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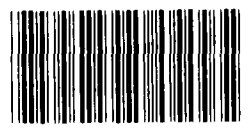
# General Accounting Office

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## State Department Should Improve Foreign National Pay Setting

State Department posts overseas are paying more than they should to their foreign national employees. When setting pay and benefits, the posts need to pay more attention to rates paid by the Department of Defense for similar jobs and more closely follow State Department instructions. Posts should also stop enrolling employees in the U.S. civil service retirement system and instead adopt local retirement and severance practices.

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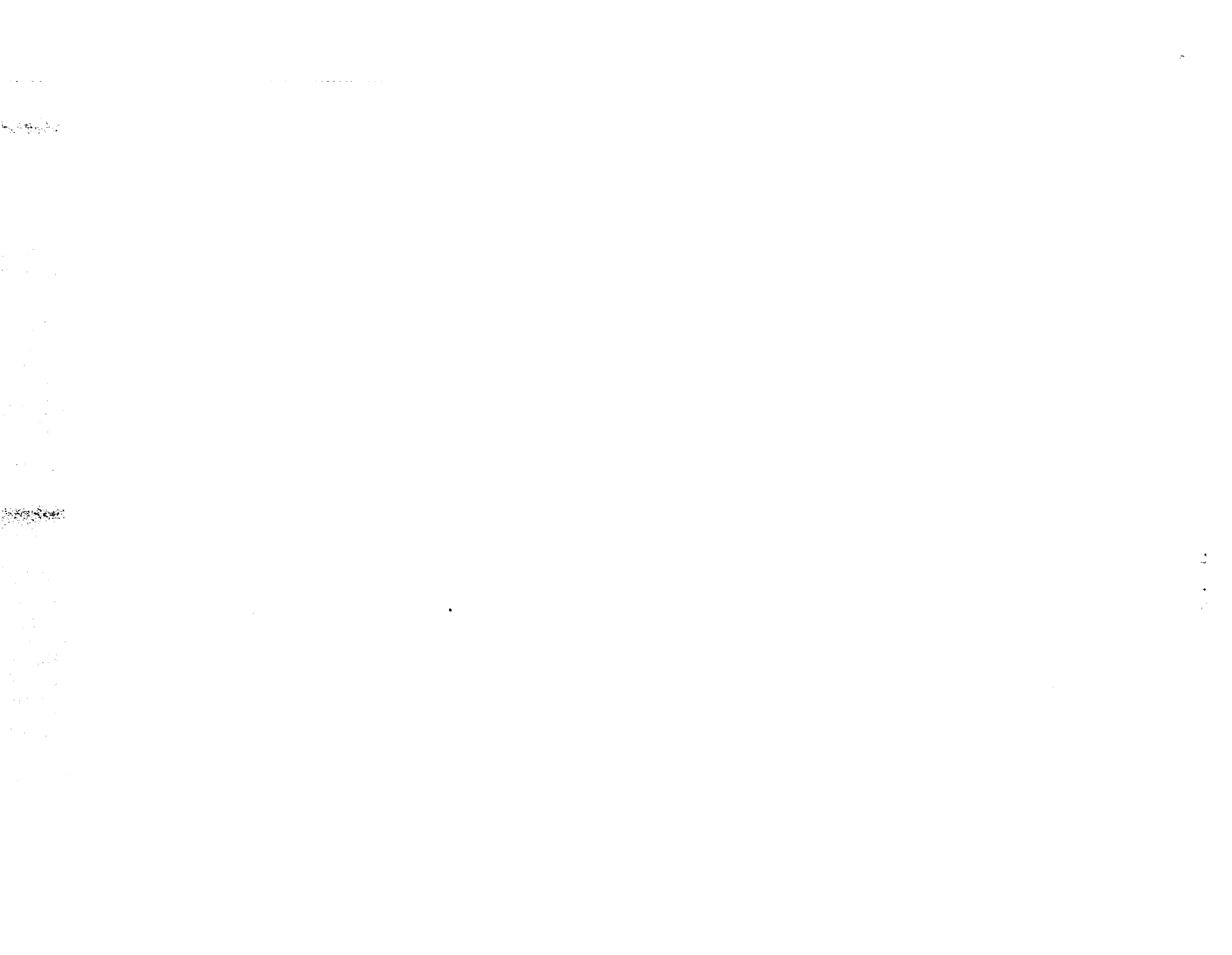


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GAO/50

FPCD-78-81  
JANUARY 8, 1979





UNITED STATES GENERAL ACCOUNTING OFFICE

WASHINGTON, D.C. 20548

INTERNATIONAL DIVISION

B-179343

The Honorable Cyrus R. Vance  
The Secretary of State

(32)

Dear Mr. Secretary:

This report summarizes our review of Department of State compensation practices for local employees at overseas posts.

We have included recommendations to you on pages 8, 15 and 22. As you know, section 236 of the Legislative Reorganization Act of 1970 requires the head of a Federal agency to submit a written statement on actions taken on our recommendations to the House Committee on Government Operations and the Senate Committee on Governmental Affairs not later than 60 days after the date of the report and to the House and Senate Committees on Appropriations with the agency's first request for appropriations made more than 60 days after the date of the report.

We are sending copies of the report to those committees and the Director, Office of Management and Budget; the Chairman, Civil Service Commission; and the Secretary of Defense.

Sincerely yours,

*J. K. Fasick*  
J. K. Fasick  
Director

(206)



GENERAL ACCOUNTING OFFICE  
REPORT TO THE SECRETARY  
OF STATE

STATE DEPARTMENT SHOULD  
IMPROVE FOREIGN NATIONAL  
PAY SETTING

D I G E S T

Federal agencies overseas employ about 178,000 foreign citizens at a cost of about \$1.5 billion annually.

Legislation provides that compensation for foreign national employees will be based on locally prevailing wage rates that are consistent with the public interest. In adopting foreign national labor provisions, Congress expected U.S. agencies in a particular locale to establish uniform wage rates and employment practices.

GAO visited Germany, Italy, Japan, Korea, and the Philippines to determine if employees were paid local rates and to what extent U.S. Government agencies coordinate compensation plans.

Overseas the Department of Defense normally sets the pay of its employees, and State sets the pay for employees of the diplomatic posts. A recent GAO report addressed Defense's pay practices overseas; this report deals with State Department practices and coordination between the two agencies.

MORE COORDINATION OF  
WAGE PLANS NEEDED

The Departments of State and Defense vary in the compensation they establish for their foreign employees, and in general, the Department of State pays more than the Department of Defense. State Department officials contended the differences were justified because of different duties

and responsibilities. GAO found little support that job demands were consistently or appreciably greater in one agency or the other. More coordination is needed and, where possible, a joint wage survey effort would broaden the base of wage survey data and improve wage comparability. (See pp. 3 to 10.)

#### WAGE SURVEY TECHNIQUES COULD IMPROVE

State Department wage survey techniques generally provided a valid base for applying total comparability principles to periodically adjust wages. Nonetheless, wage setting would be improved if (1) Embassy salary schedules reflected average private sector rates, (2) the true costs of retirement and separation pay benefits were included in comparability adjustments, (3) surveyed jobs were representative of the Embassy's work force, and (4) State Department wage survey guidance was followed more closely. (See pp. 11 to 15.)

