



**HEARING BEFORE**

**COMMITTEE ON WAYS AND MEANS, SUBCOMMITTEES ON  
SOCIAL SECURITY AND OVERSIGHT  
UNITED STATES HOUSE OF REPRESENTATIVES**

**JUNE 29, 2017**

**STATEMENT  
OF  
MARIANNA LACANFORA  
ACTING DEPUTY COMMISSIONER FOR RETIREMENT AND DISABILITY POLICY  
SOCIAL SECURITY ADMINISTRATION**

Chairman Johnson, Chairman Buchanan, Ranking Member Larson, Ranking Member Lewis, and Members of the Subcommittees:

Thank you for the opportunity to discuss Social Security coverage and the Social Security Administration's partnership with the Internal Revenue Service and State Social Security Administrators to provide for Social Security coverage of certain State employees while collecting commensurate Social Security taxes. My name is Marianna LaCanfora and I am SSA's Acting Deputy Commissioner for Retirement and Disability Policy.

### **Importance of Social Security**

Social Security is a social insurance program, under which workers earn coverage for retirement, disability, and survivors' benefits by earning wages through employment or income through self-employment. Those same wages are subject to Federal Insurance Contributions Act (FICA) or Self-Employment Contributions Act (SECA) taxes.

Social Security pays monthly benefits to more than 60 million individuals, consisting of 41 million retired workers and 3 million of their spouses and children; nearly 9 million disabled workers and almost 2 million dependents; and 6 million surviving widows, children, and other dependents of deceased workers. Last year, these benefits totaled around \$905 billion. Administrative costs were less than 1 percent of benefit payments.

### **Coverage of Earnings for Social Security**

Individuals obtain coverage for Social Security retirement, disability, and survivors' insurance benefits by establishing a history of earnings based on their wages. Wages are defined in section 209 of the Social Security Act as money paid for work or a service in an employer-employee relationship. Wages do not include payments made outside of an employment relationship, such as life insurance proceeds, tax refunds, child support payments, scholarships, proceeds from the sale of a home, court awards, royalties, unemployment benefits, public assistance, or canceled debts.

In 2017, employees and employers each pay 6.20 percent (or for self-employed individuals, the individual pays 12.40 percent) on the first \$127,200 of an employee's wages or self-employed income in Social Security taxes. If an individual's employment and earnings are covered for Social Security, he or she should pay these taxes on his or her wages.

Ninety-four percent of employees working in the United States are covered by Social Security. There are, however, exceptions to coverage for certain employees of private employers, and more commonly, for certain State and local government employees. Coverage (and coverage exceptions) are dictated by section 210 or section 218 of the Social Security Act.

Section 210 explains coverage for work performed for, among other entities, private U.S. employers and the District of Columbia. While most private work is covered, section 210 explains the exceptions to coverage for private workers (including work performed in certain

religious roles, as a Native American tribal council member, by certain students, by foreign workers, or by temporary, emergency workers).

Section 218 involves work performed for State and local government employers and explains the process by which States may request coverage for their government workers, under a Section 218 Agreement. These agreements are created at a State's discretion and, as long as they comply with relevant Federal and State laws, the Social Security Act requires the extension of Social Security coverage to the State and local government employees specified under the agreement. All 50 States, Puerto Rico, the Virgin Islands, and approximately 60 interstate instrumentalities have entered into a Section 218 Agreement with SSA.

### *History of Section 218*

When the Social Security Act was enacted in 1935, Social Security coverage was not extended to State and local government employees due to legal questions over the Federal Government's ability to tax the States. However, because many government employers did not have their own retirement system, the Social Security Act Amendments of 1950 authorized States to enter into voluntary agreements with SSA to extend coverage to their public employees. These Section 218 Agreements originally only allowed for voluntary Social Security coverage to State and local government employees who were not covered by a retirement system. The Social Security Amendments of 1954 expanded the Act to authorize the States to extend Social Security coverage to all State and local government employees who are members of public retirement systems, if coverage group members vote in a referendum for such coverage.

The coverage provided under Section 218 Agreements varies substantially between, and within, States. When a State enters into a Section 218 Agreement, employees are brought under the agreement in coverage groups. There are two types of employee groupings for coverage purposes: absolute coverage groups, composed of positions that are not under a retirement system; and retirement system coverage groups, composed of positions that are under a retirement system. The State decides which coverage groups it would like covered and the effective date of coverage, subject to Federal and State laws, and works with SSA to formalize that coverage in the State's agreement.

Each State may have only one Section 218 Agreement, but the State may request modifications to its agreement as political subdivisions, public employment positions, and retirement systems are created, or if groups decide they would like to obtain Social Security coverage. Such modifications must meet the requirements of the Social Security Act and State laws. Additionally, if the coverage group is covered by a retirement plan, the group must first vote in a referendum for Social Security coverage.

