

OFFICE OF INSPECTOR GENERAL

Management Information Report

**Financial Impact of Injury Settlements Awarding
Service Months to Qualify Railroad Employees for
Occupational Disability Benefits**

**Report No. 14-08
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RAILROAD RETIREMENT BOARD

EXECUTIVE SUMMARY

The Office of Inspector General (OIG) for the Railroad Retirement Board (RRB) conducted this review to determine the financial impact of injury settlements that awarded service months to qualify railroad employees for occupational disability benefits. Although limitations in agency systems and a lack of documentation did not allow us to identify every applicable case, we determined that at least 28 current occupational disability annuitants who purchased their service eligibility through injury settlements will cost the Railroad Retirement Act (RRA) trust funds at least \$11.9 million from the start of their annuity until they reach their early retirement age.^{1, 2} It is the opinion of the OIG that the impact on the trust funds could potentially be as much as \$2.2 billion if all the annuitants who barely qualified for an occupational disability had purchased some of the qualifying service months through an injury settlement. See the Appendix on pages 6 through 8 for the methodology and results of our data analysis.

Findings

Current law allows for creditable service months to be obtained through a personal injury award or settlement that allocates a portion of the damages as lost wages for a specific period following the date of injury.³ This allocation is referenced as “pay for time lost.” This provision of the law essentially allows railroad employees to buy an annuity from the RRB as part of their injury settlement with their railroad employer. The OIG’s concern is that while RRB is not a party to this settlement, the agency may be obligated to pay an annuity to the employee as a result of the settlement.

Also under current law, there are circumstances where pay for time lost, allocated for service months, may be fully creditable under the RRA, but taxable only to a limited extent, or not taxable at all.⁴ Therefore, the OIG is concerned that annuities can be purchased at a discount when all of the compensation is creditable, but not all of it is taxable.

The RRB is led by a three-member board (the Board). The Board’s three members are appointed by the President of the United States, with the advice and consent of the Senate. The Board exercises joint responsibility over the operation of the agency. The Board serves as a liaison with Congress and can seek legislative changes, when necessary.

¹ The occupational disability annuitants identified were in current pay status as of February 2014.

² The identification was limited to individuals who had an open settlement related debt with the RRB in 2008 or later because debts closed prior to 2008 had been purged from the agency’s receivable system. See the Appendix on page 6 for details.

³ 45 United States Code (U.S.C.) 231 (h)(2).

⁴ 26 U.S.C. Chapter 22.

On February 10, 2014, under the statutory provision of Section 5(d) of the Inspector General Act of 1978, as amended, the OIG issued a Seven-Day Letter to the Chairman of the Board to alert him of multiple concerns with the occupational disability program and the RRB's administration of the program.⁵ The ability to essentially purchase qualifying service, while allowable by law, is another troubling aspect of the occupational disability program.

Recommendations

We recommend that the Board seek legislative changes to:

1. disallow service months credited as pay for time lost through an injury settlement when determining service eligibility for an occupational disability; and
2. tax all creditable compensation.

⁵ 5 U.S.C. App. 3, § 5(d).

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INTRODUCTION

This management information report presents the results of the Office of Inspector General's (OIG) review to determine the financial impact of injury settlements that awarded service months to qualify railroad employees for occupational disability benefits.

Background

The Railroad Retirement Board (RRB) is an independent agency in the executive branch of the Federal government. The RRB administers comprehensive retirement/survivor and unemployment/sickness insurance benefit programs for railroad workers and their families under the Railroad Retirement Act (RRA) and the Railroad Unemployment Insurance Act. These programs provide income protection during old age and in the event of disability, death, temporary unemployment, or sickness.

The RRB is led by a three-member board (the Board). The Board's three members are appointed by the President of the United States, with the advice and consent of the Senate. The Board exercises joint responsibility over the operation of the agency. The Board serves as a liaison with Congress and can seek legislative changes, when necessary.

The RRA provides for annuities to railroad employees, spouses, and survivors. The RRA provides for the payment of an occupational disability annuity if an employee becomes permanently unable to perform his or her regular railroad occupation, due to illness or injury. To become eligible for an occupational disability annuity, an employee must have completed 10 years of service (120 service months) and attained age 60, or may qualify with 20 years of service (240 service months) regardless of age.