#### ALTERNATIVE TO CIVIL SERVICE RETIREMENT NEEDED

Despite State Department urgings to adopt local retirement plans, most of the Department's overseas posts still enroll foreign national employees in the U.S. civil service retirement system. Posts have been reluctant to adopt local retirement plans because of the preference of employees for civil service retirement, the recruiting inducement civil service retirement provides, and the perceived lack of acceptable alternative plans.

GAO believes the disadvantages of enrolling foreign employees in civil service far outweigh the advantages. Some of the disadvantages are (1) annuities stated in dollars but paid in local currency and thus subject to windfall gains or losses from currency fluctuations, (2) annuities adjusted according

to domestic cost-of-living indexes, and (3) minimum annuities clearly excessive in low wage countries such as the Philippines. (See pp. 16 to 22.)

#### RECOMMENDATIONS

GAO recommends that the Secretary of State:

- Improve coordination of foreign national pay systems and wage schedules with the Department of Defense and other overseas agencies to the extent that (1)
  - joint wage surveys and uniform pay schedules are adopted in countries where both agencies directly employ foreign nationals, and
  - (2) -Defense wage rates are included in State Department wage surveys where Defense operates under indirect-hire arrangements.
- Monitor overseas wage setting more closely to insure that missions
  - have salary schedules that reflect private sector average pay or average pay ranges,
    - include the cost of severance in pay adjustments,
    - survey private sector jobs that represent the mission's work force as closely as possible, and
    - correct other wage setting errors such as occurred in Korea and Italy.
- Replace civil service retirement with prevailing local plans.

#### AGENCY COMMENTS

The Department of State agreed that more uniformity in foreign national wage setting was

desirable, that some wage setting procedures could be improved, and that civil service retirement should be replaced by prevailing local plans. The Civil Service Commission also agreed that offering civil service retirement to foreign national employees was not appropriate.



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ABBREVIATIONS

GAO      General Accounting Office

## CHAPTER 1

### INTRODUCTION

The U.S. Government employs about 178,000 foreign citizens at overseas posts and installations, at an annual cost of about \$1.5 billion. We are interested in how pay and benefits for these employees are determined and how the Government is dealing with rapidly increasing labor costs at many locations. In some cases foreign employees are becoming very costly. For example, the average pay and benefits for Japanese employees of the American Embassy, Tokyo, is \$17,000 a year, and at the Embassy in Bonn, West Germany, the starting amount for the lowest salaried white-collar German employee was about \$9,300 or as high as the starting grade 5 salary under the U.S. General Schedule pay system.

The U.S. Government's overall policy for setting pay and benefits in foreign areas is that agencies should follow local prevailing customs and rates. This report discusses how the State Department 1/ carries out this responsibility and the extent to which U.S. Government agencies offer similar pay and benefits to their foreign employees.

The Secretary of State establishes compensation plans for alien employees based on locally prevailing wages and practices for corresponding jobs, as set forth in Section 444 of the Foreign Service Act. The Act also authorizes other agencies with operations abroad to administer alien employee compensation plans under the same provision.

Embassy wages and benefits are usually determined by post officials under the direction of the personnel office. State Department Headquarters published a handbook of detailed wage survey procedures, approves each post's compensation plan and periodically conducts onsite reviews.

The State Department plan usually covers the employees of all U.S. agencies at the post. Posts may or may not

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1/Of all Government agencies the Department of Defense is the largest employer of foreign nationals. Its pay practices are discussed in our report, "Department of Defense is Overcompensating Its Foreign Employees" (FPCD-78-64, Aug. 2, 1978), prepared at the request of the Senate Committee on Appropriations.

coordinate their compensation plans with Department of Defense installations in the country.

#### SCOPE

We visited State Department posts and reviewed compensation plans in five countries: Korea, Japan, the Philippines, Germany, and Italy. We also obtained information on Department of Defense compensation plans in those countries, reviewed agency files, and held discussions with officials of the Departments of State and Defense and the Civil Service Commission.

We obtained written comments on this report from the Department of State and the Civil Service Commission, and their comments are incorporated where applicable. (See apps. I and II.)

## CHAPTER 2

### NEED FOR U.S. AGENCIES IN A COUNTRY

#### TO ACT MORE AS A SINGLE EMPLOYER

In each country we visited, the Departments of State and Defense coordinated local national pay rates differently. In the Philippines, for example, State uses a modified Defense wage schedule, but in Italy the two agencies conduct entirely separate wage surveys, sometimes in the same localities. Despite valid reasons to treat some wage matters separately, we believe U.S. Government agencies overseas should coordinate more closely to develop uniform compensation rates.

#### AUTHORITY TO SET RATES

The Foreign Service Act 1/ provides:

"(a) The Secretary [of State] shall, in accordance with such regulations as he may prescribe, establish compensation plans for alien employees of the Service: Provided, that such compensation plans shall be based upon prevailing wage rates and compensation practices for corresponding types of positions in the locality, to the extent consistent with the public interest.

"(b) For the purpose of performing functions abroad, other Government agencies are authorized to administer alien employee programs in accordance with the applicable provisions of this Act."

In adopting these provisions, the Congress expected U.S. agencies in a particular locale to establish uniform wage rates and employment practices. A House report on the 1960 amendments stated that the purpose of paragraph (b) above was to

"enable all Federal agencies employing such [foreign] personnel to operate as a single employer by providing uniform employment conditions for all alien employees of the Government in a particular foreign labor market area who are working under similar conditions."

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1/Section 444 of the Foreign Service Act of 1946, as amended by Public Law 86-723, Sept. 8, 1960.

A similar explanation appears in the Senate report on the amendment. At that time the Senate Committee on Foreign Relations considered designating the Secretary of State as the single Government official to prescribe wage schedules for all foreign employees, but rejected that idea after being given evidence that agencies were voluntarily cooperating.

#### MORE COORDINATION NEEDED

In 1974 we reported 1/ that diplomatic posts and military installations were using different wage rates (with State generally being the higher of the two) and following different employment practices. We concluded that voluntary cooperation among the agencies was not working satisfactorily and that the congressional intent was not being achieved.

The Department disagreed and reported that it had never interpreted Section 444 of the Foreign Service Act to require uniformity with military bases. The Department contended that working conditions and employment circumstances between diplomatic posts and military bases were frequently quite different. For example, in some countries Defense's work force is actually hired by the host government and provided to that agency under a government to government contract that diplomatic missions should not be involved in. Nevertheless the Department said it intended to pursue with the Department of Defense the idea of joint surveys and work toward greater uniformity of wages and benefits wherever feasible.

Unjustified disparities remain between agencies and, in our opinion, should be eliminated. The situations in each country we visited are discussed below.

#### Philippines

U.S. civilian agencies in the Philippines employ about 1,300 local nationals. State provides administrative services for most of the agencies and bases compensation for its own employees on Department of Defense wage schedules. Despite the apparent coordination many unjustified differences in the various compensation plans existed. For example:

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1/Letter to the Secretary of State, B-179700, Jan. 16, 1974.

