

Chapter 1

DEVELOPMENT OF THE RAILROAD RETIREMENT SYSTEM

Priate pension plans originated in the railroad industry in 1874 when the first formal industrial pension plan in America was established. By 1927, over 80 percent of all railroad employees in the United States worked for employers who had formal plans in operation, but only a small proportion of the employees ever received benefits under these plans. The pension plans had a number of serious defects. They generally paid inadequate benefits and had limited provisions for disability retirement. Credits could not be transferred freely from employer to employer, and the employers could terminate the plans at will. With few exceptions, the plans were inadequately financed and could not withstand even temporary difficulties.

The Great Depression of the early 1930's led to movements for retirement plans on a national basis because few of the nation's elderly were covered under any type of retirement plan. Railroad employees were particularly concerned because the private railroad pension plans could not keep up with the demands made upon them by the general deterioration of employment conditions and by the great accumulation of older workers in the industry. While the social security system was in the planning stage, railroad workers sought a separate railroad retirement system which would continue and broaden the existing railroad programs under a uniform national plan. The proposed social security system was not scheduled to begin monthly benefit payments for several years and would not give credit for service performed prior to 1937, while

conditions in the railroad industry called for immediate benefit payments based on prior service.

Legislation was enacted in 1934, 1935 and 1937 to establish a railroad retirement system separate from the social security program legislated in 1935. Such legislation, taking into account the particular circumstances of the rail industry, was not without precedent. Numerous laws pertaining to rail operations and safety had already been enacted since the Interstate Commerce Act of 1887. Since passage of the Railroad Retirement Acts of the 1930's, numerous other railroad laws have subsequently been enacted.

RAILROAD RETIREMENT ACTS OF THE 1930's

The Railroad Retirement Act of 1934 set up the first retirement system for nongovernmental workers in this country to be administered by the Federal Government. However, the Act was declared unconstitutional by a Federal district court, and this decision was sustained by the Supreme Court. The Railroad Retirement and Carriers' Taxing Acts of 1935 were enacted to avoid the constitutional difficulties encountered by the 1934 Act. However, these Acts were also challenged in the courts, and a Federal district court held that neither the employees nor their employers could be compelled to pay railroad retirement taxes. The court, however, did not prohibit the payment of benefits, and the Railroad Retirement Board began awarding annuities in July 1936 under the provisions of the 1935 Act.

While an appeal was pending, railroad management and labor, at the request of President Roosevelt, formed a joint committee to negotiate their differences. The result was a memorandum of agreement which led to the Railroad Retirement and Carriers' Taxing Acts of 1937 establishing the railroad retirement system. The pensions of retired employees on the railroads' private pension rolls were transferred to the Board's rolls with pension reductions restored. The benefit payments of almost 50,000 pensioners were taken over by the Board in July 1937. There followed an immediate reduction in both the number of employed and unemployed

older railroad workers. By the end of 1938, the number of workers age 65 and over in active railroad service was less than one-half of the number two years earlier. Almost 100,000 employees had retired under the system by that date, 80 percent of them under the nondisability annuity provisions.

Features of the 1937 Act

The 1937 Act set up a staff retirement plan which provided annuities to aged retired employees based on their creditable railroad earnings and service. The amounts of retirement annuities awarded were directly related to the employee's earnings and length of service, with a maximum of \$120 a month. Creditable earnings were limited to a maximum of \$300 a month, while no more than 30 years of service could be credited when service before 1937 was counted. Annuities could be paid at age 65 or later, regardless of length of service, or at ages 60-64 (on a reduced basis) after 30 years of service.

The conditions for paying annuities based on disability were severely restricted. The disability had to be total and permanent and 30 years of service were required for full annuities. Employees could receive disability annuities at ages 60-64 after less than 30 years of service, but on a reduced basis.

The Act made little provision for dependents of deceased employees and no provision for spouse annuities. A survivor could receive a lump sum equal to 4 percent of the employee's creditable earnings after 1936, less any annuity payments already made. In addition, a retiring employee could elect to receive a reduced annuity in order to provide an annuity to his surviving spouse.