In some cases, an individual may be injured on the job or become ill and not have the necessary service months to qualify for an occupational disability annuity.⁶ The RRA allows for qualifying service months to be credited to an employee as part of a settlement with the railroad employer. For example, one employee had 216 service months when he stopped physically working for his railroad employer in January 2009. As part of his injury settlement, the railroad reported service months to the RRB for February 2009 through January 2011 giving him the 240 service months that he needed to qualify for an occupational disability. In another case, the settlement was used to award service for four months in 2006, one month in 2008, three months in 2009, twelve months in 2010, and six months in 2011 in order to qualify the individual for an occupational disability.

⁶ Our data analysis of annuitants selected those individuals with 120-125 or 240-245 service months; they would "barely qualify" for occupational disability. See the Appendix on page 6 for details of selection.

The allocation (or “purchase”) of service months as part of a personal injury award or settlement is called “pay for time lost.” The payment received by railroad employees under pay for time lost is taxable in the calendar year in which payment is made. Under the Railroad Retirement Tax Act, the taxes are paid for the calendar year in which the settlement is paid.⁷ The RRB credits the service to the period or periods that the wages were lost.

In fiscal year 2013, the RRB paid about \$2.4 billion in disability benefits to approximately 81,000 annuitants. Some of these disability benefit payments included amounts paid to individuals who are receiving occupational disabilities.

Section 5(d) of the Inspector General Act of 1978, as amended, requires an Inspector General to immediately report to the agency head “particularly serious or flagrant problems, abuses, or deficiencies relating to the administration of programs and operations of [the agency].”⁸ This section also requires the agency head to transmit the Inspector General’s concerns, along with the agency head’s comments, to Congress within seven calendar days (Seven-Day Letter).

On February 10, 2014, the OIG issued a Seven-Day Letter to the Chairman of the Board to alert him of multiple concerns with the occupational disability program and the RRB’s administration of the program. The ability to essentially purchase qualifying service is just another troubling aspect of the occupational disability program.

In light of the concerns identified in the Seven-Day Letter, the Inspector General requested our Office of Audit to conduct this review. This review also supports the agency’s goal of safeguarding customers’ trust funds through prudent stewardship.

Objective

The objective of this review was to determine the potential financial impact to the RRA trust funds when occupational disability annuitants qualified for their annuities based on service month credits obtained as part of an injury settlement with the railroad employer.

Scope

The scope of this review included annuitants listed on the agency’s February 2014 Master Benefit File (MBF) who were in current pay status and receiving occupational disability benefit payments. In the Appendix, on page 7, we explain the methodology used to identify the annuitants who were awarded service months through a settlement in order to qualify for an occupational disability annuity.

⁷ 26 U.S.C. Chapter 22.

⁸ 5 U.S.C. App. 3, § 5(d).

Methodology

To accomplish our objective, we:

- reviewed agency policies and procedures to obtain an understanding of the pay for time lost process when an on the job injury settlement is involved;
- reviewed legislation and regulations regarding pay for time lost; and
- analyzed an extract of the occupational disability cases involving an on the job injury settlement.

See the Appendix on pages 6 through 8 for the methodology and results of our data analysis.

We conducted our fieldwork at the RRB's headquarters in Chicago, Illinois from March 2014 through June 2014.

RESULTS OF REVIEW

Although limitations in agency systems and a lack of documentation did not allow us to identify every applicable case, we determined that at least 28 current occupational disability annuitants who purchased their service eligibility through injury settlements will cost the RRA trust funds at least \$11.9 million from the start of their annuity until they reach their early retirement age.^{9, 10} It is the opinion of the OIG that the impact on the trust funds could potentially be as much as \$2.2 billion if all the annuitants who barely qualified for an occupational disability had purchased some of the qualifying service months through an injury settlement.

In this report, we concluded that the financial impact to the RRA trust funds could be minimized if the Board seeks legislative changes to disallow the allocation of service months as part of injury settlements to qualify for occupational disabilities and to tax all creditable compensation.

See the Appendix on pages 6 through 8 for the methodology and results of our data analysis.

Service Months Awarded through Injury Settlements

The RRB awards service months based on the current law that allows some of the creditable service necessary to qualify for an occupational disability to be obtained through a personal injury award or settlement.¹¹ These settlements may allocate a portion of the damages as lost wages for a specific period following the date of injury. This allocation is referred to as pay for time lost. This provision of the RRA essentially allows railroad employees to purchase an annuity from the RRB as part of their injury settlement with their railroad employer. The RRB is not a party to this settlement but may be obligated to pay an annuity to the employee as a result of the settlement.

The practice of allowing an individual to qualify for an occupational disability based on service months awarded as part of an injury settlement is costly to the RRA trust funds.

Recommendation

The Board should seek legislative changes to:

1. disallow service months credited as pay for time lost through an injury settlement when determining service eligibility for an occupational disability.

