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Briefing Report to the Chairman, Subcommittee on Oversight, Committee on Ways and Means, House of Representatives

May 1989

TVA MANAGEMENT

Information on Compensation for Top Managers

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GAO United States
General Accounting Office
Washington, D.C. 20548

Resources, Community, and
Economic Development Division

B-222334

May 17, 1989

The Honorable J.J. Pickle
Chairman, Subcommittee on Oversight
Committee on Ways and Means
House of Representatives

Dear Mr. Chairman:

At the suggestion of Subcommittee Member Congressman Ronnie Flippo, you asked us to examine certain pension and other compensation-related matters involving upper level employees at the Tennessee Valley Authority (TVA). In particular, you asked that we obtain information on TVA's Merit Incentive Supplemental Retirement Income Plan and compare its features to the provisions of the Employee Retirement Income Security Act (ERISA).[1] In addition, you asked us to identify the levels and types of compensation TVA provided its top management employees. Finally, you requested that we determine TVA's legal authority for making these additional compensation payments.

On January 19, 1989, we briefed Congressman Flippo, his staff, and Subcommittee staff on the preliminary results of our work. At that time, we agreed to provide you a written report on the matters discussed at that briefing as well as an advisory legal opinion concerning certain methods of compensation provided by TVA to its top managers.

Our advisory legal opinion was provided to you on April 4, 1989. In that opinion, we held that supplemental plan or relocation incentive payments made to TVA employees that are clearly intended to circumvent TVA's statutory salary limitation, are improper. (See app. I.) As we have noted in two previous legal opinions on TVA's efforts at providing additional compensation,[2] TVA may well be experiencing

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[1]ERISA is a comprehensive federal law regulating the workings of private pension plans. It was enacted in 1974 in response to widespread indications of pension plan misuse, which had left many long-time employees with no retirement benefits.

[2]B-205284, Nov. 16, 1981, and B-222334, June 2, 1986.

difficulty in recruiting and retaining top level managers due to salary limitations imposed by the statutory ceiling. Other federal agencies are experiencing such problems as well, and we have referred to this in recent reports, including our Transition Series Report on the Public Service, GAO/OGC-89-2TR (Nov. 1988).

This report provides information on TVA's Merit Incentive Supplemental Retirement Income Plan (supplemental plan) and the levels and types of compensation provided by TVA to its top managers.

Overall, we found that the supplemental plan is a deferred compensation plan that TVA uses to provide additional compensation to recruit and retain top managers and to reward outstanding managerial performance. Available only to managers in TVA position levels M-8 and above, this plan supplements benefits provided employees covered under the Tennessee Valley Authority Retirement System and other retirement plans, such as the Civil Service Retirement System or Federal Employee Retirement System. While the plan is not subject to the provisions of ERISA, our comparison of its features with provisions of ERISA showed that the plan differed from ERISA provisions in areas such as eligibility, funding, and contribution limits.

Our work also shows that TVA provides various types of compensation to its top managers in addition to a base salary. In addition to supplemental plan credits, TVA compensates its top managers with relocation incentive payments, performance awards and bonuses and, prior to October 1, 1988, paid its employees' share of Federal Insurance Contributions Act contributions and medical and dental insurance premiums.

In terms of levels of compensation provided, TVA compensation data showed that for 220 top managers employed by TVA on October 1, 1988, the average annual base salary being provided was $72,950. In addition, for the period January 1 through October 1, 1988, 29 top managers received either supplemental retirement or relocation incentive benefits: 13 received supplemental retirement credits only, 14 received relocation incentives only, and 2 received both benefits. Supplemental plan credits averaged $31,438, and relocation incentives averaged $26,125.

Sections 1 through 7 provide details on the information you requested. Appendix II lists the major contributors to this briefing report.

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In carrying out our work, we relied on information and compensation data provided by TVA and on discussions with TVA officials. We selected a sample of the data provided to us and verified the data with source documents, such as individual employee pay records. Section 8 provides details of the scope and methodology of our review. Our review was done between November 1988 and March 1989, in accordance with generally accepted government auditing standards.

As arranged with your office, unless you publicly announce its contents earlier, we plan no further distribution until 30 days from the date of this letter. At that time, we will provide copies to the Tennessee Valley Authority and to other interested parties upon request.

If you have any questions regarding this report, please call me at 275-1441.

Sincerely yours,

Keith O. Fultz

Keith O. Fultz
Director, Energy Issues

CONTENTS

ABBREVIATIONS

ERISA	Employee Retirement Income Security Act
GAO	General Accounting Office
FICA	Federal Insurance Contributions Act
TVA	Tennessee Valley Authority
TVARS	Tennessee Valley Authority Retirement System

SECTION 1

THE COMPENSATION PROBLEM--TVA'S VIEW

- Maintaining Compensation Levels That Are Competitive With Relevant Labor Markets
- Recruiting Managers and Key Personnel--Particularly for Nuclear Power Facilities
- Retaining Managers and Key Personnel

TVA'S COMPENSATION PROBLEM

In congressional hearings and internal memorandums, TVA stated that it has difficulty maintaining a highly skilled work force for the construction, operation, and modification of its power facilities, particularly of its nuclear generating facilities. Because skilled individuals are in great demand among private utilities and organizations, TVA believes it can compete for this talent only if it offers a level of compensation similar to that offered by the "relevant labor market."

TVA is limited to paying salaries to its employees that do not exceed those received by the members of its Board of Directors. TVA's Board of Directors are currently paid at Executive Schedule level IV--$80,700--as are SES members. This amount is higher than the cap on federal general schedule pay, which is Level V of the Executive Schedule--$75,500. TVA reports that the prevailing rate of compensation for the private sector employees in positions comparable to TVA's nuclear managers greatly exceeds this cap. Overall, TVA believes it is limited to salaries that are too low to attract the needed talent, adversely affecting both its efficiency and productivity.