The system was financed by a schedule of taxes beginning with 2.75 percent each on employers and employees applicable to the first \$300 of monthly compensation.

AMENDMENTS TO THE 1937 ACT

Numerous amendments after 1937 increased benefits and added, to what began as a staff retirement system, social insurance features similar to those provided by the social security system.

The first significant sets of amendments were enacted in 1946 and 1951. By initiating coordination in certain areas with the social security system, they laid the foundation for the evolution of the system's present structure. **Amendments enacted in 1946** added survivor benefits to the railroad retirement system which were similar to those provided under social security coverage, but approximately 25 percent higher.

These amendments also introduced the first step of coordination with the social security system by dividing jurisdiction over individual survivor benefits between the Board and the Social Security Administration. Benefits to survivors were thereafter based on combined railroad retirement and social security earnings credits.

Provisions for annuities based on occupational disability—a staff retirement feature—were also established by the 1946 amendments. The provision for occupational disability annuities recognized that employees who were not totally disabled could be prevented from earning a living because they could not perform their regular jobs. The 1946 amendments also reduced the service requirements for total disability annuities, making it possible for comparatively young disabled employees to receive benefits.

In addition, the amounts of disability retirement annuities were increased through the elimination of the reduction for employees with less than 30 years of service and the extension of new minimum provisions of the law to annuities based on disability. In 1954, annuities were provided for disabled children of deceased employees. And in 1968, disabled widows ages 50-59 were added to those who could receive benefits.

Amendments enacted in 1951 added annuities for the spouses of retired railroad employees. This legislation completed the addition of social insurance features to the railroad retirement system and expanded the coordination of the railroad retirement and social security systems.

Provision was made for social security to assume jurisdiction of benefits for employees not having at least 10 years of railroad service, and a minimum guaranty was provided to ensure that railroad retirement benefits would be no less than the benefit, or additional benefit, the social security system would have paid on the basis of the railroad service involved. In addition, a financial interchange was established between the two systems to apportion the costs of benefits and taxes, related to railroad service, between the two systems on an equitable basis.

In 1965, provision was made to coordinate the railroad retirement tax base and tax rate with those of the social security system. This provision and the existing provisions for the financial interchange served as an operating vehicle through which the Medicare program was easily extended in 1965 to railroad employees and members of their families, on the same basis as it was provided for social security beneficiaries. The addition of a strictly staff benefit for career employees was provided **in 1966** in the form of supplemental railroad retirement annuities.

By 1970, amendments to the Act provided for regular annuities of more than double the amount provided under the original formula. The amounts of earnings creditable and taxable were \$650 a month in 1970 compared with \$300 originally. Tax rates had substantially increased in order to finance the new types of benefits, the increases in benefit amounts and other liberalizations in the program. The rate of regular railroad retirement taxes, still divided equally between employees and employers in 1971, was 9.95 percent on each as compared with 3.5 percent in 1946.

The annuities being paid in 1970 included a general benefit increase of 15 percent provided in that year following a social security benefit increase of 15 percent. In the following two years of an inflationary spiral in the national economy, social security and

railroad retirement benefits were again substantially increased, by 10 percent in 1971 and 20 percent in 1972. However, these three increases were provided for railroad retirement annuities on a temporary basis only. The costs of making these three increases aggregating 51.8 percent permanent without adequate financing would have jeopardized the solvency of the system. Congress directed that a Commission on Railroad Retirement be formed to study the railroad retirement system and its financing for the purpose of recommending to Congress changes in the system that would ensure adequate benefit levels on an actuarially sound basis.

Report of the Commission

The Commission's 1972 report proposed a restructuring of the railroad retirement system with two separate tiers of benefits, tier I being a social security-type benefit and tier II a supplemental staff benefit. It also recommended a phaseout of dual railroad retirement-social security benefits with some protection for the vested rights to such benefits already acquired by employees. Under the 1937 Act, an individual engaging in covered employment under both the Railroad Retirement Act and the Social Security Act was entitled to separate benefits under both Acts, assuming he or she met at least the minimum requirements for benefit eligibility. By the early 1970's, approximately 40 percent of all beneficiaries on the Board's rolls were also receiving social security benefits. Because of certain duplications in their dual benefits, considered a windfall element, the total of their benefits from both systems averaged more than the annuities of railroad employees who worked in the rail industry exclusively, and who had paid proportionally higher retirement taxes for the purpose of receiving higher benefits. At the same time, dual benefits were a cost to the railroad retirement system because they reduced the system's income from its financial interchange with the social security system. (By the mid-1970's, the costs to the railroad retirement system of dual benefits exceeded \$450 million per year and would have been a major factor in bankrupting the railroad

retirement system if allowed to continue. The cumulative total loss to the system by 1974 had been about \$4 billion.)