- State, Defense, and the Veterans Administration wage schedules have a different number of grades and steps, and salary ranges and waiting periods vary between the bottom and top steps. Other small U.S. agencies in Manila, such as a Treasury disbursing office and the American Battle Monuments Commission, use variations of State and Defense schedules.
- During our visit in 1977 civilian agencies were paying over twice as much cost-of-living allowance as Defense because civilian agencies had increased the allowance when it was decreed by the Philippine government, while Defense decided to wait until the next wage survey.
- Yearend bonuses are 125 percent of 1 month's base pay with Defense, 100 percent with the Embassy.
- Civilian agencies grant 5 more holidays to Filipino employees than Defense.
- State, Defense, the Veterans Administration, and the Agency for International Development establish position classifications independently resulting in different pay for comparable positions.
- Unlike Defense, civilian agencies have no separate wage schedule for blue-collar employees. A State Department wage classification team concluded in 1976 that paying 316 blue-collar employees on a white-collar wage scale resulted in overpayment of about 25 percent.

Overall, State's wages averaged about 9 percent higher than Defense's for a selected sample of 12 comparable positions and about 5 percent higher than the Veterans Administration. Since wages are still relatively low in the Philippines the cost of these differences is not large. But employees of all U.S. agencies are paid considerably more than going rates in the country, and if the Philippine economy continues to grow these pay practices could become an expensive burden as has happened in other countries.

#### Korea

The Seoul Embassy participates in the Department of Defense wage survey but makes only limited use of Defense's data because the Embassy feels it has few local jobs in

common with Defense installations. To determine 1977 wages the Embassy separately surveyed a few higher level jobs and combined this data with that taken from the Defense survey. As a result the two agencies granted different average raises--23.6 percent by Defense and 26.25 percent by State.

The Embassy pays more than Defense although Defense already surveys higher paying Korean firms. In 1972 we reported that State's base pay exceeded Defense's base pay by 27 percent for selected positions common to both. A comparison of total compensation for selected jobs in 1977 showed State paid 25 percent more. Embassy officials maintain that the differences were justified by the greater job responsibilities and demands of the Embassy positions, despite comparable position descriptions. While there are some differences in duties and responsibilities between Embassy and Defense jobs, we do not agree that Embassy positions consistently have more responsibilities and demands. Accordingly, we do not believe the significant differences in pay are justified.

### Japan

The potential for State and Defense to standardize their pay systems in Japan is somewhat limited because the Government of Japan controls most personnel administration matters for Department of Defense Japanese employees. Technically, the Japanese government employs Defense's foreign nationals under a master labor contract, and wage adjustments are a matter of negotiation between the two governments. Negotiations are based on amounts granted annually to Japan's civil service employees which, in turn, are based on a nationwide wage survey.

Since the State Department is not subject to these indirect hiring and wage setting practices, it separately determines pay rates for Japanese employees of the Embassy. A wage specialist contracted by the Department conducted the 1976 survey which was updated by Embassy personnel in 1977. The Embassy has been largely successful in paying employees prevailing local rates using State Department procedures. The Embassy also reclassified some positions recently to align responsibilities with the correct level of compensation. Nevertheless more coordination with Defense should improve wage setting.

Wages for Defense and State employees are determined by different methods, but both are based on prevailing local



rates. However, for 17 positions judged comparable by Embassy personnel officials, the Embassy paid about 7 percent more than Defense. In part this is because the Embassy's survey is restricted to a few progressive firms in Tokyo while Defense's wages are ultimately based on the broad nationwide survey (7,500 companies in 1977) conducted by the Japanese government. The broad based survey provides a much more reasonable basis for setting pay than the Embassy's limited study, particularly since about a fourth of the Embassy's local personnel are employed outside Tokyo. Including data on comparable Defense positions in the Embassy survey would result in more representative data and more comparable wage rates.

### Germany

Local employment arrangements for State and Defense in Germany are similar to the arrangements in Japan. The Embassy directly hires and pays its personnel while Defense is bound by a status-of-forces agreement, an indirect hiring system, and negotiations with the host government over rates of pay. As in Japan, a contractor makes a wage survey every 2 years and Embassy personnel update the data in interim years. The Embassy restricts its survey to large and progressive firms with no coordination of rates with Defense. As a result the Embassy pays more for comparable positions. In eight such positions, comprising 13 percent of the local work force of the State Department and attached agencies, Embassy pay averaged 15 percent higher than Defense pay.

### Italy

In Italy both State and Defense are responsible for local employee personnel practices and compensation setting. But the agencies conduct entirely separate wage surveys even though they may have facilities located in the same areas and sometimes survey the same private firms. In fact, military officials in Italy claimed that firms were getting wage survey fatigue and refusing to participate in the separate Defense and Embassy surveys every year. As in other countries State salaries were generally higher than Defense salaries for comparable jobs. In Naples, where the Embassy and Defense both employ Italian citizens, Embassy pay was 4 percent higher for 11 selected comparable positions.

## CONCLUSIONS

The Congress expected that agencies overseas would coordinate their local pay plans more closely than they are now doing. In the five countries we visited, State Department and other agencies attached to the U.S. mission paid up to 25 percent more for the same jobs than the Defense Department. Posts maintain that their employees are subject to more demands and responsibilities or that they desire to be competitive with the largest and most progressive firms in the country.

We found no consistent support that demands on employees are appreciably greater in one agency or the other, although specific duties and responsibilities may differ in comparable positions. This matter had not been formally studied at the locations we visited. Unless measurable differences are objectively determined to exist, pay for comparable jobs in various agencies should be the same.

Prevailing pay practices are determined by surveys of the local economy, and Defense's larger and broader surveys result in more representative rates. Also, Defense usually has more resources and expertise for conducting surveys. For these reasons, embassies should rely more upon Defense wage surveys and assure that positions representative of embassy jobs are included in those surveyed. When it is impractical to participate in Defense surveys directly, as in countries where Defense is subjected to indirect hire arrangements, embassies should consider Defense rates when setting embassy pay.

In addition, we see no inherent justification for one government agency to model its pay after a select group of the largest and most progressive firms. The integrity of any prevailing rate pay setting mechanism depends on its ability to represent the rates of a reasonable cross section of establishments of various size in various industries. This is an underlying principle of domestic pay systems for U.S. Government employees, including foreign service officials, and should be applied to foreign national pay setting as well.

## RECOMMENDATIONS

We recommend that the Secretary of State improve coordination of pay systems and wage schedules with the Department of Defense and other overseas agencies to the extent that:

- Joint wage surveys and uniform pay schedules are adopted where both agencies directly employ foreign nationals. In countries where Defense is the larger employer it should be the lead agency for conducting the survey.
- Defense wage rates are included in State Department wage surveys where Defense operates under an indirect hire arrangement, as in Japan and Germany.

#### AGENCY COMMENTS

The Department of State agreed that more uniformity in wage schedules is desirable and pledged to work more closely with Defense toward that goal. However, State does not believe that total uniformity is feasible because, (1) Defense installations are basically industrial and blue-collar, whereas State posts are basically white-collar, (2) State's local national employees are higher calibre individuals than those normally needed by Defense, and (3) State in many countries offers U.S. civil service retirement which Defense does not. Because this extra benefit figures into the setting of salaries, State salaries are thereby reduced, but Defense salaries are not.

