, primarily from State and local government officials. About 200 members of Congress also responded.

The letters overwhelmingly opposed any changes in the States' deposit procedures. The main objections were based on administrative problems and the loss of interest income.

As a result, we modified the proposed regulation to require the States to deposit 15 days after the end of the first and second months, and 45 days after the end of the third month. The change from the 15 days to 45 days is intended to allow the States to make their 3rd months' payment along with their regular quarterly wage reports. This gives the States more time to check the total deposits they made for the quarter against the detailed wage reports for each employee.

We believe it is reasonable to expect the States to resolve any remaining administrative problems by July 1980 when the deposit requirements become effective, SSA is working cooperatively with States to resolve operational problems. As all parties gain experience with the more frequent deposits, we are confident the whole process will work well.

This change will of course result in a loss of interest income to the States. However, the interest income now earned by the States usually far exceeds administrative costs. The excess has gone into general funds of the States and political subdivisions for purposes not related to social security. It was clearly the intent of Congress that as much interest income as practicable be made available to social security, to benefit all people who are covered by the program. The time has now come to adjust the deposit schedule to bring us closer to that goal.

I want to stress that States will still be able to earn substantial amounts of interest under the new rule. Assuming a conservative 5-percent interest rate, we estimate States could earn $75 million in fiscal year 1981 under the new schedule. Although this is less than the States are currently earning, it is still more than State administrative costs, including any increases resulting from more frequent deposits.

While the States believe the regulation goes too far, the General Accounting Office believes it does not go far enough. GAO has indicated that States should deposit social security taxes at least monthly—but preferably semimonthly or biweekly—because of the additional interest income the trust funds would realize. The difference in interest between the method GAO advocates and the one we propose is estimated by GAO to be over $40 million annually. We think, however, that this additional income must be weighed against the States' need for the 45-day period at the end of the quarter to be used for accounting purposes. We believe we have, at this point, struck an appropriate balance in our new rules.

I might add that we published for comment a proposed regulation on annual wage reporting for the States comparable to that recently adopted for private

employment, but the 45-day deposit schedule for the last month of the quarter would not be changed. States would continue to reconcile their liability and payments quarterly.

Finally, I should mention that President Carter has proposed in the fiscal year 1980 budget that large private employers deposit their withheld income and social security taxes more frequently than under present rules. At the same time, very small employers—those with quarterly withheld income and social security taxes of less than $1000—would deposit quarterly. These changes would be phased in during 1981 and 1982.

In summary, the Administration recognizes that it is difficult for States to give up this source of additional revenue, but we believe the broader national interest requires that this change be made. It is a change which is overdue. I would be glad to answer any of your questions.

QUESTIONS RAISED ABOUT MORE FREQUENT DEPOSITS

1. Increased paperwork burden.

State and local governments have expressed concern that HEW's new regulations will increase their paperwork burden. However, steps have been taken to minimize this.

The new requirements of HEW's regulations will not actually require any additional forms. States now file quarterly four different forms. Two of these require detailed information on individual workers' earnings and aggregate wage payments by employer. The remaining two are single page, summary forms. Copies of each are attached.

Under the new requirements, the single page summary forms will be filed monthly, but the more detailed forms will continue to be filed quarterly. Under our proposal, we continue to allow 45 days at the end of each quarter for the preparation of the more detailed forms. No additional detailed wage information will be required than is now required, and there is no reduction in the time allowed for its preparation.

In those instances in which State law requires detailed wage information from local entities before any contributions can be forwarded, the 18 months provided for implementation of the new regulations should be adequate to make any necessary adjustments in State law.

The Social Security Administration is working closely with the States to minimize any administrative difficulties which might arise during the change. We do not anticipate any difficulties that cannot be worked out cooperatively.

2. Loss of income from interest on undeposited contributions.

One of the major concerns raised by States is the loss of interest on contributions not yet deposited. Under current procedures, States are not required to deposit social security contributions until 1 month and 15 days after the end of each quarter, and could draw interest on those amounts.

Under the new regulations, that will no longer be possible and States will lose some of the income they can now realize from the interest on undeposited contributions. However, States can continue to earn substantial interest income.

We estimate that in fiscal year 1981 alone, States could earn approximately $75 million on contributions (estimated at $15.5 billion) under the new schedule. This far exceeds the administrative costs they incur, including any increase in administrative costs which may result from the more frequent deposit schedule. Moreover, $75 million is a conservative estimate, based on a short-term interest yield of 5 percent per annum. We believe the new system provides the opportunity to earn more than an adequate amount of interest.

3. Increased administrative costs.

Based on 1974 data, 41 States reported an estimated $4.6 million in administrative costs, and the expectation that monthly reporting would result in a additional $2.5 million in administrative costs. The implementation schedule now being proposed by HEW would involve less of an increase in administrative burden than was assumed for the $2.5 million estimate.

Wage increases since 1974 might cause total administrative costs before and after implementation of the new regulations to rise by as much as 50 percent. Even with such an increase, potential earnings on undeposited contributions far exceed total administrative costs to the States. In short, increased administrative costs, while a legitimate concern, should not be a critical issue.

4. Other administrative considerations.

Some States fear that it will be administratively impossible to deposit contributions 15 days after the end of each month because of the time needed to process the reports and insure accuracy. Some States have indicated that under their State laws they cannot pay the contributions due without documentation of the kind contained in the quarterly wage report.

Many localities already remit to State government monthly. In at least 17 States some or all of the political subdivisions are already required to deposit contributions with the State social security agency more then once a quarter.

Social security data processing staff are ready to work with the remaining States to devise answers to their problems between now and July 1980. For example, where precise, individual wage information is not available, States can devise ways to determine estimated contributions from aggregate wage information. Similarly, States that cannot legally make payments based on estimates should have time to enact the necessary legislative changes by July 1980.

Further, the 15-15-45 day schedule was chosen in part because it would require fewer changes in existing State procedures than the schedule originally proposed. Just as now, States will continue to have 45 days at the end of each quarter to reconcile payments made with their total liability based on the quarterly wage report. Thus, administration under the new regulations should take place smoothly once transitional problems are worked out.

5. Additional deposits in transition year.

States are also concerned that the year the new regulation goes into effect, they will be required to pay an additional 2 months' contributions.

In fact, they will not be required to make additional payments. Rather, States are only being asked to deposit contributions sooner. They are not being asked to pay more.

6. Changes in existing Federal-State agreements.

Some States regard the new regulations as a unilateral change in the agreements already in effect between each State and the Secretary of HEW. This is not true. The agreements already in place do not specify how frequently deposits must be made by the States. Instead, they provide that the States must comply with the Secretary's regulations relating to the time of payment contributions.

7. Minimum deposit requirements.

Some States have said the new regulation would impose unduly stringent requirements on small jurisdictions with very small payrolls. The States suggest that the new regulation should permit such political subdivisions to deposit social security contributions with the States quarterly.

The new regulation could not set different requirements for different political subdivisions within a State because agreements with the Secretary are agreements covering the State as a whole, and are not with individual political entities within a State. However, we are considering whether administrative guidelines can be developed which will provide greater flexibility to deal with this potential problem.

See instructions on back of this page.
Do not send this form to Internal Revenue Service.

Attachment 1

1 Reporting entity's identifying number, name, and address
69-0990001
te Auditor
/, State 99998

2 Date Quarter Ended
09-30-81

SSA Use Only
F ☐ 2 ☐ U ☐ E ☐
S ☐ 1 ☐ L ☐ T ☐
X ☐ 0 ☐ V ☐ A ☐

▶ 69-0990001

3 Total pages of this report including this page and any continuation pages ▶ 1

4. Total number of employees listed ▶ 9

5. Number of persons employed during payperiod containing March 12th. ▶

IF YOU HAVE NO EMPLOYEES TO REPORT, ENTER "NO COVERED WAGES PAID" BELOW

(6) EMPLOYEE'S SOCIAL SECURITY NUMBER (000 00 0000)	(7) NAME OF EMPLOYEE (Please type or print exactly as shown on the employee's Social Security Card)	(8) COVERED WAGES Paid to Employee During Quarter (Before deductions) Dollars Cents	(8A) Dollars Cents
999 99 9991	Smith, Achilles	4000.00	
999 99 9992	Smith, Andrew	2000.00	
999 99 9993	Smith, Brockingham	2000.00	
999 99 9994	Smith, Cora	2000.00	
999 99 9995	Smith, Geraint	2000.00	
999 99 9996	Smith, Hortense	2000.00	
999 99 9997	Smith, Isabella	2000.00	
999 99 9998	Smith, Merlin	2000.00	
999 99 9999	Smith, Wanda	2000.00	

If more space is needed for listing employees, use forms OAR-S3a (continuation sheets).
Total wages reported in column 8 for this page ▷ 20,000.00

9. Total covered wages paid during quarter ▶ $ 20,000.00

10. Contributions—Multiply the total wages entered in item 9 by ▶ $ 2,660.00

11 Adjustment for overpayment or underpayment of contributions ▶ $ 0.00

12 Contributions as adjusted by item 11 ▶ $ 2,660.00

Form OAR S3
Department of
[illegible]

DO NOT USE FORMS OF DIFFERENT DESIGN UNLESS
APPROVED BY THE SOCIAL SECURITY ADMINISTRATION

Form approved
OMB No. [illegible]

Attachment 2

RECAPITULATION OF STATE'S QUARTERLY REPORT OF WAGES PAID

Form Approved OMB No. 72-R437 3

1. AGENCY'S IDENTIFICATION NO., NAME, AND ADDRESS	2. DATE QUARTER ENDED	3.
.ate Social Security Agency City, State 99999	09-30-81 DUE DATE 11-15-81	PAGE NO 1 OF 1 PAGES

SEE INSTRUCTIONS ON OTHER SIDE

IDENTIFICATION NUMBER (4)	COVERAGE GROUP OR PAYROLL RECORD UNIT NO (5)	TOTAL WAGES ITEM 9 OF OAR-S3 OR ITEM 6 OF OAR-S4 (6)	FOR STATE'S USE (7)	(8)	(9)
00 0000000 69-0990001		20,000.00			
69-0990002		10,000.00			
OTALS FOR THIS PAGE		30,000.00			
11. TOTALS OF ALL RECAPITULATION PAGES		30,000.00			

SIGNATURE (First page only) I. M. Director — TITLE State Agent — DATE 11/12/81

FORM OAR-S2 (12-72)

Summary form OAR-S1 showing the total of the payments for the quarter. Attachment 3

FORM OAR-S1 (6-73) — Form approved. Budget Bureau No. 72-R436.5

STATE'S RETURN OF CONTRIBUTIONS PAYABLE UNDER THE SOCIAL SECURITY ACT

AGENCY'S IDENTIFICATION NUMBER, NAME AND ADDRESS
State Social Security Agency
City, State 99999

DEPOSIT NO. RECAP

[X] Non-tip Wages [ ] Tip Wages

1. Report for calendar quarter ended or, if adjustment reports, date Form OAR-S2 signed 09-30-81
2. Total net wages (item 11 of Form OAR-S2) .... $ 30,000.00
3. Contributions (see instructions on back of form) .... $ 3,990.00
4. Adjustments (see instructions on back of form) .... $ 0.00
5. Net amount payable with report (item 3 as adjusted by item 4) .... $ 3,990.00

Department of
HEALTH, EDUCATION, AND WELFARE
Social Security Administration
Baltimore, Maryland 21235

(Signature) I. M. Director
(Official title) State Agent (Date) 11-12-81

DEPOSIT TICKET — Attachment 4

DEPARTMENT OF THE TREASURY, BUREAU OF GOVERNMENT FINANCIAL OPERATIONS

DEPOSIT NUMBER	DATE PRESENTED OR MAILED TO BANK	8-DIGIT AGENCY ACCOUNTING STATION CODE OR 8-DIGIT DISBURSING OFFICE SYMBOL	AMOUNT
492	11-12-81	75-04-0003	1330.00

AGENCY USE — STATE AGENCY TITLE AND ADDRESS
ACCOUNT SYMBOL 20X8006.3 A/R
SA DEPOSIT NUMBER 099 - 121
State Social Security Agency
City, State 99999

Department of Health,
Education, and Welfare
Social Security Administration
P.O. Box 70
Baltimore, Maryland 21203

DEPOSITOR'S TITLE, DEPARTMENT OR AGENCY AND ADDRESS
DEPOSITARY: DATE, SIGN, AND RETURN THIS COPY TO DEPOSITOR

(7) NAME AND ADDRESS OF DEPOSITARY
Federal Reserve Bank
Anywhere, USA

(8) I CERTIFY THAT THE ABOVE AMOUNT HAS BEEN RECEIVED FOR CREDIT IN THE ACCOUNT OF THE U.S. TREASURY ON THE DATE SHOWN SUBJECT TO ADJUSTMENT OF UNCOLLECTIBLE ITEMS INCLUDED THEREIN.

A. J. Teller — AUTHORIZED SIGNATURE — 111481 CONFIRMED DATE

CONFIRMED COPY

DEPARTMENT OF HEALTH, EDUCATION, AND WELFARE,
SOCIAL SECURITY ADMINISTRATION,
Baltimore, Md.

Hon. GAYLORD NELSON,
Chairman, Subcommittee on Social Security, U.S. Senate,
Washington, D.C.

DEAR MR. CHAIRMAN: I wish to thank you for the opportunity to testify before your Subcommittee on regulations to increase the frequency with which States deposit social security contributions. Although I had to leave after giving my statement, members of my staff remained for the rest of the hearing. We found the hearing very helpful in giving us further insights into the problems faced by States and their subdivisions. We carefully considered the points made and have developed suggestions to alleviate the problems. Our suggestions are included in the enclosed responses to your questions.

We appreciate the opportunity to complete the record of your hearings. After reviewing the testimony and discussion of the other witnesses, I believe the record fully supports the Administration's position. We would expect to work cooperatively with the States to implement the needed changes. There is more than enough time remaining before the effective date of the regulation, July 1, 1980, to work out any remaining administrative problems. I would also note that the record makes clear that there are those who believe even more stringent rules are called for. In our view, we have struck an appropriate balance between the concerns of the States and the loss of interest to the social security trust funds.

My staff and I will be happy to give any further assistance your Subcommittee may require.

Sincerely,

STANFORD G. ROSS,
Commissioner of Social Security.

Enclosure.

Responses of Stanford G. Ross, Commissioner of Social Security, to Questions From Senate Subcommittee on Social Security [1]

Question

1. The National Conference of State Social Security Administrators presented several charts which described the amount of additional time and expense necessary to comply with the new 15-15-45 day depository regulations. The information contained in these charts differs substantially from the data you presented. The states contend the new regulations will require: 3 additional days for consolidation of local government sub-unit payments; 4 days for drawing and authorization of local government warrants; 5 days to allow the local mail to reach the state office; 5 days for the state office to reconcile the local receipts; 5 days to deposit these receipts in the state treasury and draw state warrants. Thus, the states maintain it will take a total of 22 additional days per month to comply with the new regulations. This is 7 days more than the regulations would allow.

The states also conducted a survey of 10 states. The survey shows that, on the average, 10 percent of the political subdivisions deposit less than $200 in social security contributions per quarter; 25 percent deposit more than $200, but less than $2,000; and 65 percent deposit more than $2,000. Thus, the states maintain 40 percent of their political subdivisions are relatively small depositors which should not be required to deposit on a monthly basis.

In terms of administrative costs, the states allege their current costs are $13 million a year and it would cost an additional $5 million a year plus $1 million in initial start-up expenses to comply with the new regulations.

The states also challenge HEW's estimate on the amount of interest income they will continue to earn under the new regulations. They state they will lose $80 million in 1981. This compares with HEW's estimate of $179 million. Based on this discrepancy, the states say they couldn't continue to earn $75 million under the new regulations, as you suggested in your testimony.

Could you reconcile the above data with your testimony? In addition, would you consider treating small political subdivisions differently than large ones, e.g., allow quarterly deposits for small governmental units?

Response

22-Day Time Frame

The experience of some States demonstrates that 22 days are not required to move the deposits from the local subdivisions to the Federal Reserve Banks. For example, data furnished by the States in response to the questionnaire distributed in 1976 by the House Ways and Means Subcommittee on Social Security indicates that in 17 States some or all of the social security contributions are paid to the State social security agency more than once a quarter (some as often as biweekly). We believe that the period from now until July 1980 is long enough to enable States and subdivisions which do not promptly move the funds in less than 22 days to modify their procedures to comply with the new regulations. The experience of States and subdivisions that have already solved many of the problems mentioned here and have streamlined their administrative procedures can be used to give valuable assistance to other States and subdivisions.

We have the following additional comments on the 22-day time frame described:

1. 3 days to consolidate local government subunit payments.—In many States there is no need to consolidate local government subunit payments because the subunits send monies directly to the States. For those that do not, the three days for consolidation could be reduced by centralizing the payroll of local subunits. If that is not considered feasible, because there are reasons for each subunit to do its own payroll, the subunits could arrange to report directly to the States. The Social Security Administration, upon request, will assign a payroll record unit number of any subunit that wishes to report directly so that separate payrolls are maintained but the need for consolidation at the local level is avoided. Our experience shows that 46 States now use payroll record unit number reporting.

2. *4 days for drawing and authorization of local government warrants.*—The time required to process warrants by local entities could be reduced if they established a system of continuing authority to draw and authorize warrants for payment of social security contributions. This would avoid many delays associated with treating every warrant for social security contributions like a special, one-time warrant requiring special consideration and authorization.

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[1] Hearing of Jan. 29, 1979, on regulations to increase the frequency with which States deposit social security contributions.

3. *5 days to allow the local mail to reach the state office.*—The 5 days in the local mails could be eliminated by use of wire transmission from the local entity to the State, or be establishing a State account in a local bank.

4. *5 days for the state office to reconcile the local receipts.*—While the States will need to record and account for monies deposited each month, there does not appear to be a need to reconcile the deposits each month. The 1976 survey showed while 14 States require wage reports along with deposits, only 6 States were required to do so by statute. Since the regulations will not go into effect until July 1980, there should be ample time to amend State statutes. The reconciliation could be done at the time of the last deposit one month and fifteen days after the end of the quarters. This was one of the reasons the Social Security Administration modified the 15-15-15 day regulation initially proposed to a 15-15-45 day rule.

5. *5 days to deposit receipts in state treasury and draw state warrants.*—Same comment as for 2 above.

Small political subdivisions

Based on an analysis of wage reports for State and local employees in 1978, we determined that 9 percent of the State and political subdivisions had social security liability of $200 or less per quarter—this is consistent with the 10 percent estimate that the States supplied. The States estimate that 25 percent of all subdivisions have liability between $200 and $2,000 per quarter and conclude that under IRS rules for deposits of social security and income taxes for private employers both groups of subdivisions would deposit quarterly rather than monthly. While this is true for the 10 percent with liability of $200 or less, it is not true for the other 25 percent. Under IRS rules for private employers, the frequency of deposits of withheld income taxes and social security taxes is determined by the amount of taxes due. If the combined taxes withheld at the end of any month are between $200 and $2,000, they must be deposited monthly, not quarterly. Thus, if the IRS rule applied to subdivisions, only those with a combined social security and income tax (fewer than 10 percent of the subdivisions) liability of less than $200 per quarter would deposit quarterly.

Although the new regulation does not directly treat small entities differently from larger entities, the Social Security Administration plans to follow a procedure that will permit States experiencing problems in complying with the regulation because they have a significant number of small entities to require less frequent deposits of contributions from samll entities. The procedure would be similar to a tolerance rule now used by IRS for private employers who must deposit taxes very frequently. Under this procedure, if the amounts deposited by the States each month "substantially" made up the total contributions due for the month, the State would be considered to have complied with the regulation. In most cases the contributions collected monthly from the larger entities would be sufficient to permit the States to substantially meet their monthly liability, so that the States could keep very small entities on a quarterly deposit schedule.

We are developing policies and criteria to alleviate the problem of States which have a large number of small entities and could not therefore substantially meet their monthly liability with deposits from larger entities alone. We plan to work very closely with the States in helping to resolve their problems in this area. Generally, we believe that it might be possible for the States to work out ways in which they could use the deposits of larger subdivisions to balance out problems with their smaller subdivisions.

State administrative costs

The States estimate their current administrative costs as $13 million a year and estimate an additional cost of $5 million a year plus a $1 million startup cost under the new regulation.

The Social Security Administration cannot determine State or local government administrative cost. Figures supplied by 41 States for the year 1974 showed total State agency administrative costs of $4.6 million. We do not know how the States have estimated their administrative costs. We do know that system changes will be required to accommodate the more frequent schedule unless their present system already requires monthly or more frequent payments. Without full knowledge of their current systems and the system changes required in each State, we cannot comment on the estimate of a $5 million annual increase due to the new regulation or on the estimate of a $1 million startup cost. In any case, the potential interest earnings for the States will far exceed their estimated cost if they employ sound cash management practices.

HEW's estimate of interest income States could earn

The States have challenged our estimate that they will be able to earn $75 million per year in interest under the new regulations. They base their challenge on the seeming discrepancy between our estimate that the social security trust funds will gain $179 million in interest income in 1981 and their estimate that the States will lose $80 million in 1981.

This difference, however, should not be considered a "discrepancy." Our estimate of $179 million in additional interest income to the trust funds in calendar year 1981 represents interest resulting from the earlier receipt and investment of the social security contributions from the States. The estimate is based on an assumed interest rate of 8 percent per year. (The average interest rate for new investments of the trust funds during the last 6 months of 1978 was about 8½ percent). The estimate is also based on the assumption that the total liability is received by the trust funds when due and invested immediately. Since the due date for the third month of each quarter would be no different under the new schedule, there will be no additional interest earnings on the third month's liability.

The estimated additional interest income to the trust funds is not directly related to lost interest income to the States since the latter amount would vary based on investment practices from State-to-State and entity-to-entity. It is possible, for example, that the $80 million estimate of lost interest to the States does not include interest income to the local governments and does not account for other ways in which the money might be used, such as the payment of current expenditures.

Our estimate of interest the State and local governments could earn under the new schedule—$75 million in fiscal year 1981—was based on a conservatively low interest rate of 5 percent per year. We also assumed that the liability on each employee's earnings would be invested 5 days after the employee is paid and held until the contributions must be deposited. Undoubtedly the State and local governments will continue to use the contributions to meet current expenditures for at least part of that time. Such use may permit the continued investment of other State or local government funds and, in some cases, may reduce the State or local government debt, thereby saving interest costs.

QUESTION

2. It appears that no one has conducted an in-depth study of the entire issue of States' deposits. The National Association of Counties testified they would gladly do a survey. You apparently are basing your computations on the results of a 1974 questionnaire. Therefore, would it be appropriate to defer the effective date of the new regulations for one year or until a study could be conducted?

RESPONSE

It is true that the State responses to the 1976 survey sponsored by the House Subcommittee on Social Security were based on 1974 data. However, as recently as 1978, the General Accounting Office conducted a study of State and local reporting practices and concluded that the States could report even more frequently than the Social Security Administration is requiring.

We would not favor postponing the effective date of the new regulations either for one year or until an additional study could be conducted. The regulations will not be effective until July 1890—more than 18 months after the date the final regulations were published. This start-up time seems sufficient for State and local governments to make necessary adjustments in their administrative procedures. To further defer the effective date would subject the social security trust funds to the continued unjustifiable loss of interest income.