The Social Security Amendments of 1956 authorized 23 States to divide a retirement system established by the State or instrumentality based on whether individual employees under that system desire Social Security coverage. Under the divided-vote procedures, a referendum is held for a coverage group, and the Section 218 Agreement modification provides coverage for only those members who voted for coverage, as well as all members who are newly hired after the modification goes into effect. Thus, under such a divided system, if two employees are

performing the same work in the same position for the same employer under the same retirement system, one's employment could be covered, while the other's is not.

Before 1983, a State could terminate Social Security coverage for employees covered under its Section 218 Agreement. The 1983 Social Security Amendments rescinded this provision of the Act, prohibiting States from terminating coverage. Consequently, groups of State and local government employees generally cannot have their coverage rescinded.

The Consolidated Omnibus Budget Reconciliation Act of 1985 made Social Security coverage mandatory for State and local government employees who were neither covered under a Section 218 Agreement nor members of a public retirement system (that offers, at a minimum, retirement benefits comparable to those provided by Social Security), beginning July 2, 1991.

The change of laws and the flexibility that the laws have provided to the States have led to great variability regarding coverage for Social Security. One State may, for example, cover all of its teachers under a retirement system, and choose not to extend Social Security coverage to those positions. Another State may cover its teachers under a retirement system, but also provides its teachers an option to obtain additional, voluntary Social Security coverage through a referendum and subsequent modification to the State's Section 218 Agreement. A third State may provide retirement system and Social Security coverage to its teachers, but because of the divided-vote option, some individual teachers may fall outside of that coverage. Another State may provide neither voluntary Social Security nor retirement system coverage to its teachers, resulting in mandatory Social Security coverage even though the State's Section 218 Agreement does not establish that coverage. Likewise, these examples could all be present within a single State, depending on how the State defined its coverage groups.

### **Roles of Government Agencies and Non-Governmental Groups**

Due to the complex nature of both Section 218 Agreements and the exceptions to coverage under section 210 of the Social Security Act, many groups are involved in determining employees' coverage status and, subsequently, in monitoring that FICA taxes are being paid correctly.

Employers are the first and most important group, as they are ultimately responsible for appropriately withholding their employees' taxes, including FICA taxes. Employers are also generally in the best position to differentiate between individual employees' coverage statuses because they deal with their employees at an individual, unaggregated level. Under section 210, most private employees are covered. For State and local employees, however, coverage can vary substantially between States, positions, retirement systems, and even individual employees. To determine whether FICA is applicable under section 218, the State or local employer must determine if an employee's position is covered under the State's Section 218 Agreement. If not, the employer must then determine whether the employee is mandatorily covered under section 210 by establishing whether the employee is a member of a public retirement system. Using this information, employers are responsible for determining whether an individual is covered for Social Security and if FICA taxes should be withheld.

State and local employers often receive additional help in making coverage determinations, due to the complexity inherent to Section 218 Agreements. SSA, through regulation, requires each State to have a State Social Security Administrator (State Administrator). The State Administrator is a State employee who is responsible for maintaining and administering provisions of the State's Section 218 Agreement. The administrator is responsible for determining which State and political subdivision employees are covered by approved Section 218 Agreements and modifications, facilitating the expansion of coverage through additional modifications to the State's agreement, and providing SSA updates when there are changes in covered State or political subdivision entities. They also work with State and local employers to guarantee proper Social Security withholding and reporting, provide education to State and local employers and employees, and resolve coverage and taxation questions in coordination with SSA and IRS. The State Administrator also plays a central role in communicating information between SSA and State and local entities. Because Section 218 Agreements are voluntary agreements between SSA and the States, SSA's communications to State and local entities must flow through the State Administrator. State Administrators are an essential part of this process and we appreciate the service they provide and the hard work that they do.

SSA primarily provides support by confirming coverage status under a State's Section 218 Agreement. At the State Administrator's request, we explain entities' coverage options, review proposed modifications to the State's Section 218 Agreement for legal sufficiency, and evaluate the coverage status of entities and positions when questions arise. We interpret, execute, and maintain Section 218 Agreements, as specified under section 218 of the Social Security Act and in coordination with State laws. We work closely with the State Administrators and their umbrella organization, the National Conference of State Social Security Administrators (NCSSSA), to identify coverage compliance risk factors, answer questions, and resolve any issues that arise. We also assist in educating the administrators on complex or error-prone aspects of coverage and provide them with the information necessary to understand and administer complex coverage situations under section 218. We also support State Administrators with outreach to State and local entities and by participating in educational sessions for referendum voters. Finally, we are also responsible for establishing and maintaining our earnings records based on the amount of wages paid to employees.