#### GAO Evaluation

We agree that some differences exist between State and Defense in employee duty and responsibilities. However, we believe that more uniformity of pay and benefits is feasible. While it is true that Defense installations are located in rural or suburban areas and employ more blue-collar employees, Defense's wage survey data remains a valid basis for setting State wages and benefits. First, Defense normally surveys many private sector firms in urban areas where State missions are located because rural areas have few comparable job positions. Secondly, Defense also has numerous white-collar employees, and samples and analyzes data separately for blue-collar and white-collar groups. Therefore, State Department missions would not be basing white-collar schedules on blue-collar wage data.

We have no basis for determining whether State Department needs and hires higher quality employees than Defense. However, where duties and responsibilities require greater skills, position classification procedures adequately allow for increased compensation.

The Department's statement that the use of civil service retirement results in dissimilar salaries between State and Defense refers to the fact that (1) many State posts, unlike Defense, offer civil service retirement to local employees, (2) State posts use a total comparability approach to setting compensation wherein the total cost of post pay and benefits equals the total average cost of private sector pay and benefits (see Chapter 3), and (3) the civil service retirement benefit is usually costlier than local separation plans. Therefore, a post may offer lower salaries than the private sector and Defense to make up for the fact that the post's retirement plan is more generous.

We agree that civil service retirement benefits are usually more generous than the private sector overseas. For this reason and others we are recommending in Chapter 4 that civil service retirement not be offered to State Department's foreign nationals.

In addition, the above circumstances suggest that post salaries tend to be lower than Defense salaries. But they are higher, and will increase even further under the total comparability formula when the posts' retirement benefits are reduced. This eventuality makes it even more necessary that State and Defense salaries be brought into line.

### CHAPTER 3

#### CLOSER MONITORING OF WAGE

#### SETTING TECHNIQUES NEEDED

State Department guidelines for setting wages are basically sound and contain a "total comparability" feature that should be used by other Federal pay systems. However, overseas missions did not always follow State procedures and improved wage setting would result if they did.

#### TOTAL COMPARABILITY USED

State guidance calls for adjusting foreign national compensation according to the total value of prevailing pay and benefits. Survey teams determine the difference between what Embassy and private firms pay for each pay item and benefit, net the differences, and make one adjustment to pay so that in total, State's pay and benefits equal the value of private sector pay and benefits. The chief advantage of this method is its ease and flexibility in setting total compensation at the proper amount without having to periodically adjust individual benefits on a piecemeal basis. We have recommended that similar "total comparability" adjustments be used to set wages and benefits for U.S. Federal employees 1/ and for Defense's foreign national employees. 2/

#### OPPORTUNITIES TO PATTERN AVERAGE PRIVATE SECTOR WAGES WITH AVERAGE MISSION WAGES

A key ingredient of any comparability wage plan is that average earnings in the private sector should be equated to average earnings (at each grade) of the government work force. This principle is used in the U.S. General Schedule pay system and has been recommended by us and the executive branch for the blue-collar Federal wage system as well. In response to our recommendations, the Department of Defense has also agreed to equate average private sector wages to the average wages of its foreign national work force.

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1/"Need for a Comparability Policy for Both Pay and Benefits of Federal Civilian Employees" (FPCD-75-62, July 1, 1975).

2/"Department of Defense Is Overcompensating Its Foreign Employees" (FPCD-78-64, Aug. 2, 1978).

State Department survey procedures are to base mission salary schedules on the average range of wage rates in the private sector. A survey team determines the high and low pay rate for each surveyed position, computes the average range, and uses the average as the basis for setting the pay rate at the top and bottom step in the mission salary schedule. For example, if the average range was 40 percent, then the top step at each grade level would be adjusted so that it was 40 percent above the bottom step. The Department prefers this method because it believes obtaining an accurate measure of average private sector rates actually paid would cost too much and be unreliable because of relatively small survey samples, particularly at smaller posts. (See State Department comments, app. I.)

We believe that State Department procedures are reasonable, given the resources usually available to measure prevailing rates. Basing mission salary schedules on the range of private sector rates can cause problems, however, unless data is also gathered to show how private sector employees actually fall in that range and how long it takes employees to progress through the range. Problems also arise when the mission does not adjust its salary schedule according to changes in the private sector range.

We found that embassies did not always follow State procedures. In Japan, for example, the Embassy was using a salary schedule having a 50 percent pay range at each grade although the survey showed the average private sector range was only 35 percent. Due to longevity increases, the average Embassy employee is already paid about 35 percent above the step one minimum. Therefore, when the comparability adjustment is made, the average Embassy employee is given earnings equal to the maximum private sector rate. By earning additional longevity increases, employees can earn 15 percent more than the maximum earnings of their private sector counterparts. If State Department procedures had been followed, we estimate 1977 wage costs would have been reduced by as much as \$820,000.

#### Agency comments

State replied that in this particular case the contractor who did its survey was convinced, despite the data showing a 35 percent range, that a larger range was appropriate. While subjective judgments are necessary in wage data analysis, we believe a decision costing over \$800,000 a year should be based on documented survey results. State added that the matter would be thoroughly reviewed again.

NEED TO PROPERLY REFLECT THE COST OF  
RETIREMENT AND SEVERANCE IN  
ANNUAL ADJUSTMENTS

Embassy comparability adjustments are based on the comparative value of total compensation--base pay, allowances, and fringe benefits--in the private sector compared to the Government's cost of the same items for local national employees. Thus accurate overall comparability adjustments require that these items be stated and analyzed on similar terms.

In Japan, the private sector states retirement cost as a percent of base pay, whereas the Embassy states costs as a percent of gross pay (base pay plus allowances) and compares its cost to the private sector on this basis. Since gross pay is larger, the Embassy is understating the actual percentage cost of retirement in its total compensation package. If the correct percentage had been used, base pay in 1977 would have been reduced 8 percent or about \$394,000. The Department agreed to take this factor into account in future salary adjustments.

The above comparison of retirement costs is complicated further because private sector retirement plans--and costs--also sometimes include a severance entitlement. But the Embassy does not include severance costs in the compensation analysis, thus further understating the value of the Embassy's compensation package and unnecessarily adding to the amount of the annual adjustment.

Agency comments

State commented that because of the difficulties in placing a true and meaningful value on severance pay (due to the fact payment can be precluded under certain types of separations), State advocates revisions to severance benefits separate from adjustments to regular compensation. In areas where dual retirement and severance pay benefits are common--as in Japan--the entire retirement/severance pay package of the mission is to be compared with locally prevailing plans. Had this guidance been followed in Japan, considerable cost savings would have resulted.

SURVEYED JOBS NOT REPRESENTATIVE  
OF THE WORK FORCE

Key positions which represent the entire Embassy work force are selected for survey to determine private sector pay

for every individual job. Thus, the representativeness of the jobs is a key factor in determining whether the work force will be paid in line with prevailing rates.

At some locations the work force was not well represented by the jobs that were surveyed. In Germany most survey positions represented jobs in the Voice of America whose work force was less than 10 percent of the total work force. Also survey positions such as construction engineer and exhibit specialists were not filled or had only one person employed. We identified several other positions such as accountants, personnel specialists, cashiers, and teletype operators which would have better represented the work force and we believe would have counterparts in the private sector.

In the Philippines, Embassy pay ranges are based on the Department of Defense survey and wage schedules, but less than 10 percent of the State and related civilian agency work force was represented by survey jobs. In Korea, Embassy officials used some of Defense's wage data but at the same time believed the survey jobs did not adequately represent positions in the Embassy.

