The original documents are located in Box C37, folder "Presidential Handwriting, 4/6/1976" of the Presidential Handwriting File at the Gerald R. Ford Presidential Library.

EXECUTIVE OFFICE OF THE PRESIDENT
OFFICE OF MANAGEMENT AND BUDGET
WASHINGTON, D.C. 20503

APR 6 - 1976

MEMORANDUM FOR: THE PRESIDENT

FROM: JAMES T. LYNN

SUBJECT: Forecast of Federal employee pay and annuity increases

Jim Connor tells us that you were interested in Hastings Keith's recent Washington Star article concerning the 1% add-on in Federal annuities. We strongly agree that the add-on provision should be eliminated and, as you may recall, the budget indicated you would propose doing so. Your March 24 Message to the Congress urges eliminating the add-on and fully meets the objections raised by Mr. Keith.

In reviewing the Keith article, you also asked what is forecast for next year in Federal employee pay and retirement increases.

A 5.4% increase in annuities became effective last month. Preliminary estimates of probable increases for the majority of Federal annuitants, civilian and military, are:

	% Increase	Full-year cost
December 1976..........	5.4	$795 million
September 1977.........	5.5	$911 million

These annuity increases will be 1% lower if the add-on provision is eliminated as urged in your Message. Also, as you probably know, these increases are related directly to the CPI, and will be lower if the CPI increases are lower than the current budget projections.

For pay increases, the October 1977 forecast is as follows:

	% Increase	Full-year cost
White collar........	8.6	$2,157 million
Military............	8.6	$1,903 million
Blue collar.........	3.4	$ 164 million

Since Federal pay is based on comparability with the private sector, these increases to some degree reflect the projected rate of inflation. If the actual rate of inflation is less than now projected, these increases may also be somewhat lower. The estimates will be reviewed as part of the spring preview exercise next month. The blue collar estimate assumes enactment of the Federal Wage System reforms recommended by the Rockefeller Panel.

THE WHITE HOUSE
WASHINGTON

Dick Cheney

Powerful arguments for immediate change.

What is forecast for next year in federal employee pay & retirement increases?

THE WHITE HOUSE

WASHINGTON

March 22, 1976

ADMINISTRATIVELY CONFIDENTIAL

MEMORANDUM FOR: JAMES T. LYNN

FROM: JAMES E. CONNOR JEC

SUBJECT: 1 PER CENT ADD-ON

The attached newspaper clipping was returned in the President's outbox with the following notation:

> "Powerful arguments for immediate change.
>
> What is forecast for next year in federal employee pay and retirement increases?"

Please follow-up with appropriate action.

cc: Dick Cheney

The astonishing cost of that 1 per cent add-on in federal pensi

By Hastings Keith

)n March 1, the pensions of millions of
leral retirees moved up again. This in-
ase, mandated by the Congress in 1969,
s intended to allow the retiree's pension
keep pace with increases in the Consum-
Price Index — but the fact is that since
enactment in 196^ it has overcompen-
ed federal retirees by almost $1 billion.
The "1 per cent add-on," or "kicker," as
is sometimes called, was intended to
npensate for the time-lag that occurs
ween the actual cost-of-living increase
l the effective date of the adjustment.
So the amendment adds 1 per cent to the
st of living formula each time an in-
ase takes place. The problem arises —
l the overcompensation occurs — be-
use Congress did not anticipate the fre-
ency of the adjustments, and apparently
not realize that the 1 per cents become
ermanent part of the pension, com-
nding the benefits.

'he nature and extent of the
rcompensation is so mind-boggling that
ther the federal retiree nor the public
Congress seems to grasp its signifi-
ice.

nasmuch as my own pension as a re-
d congressman with 20 years of federal
vice is quite typical of that of the upper-
el Civil Service and military retiree,
e are its significant features:

'he pension has jumped in three years
m $1,560 a month to $2,200 a month — and $200 of this $2,200 represents the 1 per cent add-ons. Thus the pension has outpaced the cost-of-living increase.

- If the cost of living goes up at a 6 per cent rate per year, my pension in 15 years (at the end of my life expectancy) will be $6,000 per month and $1,000 of this will be above the cost-of-living increase.
- At a 6 per cent annual rate of inflation, I will have received — solely as the result of the 1 per cent add-on — a total of about $30,000 above the cost-of-living increase during my life expectancy.