This issue has been under study for ten years and we seriously doubt that a study would provide information which would warrant any change in the new reporting schedule. We think that much of the information a study might elicit would merely be an update of the 1976 responses. There can be no doubt that whatever the administrative costs of the new regulation may be, they will easily be met by amounts of interest the States will still be able to earn.

We welcome the offer of the National Association of Counties to undertake a survey of current administrative procedures of subdivisions. Such a survey could yield information of great value that would enable us to better assist the States and subdivisions to modify their administrative procedures to adjust to more frequent deposits. We would be happy to work very closely with NACO in this survey and with the States and subdivisions in developing solutions to their problems.

QUESTION

3. Would it be feasible to turn the entire State deposit and collection process over to the IRS and eliminate the involvement of both the States and the SSA?

RESPONSE

Yes, this would be feasible but it would require fundamental changes in the law. Under present law, IRS is responsible for collecting withheld income taxes from employees of private business and State and local Governments as well as collecting social security taxes from private employers. If social security coverage were made mandatory for State and local employees, IRS would collect their social security taxes as in the case of private employers and the proposed regulation would not be needed. However, the issue of universal coverage is the subject of a congressionally-mandated study in HEW and until this study is completed, it would be premature for universal coverage to be considered as a solution to the frequency of deposits issue. As you know, there are far more important issues to be resolved in connection with universal coverage.

Under present law, coverage for State and local employees is provided only under agreements between the Secretary of HEW and each State, and each State is liable for the social security contributions due for covered State and local employees. To eliminate the involvement of the States would require negotiation of contracts directly with some 65,000 State and local entities. Our new regulation, in our view, represents the best solution to the problem of balancing the administrative problems of the States against the considerable loss of interest being experienced by the social security trust funds under the current depository rules.

QUESTION

4. All of the State Social Security Administrators testified that they were not consulted prior to the issuance of the final regulations on November 20, 1978. They said they had no indication the final regulations would embody a 15-15-45 day depository proposal. Is this true? If not, how were the States consulted?

RESPONSE

The Notice of Proposed Rulemaking (NPRM) published on March 30, 1978, would have required a 15-15-15 day depository schedule. The NPRM contained five options for phasing in the 15-15-15 day rule and requested comments on the options or any variation. The State responses to the NPRM indicated opposition to any change in the depository requirements. Although the States suggested no alternatives, the Final Regulation published on November 20, 1978, contained the 15-15-45 day rules which is more liberal than the rule originally proposed in the NPRM.

We advised the National Conference of State Social Security Administrators that we intended to proceed with publication of a final regulation that would require deposits on a 15-15-45 day basis. Social Security Administration staff advised the President of the National Conference at least one month prior to the publication of the final regulation that the final regulation would be the 15-15-45 day rule.

It is important to note that the States were aware of our intention to change the depository schedule long before 1978. We have been considering a monthly deposit schedule within HEW since 1969. The States have been actively involved in discussions of this at least since 1974. In 1975, the Social Security Administration and the State Social Security Administrators had extensive meetings on the question of more frequent deposits and together developed the questionnaire sent out by the House Subcommittee on Social Security to identify the problems the States would have under a monthly depository schedule. We believe we have had full consultation with the States.

QUESTION

5. Fred Henne, the Social Security Administrator for the state of Arkansas, testified that when Arkansas deposits its quarterly contributions in the Federal Reserve Bank in Little Rock, it takes 11 days before the deposits are credited to the Social Security Trust funds. He maintained this was true all over the country. Apparently, the federal reserve banks get the benefit of this money during the 11 day period.

In any event, I would think the trust funds are unnecessarily losing a substantial amount of interest. This is totally unacceptable. First of all, could you verify Mr. Henne's charge. And second, if Mr. Henne is correct, what do you propose to rectify the problem?

RESPONSE

Mr. Henne had correctly described what has been the situation until quite recently. The Federal Reserve Banks are now notifying the Department of Treasury of deposited contributions by wire within 24 hours after the deposits are made. As a result, the contributions are credited at that time to the social security trust funds and the Department of the Treasury is investing the social security contributions immediately after they are credited to the trust funds.

QUESTION

6. Your new regulations are designed to reduce the amount of time Federal funds (that is, social security contributions) are in state hands and drawing interest for the states rather than for the social security trust funds.

What system do you use in Aid to Families with Dependent Children and other major grant programs to reduce the amount of time Federal funds are available to the states before they are actually spent by the states? What do you estimate are the savings over the prior system?

If you do not already do this, would it be possible to have a system in which Federal funds would not be transferred to a state until the state actually makes out a check against those funds? What would be the savings under such a system?

RESPONSE

The procedure HEW now uses to transfer Federal funds to the States under public assistance programs allows the States to draw Federal cash on or before the day when the States pay their bills. Between the time the State checks are written and the time these checks are cashed by recipients, many States invest the Federal funds and earn interest. The average lag time between issuance of the checks by the States and cashing of the checks by the recipient is 12 days.

The President's 1980 Budget proposes a change in this procedure which would require the States to use a checks-paid letter of credit procedure. Federal funds will be drawn only after a check was actually presented to the State's commercial bank for payment, thus eliminating the 12-day lag. Implementation would begin in the public assistance programs and would be accomplished in the 10 largest recipient States in 1980. Elimination of the 12-day gap would produce a one-time outlay reduction of $400 million in fiscal year 1980 and would result in annual interest savings of $38 million based on current Treasury interest rates. (The Aid to Families with Dependent Children program would save approximately $111 million of the $400 million total.) At the same time the procedure would assure that Federal funds would be available timely to meet the needs of the recipients. The Department plans to extend this procedure to the full 50 States and health and education programs in fiscal year 1981 and fiscal year 1982.

Senator NELSON. Next, we have a panel of Mr. John Franke, chairman, Board of Commissioners, Johnson County, Kans., and chairman of the Labor-Management Policy Steering Committee of the National Association of Counties, accompanied by Mr. James Krivitz, supervisor, Milwaukee County, Wis.; Barton Russell, executive director, National Association of Towns and Townships; John Breidenberg, representing Hon. James Clark, president, Maryland State Senate, on behalf of the National Conference of State Legislatures.

Gentlemen, if you would each take a seat and then identify yourself by name for the reporter, so if you make some comment, the hearing record will be accurate.

Mr. FRANKE. I am John Franke, chairman of the Board of Commissioners, Johnson County, Kans., and also appearing as chairman of the Labor-Management Policy Steering Committee of the National Association of Counties, and also speaking on behalf of the Municipal Finance Association.

Mr. KRIVITZ. James Krivitz, Milwaukee Board of Supervisors.

Mr. BREITENBERG. John Breitenberg, representing President Clark of the Maryland State Senate on behalf of the National Conference of State Legislatures.

Mr. RUSSELL. Barton Russell, National Association of Towns and Townships.

Senator NELSON. Mr. Franke, you are making a statement on behalf of the panel. Your statement will be printed in full in the record; and you may offer it however you may desire.

STATEMENT OF HON. JOHN FRANKE, CHAIRMAN, BOARD OF COMMISSIONERS, JOHNSON COUNTY, KANS., AND CHAIRMAN, LABOR-MANAGEMENT POLICY STEERING COMMITTEE OF THE NATIONAL ASSOCIATION OF COUNTIES

Mr. FRANKE. Thank you, Mr. Chairman. I am certain that first of all we must express our obvious and very sincere gratitude for this opportunity because we feel that this is the first time to be heard with regard to the regulations as proposed and also with regard to the report to the Congress with respect to local jurisdictions, small counties, cities, townships, and local jurisdictions.

Our written testimony does address three points with regard to the National Association of Counties. I do wish to specify the primary thrust of our testimony is the administrative burden that will be imposed on local jurisdictions, including cities and counties, and that HEW and GAO in their recent reports to Congress have failed to adequately examine the impact of the regulations on local governments. Our opinion with regard to local jurisdictions is that the regulations fail to recognize that the reporting time for local jurisdictions to report to the State would be constrained to between 3 and 5 days, and that many times this would also include weekends and holidays, thereby even further constraining the reporting time.

Presently, we have four reporting times as far as cities and counties are concerned. This would increase under the regulations to 12.

We feel very strongly that the report and the regulations totally misunderstand the accounting and reporting procedures presently used by local units of government; that most smaller jurisdictions, cities and counties, have rudimentary and limited abilities with regard to our staff and payroll procedures; that most of us do not have computerized systems which most, or all, States and larger jurisdictions have; that the majority of our reporting officials are part time or voluntary; and that we feel that implementation of the regulations would add new responsibilities to county government.

Senator NELSON. The municipalities now are paying withholding taxes to the Internal Revenue Service on a particular schedule within 3 days after the pay period, excepting, as I recall, those whose withholding is below a certain amount.

Mr. FRANKE. That is correct.

Senator NELSON. I ask the same question of you that I asked the Social Security Administrator: If the municipalities were required to make out a check for depositing that money on the same schedule that they have to make out a check for depositing withholding taxes, what additional burden is there?

Mr. FRANKE. My experience is, as a county commissioner, the former mayor of a small city, and a councilman, that many of these

details are things that clerks or various people handle. My own impression is that we deposit IRS withholding funds to a fiduciary account with local banks of some type, directly to that fiduciary account.

Our social security withholdings represent a different set of circumstances in that we report to the State periodically; and in my own opinion, the routine that we take, simply by its being different and involving a different recording factor, would give me the problem as the chief elected official.

Supervisor Krivitz does have experience with regard to that and might explain it further, Mr. Chairman.

Mr. KRIVITZ. Mr. Chairman, certain States such as Wisconsin require that counties be responsible for certain subunits within those counties; for example, senior citizens' homes, or highway departments, or whatever, for the purpose of social security contributions.

While, for IRS withholding purposes, these subunits are separate reporting units; for social security deposit purposes, these subunits within the counties would have to be channeled through the county. This would be the additional paperwork that we would be looking at.

There is a time frame also. The larger counties, in particular Milwaukee County, would experience a problem from the computer standpoint, but the samller counties mostly are on manual systems and the time frames now are often not being met. Many times, as the State people will testify later on, the smaller counties are sometimes 30 days or more late with the present requirements. Any type of additional burden at all would be catastrophic.

Mr. FRANKE. Further, I can talk specifically to Johnson County. With regard to the administrative burden that we discussed, the regulations presently say that the implementing time would give sufficient time for jurisdictions to respond. July 1980, I believe, would allow 18 months for jurisdictions to work out any problems.

In Johnson County, we would be required to rewrite our data processing programs. The regulations would also require revision in our software. We would have to retrain some elements of staff as far as any minor new reporting function, and we feel we would have to add one additional clerk.

It is very minor when you talk about——

Senator NELSON. One additional clerk?

Mr. FRANKE. Yes, sir.

Senator NELSON. A municipality with how many employees?

Mr. FRANKE. Johnson County has a 250,000 population with employees of 1,200.

Senator NELSON. Why would you believe you would have to add an additional clerk?

Mr. FRANKE. Not this function alone, perhaps. It is a compounding of various mandates we have received, and one more element being added.

What we feel on this specific question—I have asked both our budget director and county clerk for a realistic comment of what this particular reporting function would consist of, and it did amount to one additional account clerk. This is a salaried person, in Johnson County, probably $700 to $800 a month, and in most respects, it sounds fairly minor, but simply because of the 12 reporting times.

When we do payroll adjustments—for example, we recently changed our pay scale, our pay dates, from the 5th to the 20th of the month, from the 1st to the 15th, to allow some 3 or 4 days leadtime for a cutoff time. This took us 6 to 8 months to implement and it sounds like such a simple decision. Each small, little straw, at some point in time, adds a clerk and adds some portion of staff time, and in the best of our opinion, this would add one clerk.

Then, if we were to do these things—incidentally, the rewriting of the data processing program, the revision of software, is not very easy for a small unit of government. We are a fairly small unit of government.

We feel, then, that it is kind of up in the air. What if this does not work out? What if the time constraints are still such that we still have a difficult time with it, and we cannot meet the State and Federal requirements for reporting in sufficient time

We feel fortunate that our county will be able to more effectively administer the regulations than most local governments because of our population, because of our property valuation methods and that we will be able to do much more than perhaps the 102 other counties in the State of Kansas.

When we talk about a possible relative impact or a possible theory that may work, we are very edgy and we try to work out an objective rationale of what it might do to us, but our biggest worry is what are those things that we have not anticipated.

We do have a comment in our testimony from smaller counties. One of them, Polk County, Wis., has 35 municipal types of government within its borders. Polk County itself said this would be a repressive action on their behalf, not even speaking of 35 other municipalities.

Senator NELSON. How did you happen to pick my hometown?

Mr. FRANKE. Even compounded further is my own county, Mr. Chairman. I am very familiar with that. We have over 400 taxing districts. We only have 40 or 50 real municipal type institutions.

As Supervisor Krivitz mentioned, if we were put into a position to speak and report on behalf of those other institutions, the mental health center operations, the library operations, county home operations and operations of that nature, it would add some burden to us but we would not know what it would be.

We do have a comment, and certainly you will hear other comments, about the loss of interest income—and, incidentally I would like to correct page 8 of the written testimony referring to Johnson County possible loss of interest income. That is $125 monthly that we compiled in 1976, so actually the record should be corrected to show a $30,000 loss of interest income.

The only other item in this area I wish to emphasize would be the Harris County, Tex., commentary. Basically their comment is directed to the effect of the regulations and to the transfer of public revenue from the local to the Federal level; and that is probably the primary reason the regulations are being issued.

I think that the Social Security Administration and GAO and certainly many elements of our society overlook the fact that State and county governments carry a basic service to the poor, the aging and the unemployed, and while it sounds like we are waving flags or

things, we are deeply committed to basic service delivery to those that are least likely to be able to pick up some of the effects of this loss of income.

For the most part, we are supplemented by Federal funds, but basic services still go through county agencies through general levies.

Senator NELSON. That is the problem. That would indicate that the municipalities and the States are making a profit on their deposits of social security funds.

Mr. FRANKE. Certainly, I did not want to speak to this greatly, because other comments will be coming, certainly, but I know in our own county, many times that is overlooked. The basic thrust of general levies and income such as this is not salted away and not used for extraneous purposes, but it used to help in providing certain basic services.

Certainly, those least likely to afford it, benefit from it. It is kind of an ancillary comment.

Senator NELSON. I understand that and appreciate what you say. However, the argument of those who are paying the tax, the social security tax, and you are the beneficiary of the social security program, is that these are, in fact, social security funds, and nobody ever intended that they be diverted in any way for general municipal or State services as though they were some kind of a general revenue sharing.

After all, these funds belong to those people who paid the tax and on whose behalf it was paid by the employer for their retirement program, and I would not be persuaded by any argument that said this takes away, in effect, general revenues from municipalities and States for other important services. I would not consider that a valid argument at all. I think that is an invalid argument. I think the States are entitled to whatever the overhead costs are, but they are not entitled. to make a profit, on funds that should be used for the retirement of people covered by social security.

Mr. FRANKE. Certainly it was not intended as an argument. I am sure those will come. Sometimes, in realism, we lose those identities, and in Johnson County, if we are talking about a $30,000, perhaps, loss of interest income, either one or two things happen: We make it up somewhere else through property taxes or some other fashion, or we reduce expenditures by that amount, one of the two. I am just making that, Mr. Chairman, as an ancillary comment.

Senator DOLE. If all the Federal grants arrived on time, you would not need to hang onto the social security money. I think that may have an impact, too, in Johnson County, or any other county.

The Federal Government gets into a program. It is all laid down. The money is supposed to arrive next month, and it is the next month maybe next year. I think that may cause some complications. It is sort of a two-way street. Maybe it is not a legitimate argument, saying you should not hold the money and profit from it, but by doing that, you offset some of the losses that you incur, and costs that you incur, the other way around.

Maybe it is not the fault of Social Security, but you have to hit where you can.

Maybe they have already been on time in Johnson County. I have had a few calls saying, "Can't you speed up the payments and grants."

Mr. FRANKE. I remember some correspondence, Senator.

The third and final element of our written testimony is that we do not feel that GAO and HEW in the report and the regulations have really contacted the local and municipal governments to receive objective comments.

We realize that the ills of the agency are of national import and many times we feel that certain mandates have not been followed with regard to the effect on local jurisdictions.

From our standpoint, from my standpoint, perhaps the State difficulties may have been addressed, although I doubt that from hearing comments of other State officials, but certainly local jurisdictions that represent the length and breadth of local taxing units of government have not been contacted.

It is a situation that, I believe, the practicability has never been addressed for local units of government. We could use very strong words.

My personal comments would be that the regulations themselves approach the onerous—are arbitrary, overbearing and inequitable. I will not use those right now, Mr. Chairman, but we feel very strongly about the regulations.

We feel these are questions, that the questions have not been asked of us. Certainly any comments that we have had have not been addressed.

We realize that we have a position and the administration must be supported and the Social Security Act must be supported. We know that it has many ills right now, and we would like to be asked what could be our part in supporting those ills?

The Commissioner did mention that he could not see any great withdrawal attempt being made by various local units of government from social security activities. Quite honestly, in discussions we have held within NAC and within the labor-management steering committee this is a valid point and could well speed up such withdrawal feelings.

If I might, I have dwelled too long, Mr. Chairman. I would like to leave it for one of the other gentlemen to make a comment.

BARTON RUSSELL, EXECUTIVE DIRECTOR, NATIONAL ASSOCIATION OF TOWNS AND TOWNSHIPS

Mr. RUSSELL. The National Association of Towns and Townships is a federation representing the interests of local government officials from over 13,000 predominantly nonmetropolitan small communities across the country.

Before beginning my testimony today, Mr. Chairman, I would like to thank you and members of the subcommittee, for inviting the association to provide the township point of view on this very important intergovernmental issue. Mr. Ed Kreuger, executive secretary of the Wisconsin Towns Association and second vice president of our national association, was originally scheduled to testify before this subcommittee but, regrettably, because of a conflicting commitment he could not be here today.

At its last meeting, the association's board of directors voted unanimously to oppose attempts by the Social Security Administration to change from the current system requiring quarterly deposits of social security contributions to a process which will require more frequent deposits.

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ADMINISTRATIVE BURDEN FOR SMALLER LOCAL GOVERNMENTS

The reasons for NATAT's deeply rooted opposition to this change are basically twofold. First and foremost, township officials are extremely concerned about the increased administrative burdens which the new regulations will result in. As you may know, many of the Nation's townships and other smaller jurisdictions are managed by part-time elected officials—an often overlooked group of local government leaders who provide a valuable service to their communities. These jurisdictions do not have the administrative resources which are found in the larger municipalities. In this day of growing social complexities and increased State and Federal mandates, these local officials are finding it more and more difficult to cope.

Let me make reference to a bill presented by Senator Danforth, the Small Communities Act of 1978. It addressed the administrative problems that townships and other small communities are facing, and it really spoke to the issue that is covered here today.

Increased Federal paperwork resulting from new regulations has many direct and visible administrative impacts which, in and of themselves, are offensive enough. However, one of the more serious negative implications not usually considered is the effect such regulatory changes have on citizen-officials who may be new to local public service. As observed recently by one veteran State social security administrator: "Too often after agreeing to serve, those local officials find that to a greatly increasing extent, the redtape is more burdensome and time consuming than they had realized would be the case. They find that they can ill afford to take time away from their jobs and many refuse to be a candidate for another term, or they resign before their term ends."

This, Mr. Chairman, is just one of the very real problems which the National Association's members have with the changes which were implemented by the Social Security Administration.

Even though assurances have been given by some Federal officials that reporting requirements will be lessened substantially in the future, township officials are somewhat doubtful that such will be the case. In many areas of the country, our members are being told by State administrators that requirements by the Federal Government for more frequent deposits will mean that they will be required to provide additional local documentation to the State.

LOCAL GOVERNMENTS WILL SUFFER FINANCIAL HARM

Redtape is not the only serious problem which will result from the new regulations. Local and State governments stand to lose substantial revenues from their treasuries once these changes go into effect. Townships and other Government entities can ill-afford to lose this money, especially in a time of rising inflation, Federal cutbacks, and increasing service demands. Needless to say, this new system could not have been proposed at a worse time.

CONCLUSION

Because of these deleterious financial consequences and the redtape which would result, the National Association of Towns and Townships, as previously stated, is absolutely opposed to changes requiring

more frequent deposits of social security contributions. NATAT supports the view outlined by Senator Nelson in a recent press release in which you stated: "The change will result in a loss of local government interest income and would create a mammoth Federal paperwork burden, resulting in increased administrative costs."

Although your remarks related to a proposal requiring monthly deposits, our association believes that they apply to the new regulations as well.

Senator NELSON. I do not know whether it is an additional paperwork burden, or not. When the proposal was first made, I thought it was. That was a year ago, so I do not know what comment you are referring to. My posture all along has been you should not add to the paperwork, the Social Security Administration must be certain that they adequately compensate the municipalities and the States for the work that they do.

Beyond that, you have a serious question if you are insisting that social security tax money ought to be used for general, municipal or State purposes. I do not think that the hundreds of millions of people who pay into social security would agree with you that funds should be diverted from retirement funds, from the payment employers are making, for local and State government employees.

I do not defend that now, and I have not in the past. I do not consider it a valid argument, for you to come in and say that if you take this away, you are putting an additional burden on us because we are providing certain services to our municipalities and States with that money.

I think that the answer to the social security recipient is that is my tax money. If you want to provide services, get it out of the general tax levies and not out of sharing from the social security funds.

That, to me, is a very unpersuasive argument.

Mr. RUSSELL. Mr. Chairman, it may not have originally been the intention to provide revenues for local governments to subsidize local services but, in fact, over 20 years, in many areas, I think they have become dependent on it, and while social security recipients may question the use of those funds for local services, and rightfully so, I think that we still have to look at the impact it is going to have on local services.

Senator NELSON. You raise a very important point that is much broader than that. We now have—and there are State legislatures represented here—we have 22 legislatures that have passed constitutional resolutions and amendments to require the Federal Government to have a balanced budget.

Those same legislatures are raising hog with me for proposing that we take away general revenue sharing for the States even though 42 States have $8 billion in surplus.

And then you have Governor Brown sitting out there in California denouncing the unbalanced Federal budget and asking for a constitutional amendment denouncing the Congress while his State is getting $10 billion worth of Federal money. I want to help Governor Brown and take away his general revenue sharing. It will help balance the budget.

To come down here and argue that you are providing general services to the community out of social security retirees' money, and you cannot afford to give it up is totally unpersuasive to me.

Mr. RUSSELL. I would like to emphasize that our primary concern is really not the loss of interest income, but rather the administrative burden.

Senator NELSON. That is a question that I wish you would address, because I think when the record is all over with, we will not hear from the witnesses here, from the Social Security Administration or the GAO an actual proof of what has happened on the paperwork issue.

You represent the towns' association. It would be very helpful for the record if you just did a sampling of your towns with employees of 3 or 4 to 50 and 100, and took the actual paperwork and did a time study, which would not be too difficult to do, so that the record would show whether or not there is an increase in paperwork for the municipalities.

That is an important factor, because the Congress does not want to increase paperwork. We would like to see it cut. But I did not get that testimony from the Social Security Administration or from the GAO and, thus far, not from this panel.

Each side is giving us their conclusions that it does not increase paperwork, and you that it does, and with no proof of what actually happens.

Mr. RUSSELL. We can only project that there will be an increased amount of paperwork. We don't know to the extent that will be, yet, because the system has not yet been implemented, and we are reflecting basically the information we are getting from State administrators who indicate that they will be forced, because of their responsibilities, to increase the reporting requirements, and so it is very difficult to project at this point exactly what that is going to mean.