#### Agency comments

State agreed with the importance of survey job selection and said it would place more emphasis in this area.

#### OTHER INSTANCES WHERE STATE DEPARTMENT GUIDANCE NOT FOLLOWED

In Korea the Embassy's November 1976 wage adjustment was based mainly on the increases granted by the Department of Defense. But, other than for a few positions separately surveyed by the Embassy, no recognition was given to the actual pay ranges for particular jobs although this is required by State's guidance. The Embassy simply increased wages at each grade by a percentage similar to that granted by Defense. Since the Embassy's pay is already higher than Defense's (see p. 6), the disparity will increase every year that the Embassy uses this wage adjustment technique.

In Italy the Embassy's compensation plan included a double payment for meals. Apparently through oversight an allowance for meals was included as both an allowance and



a part of salary. We estimated that the cost of this overpayment--which began in February 1977 and had not been corrected by May of 1978--is \$132,000 annually.

#### Agency Comments

State reported that in Korea a subsequent wage adjustment has substantially reduced the disparity between Defense and Embassy pay, and that a revised compensation plan in Italy will eliminate the double payment for meals.

#### RECOMMENDATIONS

We recommend that the Secretary of State monitor overseas wage setting more closely to ensure that missions are complying with Department guidance. In particular:

- Salary schedules should reflect private sector pay ranges (at large posts or posts where joint Defense/State wage surveys are conducted, State should consider the merits of equating private sector and mission average rates).
- The costs of severance benefits should be included in compensation adjustments, whether separately or in conjunction with total comparability adjustments.
- Jobs surveyed in the private sector should represent the work force as nearly as possible.
- Other departures from Department guidance, such as those reported in Korea and Italy, should be corrected.

## CHAPTER 4

### NEED TO DEVELOP MORE APPROPRIATE

#### RETIREMENT PLANS

In many countries the United States has departed significantly from local prevailing compensation practices by enrolling foreign national employees in the U. S. civil service retirement system. This practice seems less common now than it was several years ago (the Department of Defense stopped enrolling employees in 1951 and now follows local retirement and severance practices), but still continues at many State Department posts.

Because the civil service system is essentially domestic in nature, its use for foreign employees causes several inequities, especially in countries where the standard of living and economic conditions are substantially different than in the United States. Recognizing this and other disadvantages, the State Department has for several years urged its posts to adopt local practices, but many have been reluctant to do so. Records of the State Department were not available to readily determine the practices followed at every post or how many employees are enrolled worldwide, but in April 1978, 72 posts were providing civil service retirement, 38 were using only local plans, and 8 were using a combination of civil service and local plans. At Asian and Pacific posts, about 4,500 employees or 76 percent of the foreign work force, were enrolled.

Use of civil service retirement for foreign employees is difficult to justify in terms of the basic principle of Section 444 of the Foreign Service Act which states that compensation plans should be based on local practice. Based on its studies of post separation benefit practices, the State Department should accelerate replacement of civil service retirement with local prevailing plans.

#### STATE DEPARTMENT REVIEW OF SEPARATION BENEFITS

In 1942 Public Law 77-411 (56 Stat. 13) authorized the enrollment of foreign employees in the civil service retirement system. Before this no retirement benefits were available to these employees. In 1960 the Foreign Service Act of 1946 was amended to allow participation in host government

social security and related plans as long as they were prevailing practice and not counter to U.S. laws. The State Department officially encouraged participation in host country plans, but by 1973 posts in fewer than 20 countries were using them. Most were using the civil service retirement system and many continue to do so today.

In 1973 the State Department began a review of the justification for the use of civil service retirement, and suggested that the posts use local retirement programs whenever possible instead of the civil service system. The Department asked the posts to review their retirement plans and report any compelling local circumstances that justified indefinite continuance of civil service retirement. The results of the inquiry were not summarized but the overwhelming response of the posts was to retain civil service benefits in lieu of changing to local plans.

In 1976 the Department reiterated its policy of relying primarily on local plans and asked each post that was not using them to conduct a study and report on the feasibility of enrolling foreign employees in host government or other prevailing plans. The Department cited several arguments for local plans:

- Local separation plans are based on local conditions while civil service cost-of-living adjustments are based on U.S. prices. Also, the minimum civil service annuity is clearly excessive in many countries.
- Currency exchange rate fluctuations subject foreign civil service annuitants to financial penalties or windfalls.
- Local plans are prevalent throughout the world and benefits are improving each year. Many plans have collateral health protection benefits not available under civil service.

The Department stated it would continue to review post retirement policies, monitor efforts to enter local plans, and advise and assist in the consummation of necessary agreements and contracts for local separation plans.

Many posts, however, objected to adopting local plans. Objections most often given were that (1) generous civil service benefits were preferred by employees and were a

good recruiting incentive, and (2) host government plans did not exist or would be difficult to enter. The Department generally disagreed with these objections. It pointed out that the benefits from employment with the United States should only be comparable to local benefits, not better, if the posts are to comply with Department policy and the Foreign Service Act. The Department also stated that posts should not ignore local practices simply because there was no single separation plan followed by most employers. In such cases posts should adopt the most commonly used benefit. The Department acknowledged that civil service might need to be offered at some locations, but that many posts had not thoroughly considered the alternatives, particularly for newly hired employees.

Based on our work in various countries we agree with the Department's conclusions. Use of civil service at these locations is resulting in double separation coverage, excessive benefits to some annuitants, excess costs to the Government, and varying compensation policies among different government departments in the same country. The retirement and severance practices in each country we visited are discussed below.

#### Korea

Prevailing practice of major employers in Korea is to provide a one-time lump-sum severance payment at the time of separation. United States Government agencies also provide the benefit which at the end of a career is a significant amount--for example, after 25 years of service, it is about 50 months' base pay. But in addition to offering severance, the Embassy has also enrolled Korean employees in the civil service system since 1957. About 200 are now enrolled and will be able to draw their normal annuity plus a lump-sum severance. We estimate that a typical employee who separated after 25 years of service and invested his lump-sum severance at a conservative going interest rate would receive, from that investment plus civil service, 30 percent more than his base salary when he worked.

At the time of our visit to Korea, Embassy officials agreed that offering both severance and civil service retirement is an overly generous separation plan. Since then the post no longer offers civil service retirement to new employees.

## Philippines

As in Korea, Defense and civilian agencies in the Philippines offer different retirement plans. Defense employees accrue a lump-sum separation credit and are enrolled in the Philippine social security system in accordance with prevailing practices in the private sector. Civilian agencies allow employees to join the U.S. civil service retirement plan. Virtually all eligible employees are enrolled in civil service because of the attractive annuity payments. Not only does use of civil service ignore the local prevailing social security system, it is more costly and provides retirement benefits which are grossly out of line for the country and even exceed many employees' base salaries.

The Department of Defense retirement plan costs 11.9 percent of base pay (8.3 percent for separation accrual and 3.6 percent for social security contributions). An agency's contribution to the civil service retirement fund is 7 percent, but the full cost to the Government is much more. On the basis of actuarial studies the cost of civil service to the Government has been estimated at about 20 to 25 percent of payroll depending upon assumptions of future pay raises and inflation. State uses 23 percent when comparing the cost of Government and private sector retirement plans. Using 23 percent, we estimate the retirement plans of civilian agencies in the Philippines are 11.1 percent more costly than the Department of Defense plan. Conversion from civil service to Defense's prevailing practice plan would save about \$228,000 a year.