(I should mention that I am also receiving an additional $581 monthly pension as a retired Army Reservist, and that my active duty time counts toward both the Civil Service and the Reserve pension. Both pensions have the cost-of-living increase, and both have the 1 per cent add-on.)

Hastings Keith, a Massachusetts Republican, was in Congress for 14 years before retiring in 1973.

My pensions, of course, are much more generous than the pension of the average career civil servant — and I agree that some who retired years ago still are behind the inflationary spiral. Nevertheless, even the average federal retiree fares much better than the average individual in the private sector with 30 years of service.

In 1971, the average career civil servant received a pension of $350 a month. Three years later, in 1974, his pension was $700 a month. His benefits above the cost of living during the course of his lifetime will be approximately $40,000.

The average military retiree receives a much larger pension than the average civil servant. Military personnel retire earlier, live longer, and accordingly, their benefits above the cost of living are much greater, particularly in the latter years of their retirement.

The average career enlisted man will get a pension on retirement at about age 40 of approximately $500 a month. Over his lifetime — even without any cost-of-living adjustment — he would receive a pension totaling about $180,000. With 6 per cent annual inflation, his pension, by reason of the compounding of the 1 per cent add-on, will have reached $3,700 per month at the end of his life expectancy. This is $1,000 per month more than it would be if there were no add-on.

The lifetime cost to the taxpayer of all these add-ons will run into many billions of dollars:

- The 1 per cent add-on that went into effect this month will cost $140 million in its first year (the total annual cost of this month's 5.4 per cent cost-of-living adjustment is approximately $750 million). Over the years, the total additional future cost of this month's 1 per cent add-on — solely for the present retirees and their surviving spouses — will be at least $4 billion — all of it above the cost of living.
- Even if there are no additional add-ons, the add-ons of previous years will eventually cost us at least $20 billion — all of it above the cost of living.
- If new add-ons are not eliminated, the future cost for this feature alone will, at 6 per cent annual inflation, total at least $80 billion — all of it above the cost of living.
- Finally, if the add-on feature is continued and the 750,000 *additional* retirees forecast during the next five-year period get their projected increases, the total cost of this "kicker" would exceed the $150 billion cost of the Vietnam war.

These costs are so great that they feed the fires of the very inflation with which they were intended to cope. Beyond the fiscal aspect of the cost-of-living increases, there are social and economic implications that were not generally recognized or understood by Congress when it wrote the retirement legislation. Because the dollar costs of the add-on are fairly well known — and haven't prompted much congressional or administration response — the public should ponder some of the other effects:

- The private sector will have to work longer than it now does to support long retirement periods of public retirees.
- Interest rates throughout our economy will be driven up as the government goes further into the market to fund deficits.
- Other services and programs will have to be curtailed.
- Earlier retirements will become more and more attractive. This means billions of dollars in replacement salaries.

The immediate responsibility for correcting this condition lies with both the executive branch and with Congress. Each has given lip service to the question of repeal of the 1 per cent add-on.

The President in his recent
budget indicated his belief that
cent add-on should be eliminate
tails have been forthcoming.

Several members of Congres
spoken out on the subject, and Rep.
Henderson, chairman of the House
Service and Post Office Committe
filed a bill calling for the repeal of the
on feature. But as yet no leadershi
been exerted and no hearings held.

Two recent developments indica
"institutionalization" of inflation i
cided possibility.

One is the recent suit by the federal judges who argue that their pay must be increased to make up for inflation; their logic would make a case for tying all government salaries to the Consumer Price Index.

The other is a bill, filed recently by Rep. John H. Dent, calling for tying the minimum wage to the CPI. Dent's bill even includes a 1 per cent add-on feature.

If these — or similar suits and/or legislation — are successful, the end result would be a change in the character — and, of course, the competence — of our free enterprise system. The final destination would be a controlled economy, one without much future for either democracy or capitalism.

Another alternative — perhaps just as bad — is the continued trend toward legislating programs for everyone, ending with the socialism of Britain. Perhaps the forecast of George Orwell's *1984* is on schedule.