⁹ The occupational disability annuitants identified were in current pay status as of February 2014.

¹⁰ The identification was limited to individuals who had an open settlement related debt with the RRB in 2008 or later because debts closed prior to 2008 had been purged from the agency's receivable system. See the Appendix on page 6 for details.

¹¹ 45 United States Code (U.S.C.) 231 (h)(2).

Taxation of Creditable Compensation

Current law not only allows the purchase of an annuity, it sometimes allows this purchase at a discount because the maximum taxable amount is applied to the year paid and not to the years that the wages were lost. For example, if an employee received \$300,000 from an injury settlement in 2014 for wages lost in 2011 through 2013, the employer and employee would pay combined taxes of approximately \$32,700 based on tax rates and maximum taxable amounts in 2014. If the \$300,000 was taxed over the three years of lost wages, the combined taxes would have been approximately \$86,000 resulting in the RRB Trust Funds losing over \$53,000 for a single individual.

Recommendation

The Board should seek legislative changes to:

2. tax all creditable compensation.

DATA ANALYSIS METHODOLOGY AND RESULTS

This appendix presents the methodology and results for:

- our data analysis for the OIG opinion on the maximum potential impact if all annuitants who barely qualified for an occupational disability had purchased some of the qualifying service months through an injury settlement, and
- our data analysis to identify annuitants who qualified for occupational disabilities as a result of obtaining credited service through a personal injury award or settlement.

Data Analysis Objective and Scope

Our objective was to quantify the maximum potential impact to the RRA trust funds for all occupational disability annuitants that barely qualified for occupational disability annuities and to identify employee annuitants that qualified for a disability annuity as a result of purchasing service months as part of a settlement with their railroad employer. Our scope was limited to occupational disability annuities in current pay status in the agency's February 2014 MBF where the employee had 120 to 125 or 240 to 245 months of service.

Methodology for Determining the Maximum Potential Impact

To determine the maximum potential impact, we:

- Obtained a copy of the February 2014 MBF which had 1,347,292 records.
- Extracted the records for occupational disability annuitants who were in current pay status from the MBF, resulting in 59,519 records.
- Created a table of occupational disability annuitants in current pay status who had 120 to 125 months of service, and attained age 60. These annuitants would barely qualify for occupational disability. The resulting table had 71 records.
- Created a second table of occupational disability annuitants in current pay status who had 240 to 245 months of service. These annuitants would barely qualify for occupational disability. The resulting table had 5,782 records.
- Combined the table of annuitants with 120 to 125 service months and the table of annuitants with 240 to 245 service months to obtain all annuitants who had barely enough service month credits to qualify for an occupational disability. The OIG considers each of these 5,853 annuitants as at risk of having purchased their annuity through an injury settlement.
- Determined the approximate number of months that the RRB paid each of the annuitants from the annuity beginning date (ABD) until the annuitant reached the early retirement age of 62.

- Multiplied the number of months by the benefit amount on the February 2014 MBF to estimate the amount paid or to be paid to each annuitant from their annuity beginning date until age 62.
- Totaled the amounts paid or to be paid for each annuitant that was under age 62 on their annuity beginning date.

Results of Review for Determining the Maximum Potential Impact

Our review into the maximum potential impact resulted in an estimate of \$2.2 billion for all occupational disability annuitants who barely qualified.

Methodology Related to Identifying Actual Cases of Purchased Annuities

To identify employees who qualified for occupational disabilities as a result of obtaining credited service through a personal injury award or settlement, we:

- Obtained accounts receivable data coded as sickness benefits recoverable due to an award or settlement.¹² The resulting table had 16,060 records.
- Matched the combined table produced to calculate maximum potential impact to the table of accounts receivable data. This match produced a list of annuitants who potentially obtained service months as part of a settlement. The resulting match had 168 unique records.
- Eliminated 107 annuitant records with codes indicating that they would have qualified for a disability according to Social Security standards and, therefore, they did not need the additional service months to qualify for the occupational disability. The resulting table had 61 records.

For the 61 records, we reviewed the claims information in agency systems for each of the 61 annuitants. In the claims information, we looked for documentation of service month credit adjustments to determine if any adjustments were the result of a settlement between the railroad employee and their railroad employer.¹³

We determined that 28 annuitants had service months credited as a result of a settlement between the employee and their railroad employer. These service month credits gave them the qualifying service to meet the eligibility requirements for an occupational disability.

¹² Accounts receivable closed prior to 2008 had been purged from the agency's system.

¹³ Documentation showing the allocation of service months based on an injury settlement was not always available in agency systems.