In 1974 Public Law 93-273 provided that minimum monthly civil service annuity payments to retirees, surviving spouses and children would be equal to the smallest social security "primary insurance amount." That amount is now \$122 a month for new recipients, modest by U.S. standards but very generous in a country such as the Philippines where earnings are much lower. For example, in 1977 about 30 percent of the Mission's Filipino employees earned less base pay than the civil service minimum. If eligible to retire, these employees would receive more income from the minimum annuity than from their base pay.

According to Civil Service Commission records about 11,500 civil service annuity payments totaling \$37 million are made to foreign nationals worldwide. About 2,200 of

these are based on the minimum annuity provision of the law. Over half of those 2,200 payments, amounting to almost \$2.2 million were to recipients in the Philippines. Had those particular payments been earned annuities--that is based on the employee's years of service and salary--instead of the legislated minimum, total payments would have been 38 percent or \$827,000 less per year.

Civil service retirement annuities are also generous relative to median family income in the Philippines. In 1976 the average annual civil service annuity in the United States was \$5,940 or 43 percent of the nation's annual median family income of \$13,700. In the Philippines the average annual annuity was \$1,844 or 286 percent of that country's annual median family income of \$643. Even the minimum annuity of \$1,296 (\$108 X 12 months) in 1976 was 202 percent of median family income.

Also, currency fluctuations affect foreign annuity payments because an employee's annuity is stated in dollars but paid in local currency. Thus, a retired employee receives his annuity at the current exchange rate, although the annuity may have been earned at a different rate.

In the Philippines devaluation of the peso has benefited Filipino retirees. For example in 1969 \$1 equaled less than 4 pesos; by 1978 it equaled more than 7 pesos. Thus, the retiree received almost twice as many pesos in 1978 as he or she "earned" in 1969 though the annuity stated in dollars did not change. Of course annuitants can also be penalized if the local currency is appreciating relative to the dollar. However, some relief to this problem has been provided by another law enacted in 1976 whereby the State Department can make a supplemental annuity payment under certain circumstances to foreign retirees to offset exchange rate losses.

Despite the inequities that civil service retirement has caused, Embassy officials in Manila felt that it was a recruiting aid and they preferred to continue the program. The Embassy had not responded to the 1976 State Department study request regarding the adoption of local plans.

### Japan

Virtually all eligible employees at the U.S. Embassy in Japan are enrolled in the civil service retirement program.

Employees are also eligible for a substantial lump-sum separation payment up to 34 months of pay when they leave U.S. employment. Prevailing local retirement plans in Japan are a lump-sum separation payment, Japanese government social security, and a supplemental pension.

Because civil service annuities are calculated in dollars and adjusted by cost of living indexes in the United States, about 100 retired Japanese employees have suffered a decline in relative value of their civil service annuities. In the last 5 years consumer price indexes have increased an average of 13.1 percent annually in Japan and 7.7 percent in the United States. Also, since June 1977 the value of the dollar has declined over 30 percent relative to the Japanese yen.

Embassy officials stated that developing a retirement plan more in line with prevailing practices was deferred because of higher priority projects. They also considered civil service retirement a recruiting inducement. Based on our review, the Embassy agreed to develop a recommendation on alternative retirement plans.

#### Germany

The Embassy's local personnel retirement policy in Germany basically conforms to prevailing practice. This consists of participation in a mandatory German social security system and a supplemental retirement plan patterned after the practices of German employers. In anticipation of reliance on the social security programs the Embassy stopped enrolling local employees in the U.S. civil service system in 1965. Those enrolled in the system at the time were allowed to stay in it. In April 1977 there were 231 Department of State and U.S. Information Service employees under civil service, many of whom were expected to retire in 5 to 10 years.

#### Italy

Most of State Department's local employees are enrolled in civil service although there is a nationwide mandatory social security system for Italian workers. As a result of the State Department's 1976 request, the Rome Embassy considered adopting Italian social security which was acknowledged to offer similar or slightly better benefits than civil service. The Embassy proposed that all new employees and those present employees who could qualify for partial

benefits under both retirement systems would be enrolled in Italian social security. Employees over 45 would not be converted to social security because they would not be able to fulfill the maximum years of service required under the Italian system before reaching the Embassy's mandatory retirement age. Also current employees would not be converted to social security until they had been enrolled in civil service for 5 years and thereby eligible for a minimum annuity at age 62. The State Department agreed with this plan but the Embassy then objected because (1) employees' annuities would be larger at retirement if they remained in civil service and (2) the Italian government might want Embassy compliance with other labor laws. The Embassy therefore planned to reanalyze the costs and benefits involved and make specific recommendations on changes.

#### CONCLUSIONS AND RECOMMENDATIONS

We believe the State Department is correct in its recognition of the advantages of adopting local retirement/severance plans in lieu of using civil service. But despite the Department's efforts for nearly 5 years progress has been impeded primarily because of resistance from overseas posts. The Department of Defense has followed local practices and used local plans successfully for several years in many of the same countries that U.S. Embassies offer civil service.

We recommend that the Secretary of State give more emphasis to phasing out civil service and replacing it with whatever practice is followed in each country. In the countries where posts have made no transition plans, steps should be taken as soon as possible to stop enrolling new hires in civil service, followed by planning of appropriate treatment for employees now enrolled.

#### AGENCY COMMENTS

The State Department and Civil Service Commission agreed that foreign national employees should not be enrolled in the U.S. civil service retirement system. State added that progress in withdrawing civil service appointment authority at more posts had increased recently and that this progress should accelerate in the future.





## DEPARTMENT OF STATE

Washington, D.C. 20520

October 18, 1978

Mr. J. K. Fasick  
Director  
International Division  
U. S. General Accounting Office  
Washington, D. C.

Dear Mr. Fasick:

I am replying to your letter of September 1, 1978, which forwarded copies of the draft report: "State Department Should Improve Foreign National Wage Setting."

The enclosed comments were prepared by the Deputy Assistant Secretary for Personnel.

We appreciate having had the opportunity to review and comment on the draft report. If I may be of further assistance, I trust you will let me know.

Sincerely,

A handwritten signature in cursive script that reads "Roger B. Feldman".

Roger B. Feldman  
Deputy Assistant Secretary  
for Budget and Finance

Enclosure:  
As stated

GAO DRAFT REPORT: "STATE DEPARTMENT  
SHOULD IMPROVE FOREIGN NATIONAL WAGE SETTING"

The Department of State supports the objective of the title of the report of improving foreign national wage setting. State also supports the general thrust to attempt to adhere more closely to prevailing practices in compensating foreign nationals.

In the interest of fostering greater uniformity in the administration of foreign national employee programs overseas, the Department plans to propose the institution of regular periodic consultation sessions on foreign national employee management and compensation issues with all USG agencies employing foreign nationals overseas.

The Department agrees fully with several recommendations. There are several other recommendations with which the Department is unable to agree.