All we can say is, generally speaking, we think that it is going to result in an increased administrative burden which, by itself, will affect all municipalities negatively, but particularly the smaller ones are going to have a harder time.

They spent years basically entering into productive, positive relationships with the administrators, with the State Social Security program. Now, if they have to change, it will be very difficult for them, specially the part-time elected officials.

Senator NELSON. If you tie the two together, the Social Security Administrator testified, as you heard, that they will propose that you go to an annual report on form 941 instead of a quarterly report. It is his judgment that, combing that along with what they are proposing, the paperwork will be less. Your judgment is that it will be more; and neither side has come to the Congress with any proof of either, and that is what is bothersome.

The one proof that is clear is the statement of the Social Security Administration and the GAO, and confirmed by you people, that you are making a profit on interest earned over and above your administrative costs. You both agree to that.

Mr. RUSSELL. Yes; I would like to point out, however, in the case of township governments, the profit, as it is called, is really very marginal. That issue is really not the import one with us, but rather the redtape.

I think when the administrators of the State programs speak, they will probably be in a better position to let you known what the impact will be on smaller municipalities, because they deal with them on a day-to-day basis.

Senator DANFORTH. Let me ask you two questions just on the paperwork point. Would not the paperwork be reduced, would not your problem be solved. If there were a different rule established for very small units of governments than for the larger ones?

Is that a feasible alternative? Could we somehow define smaller units of government according to number of employees, and so on, and keep them under the present system and move larger governments into the new monthly method?

Secondly, I do not understand what is wrong with keeping the present system, if that is less paperwork, and simply charging interest to you? Why would that not work?

Maybe it would be imprecise, but it would seem to me that it would be close enough that it would solve the problem of those who say it is not equitable to be profiting at the expense of the trust fund and, therefore, that the money we are going to get, we are going to charge you for the use of it.

Would that be the tremendous paperwork burden as the Administrator indicated that it would? Why would it not be fair and reasonable?

Mr. RUSSELL. I would like to address the first suggestion that you made. I would like to say that it represents a laudible approach. We feel that is is time that the Congress and the administration recognize that small local governments have smaller capacities that the larger municipalities.

We would support methods to make it easier for them to comply with Federal regulations.

What I am talking about has to do with State requirements under Federal law. The States feel, as I understand it, that they would be required to get more local information under the proposed regulations, or under the final regulations, of the Social Security Administration.

Senator DANFORTH. That could be remedied, could it not?

Mr. RUSSELL. I am not sure whether that could be done by administrative fiat or legislative change. I suspect that it would not be difficult. But they report to their States—township officials now report to their State administrators and the State administrators are telling them that they will be required to ask more information with the eight checks per year system than under the quarterly system. That is primarily our concern.

Senator DANFORTH. If there were a quarterly system for the very small, let us suppose that there is a town of 2,000 people with three employees. Could it not be made clear that we would stay on a quarterly system and everything would be the same with respect to the very small government?

Probably it would have a very minimal effect, if any, in respect to dollars, but it might alleviate the administrative burden for those units of government that are operated on a volunteer basis by the guy who heads the local hardware store or the gas station.

The second, and more far-reaching suggestion that I would have is that the problem is money rather than forms, Why not compute the interest? Why not charge interest for local governments at any rate that we wanted to? The Federal Government now charges all kinds of interest. Why not do the same thing?

Mr. RUSSELL. I cannot state the position, obviously, of the Social Security Administration.

Senator DANFORTH. I would like your views on both those proposals.

Mr. RUSSELL. The bottom line for local officials would be better. They would break even, at least. That would be acceptable, but it would not cost them more money as a result of interest payments.

Most certainly, anything that can be done to reduce the paperwork is really the issue, and that proposal that they be kept at a quarterly reporting system, I think, is a good one.

Senator NELSON. Let me say that Senator Danforth raised a good point, The Administration has already proposed, as you know revised income tax withholding payment schedules. If a municipality has social security and income taxes of $1,000, or less that $1,000, they will be allowed to report quarterly rather than on a payroll period.

If you apply some kind of an exemption like that to municipalities to get away from reporting, as Senator Danforth says, it would not cost much money. Would that solve your administrative problem if the exemption were at a reasonable level?

Mr. RUSSELL. As discussed, I belive it would.

I would just like to close by thanking you again and by asking that if an administrative remedy cannot be proposed such as we discussed, that a legislative remedy be introduced to achieve the same end.

Thank you very much.

STATEMENT OF JAMES A. KRIVITZ, SUPERVISOR, MILWAUKEE COUNTY, WIS.

Mr. KRIVITZ. I think we are underemphasizing the possible impact on counties opting out of the system. I can speak from experience.

In Milwaukee County at the present time, there is legislation introduced to do just that. At the present time, we are trying to evaluate the fiscal impact from all sides, but it is a serious proposal and this is happening in other counties across the country also. I do not think that we should underemphasize that point.

Finally, I would hope that, at the very least, this panel would allow States and local governments to give a little more input into these proposals.

The present data that the Government people that are testifying here gave you is from 1974, and extensive contacts were not made with local units of government at that time. I understand the National Association of Counties would be willing to commission a survey to look at counties and give their input into this process, if a little more time were extended to do this.

Senator NELSON. Your concern is additional paperwork, or loss of revenues, or both?

Mr. KRIVITZ. In Milwaukee County, we lose roughly $150,000 a year. Obviously, that is not an insignificant sum, but at the same time we realize that the system is not going to stop if we do not get that money.

I think data processing is probably the major concern of many of the larger automated counties, at least automated in terms of payroll processing. We run a pretty tight ship, and the impacts of proposition 13 have been felt fairly strongly in the last couple of years. We have either held even or lowered our property tax levy in the last 5 years.

Our data processing at the present time is at a point—because of the fact that we have been able to reduce many of our own administrative procedures—where we can handle the workload that we have. I think that something like this would give input, or add some sort of an additional cost.

In fact, this is what I was provided with by our staff back home. To possibly require additions to that data processing system—these costs could run from $100,000 to $1 million, depending on the complexity of the system.

From my standpoint, from the larger county standpoint, I think the data processing question, in terms of the administration problems, would be the most significant.

Senator NELSON. You said the National Association of Counties would be willing to make a survey if they had the opportunity. Do you mean to take the proposal and do a careful study to determine whether or not it increases paperwork?

Mr. KRIVITZ. I think they would ask counties to respond specifically to how these proposed regulations would affect them in all areas, both financially and administratively.

Senator NELSON. Thank you very much.

Mr. BREITENBERG. Mr. Chairman, I have an extensive statement that has been prepared. With your permission, I will submit it for the record and summarize its contents.

Senator NELSON. It will be printed in the record, and you make the points that have not already been covered.

STATEMENT OF JOHN BREITENBERG, REPRESENTING HON. JAMES CLARK, PRESIDENT, MARYLAND STATE SENATE, ON BEHALF OF THE NATIONAL CONFERENCE OF STATE LEGISLATURES

Mr. BREITENBERG. I challenge a philosophy which seems to be widespread within the Federal bureaucracy. Too many Federal officials and the Federal regulations that they promulgate treat State and local governments as though they were profitmaking enterprises.

First, I think that we must all agree that the Federal, State, and local levels of government, together with the Government in this country, that we all serve the same master, our common constituent, the taxpayer. Secondly, Federal regulators need to recognize that the financing of new or increased mandates imposed upon us by the Federal Government must come from these same taxpayers.

Imposing an additional administrative burden on the State and local governments, and a reduction or limination of the interest revenues, will place undue pressures on the very taxes which the voters appear to like least.

While HEW and GAO point to the potential gains to the Federal Government to changing the social security deposit requirements, what we are really talking about is a shifting of taxpayer dollars from one pocket to the other. We must also recognize that there is a fundamental difference between private and public employer participation in the social security system.

Increasing the deposit schedule for State and local governments is not going to significantly alter the fiscal condition of the social security trust fund. The added administrative costs and loss of interest earnings will, however, have a significant effect on some State and local tax systems.

If implemented, the HEW proposal would raise State and local government expenditures in order to finance the administrative burdens, while at the same time reduce the revenues through the loss of the interest earnings.

It is hard for State elected officials to sit idly by while we are getting hit from all sides at once. Many jurisdictions are hard pressed to balance their budgets as a result of proposition 13. We must be concerned with the widespread adoption of limits on spending and taxing by our common constituents, the taxpayer.

The HEW regulations are not sensitive to the fiscal interrelationships which exist among Federal, State, and local governments.

We are elected to serve a common taxpayer, not a particular government entity. Therefore, the Federal Government should resist the temptation to impose mandates on States and localities in a manner which will exacerbate the fiscal pressures on State and local budgets.

Increases in State and local employee coverage, and State and local investment practices, have resulted in increased interest income to State and localities. States readily recognize that their loss of interest income would become the Federal Government's gain, and some observers point——

Senator NELSON. May I interrupt you? I do not think you really mean that. It would not be the Federal Government's gain. These are social security funds that belong to the social security taxpayers, do they not?

Mr. BREITENBERG. That is very true.

Senator NELSON. These are trust fund money. These are not general funds money of the Federal Government.

Mr. BREITENBERG. I meant gain in regard to loss of the States. Some observers point to the States' opposition to the change as a selfish reaction. However, interest earnings in the past have helped defray administrative costs of the social security collection program, which is the case in my own State of Maryland, and there is growing concern that the interest that States and localities might lose under the new schedule will not be enough to meet these administrative costs.

One of the main reasons for the HEW deposit schedule change, the obvious increase in the Federal social security increases due to frequency of social security collection, is that there has been discussion for years in equalizing public and private employees' schedules. You cannot compare State and local governments with other employees, especially when social security deposits are involved.

State governments are made up of hundreds, in some case thousands, of political subdivisions operating independently. Private organizations have a well-defined chain of command which controls the activities of a private company. The lack of a well-defined and coordinated mechanism in State government makes compliance with the new HEW regulations much more difficult for States than it does for a private company.

During the 1977 consideration of the Social Security Act, both you and Senator Danforth developed proposals which would have partially eqalized the aftertax social security burdens imposed on States, local governments, and nonprofit entities. These proposals were based on another major difference between these two classes of employers, and they sought to place public employers on a more equitable footing in regard to their social security tax liability.

If it is desirable to doubt the Federal policy which will narrow the differences between private and public employees with regard to the deposit issue, then Congress should also provide for equity in terms of the aftertax liability for these two distinct employer groups.

We are proposing a refundable tax credit which may be claimed by organizations which are exempt from Federal income taxes. This refundable credit should be considered in light of the credit that the tax system currently provides to private employers.

Social security taxes are considered a business expense for private sector employers and as such are deducted from the State and Federal income tax returns. For example, a business that pays $100,000 in FICA taxes can deduct 48 percent of this amount on Federal returns plus additional sums for State tax liabilities.

The same $100,000 contributed by a private employer cannot be offset under the tax system.

Therefore, the public employer has a greater financial burden than the private counterpart.

This inequitable treatment of public employers should be addressed by the Congress. Hard-pressed State and local governments require assistance in meeting the fiscal demands of increased social security costs.

Profitmaking organizations bear only a portion of the increased social security costs, since they can partially offset the recent payroll tax increase on the Federal and State income tax returns. In order to provide parity of treatment between public and private employer contributions, NCSL urges Congress to enact a refundable credit which could be financed with general revenues so it would not be a loss to the social security trust fund.

That concludes my statement, Mr. Chairman, and I thank you for the opportunity to testify today.

Senator NELSON. Thank you. Senator Dole?

Senator DOLE. I would like to ask one question about the ratio between administrative costs currently and your investment earnings.

What is the ratio as far as your interest earnings and administrative costs? Does the interest exceed the administrative costs now?

Mr. BREITENBERG. In my own State—I just received this information—last year the interest earnings were $2.3 million; the overhead administrative costs were around $400,000.

Senator DOLE. That would be pretty much the national ratio? That would be under the current system. Do you have any projections on what it would be if we changed it?

Mr. BREITENBERG. Yes, sir. The changes are estimated at two-thirds that. In other words, $800,000 in interest earnings for the next fiscal year. Overhead costs would rise, but it is difficult to say how much. There will be a process of reeducation. There certainly will be additional paperwork by the localities, and there will be some additional personnel required.

Senator DOLE. There may be some way to work out a credit for administrative costs. I can understand the profit motive, too, and I think that you have raised a good point about how you are treated differently from the private employer, but we have, in effect, a $2.2 billion windfall, and if you add that for fiscal 1980 on into 1981, it would be $2.6 billion, if we make certain changes in how we treat private employers.

I was going to ask the Administrator what they are going to do with the extra money, but it occurred to me, it would be a chance to reduce if, in fact, this is to be done, to reduce the social security tax to employees and employers about a total of 0.25 percent because there are pressures, of course, to do that also.

Has Maryland passed a resolution calling for a constitutional amendment?

Mr. BREITENBERG. Yes; it has. As a matter of fact, President Clark is one of the leaders of that movement throughout the Nation.

Senator DOLE. I think Senator Nelson does raise a good point. If they are going to put pressure on us to balance the budget, I guess we go right down the line and pick out every area—maybe profit is not the word, but where there is income to the States through use of Federal funds and eliminate those, plus maybe some of the programs.

But I think many of us agree on the balanced budget concept, including Senator Nelson, of course. That does not bother Senator Clark? He sees a difference between this problem and the balanced budget?

Mr. BREITENBERG. Yes, Senator; he does.

Senator DOLE. It does not bother us, either.

Senator NELSON. Thank you all very much for taking the time to come and testify.

[The prepared statements of the preceding panel follow:]

STATEMENT OF HON. JOHN FRANKE, CHAIRMAN, BOARD OF COMMISSIONERS, JOHNSON COUNTY, KANS. AND HON. JAMES A. KRIVITZ, SUPERVISOR, MILWAUKEE COUNTY WIS., ON BEHALF OF THE NATIONAL ASSOCIATION OF COUNTIES (NACo)

Mr. Chairman, and distinguished members of the subcommittee, I am John Franke, Chairman of the board of commissioners, Johnson County, Kansas and Chairman of NACo's labor/management policy steering committee. I am accompanied by James A. Krivitz, Supervisor, Milwaukee County, Wisconsin and Chairman of NACo's labor/management subcommittee on employee compensation benefits and by Charles M. Loveless, NACo legislative representative.

We are here testifying before your committee today on behalf of NACo with a membership of over 3,000 counties across the Nation.* We also would like to indicate that we are speaking today on behalf of the municipal finance officers association, a professional association of State and local government finance officials. I will make a brief statement to be followed by supervisor Krivitz who will also offer some brief comments.

Let me begin by thanking you, Mr. Chairman, for the opportunity to present the views of county government on a matter of utmost concern to us, the final regulations published in the November 20, 1978 Federal Register by the Social Security Administration. U.S. Department of Health, Education and Welfare (HEW). Specifically, I am of course referring to those regulations which require more frequent deposits of Social Security contributions by State and local governments, effective July 1, 1980.

* The National Association of Counties is the only national organization representing county government in the United States. Through its membership, urban, suburban and rural counties join together to build effective, responsive county government.

The goals of the organization are to: improve county government; serve as the national spokesman for county government; act as a liaison between the nation's counties and other levels of government; achieve public understanding of the role of counties in the federal system.

On July 11, 1978, at NACo's annual conference in Atlanta, Georgia which was attended by over 3,500 county officials, our membership adopted a resolution opposing the proposed HEW regulations on this subject which were issued on March 30, 1978 and expressing our support of Congressional efforts to retain the quarterly deposit requirements which have been in effect since 1951. A copy of this resolution is set forth below as attachment No. 1.

Only last week, on January 24, 1979, NACo's labor/management policy steering committee voted unanimously to adopt a resolution which specifically opposes the November 20, 1978 regulations and reiterates our strong support of legislation preserving the present quarterly deposit and reporting requirements. A copy of the resolution is set forth below as attacement No. 2.

NACo strongly opposes HEW's November 20, 1978 regulations and supports congressional efforts to maintain the current quarterly deposit and reporting requirements for several reasons. First, the regulations will impose an onerous new administrative burden on counties and on other units of local and state governments and will result in a significant increase in administrative costs. In some cases, as I will document below, compliance with the new regulations will be virtually impossible..

Second, the regulations will impose a substantial loss of interest earnings or cash flow on counties and other units of State and local government which are already financially hardpressed.

And finally, we believe the November 20, 1978 regulations violate the spirit, if not the letter, of the Social Security Act and of executive Order No. 12044 which requires that Federal agencies and departments not impose unnecessary burdens on State and local governments and mandates a comprehensive analysis of all regulations which have "major consequences" for State and local governments.

I. HEW'S NOVEMBER 20, 1978 REGULATIONS WILL IMPOSE AN ONEROUS NEW ADMINISTRATIVE BURDEN ON COUNTIES AND OTHER UNITS OF LOCAL AND STATE GOVERNMENT

HEW's November 20, 1978 regulations, which are effective July 1, 1980, require State administrators of social security coverage for State and local government employees to deposit their payments within fifteen days after the end of the first month of the quarter, within fifteen days after the end of the second month of the quarter and within forty-five days after the end of the third month of the quarter (hereafter referred to as the 15/15/45 day cycle). While in HEW's view thas represents a compromise between the legitimate interest of State governments and the financial needs of the social security system, we belive that HEW has failed to take into account the significant operational impact which the regulations will have on local governments.

We have been informed by various State social security administrators that the new deposit schedule mandated by the November 20 regulations will, for the first two months of the 15/15/45 day cycle, require local government units to turn over to the States employee social security contributions, together with the matching payments of local government employers, no later than three to five days after the end of the month (which may include weekends and other non-working days). This would be necessary in order that the States will have the time to reconcile, consolidate and file payments for the many local units of government within their jurisdictions by the 15th day deadline.

Under the current deposit and reporting requirements, local government reporting units (for social security purposes) are usually given up to thirty days by the States to turn over their social security contributions. Thus, the net effect of the November 20, 1978 regulations is to reduce the reconciliation and disbursement period for local units of government from approximately thirty days to between three and five days. When we also consider that the new regulations require counties and other local governments to perform this reconciliation and disbursement function twelve times a year rather than on the current quarterly basis, we can only begin to appreciate the magnitude of the administrative problem for local governments.

In our view, Mr. Chairman, the HEW regulations and the Comptroller General's December 18, 1978 report to the Congress, entitled "Liberal Deposit Requirements of States' Social Security Contributions Adversely Affected Trust Funds," indicate a fundamental misunderstanding of the accounting and reporting procedures utilized by most counties and other units of local government. Due to financial, staffing, and other limitations, most counties and other local governments do not have complex and sophisticated, computerized payroll-accounting systems. As will be substantiated by the State social security administrators present in this room, many locai reporting officials are part-time or volunteer workers; they

often are housewives or businessmen who, in effect, serve as part-time bookkeepers for local governmental units. Accordingly, there is a high frequency of turnover among local reporting officials.

We have been informed by various State social security administrators that county governments will also be responsible, at least in certain States such as Wisconsin, for performing the reporting/disbursement function for various county-owned enterprises such as hospitals and nursing homes which, for Federal income tax withholding purposes, the Internal Revenue Service treats as separate reporting units. When it is considered that these facilities frequently have separate payroll systems and employ large numbers of employees, the task of those county officials charged with remitting and reporting contributions and wages under the regulations becomes even more complex.

In our view, the operational impact of HEW's regulations on counties and other local governments may be summarized as follows:

1. Thousands of local governments will be forced to hire additional personnel to meet the demands of the increased remittance and reporting requirements and the compression of time in which payments and accompanying information are to be submitted to the States. for example, in my home, Johnson County, Kansas, with a population of approximately 238,000, the county budget director has informed me that we will be required to hire an additional accounting clerk in order to comply with the regulations.

2. Many local governments will conclude that there is no alternative but to computerize their payroll accounting systems. Such a costly innovation for an individual county will involve an initial capital expenditure of many thousands of taxpayer dollars. Even in those counties which already have computerized systems, an initial major operating expenditure will be required in order to redesign the computer software necessary to generate the required information.

3. Training programs, financed presumably by local and state governments, will need to be instituted to educate local reporting officials in regard to complying with the new regulations. When we consider that there are approximately 61,000 reporting units, such a task is obviously of enormous magnitude. Further, as there is a high percentage of turnover among local reporting officials, training programs must necessarily be of an ongoing nature.

4. A significant number of smaller counties and other local governments will simply find it impossible to comply with the new regulations. As I have already indicated, many local public reporting officials are part-time or volunteer workers, and with the increased workload imposed on them by the regulations, a significant percentage of these officials may not be able to provide accurate and timely payments and reports to the States.

Mr. Chairman, I believe the administrative burden and cost of HEW's November 20, 1978 regulations may be graphically illustrated by examining the probable impact on a county with which you are well acquainted, Polk County, Wisconsin. Polk County, has a population of approximately 30,000 and has the equivalent of approximately 235 full-time employees, according to NACo'S County Year Book (1978). Elroy Sprangenbeg, Polk County clerk, informs us that the County has a manual payroll-accounting system and currently employs one person to complete all wage records, including the social security contribution reports. Spangenberg indicates that, in his judgment, Polk County will be unable to comply with the November 20 regulations unless it changes to a computerized payroll system. Under the current system, the county accounting clerk would have to manually record the wages of all employees in order to arrive at the total figure for employer and employee contributions, and Spangenberg believes that it would be impossible for Polk County to complete the reporting and remittance process within the requisite three to five day period.

This task is further complicated by the fact that Polk County operates a home for the aged, Golden Age Manor, which employs approximately eighty employees and has an entirely separate payroll system. Spangenberg points out that Polk County would be responsible for transmitting to the State of Wisconsin in the social security contributions and wage information for the Golden Age Manor employees.

Spangenberg estimates that the initial capital expenditure required for establishing a computerized payroll system to be in the range of $75,000 to $100,000. Polk county's total tax budget for the past year was approximately $1,750,000, and he therefore believes that computerization will inevitably require an increase in local taxes. He also points out that there will be additional expenses involved in implementing the regulations primarily in the area of either training existing personnel or hiring a new employee to operate the system.

Finally, Spangenberg points out that there are thirty-five municipal governments within Polk county consisting of townships and villages, and each of these jurisdictions has a part-time bookkeeper. In his view, many of these jurisdictions will be unable to comply with the November 20 regulations and in those jurisdictions which attempt to comply, there will be significant increases in personnel and other administrative costs.

While we have no way of estimating for all county governments the total cost and increase in paperwork involved in complying with HEW's November 20, 1978 regulations, suffice it to state that the probable impact on Polk county indicates the figure will be a very significant one.

II. HEW'S NOVEMBER 20, 1978 REGULATIONS WILL IMPOSE A SUBSTANTIAL LOSS ON INTEREST INCOME OR CASH FLOW ON COUNTIES AND OTHER UNITS OF LOCAL AND STATE GOVERNMENT WHICH ARE ALREADY FINANCIALLY HARDPRESSED

The November 20, 1978 regulations will impose a substantial financial hardship on counties and other local units of government by significantly reducing, if not eliminating, opportunities for short-term investment of social security contributions. In response to a June 1976 questionnaire prepared by the Social Security Administration at the request of the subcommittee on Social Security, House Ways and Means Committee, 41 States supplied information indicating an estimated interest loss of $42 million for 1974 if a monthly deposit schedule was instituted. In the intervening five year period, it is reasonable to estimate that the amount of this loss would be considerably higher. While HEW maintains in its November 20, 1978 comments in the Federal Register on the final regulations that State and local governments would continue to earn some amount of interest income, clearly investment opportunities have been substantially reduced.