Likewise, retaining executives and other key personnel requires higher compensation levels. TVA reports that in recent years, it has experienced a loss of regular personnel and has been unable to hire replacements. It contends that people who leave TVA can make more money elsewhere. The 1984 President's Private Sector

Survey on Cost Control reported that "private sector utilities are well aware of TVA's problems and are able to capitalize on them." Their recruiters routinely "raid TVA ranks" for technical specialists and managers.

SECTION 2

COMPENSATION FOR TOP MANAGERS

- Base Salary
- Merit Incentive Supplemental Retirement Income Plan
- Relocation Incentives
- Executive Performance Bonus Awards
- Merit Pay Bonuses
- Overtime
- Other Types of Payments

COMPENSATION FOR TOP MANAGERS

TVA has developed a number of methods or programs for providing financial compensation to its top managers, including managers in its Nuclear Senior Management Service.[1] In addition to a base salary that conforms to compensation limits set for regular federal employees and executives, TVA also provides various incentives and bonuses to top managers.

Merit Incentive Supplemental Retirement Income Plan

TVA's regular retirement system, because of the way it is integrated with Social Security, provides a greater percentage of final pay as retirement income to lower paid employees than to higher paid employees. The Merit Incentive Supplemental Retirement Income Plan (supplemental plan), established separately from the

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[1]In May 1986 TVA created the Nuclear Senior Management Service as a subset of its regular management series. It was established to provide competitive compensation to top level personnel and to recognize the senior executive cadre within TVA's nuclear power programs. The Service includes top managers equal to levels of M-8 and above within the Office of Nuclear Power.

original retirement plan, is available only to TVA executive managers (grades M-8 through M-13).

TVA provides top managers supplemental plan benefits (credits) that are based on factors such as meritorious performance and comparability of compensation to that prevailing in corporations. Amounts credited to an individual's account are determined by the TVA Board of Directors and are considered deferred income, to be paid when the individual leaves TVA. The plan offers additional retirement income, taxable only upon withdrawal.

The supplemental plan is discussed in more detail in sections 3 and 4.

Relocation Incentives

At the discretion of the TVA Board of Directors, payments are made to existing employees to encourage them to relocate or accept new positions, or to outside candidates to induce them to accept positions with TVA. Relocation incentives are discussed in more detail in section 5.

Executive Performance Bonus Awards

This program was started in August 1988 but has subsequently been revised. It was designed to encourage and reward exceptional executive management performance and to assist in recruiting and retaining executive talent. Awards were to be made at the discretion of the TVA Board on the basis of appraisal of managerial performance and demonstration of managerial skills. The program allowed for bonus award commitments to be made to executive candidates prior to employment. According to TVA, the Board approved an Executive Performance Bonus Award in only one case: it committed to award a newly hired executive a $100,000 bonus after each subsequent year of service meeting "high standards of performance."

TVA revised this performance bonus plan in February 1989. About 150 managers out of TVA's 27,000 employees are eligible for this new plan, the Executive and Senior Manager Performance Bonus Plan. Bonuses are based on performance and achievements, and only in special cases will the lump sum payment exceed 30 percent of annual salary. The TVA Board makes the final decisions on all recipients and amounts of awards. Thirty-six managers have already been approved for bonus awards in 1989.

M-8 Performance Awards

These awards are available to managers at the M-8 level. Employees who are rated "exceptional" receive a $3,000 lump sum payment, and those rated "superior" receive $2,000. Employees rated below "superior" are not eligible for performance pay.

Merit Bonuses

Awards were made to 314 current on-board managers at the M-8 through M-13 levels from 1984 through October 1, 1988, at an average of $2,143 each. Table 2.1 provides the specific breakdown.

Table 2.1: Merit Pay Awards to TVA Managers, 1984-Oct. 1988

Calendar year	Total	No.	Average
1984	$154,252	80	1,928
1985	141,141	69	2,046
1986	159,815	72	2,220
1987	204,550	88	2,324
Oct. 1988	13,000	5	2,600

Other Bonuses

Other types of bonuses include the Nuclear Management Incentives, a bonus for managers who obtain and maintain Nuclear Power Plant Operator licenses and for plant management. Nuclear management personnel who receive their initial senior reactor operator license may receive a one-time lump sum payment of $5,000, and those who continue to hold that license for 12 consecutive months receive a lump sum payment of $7,000.

Employees at grades M-5 and above with major accountability for nuclear operations safety and adherence to regulatory requirements receive additional compensation if (1) they are working permanently or temporarily in a nuclear plant and (2) they are not receiving nuclear license pay. Upon supervisory recommendation, these employees are eligible for an annual lump sum payment not to exceed $5,000.

Few nuclear plant management incentive payments were made between 1984 and 1988. As of October 1, 1988, six employees had received such payment. Specifically, in 1984 five employees received a total of $15,349, and in 1985 one employee received $869.

Overtime

Because some salaried employees who work and are paid overtime receive more compensation than managers who may also work overtime but are not compensated for it, TVA has authorized uniform payment of overtime for management and nonmanagement employees.

Information concerning overtime pay to top managers was not readily available from TVA records. However, the Inspector General reported that overtime paid during calendar year 1987 to management employees (i.e., M series) totaled $18 million. Inspector General information showed that

- -- 11 managers at the M-8 level received a total of $27,000,
- -- 2 managers at the M-9 level received a total of $360, and
- -- the remainder was paid to managers at the M-7 level and below.

Because of the small number and low amounts of overtime paid to top level managers, we did not seek further information on this type of compensation.

Other Types of Compensation

TVA currently provides, or has in the past provided, other types of compensation to its top managers.

Currently, TVA reimburses the professional membership dues and fees of its management schedule employees. These reimbursed fees and dues are authorized by the TVA Board. The maximum reimbursement allowed is $200 a year for managers and $500 a year for attorneys.

Prior to October 1, 1988, TVA paid its employees' share of Federal Insurance Contributions Act (FICA) taxes for all employees at the M-8 level and above.[2] Table 2.2 shows the maximum amounts paid per employee.