The Department's comments on the recommendation contained in the report are set forth below:

CHAPTER 2 - RECOMMENDATION No. 1

-----Improve coordination of foreign pay systems, and wage schedules with the Department of Defense and other agencies to the extent that:

-----joint wage surveys and uniform pay schedules are adopted in countries where both agencies directly employ foreign nationals.

COMMENT ON RECOMMENDATION

The Department is committed to the principle of coordinating its foreign national salary and benefit surveys with Defense and other agencies. The Department agrees fully with the opinion that more uniformity in establishing appropriate pay schedules is desirable and pledges to work

more closely with Defense in an effort to bring the greatest degree of uniformity in foreign national pay setting where both agencies employ direct hires. The heavy workload within the Department has prevented detailed discussion of the subject with Defense in Washington.

However, total uniformity of pay and benefit structure is not normally feasible. This view is based on the following considerations:

- (1) The Department is thoroughly convinced that compelling justification exists for the differences in the sampling of employers used by Defense and State in the conduct of surveys. The significant differences in the nature as well as the location of their respective operations automatically establishes a requirement for differences in the sampling of employers. An analogy to a Defense installation and a State mission can easily and fairly be drawn between an industrial plant operation located in a rural area and its headquarters office located in the capitol city. Defense installations are in competition with private industrial and quasi-industrial operations in the country which employ a predominant blue-collar workforce. Just the opposite is true of State missions at which white collar employment dominates. It is our distinct impression that differences in pay and benefits often exist for the same job between a plant operation and its headquarters office. The Department's sampling of employers therefore is designed to ensure that State missions pay salaries comparable to their competitors. The Department of Defense sampling achieves the same result.
- (2) Another equally valid point relates to the type and calibre of employee being sought by Defense and State. The Department is convinced

that the type and calibre of individual needed at State missions is higher than normally needed at large Defense installations. As examples;

- a) State missions have a significantly greater need than Defense for persons whose educational and cultural backgrounds make them capable of effectively meeting the public and projecting a favorable image of the USG. Very few positions at State missions are sequestered to the extent of having no contact with the public whatsoever. Many positions of State, ICA and AID require extensive contacts with high ranking host government officials and private businessmen in which they are responsible for laying the groundwork for important decisions while at the same time projecting a favorable image of the United States.
- b) Overall, State missions have a significantly greater need for bilingual ability among employees than Defense installations. This skill is not found to the extent needed by State in the types of employers surveyed by Defense.
- (3) In many areas, State missions continue to use CSR appointments which are not provided by Defense. In measuring the value of comparable retirement benefits, the use of CSR by missions usually results in a substantial reduction in salaries reported by employers surveyed. No such reduction is involved in the development of Defense pay schedules.

#### CHAPTER 2 - RECOMMENDATION No. 2

-----Defense wage rates are included in State Department wage surveys where Defense operates under an indirect hire arrangement, as in Japan and Germany.

COMMENT ON RECOMMENDATION

In the interests of achieving greater uniformity among USG agencies, the Department concurs in the above recommendation. Our instructions to the field will be revised accordingly. Further, the Department will also ensure that separate benefit payments paid by missions and Defense in the same locality be similar not only in kind but in benefit level wherever feasible.

-----

The Department would also like to present its comments on the points which form the basis for the above Chapter 2 recommendations. These comments are set forth below.

The Philippines

The conduct of a wage survey in accordance with State procedures was planned late in 1978 to conform to Defense's schedule. Because of the protracted negotiations of the Base agreement with the Government of the Philippines, it was considered prudent to delay the planned survey and continue to apply the salary increases granted by Defense to the mission's foreign national pay plan. It is expected that most of the disparities in pay treatment between State and other agencies mentioned in the report will be corrected as soon as State conducts its own survey, hopefully next year. At that time, Veterans Administration and American Battle Monuments will be encouraged to adopt a joint civilian agency plan. State, AID, ICA, USDA, and DoD attache groups by interagency agreement will use the same position classification system. Other civilian agencies will be encouraged to adopt the same classification system. At that time, consideration will be given also to establishing a separate pay plan for blue collar employees of the mission.

Korea

The latest surveys of Defense and State in Korea considerably narrowed the differential of 25 per cent between a sample of comparable mission and Defense positions mentioned

in the report. Recently, the Department approved an increase based on a contractor-conducted survey averaging 11% whereas Defense's increase reportedly averaged 26%.

### Japan

The smaller sampling of employers used by State compared to Defense is considered justified. The Department however fully agrees that normally rates paid by employers at all constituent post localities should be used in developing any country-side pay plan. The subject will be discussed with the post and revised survey procedures developed for use in the next survey.

The Department has considered enlarging its sampling of employers particularly at large posts where salary costs are high. Experience has shown that enlarging the sampling frequently does not provide a proportional increase in data. For example, often even a large firm may provide job matches on only one-half of mission key positions. After surveying 20 or so firms, the additional firms are usually smaller and therefore provide much less useable data. Every effort will be made however to expand the sampling of employers wherever a significant amount of data can be obtained.

### Italy

The Department will take steps to ensure greater coordination of future survey activities with Defense in Italy.

### CHAPTER 3 - RECOMMENDATION No. 1

-----Overseas posts should be directed to ensure that:  
-----their salary schedules are designed so that  
          average compensation at each grade equals  
          average private sector.

### COMMENT ON RECOMMENDATION

Adoption of the foregoing approach in determining wage increases for Foreign Service nationals on a world-wide basis is not considered feasible.

The approach was considered, but rejected, as a basic survey procedure in connection with the development of a forthcoming revision in State wage-setting instructions. Several important factors militate against adoption of such a procedure.

- (1) The sampling of employers normally used by State missions is considered too small to provide statistically valid results through the system proposed. It is recognized that the system proposed is used in setting salaries of Americans under the General Schedule and would also not be inappropriate for DoD installations surveying 90 to 100 employers in setting the salaries of thousands of employees in a locality. However, State missions having, say, 200 foreign national employees may sample 20 or so employers. Often only five or so employers are surveyed at the smaller posts (having perhaps 5 to 10 employees) or at post localities where there is a paucity of data available (some African and East Asian posts, for example). Such a limited sampling of employers is certainly more susceptible to distortions brought about through the not uncommon occurrences of changes in the employers surveyed, changes in key positions surveyed, and/or individual personnel changes brought about by retirements, promotions, recruitment, reorganizations, etc. Any of these factors or, worse yet, a combination of several could substantially distort the new average and invalidate the results. Such changes as mentioned above would not normally affect the results of a Defense survey in which 90 to 100 employers are surveyed and very substantial numbers of individual actual rates are reported and weighted.
- (2) The proposed approach would require a significant increase in workload at our missions abroad. Currently, the Department

collects data on the salary ranges among employers surveyed for comparable positions. Under this system, it is not necessary to collect data on actual rates paid to personnel nor the number of incumbents at each actual rate, as would be required under the proposed method. The proposed change would dramatically add to contractor survey costs due to lengthening of the interview process and computation time. Where missions conduct their own surveys considerable extra time would be required to complete the survey compared to current procedures. Personnel officers have a difficult time allotting the necessary time to conducting survey now. This additional requirement coupled with world-wide personnel cutbacks would further minimize the Department's limited capability of conducting in-house surveys.