Current estimates on loss of yearly interest income for a selected number of county governments indicates the following;

1. Harris County, Texas will lose approximately $70,000 on interest earned in 1981, the first full year under the regulations, as is indicated in the statement of D. Gayle McNutt, Washington Representative, Harris County, Texas, which is set forth below as attachment No. 3;
2. Alameda County, California will lose $80,000;
3. Johnson County, Kansas will lose $2,500;
4. Los Angeles County, California will lose $1.5 million;
5. Polk County, Wisconsin will lose between $1,500 and $2,000;
6. San Diego County, California will lose $152,000;
7. Milwaukee County, Wisconsin will lose $150,000;
8. Harnett County, North Carolina will lose between $5,000 and $6,000.

As you know, Mr. Chairman, counties and other local and State governments are faced today with serious financial and complex management problems. Inflation and economic stagnation have increased the cost of government while tax revenues have not kept pace. Thus, we believe an inevitable effect of the November 20 regulations is either to increase the already heavy burden on local taxpayers or to reduce the level of local government services and the number of local personnel.

III. HEW'S NOVEMBER 20, 1978 REGULATIONS VIOLATE THE SPIRIT, IF NOT THE LETTER, OF THE SOCIAL SECURITY ACT AND OF EXECUTIVE ORDER NO. 12044 WHICH REQUIRES THAT FEDERAL AGENCIES AND DEPARTMENTS NOT IMPOSE UNNECESSARY BURDENS ON STATE AND LOCAL GOVERNMENTS AND MANDATES A COMPREHENSIVE ANALYSIS OF ALL REGULATIONS WHICH HAVE "MAJOR CONSEQUENCES" FOR STATE AND LOCAL GOVERNMENTS

Section 218 of the Social Security Act, 42 U.S.C. 418, provides for Social Security coverage for local and state government employees through voluntary agreements entered into between each state and HEW. Under the terms of these voluntary social security coverage agreements, the state assumes full responsibility for all aspects of the coverage, including filing wage reports and paying contributions for all covered local and state government employees.

Section 218(i), 42 U.S.C. 418(i), provides that the reporting and payment regulations prescribed for the States by the HEW Secretary shall be "so far as practicable" the same requirements as those imposed on private sector employers under title II of the Social Security Act and chapter 21 and subtitle f of the Internal Revenue Code of 1954. In adopting this statutory requirement over twenty-five years ago, we believe that Congress clearly recognized the inherent legal and other differences existing between local and State governments and private sector employers and that, accordingly, it adopted the "practicability"

standard to ensure that no onerous administrative or financial burdens would be placed on State and local governments which extended social security coverage to their employees.

It is not our purpose today to outline the various legal, financial and other distinctions which may be drawn between local and State government employers, on the one hand, and private sector employers, on the other. We have already alluded to some of these differences in previous sections of our testimony. However, it should be pointed out that one key difference may be found within the Social Security Act itself: While participation in the social security system is mandatory for most private employers, local and State governments do so on the basis of voluntary agreements with the Federal Government. Further, it should be stressed that while private employers may pass along increased social security costs to individual consumers who are not compelled to buy services or products, the increased costs to local and State governments ultimately will be paid for by all in the form of either higher taxes or a reduction in the level of services.

In 1951, HEW recognized these "practicable" differences by requiring the States to report on wages and salaries of covered employees and to deposit employer and employee contributions within thirty days after the end of each calendar quarter Indeed, in 1959, HEW, recognizing the administrative difficulties involved in reporting and depositing State and local government employee contributions, granted an additional fifteen days after the end of each calendar quarter for reporting and depositing contributions Now, twenty years later, in issuing its November 20 regulations, HEW has decided to ignore the practicability standard of section 218(i) of the Social Security Act by placing significant new administrative and financial burdens on local and State governments.

On March 24, 1978, the President issued Executive Order No. 12044, entitled "Improving Government Regulations," 43 F.R. 12661 (hereafter referred to as E.O. 12044). Among other things, E.O. 12044 directs Federal agencies to issue regulations which "* * * shall not impose unnecessary burdens * * * on State and local governments." It further mandates that agencies shall conduct a comprehensive regulatory analysis of proposed "significant" regulations (those involving a significant increase in costs or prices for levels of government, section 3(a)(1)(b), E.O. 12044) which shall include "* * * a description of the major alternative ways of dealing with the problem that were considered by the agency; an analysis of the economic consequences of each of these alternatives and a detailed explanation of the reasons for choosing one alternative over the others." Section 3(b)(1), E.O. 12044.

In our view, HEW has not complied with the mandate of E.O. 12044 in issuing its notice of proposed rulemaking published in the Federal Register on March 30, 1978 and in issuing its final regulations on November 20, 1978. As indicated above, section 3(b)(1) of E.O. 12044 requires an analysis of the economic consequences of each of the major alternative ways of dealing with the problem. Implicit within this mandate, we believe, is the requirement that the economic data on which the analysis is based reflect current fiscal realities. However, in its discussion of the loss of interest income to the States involved in implementing the regulations (see 43 F.R. 54084, November 20, 1978), HEW refers principally to the results of a questionnaire prepared by the Social Security Administration sent to the States in early 1976 which was designed to secure 1974 data on the estimated interest losses to the States if a monthly deposit schedule was implemented. While HEW acknowledges that "(T)he States indicate that the amount of those interest losses has now increased," 43 F.R. 54084, it should be noted that, to the best of our knowledge, HEW has failed to present or analyze any more current data on the amount of income loss to the States. In this regard, we believe that HEW has failed to comply with the mandate of E.O. 12044.

CONCLUSION

For the foregoing reasons, we are strongly opposed to HEW's November 20, 1978 regulations and on behalf of the National Association of Counties, we respectfully urge your consideration and support of legislation preserving the current quarterly deposit and reporting schedule for State, County and other local units of Government. While we strongly support efforts by the Congress to improve the financial position of the social security system, we believe that implementation of the November 20 regulations will do little to solve the fiscal ills of the system when compared to adverse administrative and financial impact they will have on counties and other State and local Governments. We believe the

regulations only add further incentives for our counties, cities, townships and states to exercise their right under the current law to withdraw from the system.

Thank you, and we will be pleased to answer any questions you might have.

ATTACHMENT NO. 1

RESOLUTION ON LEGISLATION TO RETAIN QUARTERLY DEPOSITS AND REPORTING FOR SOCIAL SECURITY

Whereas, Counties and other local and state units of government now deposit employees' federal Social Security deductions and contributions (FICA) with the Social Security Division on a quarterly basis; and

Whereas, HEW has already decided that it will publish a notice of proposed rulemaking to require those governments to make monthly, rather than quarterly, deposits beginning in January 1980 and has indicated that the preamble of the proposed regulations will solicit comments on the possibility of a phase-in; and

Whereas, Such a requirement would result in substantial interest income loss to county governments, and the potential administrative cost would more than triple in some cases; and

Whereas, H.R. 11117 introduced by Rep. Robert Roe (D-N.J.) proposes to retain the present quarterly deposits and reporting requirements and has been referred to the House Ways and Means Committee: Therefore, be it

Resolved, That the National Association of Counties recommend support of H.R. 11117 with supporting data on the impact on counties, and also urge each congressman on the House Ways and Means Committee to hold hearings as soon as possible to maintain the quarterly deposits and reporting requirements.

Adopted at the Annual Conference of the National Association of Counties, July 11, 1978, Fulton County, Georgia.

ATTACHMENT NO. 2

RESOLUTION ON LEGISLATION TO RETAIN QUARTERLY DEPOSITS AND REPORTING FOR SOCIAL SECURITY

Whereas, Counties and other local and state units of government now deposit employees' federal Social Security deductions and contributions (FICA) with the Social Security Division on a quarterly basis; and

Whereas, HEW issued on November 20, 1978 final regulations requiring more frequent deposits of Social Security contributions; and

Whereas, Such regulations will be impracticable to administer, significantly increase administrative costs, and result in a substantial loss of interest income to county governments: Therefore be it

Resolved, That the National Association of Counties urges Congress to enact legislation to maintain the present quarterly deposit and reporting requirements.

Adopted by the Labor/Management Policy Steering Committee of the National Association of Counties, January 24, 1979.

ATTACHMENT NO. 3

JANUARY 29, 1979.

STATEMENT BY D. GAYLE MCNUTT, WASHINGTON REPRESENTATIVE, HARRIS COUNTY, TEX.

To: Hon. aylord Nelson, Chairman,
And Members of the Subcommittee on Social Security
Senate Finance Committee.

MR. CHAIRMAN AND MEMBERS OF THE SUBCOMMITTEE: As the Representative of Harris County (Texas) Commissioners Court, the governing body of one of the largest and fastest growing metropolitan areas (Houston) in the nation, I would like to express our opposition to the Social Security Administration's announced regulations requiring monthly, rather than quarterly, payments into the Social Security Trust Fund.

I will cite a number of reasons for our opposition, but I believe the "bottom line" of the proposal—and for our opposition—is clear to all: The net result of the regulation change is to transfer revenue from the local level of government to the federal level of government.

Or more simply stated: Our local taxpayers are going to pay the costs of this proposal, either through increased County taxes, or lose the equivalent services from the County required to pay these costs.

I attach to my statement a copy of a resolution adopted by Commissioners Court soon after these regulations were proposed by the Social Security Administration last year. The minor modifications in the final regulations in no way alter our continuing opposition.

Also attached is a letter from our County Auditor certifying certain specific revenue losses that would have been suffered by our County had these regulations been in effect during the last two years.

In promulgating the new regulations, other than the financial aspects, the only reason given by the Social Security Administration for the change is that state and local governments should be placed on the same basis as private employers, or as nearly so as possible.

Such rationale is at best a rather lame justification of the new regulations. There are two basic fallacies in this argument:

1. There is no recognition of the different fiscal nature of local units of governments and private employers. The fiscal and accounting processes are considerably different for the two entities, with a major factor being reporting and payment requirements of the Internal Revenue Service for the business income of private employers. These reporting requirements carry over into Social Security. In fact, Social Security reporting requirements are not the same for all private employers. Some private employers are required to make deposits as often as weekly. Some make the deposits biweekly and some monthly. The regulations fit the type of business.

The present requirement for quarterly deposits by state and local government was made to fit their fiscal operations and from an accounting standpoint there is no reason for making the change, since it will only result in higher administrative costs.

2. There is a basic difference in the participation of private employers and state and local governments in the Social Security System: Private employers do so by federal mandate; state and local governments participate voluntarily.

Almost one-third of state and local government employees do not even participate in the Social Security program. The ones who do so are at the option of the government involved. As costs of Social Security continue to rise, more and more local governments are finding the costs to local taxpayers prohibitive and are opting out of the program. Many are finding that they can provide better worker protection and retirement benefits through private coverage than through Social Security. In fact, Harris County is now weighing just such an option. Our employes already pay 7 percent of their gross salaries iuto a fine employe reitrement plan (the same as federal employes, who do not participate in Social Security), plus the 6.13 percent Social Security tax.

Whereas increasing costs to private employers mandated by increased Social Security costs are passed along by increased prices to consumers, who do not necessarily have to buy services or products, the increased costs to local governments can only be passed along in increased taxes, which must be paid by all.

For the record, I would like to amplify the figures provided in the County Auditor's letter to some extent.

You will note that the costs are for the County General Fund and the County Flood Control District budgets only. These figures actually represent less than one-half of our total County budget. When you figure in the costs to our other entities, such as the Hospital District, etc., which are county-wide in scope and are part of the overall County government, the costs could reasonably be assumed to double and then some.

Also consider the fact, in relation to the costs to local taxpayers, that these are County government figures only. They do not include the increased costs to the the City of Houston and the other local governments and independent taxing authorities in Harris County.

Our County taxpayers do pay taxes to those entities, however, and their employes are covered by Social Security. What I want to illustrate is that the overall burden on our County taxpayers as a result of these regulations will be many times the impact cited in our figures provided by the County Auditor.

We cite those figures they are the only ones over which Commissioners Court has direct authority and which we can certify as to accuracy.

So we are not just talking about $50,000 a year in additional costs (or reduced services to our local taxpayers), but in the neighborhood of one-half million dollars or more.

Also, please note that the costs shown by our Auditor increased by 11 percent between 1977 and 1978. I believe it is reasonable to assume, considering the es-

calating rates and income levels for Social Security withholding, that the increase will continue to rise by a minimum of 11 percent each year.

Based on that assumption, the projected cost just to the funds cited in the attached Auditor's letter would increase from $50,834 in 1978 to approximately $70,000 in 1981, the first full year the new regulations would be in effect.

I believe you can see from these figures why we oppose the monthly collections on a purely fiscal basis.

I would further point out that the figures we show do not include the additional administrative expenses resulting from monthly, rather than quarterly reporting. We do not know what those costs would be at this time, but they would certainly be an added burden on the local taxpayer.

What if the Social Security Administration decided we should make our payments biweekly, or even weekly? That would certainly get funds into the Social Security Trust Fund faster, at least on paper. It would also require us to totally change our fiscal system and payroll policies, which would involve very significant additional administrative costs to our local taxpayers.

It is hard to conceive that Congress intended to allow such powers over local government to the Administrator of the Social Security program.

With the number of local government entities now considering the exercising of their right to opt-out of the Social Security program, I wonder if the Social Security Administration has really fully taken into account the possibility that the proposed change might be a decisive factor for many. It would not take the opting-out by too many local governments to more than offset any of the projected gains in federal revenues resulting from the new collection method.

In summation, the present deposit requirements are working and are in concert with the original agreement regarding voluntary participation in the Social Security program by state and local governments. The so-called "15-15-45"-day deposit regulations would actually do very little to make the payment basis any more alike for public and private employers. They would, however, take revenues away from local government and provide further incentive for local governments to exercise their right to opt-out of Social Security.

The decision by the Social Security Administration to continue with promulgation of the monthly deposit requirements in no way enhances any directive by Congress and rather would seem to violate the recognition by Congress that the participation by state and local governments in the Social Security program is inherently different from that by private employers.

Basically, the only effect of the regulation would be to transfer public revenues from the local level to the federal level.

We would urge that your Subcommittee take whatever steps necessary to reverse this arbitrary and ill-founded decision of the Social Security Administration reflected in its regulations as published in the Federal Register of November 20, 1978.

Thank you for your consideration of this matter.

D. GAYLE MCNUTT.

OFFICE OF COUNTY AUDITOR,
COUNTY OF HARRIS,
Houston, Tex., December 8, 1978.

Mr. D. GAYLE MCNUTT,
Washington Representative, Harris County, Tex., 1735 New York Avenue, NW., Suite 400, Washington, D.C.

DEAR GAYLE: Thank you for your letter of November 20, 1978 concerning the final Social Security Regulations governing payments of contributions from local governments.

We agree that the regulations will have an adverse effect on Harris County. As an example, the interest earned by Harris County on the employees' contributions was $21,500 in 1977, and $24,186 in 1978. The Flood Control District earned $1,060 and $1,231 during the same period. The interest on the matching contributions from the County and Flood Control District added to the above amounts gives a total of $95,954 interest earned for the two year period.

If the new regulations stand, the loss of income to Harris County and Harris County Flood Control District will be very significant.

We appreciate your continuing efforts to support legislation which will repeal these new Social Security Regulations.

Yours very truly,

S. G. FULLERTON,
County Auditor.

45-083—79——5

RESOLUTION

Whereas, the Social Security Administration has proposed regulations that would increase from quarterly to monthly the frequency with which governmental units deposit social security contributions on wages and salaries paid to covered employees; and,

Whereas, this move would result in an annual loss of interest income to Harris County of $21,500, and to the Harris County Flood Control District of $1,060; and,

Whereas, it appears that the main reason for this regulatory action is to take away such interest income and give it to the Federal government; and,

Whereas, the change would deprive the county of a resource that helps offset administrative expenses involved with properly accounting for the social security contributions; and,

Whereas, the county would encounter additional expenses and administrative problems with an accelerated payment scheme; and,

Whereas, Commissioners Court is desirous of showing its opposition to this proposal; Now, therefore, be it

Resolved, That the Commissioners Court of Harris County, Texas hereby notifies the Social Security Administration of its opposition to the proposed regulations affecting social security contributions as cited above.

It is hereby ordered that this resolution be spread upon the minutes of the court this 10th day of April, A.D., 1978.

Absent, Jon Lindsay, County Judge.

TOM BASS,
Commissioner.
JIM FENTENO,
Commissioner.
BOB ECKELS,
Commissioner.
E. A. LYENS, JR.,
Commissioner.
R. E. TURRENTIN, JR.,
County Clerk and ex officio clerk of Commissioners Court.

TESTIMONY OF BARTON D. RUSSELL, EXECUTIVE DIRECTOR, NATIONAL ASSOCIATION OF TOWNS AND TOWNSHIPS

INTRODUCTION

Mr. Chairman and members of the Subcommittee, my name is Barton Russell and I am the Executive Director of the National Association of Towns and Townships. NATaT is a federation representing the interests of local government officials from over thirteen thousand, predominantly non-metropolitan, small communities across the Country.

Before beginning my testimony today, I would like to thank Senator Nelson, on behalf of the Association's Board of Directors, for inviting NATaT to provide the township viewpoint on this very important intergovernmental issue. Mr. Ed Kreuger, Executive Secretary of the Wisconsin Towns Association and Second Vice President of our National Association, was originally scheduled to testify before this subcommittee but, regretably, because of a conflicting commitment, he could not be here today.

At its last meeting the Association's Board of Directors voted unanimously to oppose attempts by the Social Security Administration to change from the current system requiring quarterly deposits of Social Security contributions to a process which will require more frequent deposits.

ADMINISTRATIVE BURDEN FOR SMALLER LOCAL GOVERNMENTS

The reasons for NATaT's deeply rooted opposition to this change are basically two-fold. First and foremost, township officials are extremely concerned about the increased administrative burdens which the new regulations will result in. As you may know, many of the nation's townships and other smaller jurisdictions are managed by part-time elected officials—an often overlooked group of local government leaders who provide a valuable service to their communities. These

jurisdictions do not have the administrative resources which are found in the larger municipalities. In this day of growing social complexities and increased state and federal mandates, these local officials are finding it more and more difficult to cope.

Increased federal paperwork resulting from new regulations has many direct and visible administrative impacts which, in and of themselves, are offensive enough. However, one of the more serious negative implications not usually considered is the effect such regulatory changes have on citizen-officials, who may be new to local public service. As observed recently by one veteran State Social Security Administrator:

Too often after agreeing to serve, those local officials find that . . . to a greatly increasing extent the red tape is more burdensome and time consuming than they had realized would be the case. They find that they can ill afford to take time away from their jobs, and many refuse to be a candidate for another term or they resign before their term ends.

This, Mr. Chairman, is just one of the very real problems which the National Association's members have with the changes which were implemented by the Social Security Administration.

Even though assurances have been given by some federal officials that reporting requirements will be lessened substantially in the future, township officials are somewhat doubtful that such will be the case. In many areas of the Country our members are being told by state administrators that requirements by the Federal Government for more frequent deposits will mean that they will be required to provide additional local documentation to the state.

LOCAL GOVERNMENTS WILL SUFFER FINANCIAL HARM

Red tape is not the only serious problem which will result from the new regulations. Local and state governments stand to lose substantial revenues from their treasuries once these changes go into effect. Townships and other government entities can ill-afford to lose this money, especially in a time of rising inflation, federal cutbacks and increasing service demands. Needless to say, this new system could not have been proposed at a worse time.

CONCLUSION

Because of these deleterious financial consequences and the red tape which would result, the National Association of Towns and Townships, as previously stated, is absolutely opposed to changes requiring more frequent deposits of social security contributions. NATaT supports the view outlined by Senator Nelson in a recent press release, in which he stated:

. . . the change (will) result in a loss of local government interest income . . . and would create a mammoth federal paperwork burden, resulting in increased administrative costs.

Although Senator Nelson's remarks related to a proposal requiring monthly deposits, our Association believes that they apply to the new regulations as well.

In the event that a return to the system of quarterly deposits does not occur as a result of administrative action by the Department of Health, Education and Welfare, NATaT sincerely hopes that a legislative remedy can be justified as a result of testimony provided during this hearing.

Again, we would like to thank the Chairman and members of the Subcommittee for providing me with the opportunity to present the views of our membership on this extremely important issue.

TESTIMONY OF JOHN BREITENBERG, ADMINISTRATIVE ASSISTANT TO HON. JAMES CLARK, PRESIDENT OF THE SENATE, MARYLAND STATE SENATE, ON BEHALF OF THE NATIONAL CONFERENCE OF STATE LEGISLATURES

Mr. Chairman and Members of the Subcommittee: My name is John Breitenberg, and I serve as Administrative Assistant to the Senate President of the Maryland Legislature, the Honorable James Clark. On behalf of the National Conference of State Legislatures and Senator James Clark, I am pleased to have the opportunity to appear before you as you consider modifications to the current agreements between State and local governments and the Social Security Administration.

I challenge a philosophy which seems to be widespread within the federal bureaucracy. Too many federal officials and the federal regulations they promulgate treat state and local governments as if they were profit making enterprises. First, I think we must all agree that the federal, state and local levels of government together form the government in this country and that we all serve the same master, our common constituent the taxpayer. Secondly, federal regulators need to recognize that the financing of new or increased mandates imposed on us by federal government must come from these same taxpayers. Imposing additional administrative burdens on state and local governments and the reduction or elimination of the interest revenues will place undue pressures on the very taxes which the voters appear to like least.

While HEW and GAO point to the potential gains to the federal government from changing the social security deposit requirements, what we are really talking about is a shifting of taxpayer dollars from one pocket to the other. We must also recognize that there is a fundamental difference between private and public employer participation in the Social Security System.

As you consider changes to the relationship between states and the Social Security system, please keep in mind the constitutional principles which form the basis for different social security arrangements for public and private entities.

As you know, social security coverage for state and local employees is provided as the result of voluntary agreements between the state and the U.S. Department of Health, Education and Welfare (HEW). Up to this point in time, social security contributions which have been collected for both state and local employees are to be deposited by state governments into a Federal Reserve Bank 45 days after the end of each calendar quarter.

For the past decade, HEW has considered changing this quarterly social security deposit system to a monthly method, in order to make contributions by state governments more consistent with the requirements for contributions by private employers. Each time this change was contemplated by HEW, the outcry from state and local governments and members of Congress forced HEW to reconsider its position, and the deposit system has remained on a quarterly basis.

The Quarterly deposit schedule was originally conceived for two reasons:

1. Unlike private contributors, state assume liability for inaccuracies in the records and payments for state and local employees. State administrators have taken great care to verify the accuracy of payments made for each social security participant employed by the state's political subdivisions. The 45 day reconciliation period allows more time for state social security administrators to verify the reports from all the cities, towns and local school districts participating in the social security program within their state. In addition, the state's assumption of liability for payments insures the federal government against any losses, and the 45 day period after each quarter insures that the verification process will be as accurate as possible.

2. States face difficulty in collecting and accounting for payments from independent substate jurisdictions, and the 45 day period allows for adjustments to be made. There are many local jurisdictions which do not employ full-time administrative staff to handle the collection of local employee social security contributions; therefore those funds are collected by the state. Since the state is responsible for guaranteeing the accuracy of the earning records of local employees and payments to the social security system based on those earnings, the 45 day period allows for more time to accomplish this collection and recording process.