Table 2.2: FICA Shares TVA Paid for Top Managers, 1984-88

Calendar year	Maximum amount per employee
1984	$2,532.60
1985	2,791.80
1986	3,003.00
1987	3,131.70
1988	3,379.50

Prior to October 1, 1988, TVA also paid its management schedule employees' share of medical and dental insurance. In 1988 the amounts these employees would have paid for medical and dental insurance were $18 per month for a single policy (annual cost = $216) and $48.20 per month for a family policy (annual cost = $578). The amounts for prior years would have been somewhat less.

[2]Beginning October 1, 1988, TVA stopped paying its employees' share of FICA taxes.

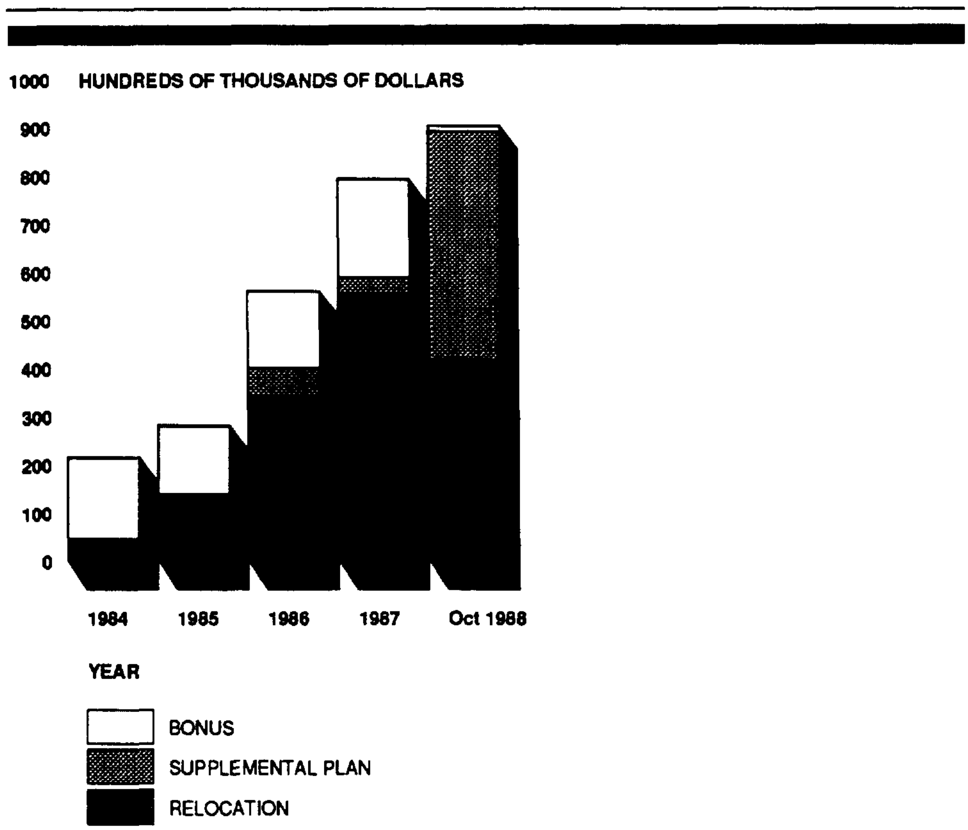
AMOUNTS OF ADDITIONAL COMPENSATION

The amount of other types of compensation TVA pays its top managers in addition to their base salaries has increased since 1984. Table 2.3 shows how the use of extra methods of compensation, especially the supplemental plan credits and relocation incentives, has grown. Figure 2.1 shows this same growth pictorially.

Table 2.3: Major Compensation Expenditures, by Year

Calendar year	No. of mgrs.	Base salary	Bonuses	Supplemental plan	Relocation incentives	Total
1984	168	$ 9,428,992	$169,601	$ 0	$ 44,000	$ 9,642,593
1985	170	10,070,491	142,010	0	138,000	10,350,501
1986	185	11,591,932	159,815	57,500	342,000	12,151,247
1987	208	14,047,756	204,550	33,500	554,000	14,839,806
10/88	220	16,049,096	13,000	471,565	418,000	16,951,661

Figure 2.1: Additional Compensation Received by TVA Top Managers



SECTION 3

PROFILE OF SUPPLEMENTAL RETIREMENT PLAN

- Deferred Compensation Plan
- Not Covered Under Employee Retirement Income Security Act
- Credits While Employed
- Full Cash Value or Annuity at Retirement or Full Cash Value at Termination
- Available for Loans
- Available for Hardship Withdrawals
- Taxed When Paid

PROFILE OF THE MERIT INCENTIVE SUPPLEMENTAL RETIREMENT INCOME PLAN

The Merit Incentive Supplemental Retirement Income Plan (supplemental plan) is a defined contribution, deferred compensation plan that the Tennessee Valley Authority uses to provide additional compensation to recruit and retain top managers, and to reward outstanding managerial performance. The plan supplements benefits provided under the Tennessee Valley Authority Retirement System (TVARS) and other retirement plans.[1]

The supplemental plan is available only to managers in pay grades M-8 through M-13, the physician pay scale, and the Nuclear Senior Management Service (with salaries ranging from $63,950 to $77,400). Although we found no statutory prohibition against TVA

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[1]TVARS is a defined benefit plan covering salaried TVA employees who are not covered by the Civil Service Retirement System or Federal Employee Retirement System. In addition to providing pensions, annuities, and Social Security benefits to retirees, TVARS provides death and disability benefits and offers a Savings and Deferral Retirement Plan.

having a deferred compensation plan, GAO holds that using this plan to circumvent statutory pay limits is improper.

Supplemental Plan Is Not Subject to the Provisions of ERISA

According to TVA, the supplemental plan is not subject to the provisions of the Employee Retirement Income Security Act of 1974 (ERISA) because it is a governmental plan operated by an agency of the United States government. We agree that the supplemental plan is exempt from ERISA.