Prior to 1987, SSA was responsible for collecting Social Security and Medicare contributions from the States and ensuring that each State paid the correct amount of FICA taxes for all employees covered under its Section 218 Agreement. The State Administrators were responsible for ensuring that State and local government employers filed timely and accurate returns and that they collected and paid the proper amount of Social Security and Medicare contributions to the Federal government.

Effective January 1, 1987, the Omnibus Budget Reconciliation Act of 1986 transferred responsibility for collecting employment taxes for wages paid under Section 218 Agreements from SSA and the States to the IRS. State and local employers are now required to file Form 941, the Employer's Quarterly Federal Tax Return, with the IRS directly, and the IRS is responsible for collecting Social Security and Medicare taxes. In addition to collecting taxes, the IRS verifies the amount of taxes owed and determines the amount that has been paid. It is also responsible for

interpreting FICA-related provisions of law and ensuring proper reporting and collection of taxes.

Finally, in addition to the important roles that employers, State Administrators, SSA, and the IRS play, employees are offered the opportunity to regularly review the taxes that are being withheld via their pay stubs and tax documentation. To assist with this and to allow individuals to review the benefits their covered earnings should provide them, individuals may access their earnings records through the *Social Security Statement*, which is available to them at any time through a *my Social Security* account.

## **Earnings Corrections**

The Social Security Act directs us to presume that our earnings records are correct as posted. Employers are responsible for classifying wages as covered or non-covered and reporting earnings appropriately. That said, there are instances in which we need to correct an individual's posted earnings.

We frequently learn of small-scale errors through what is known as the "reconciliation" process. Every year, the IRS and SSA compare the wage information that employers report to the IRS on form 941 with the earnings report information that SSA obtains from processing forms W-2 and W-3. If the employer's aggregate Social Security and Medicare wage amounts do not correspond to the W-2 and W-3 totals, then either IRS or SSA investigates and resolves the discrepancy, depending on the nature of the discrepancy. However, the reconciliation process will not catch situations where employers have misidentified their employees' earnings as covered or not covered.

We may find errors when individuals apply for Social Security benefits. In the course of reviewing an individual's application, we investigate inconsistencies, such as gaps, which may indicate an error in employer-reported earnings information. If an applicant informs us that his or her earnings record is incorrect, we request primary evidence of his or her earnings (e.g., a Form W-2 or W-2c, an employer-prepared wage statement, a statement of an employer, or a pay stub) or two pieces of secondary evidence to corroborate his or her claim. If our review of the evidence leads us to determine that our posted earnings are incorrect, we correct the Social Security wages in our system. The earnings correction determination is then sent to the IRS to alert it to the possibility of uncollected taxes.

We note that Social Security insured status and benefit payment depend upon the amount of an individual's covered earnings and not on the FICA taxes that he or she has paid. The Act bases covered earnings on an individual's wages, and not on the amount of FICA paid for that individual. If we detect an error in the earnings record, locate evidence justifying that a correction is warranted, and then correct the error, we will immediately extend insured status or will base the amount of an individual's benefit on the corrected amount.<sup>1</sup>

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<sup>1</sup> The Trust Funds are also credited based on the amount of earnings, rather than on the taxes paid. Prior to 1950, the IRS accounted for all Social Security tax receipts (including penalties, interest and additional taxes), and upon receipt immediately credited such money to the Social Security Trust Fund. This method presented two difficulties

Additionally, if a State or local employer realizes that it should have been withholding FICA for its employees and had not been, we will credit the earnings based on sufficient evidence of the wages paid to the employees. IRS is responsible for collecting all taxes (including FICA) to the extent permitted by law. Because under the Social Security Act an individual's Social Security insured status and benefit amount depend on wages paid to the individual, we credit the individual's earnings record regardless of whether FICA has been paid.

While instances do arise where FICA taxes were not paid, earnings mistakes and corrections go both ways. Many errors we see involve situations where an entity pays FICA in the mistaken belief that its employees are covered. When a State or local entity has paid Social Security taxes without an appropriate modification to the State's Section 218 Agreement, we work with the State to allow affected individuals to legitimize coverage based on the erroneous FICA contributions. However, the State has the option to either amend its Section 218 Agreement through an error modification, or to forego coverage and receive a refund of erroneous FICA payments. When the State decides to legitimize the coverage, no earnings correction is necessary, and no employee is harmed by an inability to recover FICA payments under IRS' three-year statute of limitation on refunds.