Upon the release of the Commission's report, Congress ordered that representatives of employees and representatives of carriers negotiate mutual recommendations for a restructuring of the railroad retirement system which would put it on a sound financial basis, taking into account the report and recommendations of the Commission on Railroad Retirement.

Preliminary Agreement

The preliminary recommendations of management and labor for revision of the railroad retirement system, recorded in a Memorandum of Understanding, were enacted by the Congress in 1973. The major provisions, which reflected components of an industry-wide wage settlement, effected a redistribution of railroad retirement taxes and earlier retirement as follows. Generally effective October 1, 1973, employee and employer tax rates under the Railroad Retirement Tax Act were revised so as to reduce the employee rate to the percentage rate paid by employees in social security covered employment, with the employer absorbing the difference so that total tax income to the program was maintained at the level in effect before the change. Employee rates consequently were lowered from 10.60 percent of creditable earnings to 5.85 percent; employer rates correspondingly increased from 10.60 percent to 15.35 percent. Effective July 1, 1974, all employees at least 60 years of age and having 30 years or more of creditable railroad service could retire without their annuities being subject to reduction for retirement before age 65. Under previous law, only female employees were granted this advantage.

RAILROAD RETIREMENT ACT OF 1974

The Railroad Retirement Act of 1974, reflecting the basic principles of the Commission Report and incorporating the subsequent management-labor agreement, was enacted on October 16, 1974.

Two-tier Formulas

The 1974 Act provided a tier I formula yielding amounts equivalent to social security benefits, taking into account both railroad retirement and nonrailroad social security credits. A tier II formula, based on railroad service exclusively, provides benefits comparable to those paid over and above social security benefits by other industrial pension systems. The total annuity yielded by the tier formulas continued traditional levels of railroad retirement benefits and reflected the three cost-of-living increases aggregating 51.8 percent, which had been provided between 1970 and 1972 on a temporary basis.

Dual Benefit Phase-out

The 1974 Act eliminated duplications in dual railroad retirement-social security benefits for new hires and individuals not vested as of December 31, 1974, under both programs. Dual benefits for vested employees were protected through provision for payment of an amount in their annuities referred to as a “vested dual benefit.” However, such vested dual benefit amounts were not allowed to increase because of any social security credits earned after December 31, 1974.

For career employees, vesting was defined as having 10 years of railroad service on December 31, 1974, and, in addition, having enough quarters of coverage under the social security program to be entitled to a benefit at age 62 if no further social security credits were acquired after December 31, 1974.

Vesting for employees who had fully qualified for benefits under both systems but had left the industry prior to 1974 presented a difficult problem. The 1974 Act favored employees who had remained in the railroad industry more than those who left railroad employment. Accordingly, active or long-term employees in the railroad industry in a sense were placed in the same situation as employees who had already retired, while former employees were made subject to more stringent requirements. The resulting

vesting provisions were subsequently tested in the courts and upheld by the U.S. Supreme Court in 1980.

Cost-of-living Increases

The 1972 amendments to the Social Security Act introduced provisions for cost-of-living adjustments in social security benefits on the basis of changes in the Consumer Price Index. Under the two-tier plan, the first tier railroad retirement benefit increases automatically the same way social security benefits increase. Four separate tier II cost-of-living adjustments were provided during the six-year period commencing January 1, 1975. (A fifth increase was provided in subsequent legislation.)