We compared the supplemental plan's features to the minimum requirements for pension plans subject to ERISA as well as to section 457 of the Internal Revenue Code, which applies to state/local governments and tax-exempt organizations. Standards for both ERISA and section 457 cover such features of pension plans as eligibility and funding. ERISA also covers other features discussed below.

Eligibility

As noted above, supplemental plan participation is limited to the top management grades, and these TVA employees may participate regardless of their age or length of service. For private employer-sponsored pension plans subject to ERISA, employees must not be excluded from participation in the plans if they have reached age 21 or have 1 year of employment, whichever comes later. Under section 457, covered plans must include as participants only those persons who provide services for the employer.

Funding

For the supplemental plan, funds are not set aside to finance benefits payable to participants when they leave TVA, while plans subject to the funding-standards of ERISA are required to be funded. Plans subject to section 457 are not required to set aside funds to cover the plan's liabilities.

Vesting

Supplemental plan benefits are vested (that is, become a financial obligation of TVA to the manager) as soon as credits are granted by the Board of Directors. Under ERISA's minimum standards employees generally must be either fully vested after 5 years, or partially vested after 3 years and then fully vested after 7 years.

Contribution Limits

The supplemental plan has no limits on the amounts of credits that the Board of Directors can grant. ERISA has a general limit for defined contribution plans of $30,000 per year, or 25 percent of an employee's annual compensation, whichever amount is smaller, and for defined benefit plans of $98,064.

Nondiscrimination Provisions

ERISA generally prohibits qualified plans from discriminating in favor of officers, shareholders, or highly compensated employees. The supplemental plan, in contrast, was established specifically to provide deferred compensation to highly compensated employees: for example, all of the managers who have received credits since January 1, 1986, had salaries over $70,000 per year.

Distribution Limits

For plans subject to ERISA, benefit payments made before an employee reaches age 59-1/2 may be subject to additional federal taxes for early withdrawal from the plan. Under the supplemental plan, managers are entitled to receive all credits and accrued interest amounts in their accounts when they leave TVA for any reason, and at any age without this additional tax penalty.

Reporting and Disclosure

Unlike most plans subject to ERISA, the TVA Board of Directors is not required to provide the Department of Labor with periodic reports on the supplemental plan. Also, the Board of Directors is not required to provide information on the supplemental plan, or updated information on contributions to the plan, to participants or beneficiaries.

Supplemental Plan Credits Are Given to Managers While Employed With TVA

At their discretion, TVA's Board of Directors may grant credits to the supplemental plan accounts of eligible managers. The criteria for granting credits include

- -- providing an incentive for recruiting new managers to TVA;
- -- providing managers with total compensation equivalent to prevailing pay outside TVA, as an incentive to remain with TVA;
- -- rewarding meritorious performance; and
- -- compensating managers for lost annual leave.

Credits in supplemental plan accounts accrue interest at the same rate set for TVA investments by the Department of the Treasury. This rate, according to TVA's enabling legislation, is "the computed average interest rate payable by the Treasury upon its total marketable public obligations" as of the beginning of each fiscal year. In October 1988 Treasury set TVA's interest rate for fiscal year 1989 at 8.77 percent. Interest accruals are credited to supplemental plan accounts on a monthly basis.

Managers Receive Payments When They Leave TVA

When a manager retires from TVA, either voluntarily or because of disability, the manager can take (1) a lump sum payment consisting of all supplemental plan credits and accrued interest, (2) 10 annual payments based on all credits and accrued interest, or (3) a combination of lump sum payment based on one or more credits, and 10 annual payments based on any remaining credits. If a manager leaves TVA before reaching retirement age, and does not leave due to disability, the manager must take a lump sum payment. If a manager dies while employed by TVA, or while receiving annual supplemental plan payments, his or her survivor receives a lump sum payment of the remaining balance in the manager's account.

Managers Can Borrow Against Their Supplemental Plan Accounts

Since January 1988 TVA managers have been able to borrow against their supplemental plan accounts. Loans are approved by a three-member committee consisting of the Vice President for Human Resources and two other officials appointed by the TVA Board of Directors. Repayment terms are negotiated between the committee and the borrower. Interest on the loans is 1 percent above the rate used for interest accruals on supplemental plan credits at the time repayments are made. For fiscal year 1989, this rate is 9.77 percent.

Since the supplemental plan loan program began in January 1988, two managers have received loans. The principal portion of each loan is to be paid off in a lump sum after 7 years. One loan's interest is to be paid quarterly, while the other's interest is being paid off through biweekly payroll deductions.

Managers Can Take Hardship Withdrawals From Supplemental Plan Accounts

Managers who have received supplemental plan credits can withdraw all or part of their accounts for financial hardships, such as housing and educational costs, death or disability in the manager's family, or destruction of the manager's property. Hardship withdrawals are subject to approval by the same three-member committee that approves supplemental plan loans. TVA's policies do not require that managers repay hardship withdrawals.

One hardship withdrawal has been approved thus far: a manager withdrew $13,887.40 in January 1989 to pay for unexpected home building costs and for his mother's funeral. These reasons were consistent with TVA's criteria for granting hardship withdrawals.

Supplemental Plan Benefits Are Taxed When Received

According to TVA, supplemental plan payments are considered income in the year received and are reported as income to the Internal Revenue Service. Also, hardship withdrawals are taxable when received by a manager. This is consistent with the usual treatment of deferred compensation under the Internal Revenue Code. In the sample of payment records we reviewed, we found that TVA withheld 20 percent from the principal portion of each payment for federal income taxes. We also found that 20 percent was withheld from the hardship withdrawal we reviewed.