For each of the 28 annuitants, we estimated the amount they will cost the RRA trust funds from the ABD to early retirement at age 62.¹⁴ In order to do this, we first found the benefit amount on the February 2014 MBF for each case. Then we determined the number of months for each of the 28 from the ABD to the age 62 attainment date, which would be the number of months each annuitant would receive occupational disability benefits. Finally, we multiplied the February 2014 benefit amount times the number of months receiving occupational disability benefits to calculate an estimate of total benefits.

Results of Review for Identifying Actual Cases

We estimated that the 28 current occupational disability annuitants, who purchased their service eligibility through an injury settlement since 2008, will cost the RRA trust funds at least \$11.9 million.¹⁵ See the table on page 9 for the details of our calculations for the 28 cases.

¹⁴ Each of the individuals had enough railroad service to qualify for the early retirement at age 62, regardless of disability.

¹⁵ The identification was limited to individuals who had an open settlement related debt with the RRB in 2008 or later because debts closed prior to 2008 had been purged from the agency's receivable system.

Financial Impact of Injury Settlements Awarding Service Months to Qualify Railroad Employees for Occupational Disability Benefits

Case Number	Annuity Amount on February 2014 MBF	Annuity Begin Date	Age 62 Attainment Date	Number of Months Receiving Occupational Disability ¹⁶	Estimated Total of Benefits Received
1	\$ 2,589	07/01/2009	03/05/2020	129	\$ 333,981
2	\$ 2,840	08/15/2010	04/11/2026	189	\$ 536,760
3	\$ 2,523	02/01/2009	08/19/2032	284	\$ 716,532
4	\$ 2,362	07/01/2011	12/19/2029	223	\$ 526,726
5	\$ 2,183	09/02/2007	01/01/2024	197	\$ 430,051
6	\$ 2,757	05/01/2010	12/02/2023	164	\$ 452,148
7	\$ 1,735	02/01/2008	10/03/2016	105	\$ 182,175
8	\$ 3,161	12/01/2011	10/19/2028	204	\$ 644,844
9	\$ 3,029	04/01/2013	04/13/2021	97	\$ 293,813
10	\$ 2,407	05/01/2011	04/24/2027	193	\$ 464,551
11	\$ 1,576	01/01/2008	11/14/2008	11	\$ 17,336
12	\$ 2,581	05/01/2010	06/22/2028	219	\$ 565,239
13	\$ 2,817	06/01/2010	12/17/2028	224	\$ 631,008
14	\$ 3,124	06/01/2011	03/10/2029	214	\$ 668,536
15	\$ 2,696	01/15/2013	03/07/2014	15	\$ 40,440
16	\$ 2,786	08/01/2010	01/01/2020	114	\$ 317,604
17	\$ 2,740	09/01/2007	02/20/2023	187	\$ 512,380
18	\$ 2,540	12/02/2006	03/02/2016	112	\$ 284,480
19	\$ 2,701	02/01/2011	06/27/2018	90	\$ 243,090
20	\$ 2,462	04/01/2012	03/28/2020	97	\$ 238,814
21	\$ 2,734	10/01/2008	06/22/2019	130	\$ 355,420
22	\$ 2,335	02/01/2011	11/24/2016	71	\$ 165,785
23	\$ 2,885	11/01/2008	08/22/2026	215	\$ 620,275
24	\$ 2,821	08/01/2010	04/22/2032	262	\$ 739,102
25	\$ 2,018	09/01/2010	06/10/2022	142	\$ 286,556
26	\$ 2,536	11/01/2012	08/21/2034	263	\$ 666,968
27	\$ 2,235	11/01/2012	12/02/2027	182	\$ 406,770
28	\$ 2,900	01/01/2011	05/12/2027	197	\$ 571,300
Total					\$ 11,912,684

¹⁶ This column (column 5) contains the number of months that annuitants receive occupational disability benefits prior to the date of age 62 attainment.

Overall Conclusion

Although limitations in agency systems and a lack of documentation did not allow us to identify every applicable case, we concluded that at least 28 current occupational disability annuitants, who purchased their service eligibility through an injury settlement since 2008, will cost the RRA trust funds at least \$11.9 million.¹⁷ It is the opinion of the OIG that the impact on the trust funds could potentially be as much as \$2.2 billion if all the occupational disability annuitants who barely qualified were considered.

¹⁷ The identification was limited to individuals who had an open settlement related debt with the RRB in 2008 or later because debts closed prior to 2008 had been purged from the agency's receivable system. See footnote 12 on page 7.