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HUMAN RESOURCES
DIVISION

9 JUN 1978
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Mr. Donald I. Wortman
Acting Commissioner of Social
Security
Department of Health, Education,
and Welfare

Dear Mr. Wortman:

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

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

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

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

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

Your proposal under section 213 will increase the frequency with which States and interstate instrumentalities must deposit social security contributions on wages and salaries paid to covered employees from quarterly (15th day of the 2d month after the end of the calendar quarter) to monthly (15 days after the end of each month). The present quarterly deposit requirement for States results in a substantial loss of interest earnings to the Social Security Trust Funds, and is inequitable to employers in the private sector who generally must deposit Federal income and social security taxes weekly, biweekly, or monthly.

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

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

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

Deposit within 3 banking days after the quarter-monthly period ends (end of 1st, 2d, or 3d week) if taxes are \$2,000 or more.

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

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

period as it is to be made 15 days after the end of the month as currently proposed. In this connection, we noted that:

- (1) over half of the State and local employees are currently being paid more often than monthly;
- (2) many States already require State agencies and local governments to remit social security contributions to them more often than quarterly (biweekly or monthly); and
- (3) State and local governments are remitting withheld income taxes in accordance with the IRS depository schedule.

In effect, a State which pays its employees biweekly remits the Federal income taxes it withholds to the IRS biweekly, but is not required to remit to SSA the social security contributions it deducts from the pay of these same employees until the 15th day of the 2d month after the end of the calendar quarter.

Because the States make less frequent deposits than private sector employers, the Social Security Trust Funds have lost a potential for about \$1 billion interest earnings since the States were brought under the social security program in 1951. Deposits by the States rose from about \$26 million in 1952 to over \$10 billion in calendar year 1977. Based on present wages, salaries, and interest and inflation rates, interest earnings are substantial and should become more substantial in future years. For example, assuming your monthly deposit proposal becomes effective January 1, 1980, additional trust funds interest earnings will total about \$856 million (at simple interest rates) for the 4 calendar years 1980-1983. These interest earnings would increase an additional \$54 million for the same period if deposit requirements were changed to 15 days after the end of the pay period.

PHASING IN OPTIONS

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

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

FREQUENCY OF REPORTING REQUIREMENTS

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

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

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

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

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We appreciate the opportunity to comment on your "Notice of Proposed Rulemaking" and would like to be advised of any consideration given to our comments. As you are aware, we

are currently reviewing the effects of delayed social security contribution deposits by the States under section 218 of the act, and plan to issue a report to the Congress at a later date.

Sincerely yours,

Gregory J. Ahart

Gregory J. Ahart
Director