Benefit Improvements

The 1974 Act also provided improvements in existing benefits. The initial agreement of labor and management had enabled employees to retire on or after July 1, 1974, on unreduced annuities if they met the eligibility requirements of attaining age 60 and completing 30 years of service. But an employee could not receive a supplemental annuity until age 65 nor could a spouse receive a spouse annuity until the employee reached age 65. The Act revised the eligibility requirements for these benefits so that they were coordinated directly with the employee annuity requirements.

And under the 1937 Act, the vast majority of widows and other survivors received benefits based upon 110 percent of the comparable social security benefit, and the resulting amount was generally felt to be inadequate in relation to the level of other railroad benefits. The 1974 Act survivor formula increased the calculation basis to 130 percent from the former 110 percent.

Financing

It was anticipated that the changes in the benefit formulas, the reduction in dual benefits, higher investment earnings, plus provisions for additional funds from the Federal Government to pay the

phase-out costs of dual benefits, together would place the railroad retirement system on a reasonably sound basis. However, the cost estimates made at that time did not anticipate the resurgence of substantial inflation in the latter part of the decade, which led to a recurrence of financial difficulties for the railroad retirement system.

With regard to financing the phase-out costs of dual benefits, the joint management-labor committee initially proposed that the cost of vested dual benefit payments be paid out of the social security trust funds, as this element was basically a social security benefit. However, Congress concluded that the cost should be borne by the General Treasury. It was thought that it would be unfair to impose this cost upon current and future employees who would not (except where vested rights are involved) be permitted to receive dual benefits upon retirement, or upon the railroads since the excess benefit arose out of nonrailroad employment performed by these individuals. Payment out of the General Treasury was supported by a precedent regarding military service and by the fact that the dual benefit problem had been brought about by prior congressional action repealing past dual benefit restrictions over the objections of the railroads.

1981 RAILROAD RETIREMENT AMENDMENTS

By 1980, recurring inflation and recession combined with other factors placed financial stresses on the railroad retirement system which made it clear that further financial action was needed to maintain the system. Railroad retirement amendments were subsequently enacted on August 13, 1981, as part of an Omnibus Budget Reconciliation Act. The amendments were generally effective October 1, 1981.

These amendments increased railroad retirement taxes on both rail employers and employees. While tier I taxes on employers and employees remained at the same rate as social security taxes, 6.65 percent in 1981, the 9.5 percent tier II tax paid by employers was increased by 2.25 percent to 11.75 percent and employees

assumed a tier II tax of 2 percent. The amendments also gave the Railroad Retirement Board the authority to borrow from U.S. Treasury general funds on the basis of forthcoming financial interchange income if Railroad Retirement Account funds were insufficient to pay benefits during a month.

Although the two-tier benefit structure provided by the 1974 Act was left intact, changes were made in the tier II formula and there were other changes in benefit provisions. The amendments revised the employee, spouse, and survivor formulas for annuity portions paid over and above social security levels. For retirees whose annuities are awarded on or after October 1, 1981, the simplified formula yields awards that automatically keep pace with average wage increases in the last 60 months of service. The 1981 law continued tier II employee and spouse cost-of-living increases, while revising survivor cost-of-living increases to correspond with those provided employees and spouses. It also broadened the current connection requirement applicable to certain career employee benefits. While the amended law eliminated future supplemental annuity closing dates, it restricted future supplemental annuity eligibility to employees with some service prior to October 1981. In addition, the amendments provided benefits for divorced spouses, surviving divorced spouses and remarried widow(er)s which are like those provided under the Social Security Act.

This legislation also required prorated adjustments in individual vested dual benefit payments, depending upon the amounts appropriated to the fund created for these payments, and the level of vested dual benefit payments was made contingent on the annual Federal budget and appropriations process. The amendments restricted the further award of vested dual benefit payments to vested employees with dual coverage on their own earnings, and precluded further awards of vested dual benefit payments to spouses or widows.

The 1981 amendments mandated, in the event of certain adverse financial indicators, that railway management and labor, and the White House, make further financing recommendations to Congress. And the new law required the Railroad Retirement

Board to reduce annuity levels during any fiscal year in which it appears there would be insufficient funds with which to make full benefit payments on a timely basis for every month of the year.