We fully recognize the necessity of improving the condition of the Social Security Trust fund. The National Conference of State Legislatures has been a leader in the effort to reform public pension plans at the state and local level of government. In fact we have developed "a Legislators Guide to Public Pensions" and a technical assistance program which is being used by many states to reform their pension systems. The improvements which we need to make to our federal, state and local pension systems are fundamental changes such as front end funding of increases in pension benefits, full funding of current benefits, control and funding of cost of living adjustments and the eventual integration of pension benefits and Social Security.

Increasing the deposit schedule for state and local governments is not going to significantly alter the fiscal condition of the Social Security Trust fund. The added administrative costs and loss of interest earnings will, however, have a significant effect on some state and local tax systems. If implemented, the HEW proposal would raise state and local government expenditures in order to finance the added administrative burden while at the same time reduce revenues through the loss of the interest earnings.

It is hard for state elected officials to sit idly by while we're getting hit from all sides at once. Many jurisdictions are hard-pressed to balance their budgets. We must be concerned with the widespread adoption of limits on spending and taxing by our common constituents, the tax-paying citizen. The HEW regulations are not sensitive to the fiscal inter-relationships which exist among the federal, state, and local governments. We are elected to serve a common taxpayer, not a particular government entity. Therefore, the federal government should resist the temptation to impose mandates on states and localities in a manner which will exacerbate the fiscal pressures upon state and local budgets.

When HEW issued these final regulations, it documented in its summary that they had received about 3,300 comments, primarily from state officials, local political subdivisions, governmental organizations and about 200 Members of Congress. The responses were overwhelmingly opposed to any changes in the states' deposit procedures, for a number of reasons:

1. More frequent deposits would cause administrative problems and increase administrative costs.
2. The states would lose interest income.
3. States could no longer guarantee the accuracy of reports from political subdivisions under the shortened time frame, and should be relieved of liability for contributions.
4. The proposed change was a violation of the spirit, if not the letter, of the original agreements entered into between the states and the federal government.

In addition to discussing these primary objections to the HEW and GAO proposals, I will also discuss some other matters which should be considered in this debate.

ADMINISTRATIVE PROBLEMS

States are pessimistic about HEW's assertion that the changed procedures will cause only minor administrative burdens. When the states responded to a 1976 survey, they estimated there would be added administrative costs of $2.5 million if they had to deposit monthly instead of quarterly. Some states indicated that current administrative costs could double or triple because of increased workload, the need for additional personnel, extended training, and changes in bookkeeping systems. For example, administrative costs in Wisconsin for collecting social security contributions on a quarterly basis in fiscal year 1978 was approximately $288,600. It has been estimated that, after an initial outlay of $68,000 (including start-up costs totalling $28,000 and $40,000 for two new personnel positions), Wisconsin will spend approximately $40,000 more per year on state administrative costs alone. This figure does not include the added expenses which will be incurred at the local level for additional recording and documentation burdens. Missouri estimates that it will have to triple its personnel in order to comply with enforcement standards, and may have to automate their system. Under the quarterly deposit system, Missouri spends about $100,000 annually for administrative costs—this figure could skyrocket to as much as $350,000 to $400,000 annually under the monthly deposit system, according to s Missouri social security official.

Vermont anticipates that its administrative costs will double from the $22,500 outlays in fiscal year 1978 to almost $50,000 in fiscal year 1980, due to the need for additional personnel and start-up costs, and Kansas anticipates a 41-percent increase in its administrative costs, from $130,000 in fiscal year 1978 to $215,000 if the monthly deposit system is implemented. Social Security administrators estimate that administrative costs will increase 38 percent on the average of the states.

Although there are already 17 states which require some political subdivisions to deposit social security contributions more than once a quarter, the other 33 states will have to grapple with this problem for the first time. The lead time of 18 months given the states from the date of publication of the final regulations may not be enough for these substantial administrative changes to be accommodated.

In addition, states will be strapped with added administrative burdens associated with the more frequent collection of social security contributions from state and local employers. Many local jurisdictions have no full-time administrative staff to handle the increased frequency of collection now imposed upon them, which makes the timely collection by state officials even more crucial. It may be physically impossible for states to pay contributions 15 days after the month. In addition to the problems associated with accurate reporting requirements to verify wage information, there is the problem of timely collection of monies from local governments and other political subdivisions within the state.

The states are responsible for their local governments' share of the social security contribution collection, and must deposit these local funds even if the state has not received the local payment.

LOSS OF INTEREST EARNINGS

Increases in state and local employee coverage and state and local investment practices have resulted in increased interest income to states and localities. At the request of the Subcommittee on Social Security of the House Ways and Means Committee, the Social Security Administration and the National Conference of Social Security Administrators collected information in 1976 on the estimated effects, in terms of interest earnings lost, of monthly deposits of state and local social security contributions. The study, based on 1974 contributions, is somewhat dated and should be updated in order to understand the full implications of these regulations. However, even the 1974 figures, which should be considered low by today's standards, revealed that 35 states would lose, in the aggregate, over $30 million in interest earnings if they had to deposit social security contributions on a monthly basis. Fifteen states alone would lose more than $1 million each, including California, Florida, Georgia, Indiana, Kansas, Maryland, Mississippi, Missouri, New Jersey, New York, North Carolina, Oregon, Tennessee, Texas, and Wisconsin. The same survey indicated that 19 states would lose over $12 million in interest earnings of their political subdivisions—the range of these losses by states was from $14,000 to $3 million. In your own State of Wisconsin, Senator Nelson, the interest income for the third quarter of 1978 was $180,000 for state deposits alone; if the 15-15-45 deposit system is implemented, it is estimated that interest income would drop to only $99,000 for the quarter ending September 30, 1980, which is almost a 50-percent decrease. Missouri earned an estimated $1.3 million on their quarterly deposit in fiscal year 1978—monthly deposits would lower their averaged annual interest income estimate to between $581,000 and $871,000, depending on whether a 6-percent or 9-percent interest rate was used, under the 15-15-45 rule. South Dakota estimates an interest income loss of almost $250,000 by the third quarter of 1980, Vermont will lose approximately $51,300 per quarter under the 15-15-45 rule, and Kansas will lose $1.5 million annually in interest income.

States readily recognize that their loss of interest income will become the federal government's gain, and some observers point to the states' opposition to the change as a purely selfish reaction. However, interest earnings in the past have helped defray administrative costs of the social security collection program, and there is growing concern that the interest which states and localities might lose under the new schedule will not be enough to meet these administrative costs.

FINANCIAL LIABILITY

States are now liable for all inaccurate contributions and reports. They must underwrite the payments of their political subdivisions and guarantee accuracy of wage reports as part of the terms of the social security agreement between states and the federal government. By imposing more frequent and burdensome depository requirements, HEW is jeopardizing this liability clause by forcing states to be responsible for the same contributions and accuracy reports in one third of the time. It has been suggested that the federal government relieve the states of liability for local government contributions and have the political subdivisions report directly to the Internal Revenue Service. This idea is worthy of discussion—private employers are not subject to this liability, and if one of the reasons to change the deposit schedule is to bring public employer contributions more into line with private employers, then this is a suggestion worth exploring.

DIFFERENCES BETWEEN PUBLIC AND PRIVATE EMPLOYERS

One of the main reasons for the HEW deposit schedule change, besides the obvious increase in federal social security trust fund contributions due to the additional frequency of contribution collection, is that there has been discussion for years about "equalizing" public and private employers contribution schedules. There is a sentiment felt around the country that private employers were being penalized at the expense of the lenient deposit policies afforded public employers, and that this inequity should be corrected by making public employers meet the monthly deposit just as more private employers have to.

It is incongruous to compare state and local governments as employers with all other private employers, especially where social security deposits are involved. State governments are made up of hundreds, and in some cases thousands, of political subdivisions operating independently—private organizations have a well-defined chain of command which controls the activities of the private company. The lack of a well-defined coordinative mechanism in state government makes compliance with the new HEW regulations much more difficult for states than it does for a private company.

By assuming liability for all political subdivision social security payments, states insure the federal government against any losses and also reduce the federal paperwork burdens.

One of the most distinctive features between public and private employers is that the private employers have to belong to social security, while public employers have the option to join or establish their own retirement systems. Over 70 percent of state and local government employers have contracted with the federal government to join the social security system, and one of the advantages seen by these public employers was the quarterly deposit system. The change to a monthly deposit system may discourage participation of the nearly 30% of the public employers who do not yet belong to the social security system, and it may well encourage some of the current participants to "opt out" of the social security program.

REFUNDABLE CREDIT FOR PUBLIC EMPLOYERS

During the 1977 consideration of the Social Security Act both you and Senator Danforth developed proposals which would have partially equalized the after-tax Social Security burdens imposed on states, local governments and nonprofit entities. These proposals were based on another major difference between these two classes of employers and they sought to place public employers on a more equitable footing in regard to their Social Security tax liability. If it is desirable to adopt a federal policy which will narrow the differences between private and public employers with regard to the deposit issue, then Congress should also provide for equity in terms of the after tax liability for these two distinct employer groups.

We are proposing a refundable tax credit which may be claimed by organizations which are exempt from federal income taxes. This refundable credit should be considered in light of the credit which the tax system currently provides to private employers. Social Security taxes are considered a business expense for private sector employers and as such are deducted from a business's federal and state income tax returns. A business that pays $100,000 in FICA taxes can deduct at least 48 percent of this amount on federal returns plus additional sums for state tax liabilities. The same $100,000 contributed by a public employer cannot be offset under the tax system. Therefore the public employer has a greater financial burden than his private counterpart.

This inequitable treatment of public employers should be addressed by the Congress. Hard-pressed state and local governments require assistance in meeting the fiscal demands of increased Social Security costs. Profit-making corporations bear only a portion of the increased Social Security costs since they can partially offset the recent payroll tax increases on their federal and state income tax returns. In order to provide parity of treatment between public and private employers contributions, NCSL urges Congress to consider enacting a refundable credit which would be financed with general revenues so there would not be a loss to the Social Security trust fund.

NCSL would like to go on record again as opposing the HEW regulations requiring states to make monthly deposits of social security contributions. Administrative problems will abound from the increased frequency of deposits including increased workload and paperwork, additional personnel, and revamping of record keeping systems. The interest loss on state investment of social security monies will adversely affect hard-pressed state budgets. Social Security administrators will be hard-pressed to verify wage reports and guarantee accuracy in the face of these reporting schedules.

If, after all is said and done, the HEW regulations take effect despite state, local, and Congressional opposition, NCSL would like to suggest the following:

If the federal government desires to treat state and local government employers the same as private employers in relation to social security contributions, then the

federal government should extend the same tax privileges to public employers as it does private employers. Then Congress should also let state and local governments deduct social security contributions from their tax liabilities.

NCSL appreciates the opportunity to present its views on the HEW regulations to change the social security contribution procedures from a quarterly to a monthly basis. We would actively support legislation designed to postpone implementation of these regulations until such time that it can be shown that the financial and administrative burdens incurred by state and local governments would not place undue burdens on these governments or the taxpayers.

Senator NELSON. Our next panel is a panel of State social security administrators representing the National Conference of State Social Security Administrators.

If you would all take your seats and identify yourselves so that the reporter will have an accurate record.

Mr. GALLISON. Edwin Gallison, Deputy State Treasurer from Vermont, and I am the president of NCSSA.

Mr. SLAYBAUGH. I am Gerald Slaybaugh, the State administrator for the State of Kansas and chairman of the Federal-State Procedures Committee of the Social Security Administration.

Mr. COLLINS. I am Purvis Collins, South Carolina.

Mr. BLECHINGER. I am Carl Blechinger from California. I appreciate your comments on California. I am the State administrator.

Mr. HENNE. Mr. Chairman, I am Fred Henne, executive director, Arkansas Public Employees Retirement System, and as such, the State social security administrator.

Ms. MOORE. Senator, I am Alta Moore, State social security administrator for Wisconsin.

Mr. COOK. Mr. Senator, I am Kenneth Cook, chief accountant of the Division of Pensions, appearing for Mr. Josephs who was not able to get here at the last moment, State of New Jersey.

Mr. KENNEDY. I am Robert R. Kennedy from Florida, director of the State's Retirement System and, as such, administers the social security program for public employees.

Senator NELSON. Go ahead.

STATEMENT OF EDWIN GALLISON, DEPUTY STATE TREASURER OF THE STATE OF VERMONT, ACCOMPANIED BY GERALD SLAYBAUGH, STATE ADMINISTRATOR FOR THE STATE OF KANSAS AND CHAIRMAN, FEDERAL-STATE PROCEDURES COMMITTEE OF THE SOCIAL SECURITY ADMINISTRATION, PURVIS COLLINS, SOUTH CAROLINA, CARL BLECHINGER, STATE ADMINISTRATOR, CALIFORNIA, FRED HENNE, EXECUTIVE DIRECTOR, ARKANSAS PUBLIC EMPLOYEES RETIREMENT SYSTEM, ALTA MOORE, STATE SOCIAL SECURITY ADMINISTRATOR, WISCONSIN, KENNETH COOK, CHIEF ACCOUNTANT, DIVISION OF PENSIONS, STATE OF NEW JERSEY, ROBERT R. KENNEDY, DIRECTOR, STATE RETIREMENT SYSTEM, STATE OF FLORIDA

Mr. GALLISON. Senator, we want to thank you very much for the opportunity to appear today. We hope we can answer some of the questions you had asked earlier in the morning.

We feel that the administrative burden and the problems that would be created by the regulations are our largest opposition to the regulations that are published, in spite of some releases that have indicated that the loss is the objection, we feel that we can demonstrate to you here this morning how the regulations are not administratively workable from the State and local level.

Mr. Slaybaugh can proceed to show you with a chart demonstration how long it would take the deposits to flow from the local entities from the time after the payroll is written, to the States, and then to the social security trust fund.

We believe there are major differences between the private sector coverage and public sector coverage, the fact that you have divided retirement system groups. We do not have the universal coverage in the public sector that you do in the private sector, and we think that universal coverage is key here, because of the attractiveness of the size of the contribution we are talking about here.

Now we have attained a level of 73.8 percent, this money becomes much more attractive for everybody.

Senator NELSON. Of all public employees that are covered?

Mr. GALLISON. Yes. State and local covered employees.

Senator NELSON. What is the peak percentage that you have ever had?

Mr. GALLISON. That is the peak.

Senator NELSON. That is the peak percentage?

Mr. GALLISON. Right.

Senator NELSON. May I ask one more question for the record? How does that compare with 1970, say?

Mr. GALLISON. I would say 1970 is 5 percent less. We have a gradual growth.

Senator NELSON. 1970 was 5 percent less?

Mr. GALLISON. Gradually covering more and more public employees all the time.

Senator NELSON. A higher percentage?

Mr. GALLISON. Yes.

Senator NELSON. You say in 1970, in your estimate, it was 5 percent lower for public employees covered?

Mr. GALLISON. Yes, sir.

Senator DANFORTH. That is very surprising to me. I thought that there was an opting out.

Mr. GALLISON. You have had a lot of notifications, serving notice to opt out; several have opted out. But the Social Security Administration informs us nationally that there has been a net gain in covered employees over that period of time.

There have been more coverage units added than have withdrawn. That is not to say—and perhaps Mr. Blechinger can best speak to what might happen as far as terminations that are proposed are actually implemented.

Carl, do you want to speak to that?

Mr. BLECHINGER. If I might, as an example, what happens on the increased coverage, Senator, the University of California just brought its retirement system under social security last year. Out of 56,000 employees there were only 8,000 who selected social security coverage, so you have a built-in increment there of the difference between 8,000 and 56,000.

This is why you would have an automatic increase in coverage. California is one of the States that leads the Nation in the number of actual termnations and the number of agencies that are giving notice of termination. We feel that this additional burden on the local agencies where there is a strong feeling that the raise in social security taxes and the raise in social security covered wage amounts, as you have in the private sector, the additional amount, the additional burden of this would cause additional terminations.

Senator DANFORTH. You think this would be the straw that breaks the camel's back?

Mr. BLECHINGER. We do not know if this will be or universal coverage would cause it. If there is a definitive action, we feel strongly that a number of large agencies would immediately get their 2-year notice in.

Senator DANFORTH. Let me ask you, of the burden of this particular straw, how much of that would you attribute to administrative burden, and how much to loss of the float?

Mr. BLECHINGER. I think the difference would be on those agencies that make a great deal of money out of the float and those agencies that do not make a large amount of money then the additional paper burden would be the cause, Senator.

There is no way that I know of to give numbers to it in terms of agencies, or number of people.

Senator DANFORTH. Which part of that trouble is the worst, the loss of money or the administrative burden?

Mr. BLECHINGER. The administrative burden, because they do not get any of the moneys.

Senator DANFORTH. How about the rest of you?

Mr. GALLISON. We all agree. I can speak definitely for the conference. We feel we are being saddled with a regulation that is impossible for us to comply with. Perhaps now it would be, Jerry, for you——

Senator DANFORTH. Do all of you agree?

There are eight of you. How many of you think that the administrative burden is the greatest problem?

[A show of hands.]

Ms. MOORE. We already know that. I want to speak for Senator Nelson's home State. I figured yesterday, just yesterday, that almost 60 percent of the entities in Wisconsin under our present IRS rules would be reporting quarterly or monthly anyway. They would not be reporting weekly, so I hope something is done about those small entities.

Senator DANFORTH. I raised the question earlier about small entities. Let me ask you this. It seems to me that as I understand it, what the Social Security Administration wants to do is to collect more money, not more paper.

Now, what is wrong with them collecting more money from you and not more paper, if that is the objective? Why not simply figure out—let me give you an example. It would be in rough terms. It would not be with finicky precision, but what would be wrong with, for example, guessing the difference, estimating the difference, between revenues to the social security system with or without monthly deposits and then estimating how much the Social Security—we know that—gets with quarterly deposits and then simply charging you the differ-

ence so that you still make your deposits quarterly, but instead of depositing x dollars as you are doing now, you deposit x dollars plus 6 percent or whatever, whatever is fair?

Would that not solve the paperwork problem and collect the same amount of money?

I do not understand why the big fuss about monthly versus quarterly depositing except that it is my understanding that, by depositing quarterly rather than monthly, State and local governments get the use of the money for that length of time and the use of money for an additional couple of months is worth money and you make money. Therefore, the trust fund does not get money and make money.

If everybody feels that is unfair, you might say we want the money., but supposing the Congress does not agree? Supposing that the Feds do not agree, and that we say we want the trust fund to have the money?

Senator Nelson has made that point. If we reach the conclusion that we want the trust fund to have the money and your biggest problem is not the loss of cash but the reporting requirements, is there something that I just do not see here where we could keep the quarterly deposit system and yet collect more from you, which would be very simply computed. You just put a percentage on it.

Am I wrong?

Mr. GALLISON. I think that there are some things that perhaps we are missing. I think that we would tend to agree with Commissioner Ross, that this would generate paperwork.

Senator DANFORTH. How?

Mr. GALLISON. Because we would have to document.

Senator DANFORTH. Why?

Mr. GALLISON. We would have to document why we were remitting x number of dollars of interest income from the State of Vermont versus the State of Arkansas, for instance, because our investment regulations vary substantially.

Senator DANFORTH. No; we do not care what your investment regulations are. You can have regulations in so far as we are concerned that do not permit you to invest a dime. We are simply charging you what you would remit anyway plus a percentage that we would determine here in Washington.

Mr. GALLISON. In the case of Arkansas, which has very strict investment regulations, they would not be able to earn——

Senator DANFORTH. That is a problem for your State legislature. We cannot solve everything in Washington.

Mr. BLECHINGER. Are you assessing the State the charges or each local subdivision the charges?

Senator DANFORTH. The State.

Mr. BLECHINGER. That is the key for the whole thing.

Senator DANFORTH. The State.

Mr. BLECHINGER. This is where it transfers to so much at the local level.

Senator DANFORTH. Why?

Mr. BLECHINGER. The broad diversity and, as was pointed out the very small number of employees at the local level. The big agencies do not give us these problems.

Senator DANFORTH. Let me ask you this. Let us suppose right now that you have got—who is from Arkansas—now, the great city of Beulah. All right. It is located on the border between Arkansas and Missouri.

Let us suppose that Beulah, Arkansas, has one employee and that employee is covered by social security. Is there not a collection for that employee today?

Mr. HENNE. Yes.

Senator DANFORTH. It is quarterly, is it not?

Mr. HENNE. Yes.

Senator DANFORTH. What happens to that money?

Mr. HENNE. The money is sent to our office at Little Rock, sir.

Senator DANFORTH. The money is sent to Little Rock.

Mr. HENNE. Plus the report.

Senator DANFORTH. Do you know how much that money is?

Mr. HENNE. When we get the report.

Senator DANFORTH. It is x number of dollars for that employee's social security payment, right?

Mr. HENNE. Correct.

Senator DANFORTH. There is a dollar figure. It is ascertainable, right?

Mr. HENNE. Yes.

Senator DANFORTH. Supposing they compute that dollar figure and just add, say, 6 percent or something. Is that hard?

Mr. GALLISON. They do not have the use of all that money for the full period of time, and it would depend on the payroll period.

Senator DANFORTH. We can figure out a time, can we not? What are we talking about here? We are talking about money, and that money is the aggregate of what is collected from all over the country and sent in either quarterly or monthly. Why can we not just charge you a percentage?

Mr. GALLISON. I think you have two factors. One is the contractual relationship that exists between the Department of HEW and the States which points out the basis on which coverage is obtained and administered for public employees in that State and the agreements that have been entered into between the States and the local entities which, at this point, have said nothing about any interest assessments.

Senator DANFORTH. Who is getting the advantage of the float?

Mr. GALLISON. The advantage of the float could be some at the local level, the State level. It depends on the time that the deposit is remanded to the State and from that point on, the time at which the deposit is remitted to the Social Security Trust Fund.

I think, really, the question boils back down again to universal coverage and the fact that we are having a study about universal coverage and the feasibility of whether we should have it or not, and, if we should how it should come about.

I think that this is also generated by the same thing, the amount of money we are involved with, and there are windfall benefits payable from the trust funds to public employees who do not remand or contribute on all of their compensation.

I think that if the time comes—and it may very well, very soon—when universal coverage is considered to be a fact of life, at that point would the States administer coverage for the public employees? We think probably they would not. There would be no reason for us to be

involved, because there would not be the variances between the private sector and public sector. If you are talking about universal coverage, public employees, two or three or four——

Senator DANFORTH. Who is talking about that?

Mr. GALLISON. I think Congress is. There is a study mandated——

Senator DANFORTH. I want to tell you something. First of all, I think it is a constitutional problem. I think it would be challenged if Congress ever did it. It would be challenged in the courts.

The most unpopular thing I have done in my short span in the Congress was not the Panama Canal Treaty vote; that was second. The most unpopular thing was to suggest in this room 1 day that we have universal coverage.

Within an hour, my office was teeming with lobbyists for public employees. I could hardly fit in the place. My mail on that issue was more lopsided than on any other issue—843 to 1 against universal coverage. Universal coverage, I think, is going nowhere. I do not think we should even think about that.

What is wrong with my idea?

Mr. GALLISON. I think your idea is workable. It is not one that we have spent a lot of time studying.