SECTION 4

SUPPLEMENTAL RETIREMENT PLAN--OVERALL ACTIVITY

- 1979 to November 30, 1988

- Credit value	$1,466,461
- Average credit	$4,326
- Lowest credit	$300
- Highest credit	$47,000
- Total payments	$954,607
- Average payment	$3,434
- Lowest payment	$108
- Highest payment	$65,981

- Activity

  1984 and 1985 - no credits

  1986 - $98,000 to 5 managers, average $19,700

  1987 - $33,500 to 1 manager

  November 30, 1988 - $471,565 to 15 managers, average $31,438

SUPPLEMENTAL PLAN TRANSACTIONS BETWEEN 1979 AND NOVEMBER 1988

Supplemental Plan Credits

Between 1979 and the end of November 1988, TVA credited about $1.5 million to supplemental plan accounts for 209 past and current top managers (see table 4.1). Of these credits, almost a third ($472,000) was granted during the first 11 months of 1988. No credits were made between June 1, 1981, and December 1985, in response to public and congressional opposition to additional compensation for top TVA managers.

Supplemental plan credits were generally less than $10,000 for the period 1979-81; since 1986, however, while a smaller number of credits has been granted, the size of the individual credits has increased, as shown in table 4.1.

Table 4.1: Supplemental Plan Credits Received by Top TVA Managers, 1979-Nov. 1988

Calendar year	No. of credits	Total credits	Average credit	Range of credits	
				Lowest	Highest
1979	137	$ 380,667	$ 2,779	$ 400	$10,500
1980	180	479,439	2,664	300	10,500
1981	1	3,000	3,000	3,000	3,000
1982	0	0	0	0	0
1983	0	0	0	0	0
1984	0	0	0	0	0
1985	0	0	0	0	0
1986	5	98,500	19,700	5,000	36,000
1987	1	33,500	33,500	33,500	33,500
1988[a]	15	471,565	31,438	7,500	47,000
Total	339[b]	$1,466,671[c]	$ 4,326	$ 300	$47,000

[a]Includes credits received through November 30.

[b]A total of 209 TVA managers received credits through November 30, 1988; many received credits in 2 different years.

[c]In addition, $934,000 in interest had accrued on supplemental plan accounts as of November 30, 1988.

Supplemental Plan Payments

Between 1980 and the end of November 1988, TVA paid over $950,000 from supplemental plan accounts. Some former managers are receiving annual payments instead of one lump sum, while one former manager (1) is receiving an annual payment of one credit and (2) has received a lump sum payment of another credit. The largest payment thus far is a lump sum payment of $66,000. This payment covered credits totaling $50,500 and over $15,000 in accrued interest. Supplemental plan payments by year appear in table 4.2.

Table 4.2: Supplemental Plan Payments, 1980-Nov. 1988

Calendar year	No. of payments	Total payments	Average payment	Range of payments Lowest	Range of payments Highest
1980	10	$ 25,276.32	$2,527.63	$108.16	$ 7,254.21
1981	22	59,142.80	2,688.31	118.93	7,013.87
1982	24	96,157.03	4,006.54	134.27	13,751.78
1983	17	39,315.76	2,312.69	151.47	8,740.49
1984	30	99,200.95	3,306.70	168.92	25,651.82
1985	30	72,065.77	2,402.19	189.11	11,385.30
1986	33	171,833.95	5,207.09	190.79	65,981.33
1987	41a	107,136.94	2,613.10	201.87	23,988.55
1988[b]	71	284,477.75	4,006.73	220.78	30,961.65
Total	278[c]	$954,607.27	$3,433.84	$108.16	$65,981.33

[a]In 1986 TVA made an exception to its policy of withholding supplemental plan payments until a participant left TVA's employ. A manager who received a credit in 1986 could choose to receive a lump sum payment at a specified future date, without first leaving TVA. One manager took advantage of this option and received his lump sum payment during 1987.

[b]Includes payments made through November 30.

[c]A total of 153 former TVA managers, plus the manager mentioned in footnote [a] above, received payments through November 30, 1988.

RECENT SUPPLEMENTAL PLAN ACTIVITY

Between 1986 and the end of November 1988, the TVA Board of Directors granted 21 supplemental plan credits to 18 managers, totaling $603,565. Of these credits, 15, totaling $471,565, were granted during 1988.

We reviewed justification documents for all credits granted by TVA's Board of Directors from January 1, 1986, to November 30, 1988. Six of the 18 managers received credits as part of job offers to join TVA. Three of these six managers were offered credits over more than 1 year: one was offered a minimum of $40,000 in each year of employment with TVA, with a Board of Directors option to increase the amount of the credits in future years.

In at least six other cases, supplemental plan credits were justified as incentives to keep managers from leaving TVA: five of the six managers had received offers from the private sector. In two other cases, supplemental plan credits were granted to managers whose positions had been abolished and who were asked to accept lesser positions. None of the credits appeared to violate TVA's criteria for granting supplemental plan credits.

SECTION 5

RELOCATION INCENTIVES PROGRAM

- Relocation incentives are additional compensation for recruitment or retention of TVA's top managers.
- Although all TVA employees in the manager or physician series are eligible for relocation incentives, we looked only at the top six managerial levels--M-8 through M-13.
- Relocation incentives have grown from 7 awards in 1984 averaging $9,286 to 18 awards in 1988 (through Oct. 1, 1988) averaging $25,000. Thirty-nine awards averaging $21,231 were given in 1987.

RELOCATION INCENTIVES

Relocation incentives, officially known as the "Management and Physician Staffing Arrangement Program," or the "Recruiting Incentive Program," are an additional form of compensation TVA provides to induce job candidates to accept or current employees to remain in TVA top management positions.[1] Employees in TVA's management series (M series) or physician series (P series) are eligible for these incentives.

Payments of relocation incentives are justified by TVA in the following circumstances:

-- When TVA directs the transfer of a manager.

-- When few qualified candidates exist for a given position.

-- When a manager is moved to a new location or into a new position and no promotion is involved.

-- Where a position is critical to program success.

[1]TVA's relocation incentives are in addition to the travel and relocation expense reimbursements provided for in General Services Administration regulations. TVA reimburses employees for travel and relocation in accordance with these regulations.

-- Where a position exists in a critical shortage occupation.

The relocation incentives program was established by TVA in 1980. At that time TVA policy limited the amount of incentive payment per individual to $5,000. Since its inception in 1980, TVA has increased the amount of the maximum incentive payment to reflect increases due to inflation as well as other changed circumstances. These changes are summarized in table 5.1.