In the first half of 1981, when the amendments were developed, it was anticipated that the financing arrangements would provide the railroad retirement system with adequate funding throughout the 1980's. However, the continuing recession in the national economy depressed rail traffic levels to the extent that large-scale layoffs were underway by the first quarter of 1982. Average monthly employment in fiscal year 1982 dropped to 457,000 from the 512,000 average of the previous year, and it subsequently declined to 388,000 in the first quarter of 1983. The decline in employment limited payroll tax income accordingly. In addition, increased unemployment benefit payments resulting from the layoffs made such unprecedented demands on the Railroad Unemployment Insurance Account that it owed \$500 million to the Railroad Retirement Account by the end of March 1983.

The condition of the Railroad Retirement Account consequently deteriorated to the point that the Board was required to prepare to reduce annuity levels on October 1, 1983, by an estimated 40 percent of tier II portions, in the absence of remedial financial legislation.

RAILROAD RETIREMENT SOLVENCY ACT OF 1983

The scheduled annuity reductions were averted by enactment of the Railroad Retirement Solvency Act on August 12, 1983. The 1983 Act was based on negotiated recommendations of management and labor, and also incorporated recommendations of Congress and the Administration. The amendments were, in part, patterned after major social security amendments enacted earlier in the year, which had already effected changes in railroad retirement taxes and benefits through coordinating provisions in the Railroad Retirement Act.

Taxes

Under the Railroad Retirement Solvency Act, tier II taxes on employers increased from 11.75 percent to 12.75 percent in January 1984, to 13.75 percent in January 1985, and to 14.75 percent in January 1986. Tier II taxes on employees increased from 2 percent to 2.75 percent in 1984, to 3.50 percent in 1985, and to 4.25 percent in 1986. And since 1985, railroad retirement taxes are applied to earnings on an annual, rather than a monthly, basis. As a result of the 1983 social security amendments, tier I taxes on employers and employees increased from 6.70 percent to 7 percent in January 1984, to 7.05 percent in 1985, to 7.15 percent in 1986, to 7.51 percent in 1988 and to 7.65 percent in 1990.

The 1983 social security amendments subjected railroad retirement tier I annuity portions to Federal income taxes on the same basis as social security benefits and the Solvency Act made tier II benefits and vested dual benefit payments subject to Federal income tax on the same basis as private and public service pensions, beginning with tax year 1984. The revenues raised from income taxes on tier I and vested dual benefits are used for benefit payments. Revenues raised by the tax on tier II benefits were to be used for benefit payments through fiscal year 1988, after which the revenues would remain in general Treasury funds. Subsequent legislation extended these transfers permanently.

Other Financing Provisions

The Railroad Retirement Account was reimbursed in three installments from the general fund of the Treasury for shortfalls in vested dual benefit appropriations between 1975 and 1981. The railroad retirement system's authority to borrow general U.S. Treasury funds until the Board receives financial interchange funds from the social security system was broadened to place financial interchange monies in the Railroad Retirement Account effectively on a current basis.

Benefit Provisions

The 1983 social security amendments deferred July 1983 cost-of-living increases to January 1984 and required that future

increases be made in January of subsequent years. This deferral applied to railroad retirement tier I annuity amounts as well as social security benefits. The Railroad Retirement Solvency Act correspondingly changed the future payment dates of tier II cost-of-living increases from July 1 to January 1, with the first increase payable on January 1, 1985. It also required an offset of the dollar amount of the next five percent of tier I cost-of-living increases from tier II benefits.

The Act modified early retirement provisions for 30-year employees attaining age 60 after June 1984 by applying certain reductions to the tier I portions of their annuities if they retired before age 62. The reductions did not affect tier II benefits, and employees who acquired 30 years of service and attained age 60 before July 1, 1984, could still retire at any time with full benefits, as under prior law. (The Railroad Retirement and Survivors' Improvement Act of 2001 as described on pages 17-20 eliminated these reductions for 60/30 employees retiring after 2001.) The 1983 law established a five-month waiting period for railroad retirement disability annuities, just as for social security disability benefits, and altered the tier I computation of annuities subject to reduction for certain non-covered service pensions. It required the Board to honor court orders that treat non-tier I railroad retirement benefits as property subject to division in proceedings related to divorce, annulment or legal separation. And the Act limited the retroactivity of applications for benefits to a maximum of six months to conform to the Social Security Act, except for disability benefit applications, which can retroact 12 months.