Senator DANFORTH. Would you rather have my idea or would you rather have Commissioner Ross's idea? If you had your druthers, would you rather have what the Commissioner was suggesting, or would you rather have quarterly reporting plus an interest charge?

Mr. GALLISON. I would want to see more specifics about your recommendation, how the interest that we would turn over to the trust fund would be calculated and how it would affect all the States.

Senator DANFORTH. You would calculate on a fixed percentage of what you would otherwise send in.

Mr. GALLISON. We would want to see what percentage it is and over what period of time it is going to be calculated and what principle we are going to base that calculation on.

Senator DANFORTH. Supposing the percentage is no greater than the additional amount you would be remitting, given monthly deposits?

Mr. GALLISON. I think you have made your points very well, and Senator Nelson, of the entitlement of the social security trust fund to that interest. That is not our problem with the regulation, really, not our problem, as long as the States could not show we were losing money, there might not be any strong arguments. We would want to make sure of that, however, and study it very carefully.

Mr. HENNE. Senator, may I go back to Beulah and maybe answer your question. Let us suppose we are in Beulah and we have this one employee in the public sector and right across the street from him we have another employee, but he is in private industry.

Let us compare or contrast what happens in those particular situations. First, let's take the private situation.

What happens to his FICA tax? What happens to his Federal withholding tax? Obviously, he sends it to IRS, both of them, on whatever schedule that IRS has, and that is sent from IRS to social security on the prescribed forms of IRS.

Let us take the other section over here in the public sector, in the withholding. He sends it to IRS but in social security, he sends it to us, again at Little Rock, to the Social Security Administration. Entirely new set of forms, different than what IRS had sent over here in the private sector.

We have an additional layer of government which, in this case, are the States. The question that I would like to ask, why would it not be more reasonable to turn the whole process over to IRS because they have the necessary forms. They already are doing it. Why should we be involved in the process in the first place?

We were concerned earlier today about more paperwork. In addition to more paperwork, I am also concerned about additional layers of government involved in the same process. IRS is already doing it, so why should they not continue on with it?

The States are having to guarantee the liabilities. What I am saying is, possibly consider legislation to give the entire process to IRS and remove the liabilities of the State? To me, we would solve a very major problem which was the one on paperwork and the one I was indicating a minute ago about this additional layer of government.

Senator DANFORTH. Does everybody agree with that?

Mr. KENNEDY. I would like to respond, from Florida.

The problem we have in Florida is all of our social security coverage, I would say 80 percent of it, is tied to membership in a retirement system. Unless they are enrolled in the proper retirement plan, most of Florida's public employees do not have social security coverage.

To do what he is suggesting, I think you have to repeal section 218 of the Social Security Act and go ahead with mandatory public employment coverage, which you are shaky about.

Mr. GALLISON. We would like to demonstrate to you why regulation is administratively unworkable. Mr. Slaybaugh will now show you a timeline of what would have to happen with the regulations as they are now. We will miss the point if we do not speak to the regulations. Maybe there are alternatives we have not discussed yet, or which have not been proposed to us.

Go down through the list of problems that we can demonstrate to you.

Mr. SLAYBAUGH. These problems, Senators, that we have listed here are six in number. The black represents dealing with local units; the red, the State units.

Over on the right-hand side, you can see numbers in brackets. These are the estimated number of days it takes to accomplish this task, beginning with the consolidation of subunit payments by local units. The prime example in the State of Wisconsin under 66.042 where the local county unit must receive the moneys from the subunits and transmit it to the administrator in Wisconsin. This is estimated to take 3 days.

Next, drawing in all varieties of local warrants, either with the smallest entities which would be the township and then Kansas, during harvest time, to get three farmers together at night after they have been in the field all day to sign a Federal piece of paper, or even a check for Federal moneys. We say that is going to take at least 4 days. Also, the larger entities would have to go to the EDP process of submitting vouchers, submitting authorization. To draw that, it is going to take 4 days.

The mail constraints. Some of our States, as you know, Alaska, Montana, my own State of Kansas, it takes many days to get a piece of mail from western Kansas into Topeka to me. We did a survey 2 years ago. I asked six county clerks on the western edge of Kansas to

send me a letter that very moment and all they put on there was the date and the time that they put that piece of document in the mail and sent it to me. It was from 3 to 5 days getting to me. The shortest was 3 days.

We said, nationwide that was going to take 5 days. Now, we have the money in the State office. The accountability of local receipts, the administrators have to account for 65,000 receipts, that many entities covered. This takes 5 working days.

The deposits, the receipts in the State treasury, we say, will be accompanied by the accountability of the receipts and drawing of State warrants. The absolute minimum amount is 5 days.

Add all these bracket figures together, you have 22 working days which is the full calendar month. This is why we believe that the administrative rule is impossible to meet under our current contracts.

Senator NELSON. Is that chart submitted for the record, in writing?

Mr. SLAYBAUGH. It will be, Senator.

There are special circumstances we have not even tested, such as computer downtime; if a holiday would fall in any one of these; the various staff leave; and finally miscellaneous, snow, what have you.

These would all add to the time frame up here. There is no way that we could follow the 15-days after the end-of-the-month rule when it will take us 22 days to do the work.

We have been talking this morning, we have heard testimony on depositing under IRS rules. Taking a look at the 65,000 political subdivisions, 10 percent of them transmit to us now less than $200 in any one quarter; 25 percent, less than $2,000. There is 35 percent right there that fall under the minimum guidelines of IRS.

Senator NELSON. That first 10 percent is not included?

Mr. STAYBAUGH. That is right. It is not included in this; 35 percent under $2,000. These people here with less than $200 can submit to IRS on a quarterly basis. Those with over $200, but less than $2,000, can submit within 30 days after the end of the month; more than $2,000, 65 percent, they have to submit 3 days after the quarter monthly period, and it is not 3 days after the payday. There are 3 quarter monthly periods in a month and 3 days after the end of those periods.

In Wisconsin, we have a good example here. Four percent submit less than $200; 49 percent submit less than $2,000.

Ms. MOORE. Those little towns are going out, they are going to the legislature to get permissive language to get them out, those little towns.

Mr. SLAYBAUGH. Kansas, $0 to $200, 22 percent. This is the way it is in every State.

We also heard Commissioner Ross talk about administrative expense. I was not able to determine when he said $2.5 million whether the figure was supposed to be under the present system or what it would cost under the new system.

We took a statistical sample, an accurate one, we believe, and based upon 10 States that make up 25 percent of the coverage in the country, our present costs right now run $13 million to administer this program. We estimate that $5 million will be needed on an ongoing basis, a 38-percent increase, and it ranges from a low of $25,000 in one State to a high of $275,000 in another State, which would include your addi-

tional stafftime, space, equipment, and electronic data processing changes; startup costs, purchase of equipment, capital improvements, we estimate to be $1 million, and these are conservative figures.

Senator NELSON. $13 million for what period? Annually?

Mr. SLAYBAUGH. He was testifying that $5 million would cover the administrative costs of 5,000 to 60,000 units reporting annually.

We cannot reconcile that figure at all, sir.

Another thing we must recognize is the delinquency. Senator Danforth was talking about charging us interest. We are charged interest presently on any delinquent report. If we go under a more frequent deposit, 15 days after the end of the month, our delinquency rate will be significantly higher. We are running 16.5 percent delinquency on a quarterly system.

We do guarantee and we do send to the trust fund 100 percent of all moneys due. That is something that no one in the private sector can say about the private enterprise system.

We estimate that if we go under a 15-day deposit, our interest assessments based on delinquency will be $4.5 million a year. We will be charging our local units of government $4.5 million for not being able to complete the paperwork on time that is caused by this regulation, and we will submit these charts, Senator, with the written testimony.

Mr. GALLISON. I think the 100-percent guarantee to the State really has to be emphasized and that has to be worth something to the Social Security Trust Fund.

As Mr. Slaybaugh pointed out, there is another level of government, the States, standing behind every local entity. If a private employer or corporation goes bankrupt, certainly the taxes and social security taxes are the first thing to be collected in any bankruptcy process, but there are many, many dollars every year, I am sure you will recognize, that are not collected; there are no assets.

Here, if any local entity is unable to meet their obligation, the State has a contractual obligation with the Department of Health, Education, and Welfare to make that payment on behalf of the entity.

We were talking yesterday about what it is worth, and maybe this relates to Senator Danforth's question. If you want to relate it to a credit card application, if you go into a store and purchase goods with a credit card, you are really getting a 4-percent discount of paying that as a cost of money.

We are really guaranteeing that as a third party, very similar to a credit card operation. There has to be a value there.

We think that GAO did not do a very thorough job in not studying the feasibility of the 15–15–45 regulation. I think that they admit that in their report.

They state flatly that they did not really study the reasonableness of the 15-day deadline, yet they come in here this morning and testify that they really would support a more frequent deposit schedule than that.

We feel, unless a study is thoroughly made—we would like to be cooperative and participate in that study—we feel that a deferral should be imposed upon the implementation of these regulations and other alternatives perhaps looked at.

I think that we are here again to express our appreciation for your hearing this morning and to request that you do recognize our points, that the administration of these regulations is unworkable and that you should study them very, very carefully and perhaps, until a decision one way or the other on universal coverage is made, we be allowed to continue on under the present schedule and then seriously consider turning it over to IRS if universal coverage becomes a factor, perhaps another alternative if it does not.

Senator DANFORTH. Again, there are very few things that are certain in this life. One of them is that universal coverage will not come of age, in my opinion.

Senator Dole asked an earlier witness if you had knowledge as to the ratio now between income earned on the interest and administrative costs of administering the social security system, do any of you have any information on that?

Mr. SLAYBAUGH. Senator Danforth, that is one of the big problems we have. We can very accurately estimate the amount of expenditures that we have and what they will be. We have done that to the tune of $19 million versus $13 million.

There seems to be a large disparity between the figures that GAO has come up with on interest earnings, what SSA has come up with, and what our actual statistical sampling shows.

They are talking in terms of $179 million in 1980 and $216 million. Our sampling shows approximately $80 million, and I think we are very, very close.

Senator NELSON. Do you mean the interest that is earned, that goes to the municipalities and the States?

Mr. GALLISON. We feel this is what we would have as lost interest revenue if the schedule were implemented. They were putting figures forth of $179 million from SSA in 1981.

Senator NELSON. A loss?

Mr. GALLISON. A gain through the trust fund. They do not reconcile that there are going to be two or three times as much of a gain to the trust fund as we can document as a loss to us.

Senator NELSON. As I understood the Administrator this morning, he was saying that the loss currently is $200 million. Then he went on to say that it would be $1 billion in 5 years, either he or the GAO, I have forgotten which. I thought they were talking about the loss, then, being $125 million, or the muncipalities and the States getting $75 million. Was that not the testimony?

Mr. GALLISON. They were projecting, I believe, that the States could earn $50 million to $75 million on what is left with the 15–15–45 schedule.

If you look in the supplemental information submitted with the regulation from SSA, they are estimating $179 million of additional revenue to the trust funds in 1981, with the 15–15–45 schedule.

The GAO report estimates $216-plus million in 1981. Our sampling shows a loss to us in 1981 projected of about $80 million. So there seems to be some disparity between what we would lose and what the trust funds would apparently gain.

Senator NELSON. We will ask the Social Security Administrator to comment on that.

Mr. GALLISON. I believe Mr. Henne would like to make another comment.

Mr. HENNE. Mr. Chairman, I would like to address myself to two other comments.

Senator NELSON. Let me say that I have to leave in a few minutes. Maybe Senator Danforth will stay a few more minutes. I am sorry, I have another commitment to meet. I am running late now. Why do you not go ahead? At quarter after, I will leave.

Mr. HENNE. The first comment concerns itself with the remark that the Commissioner made this morning with respect to the consultation of the States. Recognizing the fact that Mr. Ross has been Social Security Commissioner only for a short period of time, I would like to indicate and refresh the committee's memory with respect to the two regulations. One is the proposed rule and regulation that came out on March 30 and the other, which was the final regulation that came out on November 20 of last year.

If you will remember the proposed rule and regulation gave five or six different alternatives in so far as graduated implementation was concerned, but the bottom line was 15–15 which meant that the States would be required to transmit 15 days after the close of each calendar month.

The November 20 final regulation came out with 15–15–45 an entire deviation from any proposal that had been made in the Notice of Proposed Rulemaking on March 30.

I would like to say here that we were not consulted with respect to the final regulations. I attended a lot of these consultation meetings in Baltimore. I was not aware that the Administration was going to come out with that situation.

Senator NELSON. Were none of the Social Security Administrators consulted on the final regulation?

Mr. GALLISON. Not specifically on the 15–15–45.

Mr. SLAYBAUGH. Only to the point that we were notified the week that the regulation came out. I was called personally and told they had made up their mind 15–15–45. I said, that does not fit into anything you told us before. They said, that is our decision.

In that respect, they received—and the Commissioner admitted—over 3,000 letters on this one regulation yet they still do not understand our administrative problem. It was spoken of by three local governmental units. They must not have read the letters.

Mr. HENNE. I am also aware, and mindful of the fact, that Members of the Senate last year signed a letter and cosigned a letter addressed to the Secretary of HEW and also the Social Security Commissioner in which the indication was, or as least the letter indicated, as best I remember, let us have some more time so that this can be studied. The same thing was done with respect to the House Members; about 200, I think, signed those letters. I am not sure there was any consultation given to that.

With respect to that, one final situation with respect to consultation. Even though we have received this final regulation, there has been nothing that has accompanied the regulations indicating any guidelines of implementation specifics so, in some areas, we are really at a loss to comment on any of it because of the fact that we do not have the specifics.

The final item I would like to indicate—and a lot has been said this morning—we want to earn more for the social security trust funds. I agree with that principle. These moneys are the Federal trust fund's and everything should be done to earn more money for these trust funds including interest income thereon.

In mid-1978, or the summer of last year, I became aware of the fact that when I deposit my social security trust funds in the Federal Reserve Bank at Little Rock, it takes 11 days for that money to be credited to the social security trust fund. I do not understand why it takes that long.

If you presume that your going rate today is 9 to 10 percent on your money, that you can draw that much money, we are losing something like $3,000 or $3,300 on every million dollars' worth of contributions that are deposited by all the 50 States and the 100 interstate instrumentalities.

Gentlemen, I submit to you that that is the loss of a lot of money.

Senator NELSON. Who gets the 11 days' benefit of the money?

Mr. HENNE. It is in the Federal Reserve System.

Senator NELSON. It is not going to social security?

Mr. HENNE. No.

Senator NELSON. You say it takes 11 days from the time that the State of Arkansas deposits it before it is credited to the Social Security Administration?

Mr. HENNE. That is right, sir.

Mr. GALLISON. We were informed by the Social Security Administration that this is the case across the country. We are not leading you to believe this is in Arkansas only.

Senator NELSON. That means that it is worse than if it were only Arkansas.

Mr. COOK. I can back up that last statement very well, Senator. For the third quarter of 1978, the State of New Jersey mailed and had time-stamped at the post office their contributions on the 14th of the month of the due date. They were not credited until 6 days later having had to go 16 miles by postage from Trenton to Philadelphia. Therefore, I think it is universal.

But there is a dramatic lapse of time in the Federal Reserve Banks, the Federal's own banks, getting the money to the Trust Fund.

I would like to go back, just for 30 seconds, and say that it is inconceivable for anyone to think that there cannot be more paperwork when we will now do 12 times when we have recently done 4. Although reports will not be as extensive on a monthly basis, they will be there.

The State of New Jersey, for the last quarter, received 2,235 reports from local entities. This timespan, the 15 days, is impossible. There is no way that we can collect and properly control. This is what I think we are missing.

Nobody has talked yet to the proper control of these moneys. It is not a matter of getting a check in, depositing it and sending it into the Federal Government; it is much more than that.

With regard to 2,235 reports, I do not know of any industry that is that large that can do that. I do not think industry can do it. I know that the State of New Jersey cannot do it and I question whether the Social Security Administration could do it.

But even more important, in that we are now forced in our State, and I know there are others, to spend State appropriations of considerable funds without any real backup validation approval.

In our State, we happen to underwrite and subsidize those social security costs for all teachers. On a quarterly level, we are able to verify that every person reported as a teacher is properly reported and when a warrant or voucher goes over to be signed, we are in effect saying to the taxpayer and to the legislatures that here we are properly spending your money.

You might say, can you not do the same thing on a monthly basis? The answer is yes, except the first 2 months of every quarter is going to be guesswork, not validation, except what we perceive from the local employers. But looking ahead where there is an aggressive movement, evidently, for annual reports, they are going to ask us now to spend hundreds of millions of dollars in one State for 11 months on an estimate basis, hoping that at the end of the 12 months, everything we receive from 2,000 or more local employers is going to add up.

Personally, I do not think it is going to add up, because it does not add up now on a quarterly basis, and we do have problems. We have turned over—we have payroll clerks who are so far removed from some of these problems that they do not much care and they will send us what they think is right, especially the small entities which you are talking about now.

We have sent field representatives out when we were getting close to the deadline and had social security forms signed on the back fence by some guy as a part-time job, and that is it.

I do not think that the time limit that is being proposed or suggested by GAO or by the administration is very realistic. I do not think that the General Accounting Offices, they have been to visit New Jersey. I think they read what we said. I will be a little stronger than Jerry: I do not think they cared what we said.

They had an ax to grind, which is their money, and I do not blame them. Being an accountant, I would take the same stand. But I think there has to be a certain degree of reasonableness with times allotted to do a job which we cannot physically do any sooner.

There has to be a recognition that the delinquency problem will definitely increase. On one hand, interest rates are good. On the other hand, with so much of our Federal programs being cut back, many jobs are being cut back at the local level.

So we are sitting here. We want you to do more work. We want you to get this stuff in sooner, but, in effect, we are requiring you to do it with less hands. This does not always add up either.

Basically, that is all I want to say. I just think that we have not talked to the responsibility of accountability. I think it is there, and it has to be considered. Thank you.

Mr. GALLISON. I think the regulations and the law require the administration of the public sector coverage to be in so far as practicable the same as the public sector.

We are saying, "What is practicable?" and we feel that there has not been sufficient indepth study of the impact at the State and local levels of the administrative problems and so forth, and the paperwork burden which will be increased at the local level if they have to deposit

with us with some kind of documentation 12 times a year in place of 4 times a year, as it is now.

We feel a further study is needed before you can say that; it is not practicable, as the law says.

Senator NELSON. Thank you.

Yes?

Mr. KENNEDY. I just wanted to respond to Senator Danforth's question. He was asking about the ratio of the cost and the interest earnings. It would take about two minutes, if you would care for me to respond to this.

Under the new regulation, Florida, which does have monthly reports—and we could implement your suggestion about interest. A lot of these States that do not have monthly reports could never, I think, work it out very reasonably.

However, Florida has a law that all the interest earnings go, not to general operations, but the retirement system trust fund because all of our members, 80 percent of our members, have social security and retirement coverage jointly.

The interest earnings now go to that fund. We, under the new regulations, would still be able to earn interest, but all States do not provide the same services for the social security participants.

We do a lot of work. We have computerized everything. We send in one tape quarterly to Baltimore. They do not have to do any of the keypunch, or any of the computerizing of the data. The fact that we stick out like a sore thumb as far as the cost of administering the program, but we are doing a lot of the work that the Social Security Administration would have to do if we had not computerized.

Under the new regulations we would still be short under our estimates of enough money to pay the cost of what we are actually performing, the services for the social security participants.

Senator DANFORTH. Just one question. My inclination is to forget about the idea about the inputed interest, for lack of anything but questions raised not only by the Commissioner, but by everybody on this panel.

A second idea would be to treat smaller units of Government differently from larger ones. How would you feel about that?

Mr. GALLISON. I think if you are going to require more frequent deposits of some sort, I think that it has to be recognized that smaller units should not be forced to deposit on a bais more frequently than they were administered under the IRS.

Here, though, you are creating another problem of stratifying our group again by some other arbitrary measure and making us administer that.

Senator DANFORTH. Your view is that that would be a mistake also?

Mr. GALLISON. It could be.

Senator DANFORTH. Basically, your testimony, as I understand it, is blanket opposition to the regulation?

Mr. GALLISON. We feel there are valid reasons for putting the administration of the public sector coverage under States. There were valid reasons for setting up the quarterly deposit schedule in 1951. fact, the only modification to the schedule was made in 1958 to 1959 to extend the period of time that we needed to file the quarterly report.

Senator DANFORTH. You would say to me that if you were thinking about a separate rule of quarterly deposits for units of government with social security tax liability of, say, under $2,000 a period, you would say forget about that. That would be more trouble than it is worth?

Mr. GALLISON. I think it would, sir.

Senator DANFORTH. In other words, your basic view is opposition to the regulation, all or nothing?

Mr. GALLISON. That is our position.

Senator DANFORTH. You would just as soon sink or swim?

Mr. GALLISON. Yes.

Senator DANFORTH. I think you are going to sink.

Mr. COOK. Excuse me. I would say, in answer to that question, not worrying about the size of the report, but to give us the time to do them and do them properly, regardless of their size.

Ms. MOORE. I think in our State, as Senator Nelson knows, we do have this provision in the statute whereby the larger entities must be a collection agency also, which was mentioned once before today. And, in addition, we do not have any authority that I have ever seen to treat Milwaukee County any differently from the town of Podunk. Maybe something could be done by the legislature to help us with it.

So far, I have treated Milwaukee County in the same way as I treat the town of Podunk. That is all the authority I have, at the present time.

Senator NELSON. Thank you all very much. We appreciate your very useful contribution to these hearings.

[The prepared statements of the preceding panel follow:]

STATEMENT OF EDWIN GALLISON, DEPUTY STATE TREASURER OF THE STATE OF VERMONT

Mr. Chairman and members of subcommittee, my name is Edwin C. Gallison, Deputy State Treasurer from the State of Vermont and the President of the National Conference of State Social Security Administrators (NCSSSA). The NCSSSA is an organization which was established in 1951, the first year public employees could be covered by social security, and Section 1 of our Constitution states our purpose quite concisely:

"Since the Federal government by law and regulation has imposed upon the states specific administrative obligations pertaining to the inclusion of public employees under the Federal Old Age, Survivors, Disability and Health Insurance System, it is essential that the administrators designated in the respective states have a medium for the consideration of common problems and the exchange of ideas and information. As an instrument therefore the National Conference of State Social Security Administrators is herewith created."

Our organization was encouraged by the Social Security Administration in its early years and has worked well over the years to enable the states and the Social Security Administration to administer social security coverage for public employees more effectively and efficiently, we believe, than the private sector administration under IRS. The states assume full liability for all contributions due under the coverage agreements. This includes liability for any interest assessments as well. Most states have established field audit staffs to educate local reporting officials and monitor the compliance with the varied coverage provisions as well as prove the fiscal correctness of the reports.

The Chapter 1 Introduction of the Report of the General Accounting Office dated December 18, 1978 accurately summarizes the states' role in administering social security coverage for public employees through voluntary agreements between HEW and individual states to avoid the constitutional question of federal authority to impose social security taxes on state and local government employers. This summary also reflects the growth of the program over the years to a point where over 9.4 million state and local government employees are covered for whom over $10 billion was deposited in 1977. It would appear that this voluntary program's expansion to cover 73.8% of state and local employees and the tremendous increase in contributions (due mostly in recent years to the meteoric rise in

rates and covered wage base) when combined with the funding problems the system faces, has brought about a change in attitude toward public employee coverage. This has resulted in (1) the attempt in 1977 to legislate mandatory universal social security coverage for public employees and (2) the regulation we are concerned with today to accelerate cash flow from these covered public employers and employees into the trust funds. While it may not seem that these issues are directly related, I believe they are and I will explain why I believe so as I proceed.