Table 5.1: Changes in Relocation Incentive Program, 1980-Aug. 1988

Calendar year	Maximum allowed	Employees' levels
1980	$ 5,000	Members of M series
1982	12,000	M-8 through M-12
1985	12,000	M-1 through M-9
1985	24,000	M-10 through M-12
1985	Additional $24,000	Outside candidates who fill critical positions
Aug. 1988	Amount determined by TVA Board	Outside candidates who fill critical positions

Relocation incentives have grown in amount paid and number awarded through 1987, the last full calendar year for which we collected data. Table 5.2 reflects this.

Table 5.2: Relocation Incentives Paid, 1984-Oct. 1988

Calendar year	Number $<10,000	Number $10,000+	Number $20,000+	Number $30,000+	Number $40,000+	Number $100,000	Total
1984	5	1	1	0	0	0	7
1985	10	8	2	0	1	0	21
1986	4	9	12	1	1	0	27
1987	5	17	7	3	7	0	39
Oct 1988	2	6	6	1	2	1	18
Total	26	41	28	5	11	1	112

TVA's Inspector General reviewed a random sample of the relocation incentive program payments made to all management levels between January 1, 1986, and October 25, 1987. The 1988 report of the Inspector General's review cited several findings. Among them were the following:

-- Incentives were paid for some positions that did not appear to be critical or hard to fill.

-- There were no comprehensive, TVA-wide criteria to determine who should receive payments.

-- Some incentive payments were made without complete information.

In response to the Inspector General's report, TVA amended its procedures to require Board approval of all relocation incentive payments.

SECTION 6

OVERALL COMPENSATION LEVELS

OF TVA'S CURRENT TOP MANAGERS

- Average Base Salary of 220 Top Managers: $72,950
- Twenty-nine Also Received Supplemental Retirement and/or Relocation Incentives:
  - -2 received both
  - -13 received supplemental retirement only
  - -14 received relocation incentives only
- Amounts of Total Compensation Provided for the 220 Managers Including Base Salary, Supplemental Retirement Credits, Bonuses, and Relocation Incentives:
  - -Range, $63,950 to $217,300
  - -Average, $77,053
- Of the 29 Who Received Supplemental Retirement and/ or Relocation Incentives, the Total Compensation Provided:
  - -Ranged from $75,515 to $217,300
  - -Averaged $105,767

OVERALL COMPENSATION LEVELS

In 1988, based on data through October 1, 1988, the base salary for all of TVA's top managers was under the salary limit established for the TVA Board members--Executive Schedule level IV, or $77,500. During 1988 the average base salary paid to the 220 TVA top managers at grade series M-8 through M-13 was $72,950. The maximum base salary was $77,400, and the minimum, $63,950.

Top managers currently at TVA may receive two main types of compensation in addition to their base pay: credits to their supplemental plan account and/or relocation incentives. Performance bonuses at TVA were only a minor source of additional compensation for managers: through October 1, 1988, only five bonuses were awarded at an average of $2,600 each.

For that same period, just under 13 percent of TVA's 220 top managers received one or both types of these additional compensations in 1988. For this group of 29 employees, supplemental plan credits ranged from $7,500 to $47,000, with an average of $31,438. Relocation incentives ranged from $5,000 to $100,000, with an average of $26,125.

Such additions to base salaries brought average compensation for these top 29 managers from $77,053 (average compensation for all 220 managers) to $105,767 (average compensation for the 29 managers). Of these 29 managers, more than half were provided $100,000 or more in compensation annually. Table 6.1 shows the distribution of compensation levels for TVA's 220 top managers as well as the 29 managers who were provided other forms of compensation in addition to their base salaries.

Table 6.1: Total Compensation of Current Top TVA Managers as of Oct. 1, 1988[a]

Compensation range	Total no. of top managers	No. of top managers receiving compensation in addition to base salary
$ 65,000+	31	
70,000+	99	
75,000+	63	2
80,000+	2	2
85,000+	3	3
90,000+	2	2
95,000+	4	4
100,000+	3	3
105,000+	3	3
110,000+	3	3
115,000+	2	2
120,000+	3	3
125,000+	1	1
$200,000+	1	1
	220	29

[a]Compensation includes base salary, supplemental retirement credits, relocation incentives, and bonuses.

TOP MANAGERS WHO LEFT TVA JANUARY 1, 1984-OCTOBER 7, 1988

In addition to top managers on board as of October 1, 1988, we obtained data on the total compensation provided to top managers who terminated their employment during the period from January 1, 1984, through October 7, 1988. According to data provided by TVA, 150 individuals who had been employed at the M-8 through M-13 levels left during that time period. Table 6.2 summarizes the average level of compensation TVA provided the individuals in the year their employment with TVA ended, as well as information reflecting the length of time these individuals had been employed by TVA. We noted that only three of these individuals were provided with a supplemental plan credit or a relocation incentive payment during the year in which their employment ended.

Table 6.2: Characteristics of Top Managers Who Left TVA 01/01/84-10/07/88

	1984	1985	1986	1987	1988
Number of managers who left	16	13	16	23	82
Average total compensation (in dollars)	64,616	63,369	69,693	69,722	72,894
Average TVA service time (in years)	33.6	22.4	25.3	24.6	23.1
Minimum and maximum service times (in years)	12.5 43.5	5.0 38.6	6.5 38.9	1.9 39.8	0.1 41.4
Number receiving additional compensation	0	0	1	0	2
Number of managers by M series:					
M-8	7	6	9	13	47
M-9	0	2	1	2	14
M-10	7	5	4	4	17
M-11	1	0	1	1	2
M-12	1	0	1	2	0
M-13	0	0	0	0	0
M-1N[a]	0	0	0	1	2

[a]Managers in TVA's Nuclear Senior Management Service.