The report cites as the example of the need for the above proposed change the situation uncovered in Japan. It is clear from the survey results that the average range among employers surveyed in the 1976 survey was 35% and the average range used by the mission is 50%. The contractor who proposed establishment of the range however was convinced based on conversations with employers surveyed that despite the data, it was clearly the long standing practice among Japanese employers to give small annual increases throughout each employee's career. As an example, it is reported that a chauffeur with long service can earn more than some starting professionals. This practice in the contractor's opinion superseded the actual maximum rates reported by employers. Therefore, a schedule with 20 steps of only 2.5% each was considered to more appropriately reflect prevailing pay practices than that reported by employers. The Department saw sufficient legal basis for the proposal and approved the recommendation. The entire matter will be reviewed thoroughly again because of the concerns expressed in the report.



CHAPTER 3 - RECOMMENDATION No. 2

-----Ensure jobs surveyed in the private sector represent the workforce.

The Department agrees with the recommendation. Selection of jobs surveyed which best represent the mission's workforce has been a basic tenet in the job selection process. Greater emphasis will be placed on the point in the forthcoming revision in our wage-setting handbook. In the meantime, all contractors will be briefed to ensure compliance.

CHAPTER 3 - RECOMMENDATION No. 3

-----Revise Department wage survey procedures so that the true cost of retirement and separation pay plans are considered in comparability adjustments.

While totally agreeing in concept with the recommendation, the Department sees no need to revise its regulations to ensure equity in this connection. The instruction in the Local Employee Compensation Handbook of not making any adjustments for differences in severance pay benefit between the mission and an employer is cited as evidence that severance pay costs are not taken into account.

For the past several years, the Department has been reviewing during its salary surveys all benefit plans for foreign national employees. Because of the difficulties in placing a true and meaningful value on severance pay (due to the fact that in most cases payment is precluded under certain types of separations), the practice of making no adjustments to pay has been used where differences exist between the benefit level of the mission's severance pay plan and that paid by an employer surveyed. However, where the mission's severance pay plan exceeds local law or prevailing practice, a downward adjustment of the benefit level of the mission's severance pay plan is effected.

In addition, in areas where dual retirement and severance pay benefits are common, the entire retirement/severance pay package of the mission is compared with locally prevailing plans. If it is determined that the combination

of CSR and severance pay exceeds local practices, the Department has imposed an appropriate ceiling on further accumulation of severance pay benefits for employees under CSR. Thus, the Department does equate its severance pay levels with that prevailing locally, not in the comparability adjustment process in development of rates but in establishing the actual benefit levels of the mission's severance pay plan.

As further evidence of the lack of comparability adjustment, the report cites the situation in Japan in which CSR costs are a percentage of gross rates whereas private employer retirement costs are a percentage of base. The 23% costs of CSR is being phased in---the 1978 costs being 16%. The Department is aware of the differences on the base for computing CSR versus host government social security and will take that factor into account in determining the final adjustments to pay in comparing respective systems.

#### CHAPTER 3 - RECOMMENDATION No. 4

-----Review the wage adjustment practice of overseas posts to ensure that they are following Department guidelines.

The Department concurs fully in the recommendation. With regard to Korea, the report states that since the mission's salaries are already higher than Defense, the disparity will increase by continued application of the average percentage increase which DoD obtains in its surveys to the mission's pay plan. As mentioned in our comments on Chapter 2 recommendations above, this disparity has been substantially minimized by subsequent developments.

With regard to Italy, a State contract team recently completed a salary survey which is now being reviewed in Washington. The separate allowance for meals will be eliminated as of implementation of the revised local compensation plan.


CHAPTER 4 - RECOMMENDATION

-----Replace civil service retirement plans with prevailing local plans.

COMMENT ON RECOMMENDATION

The Department concurs fully in the recommendation. Whereas progress in this connection for some years was slow, progress has shown marked improvement over the past year. At present, CSR appointment authority has been withdrawn from 50 posts (over 1/3) throughout the world.

The pace should accelerate soon by virtue of the anticipated passage of legislation which will lift the ceiling on the amount of leave which can be provided to foreign nationals.



Robert S. Gershenson  
Deputy Assistant Secretary  
for Personnel



UNITED STATES CIVIL SERVICE COMMISSION  
 BUREAU OF RETIREMENT, INSURANCE, AND OCCUPATIONAL HEALTH  
 WASHINGTON, D.C. 20415

IN REPLY PLEASE REFER TO

YOUR REFERENCE

OCT 13 1978

Mr. H. L. Krieger  
 Director, Federal Personnel and  
 Compensation Division  
 United States General Accounting Office  
 Washington, D.C. 20548

Dear Mr. Krieger:

This is in response to your request for our comments on the General Accounting Office's draft report entitled "State Department Should Improve Foreign National Wage Setting."

Your letter of August 31, 1978 requested that we comment on Chapter 4 of the report, "Need To Develop More Appropriate Retirement Plans." This Chapter recommends that the State Department give more emphasis to phasing out U.S. Civil Service Retirement (CSR) coverage for their foreign national employees and replacing it with the practices followed in the various countries.

Three principal reasons are cited in the report for eliminating CSR and using local plans instead:

- (1) annuities are stated in dollars but paid in local currency and thus subject to windfall gains or losses from currency fluctuations;
- (2) annuities are adjusted according to our domestic cost-of-living indexes;
- (3) minimum annuities are excessive in low wage countries such as the Philippines.

Since the U.S. Civil Service Retirement program is closely tied to our own economy by way of cost-of-living increases and the Social Security minimum, the systematic use of the program in other countries creates both inequities and excessive benefits. As the report points out, the Defense Department has successfully made the change to using local retirement plans in lieu of CSR. Since 1952, as a matter of policy, the Defense Department has given local aliens excepted indefinite appointments thereby excluding them from CSR coverage. The State Department has encouraged the use of local plans instead of CSR, but has left appointment and retirement coverage matters to the individual embassy.

THE MERIT SYSTEM—A GOOD INVESTMENT IN GOOD GOVERNMENT

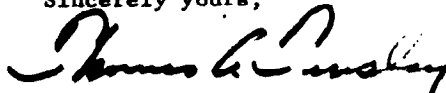
The guaranteed minimum annuity provision as it applies to non-citizen/non-resident annuitants is of particular concern. The rationale for the provision (5 U.S.C. 8345(f) ) is that Federal employees are generally covered under either Social Security or CSR, and that the employee whose work is covered under CSR should receive no less in retirement benefits than he or she would receive if the employment had been covered by Social Security. However, non-citizen/non-residents are excluded from U.S. Social Security coverage, so the rationale does not apply to them.

We have encountered numerous cases of excessive annuities in these low income countries as a result of the minimum annuity provision. Because former employees in such situations may receive more in annuity benefits than they can earn while employed, many retire rather than continue to work. In addition, we have encountered problems with individuals in low wage countries fabricating evidence of Federal employment and Civil Service Retirement coverage in order to take advantage of this minimum annuity provision.

We estimate that payments to non-citizen/non-resident annuitants under the guaranteed minimum provision are made at an annual cost to the retirement fund of about \$2,400,000.

Thank you for the opportunity to comment on this draft report. I hope this information is helpful to you.

Sincerely yours,



Thomas A. Tinsley, Director  
Bureau of Retirement, Insurance,  
and Occupational Health

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