The Solvency Act eliminated annuity reductions made under prior law when military service was counted as railroad service and was also the basis for benefits under another Federal law. It conformed railroad retirement student benefit provisions to social security student benefit provisions and eliminated age reductions applied to disabled widow(er)s' annuities for months they were under age 60 when their annuities began.

LEGISLATION ENACTED 1985-2000

The **Balanced Budget and Emergency Deficit Control Act of 1985**, known as the Gramm/Rudman/Hollings Act, enacted in December 1985, required decreases in vested dual benefit payments during the 1986 fiscal year and suspension of the January 1986 cost-of-living increase in the tier II portions of railroad retirement annuities. Gramm/Rudman and/or related budget legislation reduced vested dual benefits and supplemental annuities periodically in subsequent years.

Budget reconciliation legislation enacted in April 1986 included changes in Internal Revenue Code provisions increasing income taxes on some railroad retirement annuities. Effective with tax year 1986, the tier I portion of a railroad retirement annuity, which is treated as a social security benefit for Federal income tax purposes, was limited for tax purposes to amounts actually equivalent to social security benefits. This primarily affected tier I early retirement benefits payable between ages 60 and 62 and some occupational disability benefits that are now treated like private and public service pensions. The **Tax Reform Act of October 1986** eliminated, for annuities beginning after July 1, 1986, the three-year recovery rule for contributory pensions, making railroad retirement benefits exceeding social security equivalent levels taxable immediately upon retirement. For tax reporting purposes, benefit payments are prorated on the basis of estimated life expectancies to exempt an employee's previously-taxed pension contributions.

In 1987, the continuing decline in railroad employment led to concern over the system's financing in the next century. A Federal budget deficit reduction bill consequently increased tier II tax rates in January 1988 to 16.10 percent on employers and 4.90 percent on employees, and extended for one year, until October 1, 1989, the time during which revenues from Federal income taxes on tier II railroad retirement benefits could be transferred to the Railroad Retirement Account for use in paying benefits.

Amendments enacted in 1988 eliminated the provision suspending annuities of retired employees and spouses who work for their last pre-retirement nonrailroad employers, but provided for tier II earnings deductions in such cases. These amendments also increased the amount disabled railroad retirement annuitants can earn without reducing their benefits from \$200 per month to \$400 per month, exclusive of work-related expenses.

In addition, these amendments provided a lump sum, equal to railroad retirement tier II payroll taxes deducted from separation or severance payments made after 1984, to be paid upon retirement to employees meeting minimum service requirements if the separation or severance payments did not yield additional railroad retirement service or earnings credits.

The **1989 budget laws effective in 1990** increased the amount of earnings subject to social security and railroad retirement payroll taxes, and specified that 401(k) contributions and some employer-paid life insurance premiums are subject to railroad retirement payroll taxes, conforming railroad retirement with social security.

Omnibus budget legislation in 1990 permanently exempted supplemental annuities from reductions under the Gramm/Rudman Act. It also increased the maximum compensation subject to Medicare hospital insurance payroll tax and mandated an expedited payroll tax deposit schedule for large employers covered by social security or railroad retirement. **Budget legislation enacted in 1993** made all earnings subject to the Medicare payroll tax and, for those in high tax brackets, made a larger amount of social security and railroad retirement tier I benefits subject to Federal income tax.

The time during which revenues from Federal income taxes on tier II railroad retirement benefits could be transferred to the Railroad Retirement Account for use in paying benefits was extended one year in 1989, and 1990 budget legislation further extended the date until October 1, 1992. In **1994, legislation** extended the transfers, retroactive to October 1992, on a perma-

ment basis which improved the financing of the railroad retirement system.

Legislation enacted in April 2000 eased the earnings restrictions affecting social security beneficiaries working after full retirement age. The legislation also applied to railroad retirement annuitants but it did not change the railroad retirement work restrictions applying to last pre-retirement employment which are not included in the Social Security Act.