COMPENSATION OFFERS MADE IN 1987 AND 1988 IN THE OFFICE OF NUCLEAR POWER

As requested, we also looked at compensation offers made to top level managers in TVA's Office of Nuclear Power during 1987 and 1988. According to TVA, it offered employment to 72 people from January 1987 to October 1, 1988. Of these offers, 11 were rejected and 61 accepted. Twelve of those accepted were hired in 1988 (through October). Another 12 of those who had accepted TVA offers made in this period subsequently left TVA in 1988. The total compensation packages offered ranged from $73,000 to $217,300, with an average of $94,850. Among those who rejected TVA's offer, compensation packages ranged from $73,950 to $122,100, with an average of $92,713.

All but 1 of the 72 offers made included relocation incentives. These incentives ranged from $9,000 to $100,000, with an average relocation offer of $23,099. Among those people who rejected TVA's employment offer, relocation incentive offers ranged from $10,000 to $48,000.

In addition, four candidates were offered supplemental retirement credits. The supplemental plan credits offered ranged in value from $30,000 to $45,000 each. All who were offered supplemental plan credits were subsequently hired.

SECTION 7

COMPENSATION PROVIDED 12 NEW MANAGERS EMPLOYED BY TVA BETWEEN JANUARY 1 AND OCTOBER 1, 1988

Of the 12 New Top Manager Hires:

- 1 Received Base Salary Only
- 8 Received Only Relocation Incentives in Addition to Base Salary
- 1 Received a Base Salary as Well as Supplemental Retirement Credits for 3 Years
- 2 Received Supplemental Retirement Credits and Relocation Incentives in Addition to Their Base Salary
    - 1 of These 2 Also Has the Potential for Substantial Annual Executive Bonuses

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COMPENSATION PROVIDED 12 NEW MANAGERS EMPLOYED BY TVA JANUARY 1 THROUGH OCTOBER 1, 1988

TVA hired 12 new managers between January 1, 1988, and October 1, 1988, at an average annual base salary of $74,075. The salaries ranged from $70,515 to $77,300. Half of the new hires were employed at the M-8 level.

Only one of the new hires received only salary to join TVA. The remaining 11 received some combination of additional compensation. Eight received only relocation incentives, ranging from $12,000 to $40,000, with an average of $22,875. Three received supplemental retirement credits, ranging from $15,485 to $40,000, or an average of $26,828. One of these also received the guarantee of 2 additional years of supplemental plan credits of $25,000 each. Another of these three received a promise of annual executive bonuses for every subsequent year of satisfactory employment.

SECTION 8

OBJECTIVES, SCOPE, AND METHODOLOGY

In an October 18, 1988, letter, the Chairman, Subcommittee on Oversight, House Committee on Ways and Means, requested at the suggestion of Subcommittee Member Congressman Ronnie Flippo that we examine certain pension and compensation related matters involving top managers of the Tennessee Valley Authority. In general, we were asked to describe TVA's Merit Incentive Supplemental Retirement Income Plan and compare its provisions to the minimum standards set by ERISA and to the tax treatment afforded to state, local, and some private pension plans. We were also asked to identify the types and levels of compensation provided the top level TVA employees, the compensation offers TVA made to prospective top level employees since January 1987, and the compensation "packages" provided to top level employees employed since January 1, 1988. We reviewed the most current data TVA provided on each of these subjects.

We reviewed TVA's Merit Incentive Supplemental Retirement Income Plan (supplemental plan) that augments TVA's regular retirement plan and provides additional retirement income to top managers. We looked at the features of the plan, determined whether it was subject to ERISA, and checked for compliance with the Internal Revenue Code. We also obtained information on supplemental plan transactions from 1979 through November 30, 1988. For all credits and payments granted since January 1, 1986, we reviewed documents showing the TVA Board of Directors' approval, and the rationale for granting the credits.

We verified the accuracy of TVA's data by testing them against transaction records, as follows:

- -- We verified all credits to a sample of accounts for 21 of 209 managers who received supplemental plan credits since January 1, 1986. In total, we verified 51 of the 339 credits (15 percent).
- -- We verified 49 of 278 payments (18 percent) made to former TVA managers since 1979.
- -- We verified a sample of interest accruals made January 1 through November 30, 1988, to the accounts of 63 managers.

There were no errors in the transactions we verified.

As agreed with Subcommittee staff, to address the compensation related questions, we focused on compensation provided between January 1984 and October 1988 to those TVA employees holding positions in TVA's management series M-08 through M-13. Those positions are held by employees considered by TVA to be top level managers. We also looked at compensation offers made to top managers in TVA's Office of Nuclear Power.

In carrying out our work, we relied on information and compensation data provided by TVA and on discussions with TVA officials. We also examined source documentation for selected amounts of compensation provided TVA employees to determine accuracy of data provided by TVA. Our examination of source documentation in these cases showed that the data provided by TVA were consistent with the source documents we reviewed.

Our review was performed between November 1988 and March 1989 in accordance with generally accepted government auditing standards.

Comptroller General
of the United States

Washington, D.C. 20548

B-222334.4

April 4, 1989

The Honorable J. J. Pickle
Chairman, Subcommittee
on Oversight
Committee on Ways and Means
House of Representatives

Dear Mr. Chairman:

In your letter of October 18, 1988, you asked that we review certain pension and compensation-related matters involving upper level employees of the Tennessee Valley Authority (TVA). Our report which will respond to the several questions posed in your letter will be issued shortly.

As also requested, this letter sets forth our legal opinion on the authority of TVA to make payments to its employees which might exceed the statutory limitation of Level IV of the Executive Schedule (currently $80,700) on the salary of TVA employees.1/ For the reasons set forth below, it is our opinion that certain payments which are clearly intended to circumvent the salary limitation are improper.2/

BACKGROUND

TVA's Methods of Compensating Top Managers

In addition to the salary for certain top management positions, the TVA Board of Directors has authorized the creation of (1) the Merit Incentive Supplemental Retirement Income Plan (MISRIP), (2) the Relocation Incentive Plan, and (3) the Executive and Senior Manager Performance Bonus Plan.