Both the General Accounting Office Report and the supplementary information included with the published regulation cite the substantial losses of income to the Social Security Trust Funds and the significantly more liberal requirement for deposits of public contributions than the requirement imposed by the internal revenue code on the private sector. Both documents acknowledge that losses were not significant in earlier years and that now, with more contributions and higher rates, the trust funds should reap the rewards. Both the General Accounting Office Report and NCSSSA recommend turning the collection process over to IRS. This recommendation was rejected on the grounds that this would require a change in the law. It is mentioned, on the other hand, that several states may have to amend their laws to comply with the new regulation. This was obviously not considered reason enough to reject the new regulation, however, and the eighteen month period before implementation is supposed to be sufficient for all states to remedy any legal and administrative problems.

WHY DO STATES OPPOSE THE NEW REGULATIONS?

As indicated in the GAP report and the supplementary information published with the regulation, the states and local entities strongly opposed the proposed regulation. Let us set forth the reasons for our opposition in the order in which they most concern us as state administrators.

1. Administrative problems

We maintain that it is administratively impossible to comply with either the proposed regulation or the modified regulation as finally published. The Social Security Administration's response to our insistance that these problems really exist and that they are major is, "We do not believe the problems are so extensive and severe that the states will not be able to devise processes which will enable them to comply with more frequent deposits." They go on further to discuss estimation of contributions and amending state laws to allow payments to be based on estimates. This seems to presume that states are going to advance contributions for local entities, which I am sure all states would be very reluctant to do and many could not legally do. This would not only require statutory amendments to enable such practice, but would require appropriation of funds for the advances. They totally ignore the real world problems in administering social security coverage for local government.

(*a*) Small entities make up a large percentage of the covered units (See Appendix B) and no tolerance levels are provided. Therefore, we must assume that our monthly deposits must include contributions from every covered entity, no matter how small. The internal mechanism of local government is such that prompt remittance and compliance with frequent due dates cannot realistically be expected. Many reporting officials are part-time or volunteer public servants while full-time farmers, tradesmen or businessmen. Requirements for prior signatures of approval on warrants before remittances can be made is a problem when school boards or local boards of trustees or selectmen meet once or twice a month. Mail service from remote rural areas in many states will use up a good part of the period from the end of the month to the due date (See Appendix A). These are real problems not addressed in either the General Accounting Office Report or the Social Security Administration response to the issues raised in opposition to the NPRM.

(*b*) While larger entities might be expected to have more sophisticated procedures and systems, they are not altogether without their problems either. I know the State of Vermont, with a relatively elaborate computerized accounting system with check writing as a by-product, routinely takes over two weeks from the time a voucher goes in one end before a check comes out the other. (We understand the Federal system of processing payments may not be that prompt either.) Some of these larger entities may not have the sophisticated systems you might expect. Some even have cash flow problems. Don't forget the state retains liability under the regulations. There is no risk or collection expense for the Social Security Administration.

(*c*) The states must collect the contributions from each covered entity, deposit and record each remittance received, consolidate all remittances received

and make the single deposit in the Federal Reserve Bank 15 days after the end of the month for the first and second month in each quarter. (Attached as Appendix A is a list of steps involved and an average number of work days required to accomplish each.) In the third month they must collect the contributions and a quarterly report, reconcile the report to remittances received for the three months and remit 45 days from the end of the quarter. At the end of that process (the last 15 days) the first remittances for the new month in the next quarter are also flowing in to compound the confusion.

At this point I would like to clarify a statement that appears on Page 11 of the General Accounting Office Report regarding collecting and depositing funds and reporting. (This comment relates to the 5 states they visited before issuing their report—Arkansas, Louisiana, Maryland, New Jersey and Texas.) "With regard to the timeliness of collecting and depositing funds and the frequency of reporting, three of the five states require state agencies and local governments to remit social security contributions to them more than quarterly (semi-monthly, bi-weekly, and monthly). In these instances, the funds are already deposited with the states and the additional administrative work, other than reconciling contributions to to the entities' quarterly reports, has already been accomplished."

This statement is very misleading. The only contributions remitted to state social security agencies in these states more frequently than quarterly are state agencies, not local entities, except Maryland. Maryland collects monthly with a due date of the 20th of the month. Their delinquency rate is very high. A few other states, not visited by GAO, collect from local entities monthly with reporting procedures tied to retirement system administration. I know of no deadline in any of these states that would allow compliance with the 15-15-45 deposit regulation. We readily agree the states, as employers, would be capable of complying with the regulations. To collect and be liable for 65,000 local subdivisions on the same schedule, however, is a different matter.

On Page 13 of the General Accounting Office Report they admit "We did not study the reasonableness of the 15 day time frame for depositing monthly contributions. Although 15 days seems to be a reasonable amount of time to make deposits to the trust funds, the exact number of days should be determined by HEW after consulting with the states." We submit that the 15 day time frame is unreasonable and should not be implemented.

2. Financial liability

This concern ties very closely with the administrative problems. While the states are liable for all contributions due for covered wages of all covered employees, they pass any interest assessments for delinquent remittances back to the appropriate local entity. This requires assessment procedures and accounts receivable systems to provide adequate controls. With no minimum deposit provisions or defined tolerance levels, delinquency rates will be very high. Controlling assessments for late remittances will cause substantial workload increase and expense.

3. Additional costs to States (see appendix C)

The increased workload generated by the accelerated deposit regulation will require substantial increases in staff in some states and development of automated systems in some states. This comes at a time when many if not most states are experiencing some form of budget control legislation or tax revolt. Looking ahead to the study on universal social security coverage, we recognize the strong probability the report will recommend implementation of universal coverage for all public employees. At that point, would states continue to administer local coverage? We think it unlikely. Does it make sense to gear up our operation now, hire and train staff, buy hardware and develop software only to retire the system in a few years? It doesn't make much sense to us.

4. Loss of interest income (see appendix D)

Many may be surprised to find this item so far down in the order. Much has been said on both sides regarding the use of the monies. The General Accounting Office and the Social Security Administration claim the trust funds are entitled to this income. Others claim this loss of income to state and local governments amounts to reverse revenue sharing. While the General Accounting Office Report and the Social Security Administration published information do not agree on the amount of interest involved, it is substantial by any standards. To be simplistic, their gain is our loss.

There may be other factors you should consider, however. How much would not have been collected in taxes if IRS had been the collection agency? How

much is the states guarantee for full payment of contributions and interest assessments worth? How may entities would not be covered if social security administrators and their staffs had not sold the program? How many covered entities or even states will terminate coverage if these regulations are implemented? How many entities would have already terminated coverage if we had not persuaded them to reconsider? How many entities will take advantage of sick pay exclusions, employer pick-up of contributions and other legal means of making up their losses? What will the bottom line be? Will the trust funds really gain as much as the federal agency reports indicate? We believe they will not unless universal coverage is mandated and these loopholes closed.

The Social Security Act requires that, as far as practicable, the same requirements shall apply to states as apply to other employers. The question seems to center around the definition of "practicable". There are differences between private sector coverage and public sector coverage. Theses differences will remain until universal coverage is accomplished. We believe there were valid reasons for establishing the deposit and reporting procedures which have been in effect, basically unchanged, for 28 years. Expansion of the coverage of 65,000 entities and nearly 10 million employees has not eliminated problems in administering this program. If it is the desire of the federal government to receive deposits from the public sector, then we strongly suggest it be administered the same way, by the system and procedures already established, by the same federal agency that administers the collections process from the private sector. We believe the General Accounting Office Report makes a strong case for social security contributions to be collected by IRS along with the federal income tax withholdings.

If the Social Security Administration is concerned about the ability of IRS to administer coverage and collections for the public sector, and if they recognize the value of the states guarantee and the other factors we mentioned earlier; then we suggest no changes be made in deposit and reporting procedures which would increase costs at the state and local level, until a decision has been finalized regarding universal coverage for public employees, and then only after a thorough study has been made on the effect of the regulation with regard to:

1. Increased paperwork and administrative problems at state and local level;
2. Reasonableness of time frame;
3. Administrative costs;
4. Realistic trust fund interest gain.

APPENDIX A

Administrative problems

	Days
Local:	
1. Consolidation of sub-unit payments by local units (Such as required by Wisconsin statute 66.042)	3
2. Drawing and authorization of local warrants	4
3. Mail constraints (geographical—climatic—seasonal)	5
State:	
4. Accountability of local receipts	5
5. Deposits of receipts in State treasury	-
6. Drawing of State warrants	5
Total average work days to administer collections	22

NOTE.—Estimated average days shown do not consider special situations which could delay process further, such as: Computer down time, holidays, staff leave, and miscellaneous.

APPENDIX B

Average entity deposit (quarterly)

	Percent
Less than $200	10
$200.01 to $2,000	25
More than $2,000	65
Wisconsin:	
0 to $200	4
$200.01 to $2,000	49

NOTE.—Based on sample of 10 States for quarter ended September 30, 1978.

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APPENDIX C

Administrative Cost Increase

Present.—$13 Million.

Projected additional.—$5 Million (38 percent average increase) Range $25,000 to 275,000. Additional: Staff; Space; Equipment; and EPD.

Start-up costs: $1 Million.

Delinquency Rate—Significantly Higher.

Estimated Interest Assessments—As much as $4.5 Million Quarterly.

APPENDIX D

1981 interest loss	*Million*
NCSSSA	[1] $80
HEW	[2] 179
GAO	[3] 216

[1] Based on statistical sample of ten (10) States.

[2] Per supplementary information filed by HEW with final regulations published in Federal Register, vol. 43, No. 224—Monday, Nov. 20, 1978 (p. 54084).

[3] Per General Accounting Office report dated Dec. 18, 1978 (p. 4).

Statement of Alta E. Moore, State Social Security Administrator of Wisconsin

It is clearly apparent that the Federal bureaucrats who concocted the arbitrary and unrealistic proposed scheme for more frequent deposits by states of Social Security payments were thinking of what procedure could be devised for a state government itself, for a city like Milwaukee, Wis., for a metropolitan country like Dane County, Wis.—governments which have sophisticated accounting and processing equipment and trained career accounting and clerical personnel.

No consideration whatever could have been given to what actually exists out at the grass roots democracy in this nation—in the thousands of small cities, rural counties, villages, towns or townships, school districts, and special municipal districts.

It is quite amazing to me that members of Congress seem to be forgetting what actually transpires out where many of them originated, For example, Senator Nelson was born and educated through secondary school in Clear Lake, a small village in northwest Wisconsin, with a current population of something over 700 souls, Senator Nelson's home county is rural Polk County, Wis., as has been mentioned previously in this hearing—the present population being less than 30,000 people.

To foist such a proposed procedure as that published November 20, 1978, on simple operations of local government such as Clear Lake Village or even Polk County is quite absurd as I will point out in detail in this statement.

I administer Social Security coverage and reporting for state and local public personnel in Wisconsin under Section 218 of the Social Security Act. This is in accordance with the provisions of the compact between the state and the Federal Government for such coverage.

I have been associated with this program since 1951.

There is coverage under the compact in Wisconsin for from 275,000 to 300,000 persons, depending on the season of the year. More than 2,000 political subdivisions now are included for the coverage to varying extents, that is, not all included subdivisions have coverage in the same degree. It is estimated that there are a maximum of 3,000 eligible units of government in the State of Wisconsin.

Under the master compact the state not only initiates the coverage under authority in state law and administers the coverage for state agencies and included political subdivisions after having entered into agreements with the Federal Government for such coverage, but the state must guarantee and underwrite all payments—both employer and employee—from all covered subdivisions.

It has been a challenging education process over more than a quarter century to discharge the state's obligations under the agreement and to procure compliance, but we are quite proud of the fact that as the result of great efforts, we have achieved a standard of reporting which the SSA concedes is of higher quality than the IRS has been able to achieve for private employers.

The impending Federal mandate to accelerate the deposit frequency is typical of the simplistic thinking by persons who fail to comprehend what the actual facts are.

Neither jurisdiction which I have mentioned in speaking of Senator Nelson's origins has sophisticated accounting or processing equipment which GAO, SSA, HEW and others state inaccuractely are common and even prevalent in local government jurisdictions.

In Wisconsin 10 percent of our jurisdictions make 75 percent of the total contributions under Section 218 coverage. A few large entities account for the majority of people and dollars, but a large majority of entities, many of which are served by part-time citizen officials, doing their Government work in their spare moments. simply have to be recognized for the problems they have and the needs they represent.

More than half of the political subdivisions included in the Wisconsin Section 218 agreement would be required under the July, 1980, scheduled change to remit Social Security payments more frequencly than if IRS rules were applicable; many of these have no income tax withholding obligation at all. This does not make much sense!

At the state level however it is difficult to vary requirements of local governments on the basis of size in the type of service I represent. In addition the larger jurisdictions have many semi-autonomous subordinate units for which the central treasury of the jurisdiction is liable. Section 66.042, Wis. Stats., requires that all disbursements must be from the treasury of the subdivision and that "when any board, commission or committee of any county, city, village, town or school district is vested by statute with exclusive control and management of a fund, including audit and approval of payments therefrom, independently of the governing body, such payments shall be made by order checks issues by the county, city, village, town or school clerk upon the filing with him of certified bills, vouchers or schedules signed by the proper officers of such board, commission or committee, giving the name of the claimant or payee, and the amount and nature of each payment."

The facts as we see them are that it will not be possible for Wisconsin to comply with the federal mandate in the new rule.

It is simply is not possible for our political subdivisions within the unrealistic time schedule posposed.

First, to determine the amount of contributions payable in a month—and for large agencies to gather the deductions from several sub-units such as highway departments, utilities, libraries, hospitals, nursing homes, et cetera.

Second, to have a check prepared and signed after computing and adding the employer share.

Third, to send the check representing employe and employer contributions on gross covered wages paid in the previous month through the U.S. mail system to the state agency—keep in mind that the state is another party here—the total contributions are not just taken to a depository bank and considered timely filed if this is done within a given period of time—we must allow an absolute minimum of 2 days for delivery of mail to the state agency which has been charged with the guarantee and must be responsible for the total payment—the accountability factor.

Fourth, for the state agency to accumulate the contributions, both employe and employer, for all state departments, boards, and commissions, and for all included separate employer political subdivisions.

Fifth, for the state agency to keep a record of how much was received from what employer—to identify the employe and employer shares—to make certain that all sub-units and operations for which each subdivision is ultimately responsible are represented, et cetera.

Sixth, for the state agency to prepare a voucher for the State Bureau of Finance for the total contributions received and then have the State Treasury write a check made payable to the U.S. Treasury—this process takes at least 2 days at the minimum.

Finally for the state to deposit the contributions in the closest Federal Reserve Bank or to otherwise transmit them to the appropriate federal treasury account.

All of this within 15 days. Depending on what record of transactions will be required by SSA, there may be even more steps than I have indicated.

We think it is not possible to comply. If collections cannot be made, the interest income figures being bandied about so freely are meaningless.

Basic to the voluntary Social Security coverage compacts between the states and the Federal Government is the fact that quite a different arrangement exists and is necessary in the public sector which is totally different from what prevails in the private sector. So the argument that the new rule merely tries to extend

private employer practices to the public sector only emphasizes that the ivory tower bureaucrats who devised this Rube Goldberg monstrosity have no conception of what is actually involved.

As has been pointed out the Federal Government is completely protected against any loss in collections. There is a 100 percent guarantee written into the compact. Moreover the federal government is paid substantial interest when such payments for state and local public personnel are not deposited within the established time deadlines.

This is quite different from what has prevailed in the private sector.

In the first place the SSA does not really know how effective the performance of the IRS has been in collecting Social Security contributions from private employers. But the SSA has repeatedly conceded that it appears obvious that the states do a much more effective job than does the IRS.

This is of course confirmed by reports submitted to Congress first by former Senator John Williams of Delaware and later by Senator William Proxmire of Wisconsin. These reports have repeatedly disclosed serious delinquencies in the performance of the IRS in the Social Security collections function.

But as has been emphasized, in the public sector under administration by the states the Social Security trust funds are protected 100 percent. Despite the lack of concern by the SSA in policing operations in the private sector that agency has repeatedly checked upon the performance of the state Social Security administrators—sometimes almost to the point of harassment—and such discrepancies as have been found are ordinarily minor in character and pertain to borderline cases.

Implicit in this situation is the fact that whereas coverage for private employers is uniform and mandatory—for public personnel under Section 218 of the Social Security Act the coverage is exceedingly complex.

I must emphasize again very briefly some of the many differences between state operations under Section 218 and IRS operations under FICA:

1. Because under the Federal constitution coverage is not mandatory but can be provided only through state compacts there must be precise knowledge of any conformity with the detailed provisions of the compacts—this kind of knowledge is possible only at the state level. In Wisconsin, for example, there are complex integration provisions for public employe retirement systems with Social Security, some of these on a "divided system" basis; there are local governments covered under Social Security only for retirement system covered positions; there are local governments not covered by Social Security at all; there are local governments covered to the maximum degree under Social Security; there are all kinds of varied coverage conditions.
2. Coverage is not uniform as in private employment; there are various statutory exclusions mandated by Section 218.
3. There are numerous optional exclusions permitted under Section 218.
4. The optional exclusions vary from state to state and from political subdivision to political subdivision within the states.
5. While optional exclusions cannot be added they can be removed and the removal can be made retroactive—for periods which are not uniform.
6. While an employer-employe relation is relatively simple to establish in private employment, because of the intricacies of government organization at various levels—differing from state to state—it is not always simple to establish which entity is the employer in some instances or even whether an employment relationship with a government jurisdiction exists.
7. Although a private corporation has complete control over all phases of its operations from top to bottom, in the case of a state which is stuck with the underwriting guarantee for all political subdivisions, the state has little control over the operations throughout the state in the counties, cities, villages, towns and townships, school districts, etc.
8. A private corporation has full control over those responsible for Social Security reporting at each installation. Unfortunately this is not true of the control exercised by state Social Security administrators—this administrator must in many cases work with citizen officials performing a civic duty as part-time clerks of political subdivisions who frequenty find they encounter more headaches and spend more time in the public office than they anticipated, thus becoming a link of a chain of frequently changing clerks or treasurers requiring a constant education effort from the state administrator's office.

9. Obviously the enforcement obligations of a state Social Security administrator are much more complex than are those of the Internal Revenue Service in private employment.

So it is quite apparent that the task of a state Social Security administrator in discharging the state's obligations under a State-Federal compact is quite difficult and is completely different from what exists in the private sector!

Because the states have underwritten and guaranteed all payments due from all covered political subdivisions, it is essential that to protect the state treasury there should be an effective system of checking and controlling all Social Security reports.

To do this well requires considerable time and detailed administration. It obviously cannot be done within the time frame mandated by the new regulation.

What scares me as much in the proposal made by the Federal bureaucrats who seem to know so little of the facts is not only the chaos that will result because of the incorrect reporting that will ensue in the confusion—but also that there will be a wholesale scurry of these part-time officials to unload their responsibilities and let someone else worry about the problems that will result.

Our local reporting officials are tired and frustrated with increased Federal Government regulations and with the whole Federal bureaucracy. Already we see a great turnover in local officials. The majority of included political subdivisions are small and many have only part-time officials—often underpaid—who are serving as a civic duty. Another onerous regulation can only increase this turnover!

Federal officials quite generally have no comprehension of the problems encountered by the states in procuring the present standard of reporting of wages in a system the state must attempt to control, but which it cannot and does not want to dictate.

I am not talking theory. Instead I speak from bitter experience learned from working with grass roots democracy for more than a quarter century.

The people in the executive Federal agencies can present their pipe dreams to this subcommittee and to other congressional committees, but they should get off their high horse—go out on the firing line—and learn something of the facts of life at local governments levels. They would quickly change their tune!

Let me summarize by enumerating the specific points of disagreement of my state with the Federal executive bureaucracies in this controversy:

1. The State of Wisconsin and its approximate 3,000 political subdivisions are not comparable with a big private corporation and its hundreds of branches; the administrative procedure is not in the least similar; a state guarantee for hundreds of separate political jurisdictions is based on a constitutional premise underlying our system of government—this does not mean the state runs the affairs of its municipal corporations and other units of government. I am sure members of the subcommittee are aware that this is so even though the executive bureaucracies apparently do not understand this fundamental fact.

2. The same reasons exist today as existed previously for an adequate time allowance for the state to substantiate its payments to the Federal Government under complex coverage terms through a contractual arrangement; the situation is not similar in the least to the conditions in private industry where the coverage is mandatory and across-the-board. Again members of Congress acquainted with state and local government must realize this even though those who run HEW, SSA, and other bureaucracies do not realize this fundamental principle in the current controversy.

3. Under the Section 218 contractual arrangement each state guarantees the Federal Government against any losses, an element entirely lacking in the private sector. Again this is a fundamental premise.

4. Statements by Federal officials to the effect a monthly deposit schedule for the states on behalf of the myriads of local government units would present no administrative, legal, or time difficulties are outrageous misrepresentations of fact.

The facts are that administrative costs must skyrocket if it would be possible to to the job at all—with the result that already financially squeezed local governments would lose people who have been counted on to do the job properly; the state treasury would have to be opened to potentially damaging liabilities; conditions will be created under which withdrawal from the program will be a certainty, if not by direction or permission of the state legislature, then by default because of being unable to comply.

Local officials indicate time restrictions in arranging disbursements from the public treasuries to which they are accountable; many local units must depend on the timeliness of state or federal aids to meet the employer costs of Social Security; the non-availability of tax receipts when bills become due force borrowing costs; there are many such factors to consider.

5. The purpose of the Social Security program is the protection afforded in retirement benefits in old age and payment of benefits under conditions of survivorship, disability, disease, and death; the collection of contributions is a means to an end, not an end in itself.

6. The HEW and SSA authorities are proposing unilaterally to disrupt a system under Section 218, which is supposedly a bilateral contractural arrangement, that the states have demonstrated they can control.

Why destroy something that works and is being improved each day, especially when the substitute procedure most assuredly will guarantee neither accurate deposits nor quality reporting of the wage records on which benefit payments are computed, thereby causing more expense of corrections and mounds of paperwork at all levels—local, state and federal.

7. SSA and HEW authorities cannot have it both ways. If they want quality reporting and accurate payments by the state for the thousands of local government units in this country then there must be some understanding of what is involved in the guarantee by the states to pay. If this is not the purpose they should remove the state guarantee and look only to the collection of money chiefly from the big employer entities and ignore the needs of the hundreds of small communities which generally have opted for Social Security as their only protection for their employees.

8. If the ensuing chaos mandated by the Federal bureaucracies undermines and destroys the level of accuracy achieved with great effort by state administrators over more than a quarter century then many covered individuals and their dependents will be seriously harmed because their wage records will be incomplete or inaccurate—thus impairing the benefits to which they are entitled and which Congress blithely assumes they will receive.

Universal coverage is being studied by the Secretary of HEW and others as provided in Public Law 95-216 If as seems probable universal coverage to include all government personnel, Federal as well as state and local, is in the foreseeable future, why force an uncontrollable procedure on the states at this time?

It seems to me to be utter nonsense and also completely wrong for one party to a contractual arrangement to create chaos against the wishes of the other party when studies appear to indicate that the Federal Government eventually will succumb to the pressure to include its own employes under the national system and to find a way to resolve the constitutional issues which underline Section 218.