THE RAILROAD RETIREMENT AND SURVIVORS' IMPROVEMENT ACT OF 2001

The Railroad Retirement and Survivors' Improvement Act of 2001, signed into law December 21, 2001, liberalized early retirement benefits for 30-year employees and their spouses, eliminated a cap on monthly retirement and disability benefits, lowered the minimum service requirement from 10 years to 5 years of service if performed after 1995, and provided increased benefits for some widow(er)s. Financing sections in the law provided for the investment of railroad retirement funds in nongovernmental assets, adjustments in the payroll tax rates paid by employers and employees, and the repeal of a supplemental annuity work-hour tax. The law was based on joint recommendations to Congress negotiated by a coalition of rail labor organizations and rail freight carriers.

60/30 Retirement

The law amended the Railroad Retirement Act by eliminating the early retirement reduction applied to the annuities of 30-year employees retiring between the ages of 60 and 62 if their annuities begin January 1, 2002, or later. The spouses of such employees are also eligible for full annuities at age 60. Full 60/30 benefits had not been payable since 1983 legislation reduced such early retirement benefits.

Maximum Provision

The law eliminated, effective January 1, 2002, a maximum on the amount of combined monthly employee and spouse benefit payments which had been intended to prevent benefits from exceeding an amount based on an employee's earnings immediately prior to retirement. This maximum provision had the unintended effect of reducing benefits for former employees with no earnings, or low earnings, in the 10-year period prior to retirement, and for long-service employees with moderate earnings.

Basic Service Requirement

The legislation lowered the minimum eligibility requirement for regular railroad retirement annuities from 10 years (120 months) of creditable railroad service to 5 years (60 months) of creditable railroad service for those with 5 years of service rendered after 1995. Benefits payable on the basis of this provision are not retroactive and are not payable earlier than January 1, 2002.

Widow(er)s' Benefits

The legislation established an "initial minimum amount" based on the two-tier annuity amount that would have been payable to the railroad employee at the time the widow(er)'s annuity is awarded, minus any applicable reductions. Widow(er)s' annuities computed on the basis of the new initial minimum amount will not increase until the amount payable under previous law plus cost-of-living increases is higher than the initial minimum amount.

This provision was effective February 1, 2002, and was not retroactive. It applies to widow(er)s on the rolls before the effective date only if the annuity the widow(er) was receiving on the effective date was less than she or he would have received had the legislation been in effect on the date the widow(er)'s annuity began.

Investment Changes

The legislation provided for the transfer of railroad retirement funds from the Railroad Retirement Accounts to a new National Railroad Retirement Investment Trust, whose Board of seven trustees is empowered to invest Trust assets in non-governmental assets, such as equities and debt, as well as in governmental securities.

The Trust is not treated as an agency or instrumentality of the Federal Government and its trustees are subject to reporting and fiduciary standards similar to those under the Employee Retirement Income Security Act.

Effect on Payroll Tax Rates

The legislation reduced tier II tax rates on rail employers, including rail labor unions, in calendar years 2002 and 2003, and beginning with 2004 provides automatic adjustments in the tier II tax rates for both employers and employees. It also repealed the supplemental annuity work-hour tax rate paid by employers, beginning with calendar year 2002.

The tier II tax rate on rail employers and rail labor organizations was reduced from 16.10 percent to 15.60 percent in 2002 and to 14.20 percent in 2003. The tier II tax rate for rail employee representatives is 14.75 percent in calendar year 2002 and 14.20 percent in 2003.

While there was no change in the tier II tax rate of 4.90 percent on employees in the years 2002 and 2003, beginning with the taxes payable for calendar year 2004 tier II taxes on both employers and employees will be based on the ratio of certain asset balances to the sum of benefits and administrative expenses (the average accounts benefits ratio). Depending on the average account benefits ratio, tier II taxes for employers will range between 8.20 percent and 22.10 percent, while the tier II tax rate for employees will be between 0 percent and 4.90 percent.

Supplemental Annuity Funding

In addition to repealing the supplemental annuity work-hour tax, the legislation eliminated the separate Supplemental Annuity Account. Supplemental annuities are now funded through the new National Railroad Retirement Investment Trust.