Briefly stated, the MISRIP is a deferred compensation plan under which an employee receives certain credits while

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1/ 16 U.S.C. § 831b (1982).

2/ Our opinion is advisory only since TVA has final settlement authority over all claims and expenditures. 16 U.S.C. § 831h (1982). See B-222334, June 2, 1986.

employed by TVA which become payable upon separation or retirement. No taxes are due until the amounts credited are paid to the employee, but the amounts credited are available for loans to the employee. Under the Relocation Incentive Plan, a newly-hired or transferred TVA employee receives a lump-sum payment as an inducement to relocate and accept a top TVA position. It is our understanding that such payments are in addition to the reimbursement of normal relocation expenses. Finally, TVA has recently announced a new performance bonus plan under which about 150 managers and executives will be eligible for bonuses not-to-exceed 30 percent of their annual salary.

The following are examples of payments to employees whose base salary was in excess of $70,000 per year:

--a Senior Vice-President received a $100,000 Relocation Incentive payment and a $40,000 MISRIP credit in 1988;

--a Vice President received a $48,000 Relocation Incentive payment in 1987 and a $30,000 MISRIP credit in 1988;

--a Site Director received a $48,000 Relocation Incentive payment in 1987 and a $36,000 MISRIP credit in 1988;

--a Task Force Manager received a $48,000 Relocation Incentive payment in 1985, a $17,000 MISRIP credit in 1986, and a $47,000 MISRIP credit in 1988;

--a Plant Manager received a $48,000 Relocation Incentive payment in 1987 and a $43,080 MISRIP credit in 1988; and

--the Inspector General received MISRIP credits of $33,500 in 1986, 1987, and 1988, along with a Relocation Incentive payment of $22,000 in 1986.3/

TVA Comments

In response to our request for comments on this inquiry, the General Counsel of TVA, by letter dated February 22, 1989, advised our Office that the above-described compensation arrangements are "fully within TVA's legal authority." The letter states that TVA has broad authority which is

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3/ See B-222334, supra, for a further discussion of these payments to the Inspector General.

analogous to that conferred upon a private corporation to fix the compensation of its employees, and the letter goes on to distinguish "compensation" from "salary," the latter of which is specifically limited by statute. The TVA General Counsel argues that our Office has specifically recognized and accepted that these payments are not part of the salary of a TVA employee.4/ In addition, the letter asserts that the MISRIP credit is an unfunded promise to pay which is not taxable when credits are made and which, therefore, cannot be considered part of the employee's salary. Finally, the letter argues that the relocation payments and performance bonuses, which are one-time, lump-sum payments, are elements of compensation and are clearly not treated as salary for the purposes of the TVA Act.

OPINION

We have addressed some of these issues on two prior occasions in 1981 and 1986, and we find nothing in the TVA arguments which persuades us to change our opinion. The MISRIP and Relocation Incentive "compensation" plans represent a clear and direct circumvention of the salary limitation imposed by the Congress on the salary of TVA employees. That limitation is contained in 16 U.S.C. § 831b, and it states that no employee of TVA shall receive a salary in excess of that received by members of the TVA Board of Directors, currently level IV of the Executive Schedule which is paid $80,700 per year. 5 U.S.C. § 5315 (Supp. IV 1986). This salary limitation will have no meaning if TVA continues to circumvent the limitation by characterizing these payments as "compensation."

In 1981, we considered a proposal by TVA to make payments over a period of 3 years to certain top executives who agreed to remain with TVA.5/ In support of its proposal, TVA argued the distinction between "salary" and "compensation" and argued that such payments were not covered by the statutory salary limitation. We disagreed and held that the proposed retention payments were clearly designed to set a higher rate of compensation for TVA's top executives in contravention of the statutory salary limitation.

In that same opinion we recognized that overtime compensation, occasional bonuses based on job performance or special circumstances, retirement fund contributions, and miscellaneous fringe benefits were not part of "salary" and

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4/ B-205284, Nov. 16, 1981.

5/ B-205284, *supra*.

therefore were properly considered "compensation." However, we specifically held that retention payments of $36,000 per year were designed to set a higher rate of basic pay for TVA's top executives and must be considered part of their "salary." B-205284, supra.

In 1986, we were asked about certain payments to top TVA executives, specifically MISRIP credits and a Relocation Incentive payment to the TVA Inspector General. We held that, to the extent that such payments or credits would exceed the statutory ceiling on salary, they were without legal authority. B-222334, supra. To our knowledge, there have been no significant changes to the MISRIP or Relocation Incentive plans since we issued our opinion in 1986 which would warrant a different conclusion today.

With regard to TVA's performance bonus plan, we note that in a March 1989 announcement, TVA stated the plan would be similar in concept to the Senior Executive Service (SES) bonus plan in existence in many federal agencies. TVA News Release dated March 15, 1989. We recognized in our 1981 opinion that occasional bonuses based on job performance or special circumstances were not subject to the salary limitation. Therefore, if TVA makes payments under a performance bonus plan modeled after the federal SES plan, we would have no objection to such payments.

However, to the extent that TVA uses the plan to circumvent the salary limit in the manner it has used the MISRIP and Relocation Incentive plans for that purpose, we would object to such payments for the reasons set forth above.

As we noted in 1981 and again in 1986, TVA may well be experiencing difficulties in recruiting and retaining top executives due to the salary limitations imposed by the statutory ceiling. We have recognized these problems in many federal agencies, and we have referred to those problems in recent reports. See our Transition Series Report on The Public Service, GAO/OCG-89-2TR (Nov. 1988). If TVA is convinced of the need to raise its salary levels in order to recruit and retain top executives, we believe that TVA should bring that matter to the attention of the Congress for amendment or repeal of 16 U.S.C. § 831b.

We trust that this is responsive to your request for our legal opinion on these matters. We will delay distribution of this letter for 30 days unless we receive further instructions from your office.

Sincerely yours,

Milton J. Socolar

for Comptroller General
of the United States

5 B-222334.4

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