What I am asking for today is some real understanding of the facts that exist—facts that cannot be ignored. There are basic differences in operations that are necessary in the public sector from those in the private sector and these differences must be taken into consideration.

Senator NELSON. Our last witness this morning is Mr. Charles P. Smith, Wisconsin State Treasurer and vice president, Association of State Treasurers.

STATEMENT OF CHARLES P. SMITH, TREASURER, STATE OF WISCONSIN AND VICE PRESIDENT, NATIONAL ASSOCIATION OF STATE TREASURERS

Mr. SMITH. Senator Nelson and members of the committee, in the interest of your time, I will be very brief.

Today, I am representing primarily the National Association of State Treasurers as its regional vice president. This organization, as well as the National Association of State Auditors, Comptrollers, and Treasurers, to which I also belong, have taken a strong, consistent, and unanimous stand against the regulation for the acceleration of the frequency of social security deposits under section 218 of the Social Security Act.

Also, I am appearing on behalf of the State of Wisconsin and am taking the liberty of speaking for over 2,700 units of local government reporting groups, some of them being here today to speak on their own behalf.

Social security administrators have given a detailed account of the serious impact of this proposed regulation on State and local governmental units.

I find it rather curious that in light of the strong opposition to this proposed rule change over the past several years, by State financial officers, and those acting in a similar capacity at all levels of State government, that the Social Security Administration and its parent HEW, persist.

There cannot be a Congressman or a Senator who has not received much negative and even outraged correspondence from the two national organizations I belong to, from other financial officers of their various constituencies, from the county and town board associations, the State social security administrators, and I would expect from many Governors as well.

In my State, former Governors Lucey and Schreiber have expressed strong concerns to HEW officials and to our congressional delegation I have received personal assurances from Wisconsin's entire congressional delegation in support of continuing quarterly remittances with the exception of Senator Proxmire who did acknowledge my concerns.

Also, I have in my possession a letter to Mr. Donald I. Wortman, Acting Commissioner of the Social Security Administration, signed by 54 Members of the U.S. Senate requiring the Social Security Administration to withdraw the proposed regulations until such time as to legislative process has run its course.

Secretary Califano and Commissioner Wortman have consistently stated that the loss of interest income to the States and its subdivisions is the overriding concern. This is simply not true.

The overriding issue is the administrative burden and chaos that would result at all levels of government; undermining the accuracy of reporting, the placing of intolerable time limits for payment on the States, while still requiring the States to guarantee 100-percent contributions. The interest income generated by the temporary investment of collections by the States and their political subdivisions is a byproduct, an offset against administrative expense, a sound management practice—not the primary concern of the States as Secretary Califano and Commissioner Wortman would have us believe.

The truth seems to be that HEW and SSA want it both ways—a State guarantee which insures the Federal Government against losses and a deposit frequency within a time frame that makes it impossible for the States to comply. It is absurd to suggest that the States be required to underwrite and guaranteee all coverage and collections from included political subdivisions if the conditions in which the effective controls which have been developed and maintained by the States are to be taken away.

As Senator Nelson has said, and I quote: "It is patently unfair to force the States into a situation where they must underwrite the payments of their political subdivisions and, at the same time, jeopardize the accuracy of their reporting systems by imposing more frequent and burdensome depository requirements."

Senator NELSON. If, in fact, that is what happens, so you do not misunderstand me.

If they do not increase the paperwork and if the municipalities and the State get adequately compensated for their work, I do not defend the proposition that you ought to take social security funds that belong to retirees and use them for general purposes of government. I have never taken that position in support of that proposition.

Mr. SMITH. Right, I understand that, sir.

The matter at issue seems to be: "Shall the terms of and long-standing administrative practices under the master State-Federal social security agreements be modified unilaterally by one party to the agreement?" I think not.

This effort by HEW to accelerate remittances appears to be a unilateral abrogation of longstanding, two-party agreements between HEW and each of the States. This may require renegotiation of the agreements rather than HEW changing the agreements by a questionable use of its rulemaking authority.

If HEW prevails on this issue, I will ask my attorney general to join the several States that are contemplating litigation of this issue.

Thank you.

Senator NELSON. Senator Danforth?

Senator DANFORTH. No questions.

Senator NELSON. Thank you very much for coming to testify on behalf of the Association of State Treasurers. I appreciate it very much.

That concludes the hearings. We will be submitting some additional questions to the witnesses who appeared today well as asking for a response from the Social Security Administration to the issues that were raised here in the testimony.

Thank you.

[Thereupon, at 12:40 p.m., the hearings in the above-entitled matter were recessed, to reconvene at the call of the Chair.]

[By direction of the chairman the following communications were made a part of the hearing record:]

TESTIMONY OF SENATOR DALE BUMPERS

STATES' SOCIAL SECURITY DEPOSITS

I commend the Senate Finance Subcommittee on Social Security for holding hearings on the regulations issued by the Department of Health, Education, and Welfare which modifies the method under which States file Social Security contributions. Now States file quarterly reports within 45 days after the close of a calendar quarter. Under the new regulations, depostis are required 15 days after the end of each of the first two months of a calendar quarter, and 45 days after the end of a calendar quarter.

I have three principal reservations about this proposal. (1) It will place severe time constraints on State Offices. (2) State and local governments will have more paperwork. (3) The change is likely to lead to more errors according to state and local government officials.

Under the best of circumstances, mail takes from two to five days to reach Little Rock from the other areas of Arkansas. Once the payments reach the State Office in Little Rock, they must be verified and processed. The State Office makes a deposit in the Federal Reserve Bank in Little Rock. Fred Henne, Administrator of Arkansas' State Office, in his testimony before the Subcommittee, stated that it took eleven days from the time he personally hands over the check to the Federal Reserve Bank before the funds are credited to the Social Security Trust Fund account. Thus, if the mail from most jurisdictions takes three or four days

to get to Little Rock, the State Office only has two days at the most to verify, process those reports, and deposit the state's payment to avoid a penalty. This time constraint allows no time for delayed mail service, equipment breakdown, adverse weather conditions, or any one of a number of problems which might occur.

The increased number of reports will place an additional burden on local governments which already spend an inordinate amount to time filling out forms to comply with federal and state regulations. Additional personnel will be required, driving up costs to the State government.

The combined effect of the above will jeopardize the admirable record Arkansas has achieved over the years. The increased paperwork and tight time constraints can only invite errors that will be neither to the State's nor the Social Security Administration's advantage.

I do not question the premise that the Social Security Administration should maximize the benefits derived from the Social Security Trust Fund contributions. The regulations that are intended to achieve this goal, however, do not take into account the costs to States and local government.

I urge the Social Security Administration to reconsider these regulations in light of the testimony that the Social Security Subcommittee has received in this hearing.

STATEMENT OF CONGRESSMAN JACK BROOKS

Thank you Mr. Chairman. I appreciate the opportunity to share with you and the committee my views on the need for more frequent deposits by States of social security contributions.

As you know, participation by State and local government workers in social security is by a voluntary arrangement with the States, and about 9.4 million, or 74 percent, of all such employees are covered. Their contributions, and the matching employers' share, amounted to over $10 billion in 1977.

The law authorizing their participation directs the Secretary of HEW to impose the same implementing requirements on the States as are imposed on private employers so far as practicable. Private employers are required to deposit both social security taxes and money withheld from employees' income on a monthly, semi-monthly, or weekly basis, depending on the amounts involved. States must meet the same schedule for depositing their employers' share and the contributions of State and local government workers.

Since 1959, however, States have had 45 days after the end of each quatrer to deposit social security payments to the Treasury, retaining the interest earned in the interim for themselves. According to a recent GAO report, this practice has cost the Social Security Trust Fund about $1.1 billion in interest for the years 1961 to 1979.

On November 20, 1978, Secretary Califano issued new regulations, to take effect July 1, 1980, which will require monthly deposits but will permit the States to retain the final month's deposit in each quarter for 45 days. Despite these new regulations, GAO believes that the trust fund will continue to lose substantial earnings in the future. The GAO recommends that HEW implement regulations requiring semi-monthly deposits by the States which would earn $281 million more for the trust fund during the five year period beginning July 1, 1980.

I support GAO's recommendations for more frequent deposits. While HEW is to be commended for moving to recover some of the money, I can see no justification for permitting the States to retain any interest on earnings on social security contributions. This money should be going into the Social Security Trust Fund, especially since the fund is experiencing financial problems that have caused Congress to raise social security taxes.

I am particularly disturbed by reports that HEW revised its more stringent March 30 proposed regulation, which required States to switch from quarterly to monthly deposits, due to opposition by the States. According to the GAO, the States base their objections on the loss of earnings and cash flow that would result from more frequent deposits. This argument is fallacious. Social security contributions were never meant to provide States with interest earnings or cash flow. HEW is ducking its responsibility in the law by permitting this disguished form of revenue sharing to occur at the expense of the Social Security Trust Fund.

I, therefore, join with GAO in criticizing HEW deposit regulations which allow States to earn interest on investments using funds which should be on deposit for the trust fund. This practice is detrimental to the financial stability of these funds, and cannot be rationally justified.

I urge the committee to support GAO's recommendation that the HEW Secretary revise the November 20 regulations to require States to make semimonthly deposits.

NATIONAL GOVERNORS' ASSOCIATION,
February 1, 1979.

Hon. GAYLORD NELSON,
Chairman, Senate Subcommittee on Social Security,
Washington, D.C.

DEAR SENATOR NELSON: To my regret, I was unable to appear at the hearings you held on January 29 to discuss deposit requirements for state and local contributions under the social security system.

The position of the National Governors' Association on the Department of Health, Education, and Welfare (HEW) regulations to increase the frequency of such deposits is clear. You will find enclosed a copy of the policy which the Governors adopted at the NGA annual meeting last summer.

I am very much concerned by the administrative complexities that will result from the requirement for deposits of state and local social security contributions on a fifteen/fifteen/forty-five day schedule. These problems were outlined in testimony at your hearing by the National Conference of State Social Security Administrators, and I will not duplicate the data you have already received by repeating them here. Unless these administrative problems are resolved, serious disruptions will occur in the operation of the program and, perhaps, even in wage records maintained for beneficiaries.

Throughout the debate, our assertions that severe administrative difficulties will result from changes in the deposit schedule have been ignored. Even the eport recently prepared by the General Accounting Office (GAO) failed to review the feasibility of a fifteen-day deposit schedule. Like HEW, GAO asserts that a fifteen-day deposit deadline can be met but fails to refute the points raised by states.

We hope that you will continue in you efforts to ensure that states have a fair hearing on this issue by urging GAO and HEW to cooperate on a short-term but thorough study of the administrative problems in the new deposit schedule that we have identified. The effective date of the HEW regulations should be changed to eighteen months after the completion of the study.

I hope that we can work together in the months ahead to resolve the potentially serious problems with the changed procedures. In the meantime, I would appreciate it if you would include this letter and its enclosure in the record of the January 29 hearings.

Sincerely,

GOV. RICHARD A. SNELLING,
Chairman, Committee on Executive Management and Fiscal Affairs, National Governors' Association.

Enclosure.

STATE DEPOSITS OF SOCIAL SECURITY FUNDS

The Department of Health, Education and Welfare has proposed regulations that would require the states to make monthly transmittals of social security contributions instead of the present quarters transmittals. Deposits of all social security contributions would have to be made not later than fifteen days after the close of each month. At present, these deposits are made not later than the forty-fifth day after each calendar quarter. The new regulations are to become effective sometime in 1980.

The unilateral action of the secretary is not in keeping with the agreements between state participants in the social security program and the federal government. Further, the action is premature because it fails to take into account a study of the social security program under way at HEW. The study report, due in 1980, is expected to find the need for far-reaching changes in the social security system. The revision of existing, effective state procedures just prior to a more extensive overhaul of the system seems unnecessarily disruptive to us.

The National Governors' Association favors retention of the quarterly deposit system for social security funds and supports legislation necessary to maintain the current system.

EMPLOYEES RETIREMENT SYSTEM OF TEXAS—STATEMENT ON MONTHLY SOCIAL SECURITY DEPOSITS

The Employees Retirement System of Texas is the state agency responsible for the collection of social security wage reports and contributions from 1,915 groups of local government and 246 units of state government. Through this program 495,879 employees of state and local government are contributing to the Federal Old Age, Survivors, Disability and Health Insurance Program. For the calendar year of 1978 the state will timely deposit to the United States Treasury more than four hundred and ninety million dollars. Due to the experience of this state since this program began in 1951 we feel qualified to express our opinion on the proposed regulation by the Federal Social Security Administration regarding monthly deposits of social security contributions.

When this program began in 1951 Federal regulations required quarterly social security reports and contributions to be remitted by the end of the month after each calendar quarter. As coverage increased under this program the states became less and less able to meet this deadline. This matter was presented to the Federal Social Security Administration and obviously the policymakers in that agency at that time recognized some of the problems. The federal agency agreed to change the reporting date to 45 days after the end of each calendar quarter. Under this regulation this state has been able to effectively administer this program.

The procedure and liability of the Internal Revenue Service as compared to that of the states is totally different. In this state we are required to deposit the withheld contributions from the employees after it is remitted to this office by the employer. Additionally, for the 246 state agencies the next step is to obtain the matching money which comes from a multitude of funds since our state law requires the matching money to be paid from the fund from which the employee is paid. Once the matching money is obtained state law requires that this money also be deposited in a special state fund. The procedure is then to draw a voucher requesting another state agency to write a warrant. This often requires several days, and upon receipt of the warrant this agency then deposits this amount in the Federal Reserve Bank at Dallas. We suspect a procedure similar to this exists in all states. We know of no other method to legally administer this program because most states do require certain safeguards in money transactions.

It would be interesting to observe how long it would require the General Accounting Office to collect social security contributions from all the federal agencies, deposit this money in a special fund, obtain matching money for all agencies from the fund from which each employee is paid, prepare the proper document for a check to be written at the pleasure of another federal agency, obtain the warrant, and deposit it in a Federal Reserve Bank.

Under the proposed federal regulation to be effective July 1, 1980, the states will be required to deposit social security contributions for the first 2 months of each calendar quarter within 15 days after the month ends and to deposit the contributions and remit the quarterly wage report within 45 days after the third month of the calendar quarter. This state could possibly administer this program if we were allowed 30 days after the first 2 months and 45 days to remit the deposit and file the wage report after the third month of each quarter. Most people when discussing a 30-day time period versus a 15-day time period automatically have a vision of the federal agency losing 15 days of interest each month forever. This opinion is not correct. If the states were given 30 days instead of 15 days the only loss to the trust funds would be the interest earnings for a period of 15 days for one time only. Once this procedure is established the deposit would be made at 30-day intervals which is the same interval that would be followed under the 15-day plan. It is not reasonable nor understandable that a federal agency would be permitted to impose upon the states an impossible burden forever simply for the sake of earning interest for one 15-day period.

We appreciate the opportunity to have these brief remarks included in the testimony regarding this issue.

JOSEPH N. MURPHY, Jr.,
Executive Director,
Employees Retirement System of Texas.

STATEMENT OF THE NATIONAL LEAGUE OF CITIES

The National League of Cities, on behalf of its 48 state municipal leagues and representing 15,000 member cities, submits the following statement strongly opposing HEW's November 20, 1978, regulations mandating that state and local governments contribute social security payments on a monthly, rather than quarterly, basis.

In summary, our statement deals with the following issues:

The voluntary nature of state and local government participation in the Social Security system;

The absence of a fiscal impact statement accompanying the regulations;

The additional costs required to implement the new system;

The inadequate involvement of local governments in developing the regulations; and

The argument that the regulations will result in equity of treatment with the private sector.

State and local government participation in the Social Security system is currently entirely voluntary. Over seventy percent of state and local government employees have opted for inclusion under Social Security. The recently-enacted increases in Social Security tax rates and the taxable wage base has spurred intensive examination by local governments of the feasibility of withdrawing from the system entirely. The loss of several months interest on social security contributions could well provide the compelling incentive for local governments to withdraw from the system. It should be obvious that a significant number of withdrawals from the system will be far more costly in terms of revenue loss to the Social Security Trust Fund than the interest lost as a result of the existing system of quarterly contributions.

We believe that an economic impact statement should have been prepared to accompany the new regulations. The analysis required by Executive Order 12044 requires agencies to prepare a "regulatory analysis" for all regulations identified as significant. Such as analysis is required to "involve a careful examination of alternative approaches early in the decisionmaking process." Furthermore, in his March, 1978 Urban Policy Message, the President pledged that the Administration would prepare urban impact analyses on important proposals affecting state and local governments. These assessments have not been made. Given the recent adoption of such tax and spending initiatives as the Jarvis-Gann Amendment to the California Constitution, we believe this is a most inappropriate time to alter existing procedures without knowing precisely the potential fiscal impact on State and local governments.

Not only is the information on the fiscal impact from the perspective of lost interest income inadequate, but no valid and thorough study has been made of the additional costs to local governments—in terms of personnel, equipment, and so forth—of complying with the new contribution requirement. Nearly 65,000 general and special purpose units of government will be affected by the new regulations. Many will be small jurisdictions, with only part-time staff to manage payrolls. There has been no attempt to ascertain the financial capability of these jurisdictions to absorb additional costs in order to comply with the regulations. We believe it is essential that this information be accurately assembled and evaluated prior to imposing any changes in the existing system.

While we understand that the Social Security Administration consulted at length and in detail with the appropriate agencies of State governments in developing these regulations, there was minimal consultation with units of local government. This lack of adequate consultation with local governments is wholly inconsistent with the President's urban policy proposals referred to earlier. HEW justifies the new regulations, in part, by asserting that there would be parity between the public and private sectors. We believe this argument is invalid. There are numerous inequities between private and public sector participation in the Social Security System that have not been addressed. States guarantee contributions to the Trust Fund on their own behalf, as well as on behalf of local governments within their jurisdictions. Private sector contributions, on the other hand are not guaranteed, and failure of an individual employer to remit social security payments results in a net loss to the Trust Fund.

Furthermore, private sector establishments are entitled to deduct the cost of Social Security payments from their income taxes—a substantial financial benefit to private employers, far in excess of the loss the Social Security Administration claims because of quarterly contributions by state and local governments. While recognizing that income tax deductions do not impact on the Social Security

Trust Fund, one can scarcely claim parity when non-taxed local governments are not accorded similar favorable treatment in reducing actual financial outlays.

The National League of Cities urges that implementation of the new regulations be delayed to provide an opportunity to obtain more accurate and comprehensive information on all aspects of their impact. The Federal Government has a responsibility to insure that changes in established procedures do not impose financial burdens on already hard-pressed local governments.

RESOLUTION No. 5—TO OPPOSE THE SOCIAL SECURITY ADMINISTRATION REPORTING AND DEPOSITORY PROCEDURES

Whereas on March 30, 1968, the Social Security Administration published in the Federal Register a notice of proposed change affecting the remittance procedure for state and local governments; and

Whereas if implemented these regulations would require that every public employer who is covered for social security would be required to submit its contribution payment at the end of every calendar month instead of the current quarterly system; and

Whereas in order to begin more frequent deposits, the employer's appropriation for the fiscal years would have to be increased by at least twenty percent; and

Whereas the money would not remain with the employer until the end of the quarter and any interest income now derived on employee and employers contributions held during that quarter would be lost to the community; and

Whereas altering the long and established payment schedule would add to the administrative cost and to the already burdensome federal reporting requirements; now, therefore, be it

Resolved, That the National League of Cities urges the Congress of the United States to enact legislation mandating continuation of the current system of quarterly deposits and reporting procedures; be it further

Resolved, That the National League of Cities opposes proposed regulations to require public employers to report this information on a monthly basis as unnecessary; be it further

Resolved, That the National League of Cities opposes any attempt by the federal government to collect the interest on accrued Social Security deposits in lieu of changing the deposit and reporting requirements.

NOTE.—Approved by the Membership of the National League of Cities, Annual Business Meeting, November 29, 1978, St. Louis.

COMMONWEALTH OF VIRGINIA,
OFFICE OF THE GOVERNOR,
February 15, 1979.

Hon. GAYLORD NELSON,
U.S. Senate, Washington, D.C.

DEAR SENATOR NELSON: I wish to take this opportunity to inform you of the position of the Commonwealth of Virginia on the Social Security Administration's regulations requiring states to deposit Social Security employer/employee payments with the Federal government on a more frequent basis.

The approach taken by the Social Security Administration is of particular concern to me.

I believe all financial and administrative matters on this complex issue should be given fuller consideration. I refer specifically to the following:

1. The Federal Government does not recognize the relationship between the state and its local governments. It is impossible for the state to collect and obtain documentation from the various employer jurisdictions on employee and employer contributions within five to seven days after each month, and then guarantee the total payment to the federal treasury. This cannot be done, with any degree of accuracy, by the 15th day after each month. With 733 reporting jurisdictions in Virginia, you can imagine how difficult this process would be in the time allotted to the state.

2. Most of the states use interest income (over $3 million in Virginia) for the substantial cost of administering the program. The regulations would not only deprive Virginia and the other states of the interest income to finance these costs, but the added bureaucracy required by the regulations would greatly increase administrative costs at state and local levels. This would impose an additional burden on state and local taxpayers. In Virginia, any interest income above the

cost of administering the program is used for the retirement benefits of those members contributing to the system. The money is not placed in the state's general fund.

3. The projected shift from the long established quarterly reporting to monthly reporting will impose a 20 percent cost increase upon the states and the political subdivisions covered by the program in the first year because they will be required to finance payments for 14 months instead of 12. This will disrupt state and local financing patterns and will create serious problems in financing the additional 2 months in the first year.

4. The Federal Government has attempted to show that it merely proposes to treat the state and local governments in the same manner as it does the private sector. However, the Social Security trust funds are deprived now of considerable sums paid to the Internal Revenue Service for administration of coverage and reporting in the private sector. Moreover, the SSA has repeatedly acknowledged that all studies show the states have done a superior job of administration in the public sector as compared with what the IRS has done in the private sector—and under far more complex and difficult coverage conditions in the public sector, as compared with the private sector.

Because of this and because the states are required to guarantee and to underwrite all employer and employee contributions for all included political subdivisions, as well as for included agencies and departments of the state government, the trust funds have been completely protected for money due for public personnel. The State of Virginia assumes the liability for over 300 million dollars per year in Social Security contributions. It is common knowledge, however, that in the private sector, because of the less effective administration by the IRS of this type of coverage and collections, and the absence of any guarantee by the IRS of the type required of the states, the Social Security trust funds are deprived of substantial revenue.

5. In many states taxpayers will be harmed because those states have been able to procure a higher rate of interest return on the temporary investments than will be the case for the Federal Government.

As we stated by the Governors at their meeting in Boston last August, the proposed accelerated deposit regulation is premature. It fails to take into account the current studies of the Social Security program. In their statement, the Governors said, "To revise existing effective state procedures just prior to a more extensive overhaul of the system seems unnecessarily disruptive to us."

An acceptable alternative to the revised state procedures, and one that would treat public and private sectors in the same manner, would be to turn over to the IRS the entire collection process.

A number of national organizations, in addition to the National Governor's Association, are working to encourage the enactment of legislation which will override the new Social Security Administration regulations. Your leadership and support toward this end will be greatly appreciated by the Commonwealth.

With all good wishes, I am

Very truly yours,

JOHN N. DALTON.

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