### **Recent Improvements to the Administration of Section 218 and Our Partnerships**

To strengthen our efforts in this area, we took several actions in response to the Government Accountability Office's 2010 audit, "Social Security Administration: Management Oversight Needed to Ensure Accurate Treatment of State and Local Government Employees."

#### *Increased Communication with NCSSSA and IRS*

Since then, we have strengthened our relationship with the NCSSSA and the IRS through the creation of the Section 218 Council, which is a collaboration established to increase communication between the Federal agencies and the State Administrators. We regularly meet and have informal conversations to discuss coverage risk factors, work collaboratively when issues arise, and offer ongoing training in areas that SSA and IRS have determined may require extra attention. We also participate in quarterly Section 218 Council meetings, meet annually with NCSSSA leadership, and provide substantive training for State Administrators at NCSSSA's annual conference. During the 2016 NCSSSA conference, which was open to all State Administrators, we presented at length on a variety of topics, such as completing Section 218 Agreement error modifications after mandatory coverage; mandatory and voluntary

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for SSA: first, while cash flow out of the Trust Fund occurred at periodic intervals on a predictable basis, cash flow into the Fund fluctuated considerably and irregularly; and second, SSA received no money for employers who had forwarded individual wage data, but then did not pay their taxes.

Congress changed the law to alleviate these problems in the Social Security Act Amendments of 1950. This law provided that Social Security taxes to be transferred to the Trust Funds would be computed by applying the appropriate tax rate to the wage and self-employment records established and maintained by the Secretary of Health and Human Services (formerly Health Education and Welfare), as certified to the Secretary of the Treasury. This, in effect, meant that SSA's Trust Funds would be credited upon the basis of employer tax liability, not necessarily payment.

coverage and their exclusions; how to fix Section 218 Agreement errors; coverage considerations for rehired annuitants; and how State and local entities can evolve. In recent years, SSA has also provided training on critical and developing issues, including the treatment of charter schools and coverage for police and firefighters who are under retirement systems.

#### *Developed Comprehensive Training Materials, Guidance, and Resources*

We created comprehensive material for our website, the State and Local Coverage Handbook, and a dedicated training website designed for use by the State Administrators. In the past several years, we have diligently updated and expanded our online training materials to better equip State Administrators with the information, tools, contacts, and resources that they require to perform their jobs optimally. We provide the State and Local Coverage Handbook for the State Administrators' use, which is SSA's unredacted policy on the subject matter. The section 218 training website entails basic and advanced training courses that provide more detailed guidance on how to administer section 218. In addition, we developed an internal tool where we consolidate policy, procedures, and resources by topic so SSA employees have easy access to information relating to section 218 and how it is administered in one spot.

#### *Established Regional Experts*

In addition to creating these valuable training resources, we have stepped up our efforts to assist State Administrators with their frequent requests for guidance and evaluations on whether specific groups of employers are covered by their State's agreement. Each SSA region has a specialist who is the point-of-contact for all questions from State Administrators in that region. The regional specialist works to quickly resolve any questions that State Administrators may have. At a State Administrator's request, we will also assist with communicating information to State and local entities, through educational sessions and informational meetings.

#### *Helped to Develop IRS' Compliance Self-Assessment Tool*

To offer an additional tool to the States, we assisted the IRS, in collaboration with NCSSEA, with the creation of the Federal, State, and Local Government Compliance Self-Assessment tool (IRS Form 14581). We promote this tool on our external section 218 website, as a way to allow employers to test their coverage compliance and to identify areas where there may be issues or that may require their increased attention. It also explains several common types of errors and offers resources for States' use.

#### *Created a Section 218 Agreement Database*

We are also streamlining our coverage review process by allowing greater internal access to relevant documents. We have created a database of Section 218 Agreements, modifications, and related documents, which will allow us to complete a portion of the research needed for State-requested coverage determinations with greater ease. Once fully functional, this database will allow our employees to search for entities among a State's Section 218 Agreements and modifications, saving our legal team valuable research time.

## *Reviewing State and Local Regulations, Standardizing Lists of Covered Entities*

SSA's role within the coverage and tax withholding compliance process is limited. Our primary function is to assist State Administrators in executing coverage modifications that effectuate the State's coverage scheme; to interpret and confirm the coverage provisions contained in State Section 218 Agreements; and to serve as a partner and educator to the IRS and the States. But we are redoubling our efforts to complete our role more effectively and to assist our government partners. To that end, we are currently reviewing our regulations and guidance related to State and local government coverage. We are looking for ways to streamline, clarify, or eliminate such guidance, while keeping our underlying policy and business processes intact. These changes should provide better clarity for our employees as they evaluate and execute Section 218 Agreements. We are also looking to standardize the maintenance of comprehensive lists of covered entities for each State. These lists provide a quick reference of covered entities under each State's agreement and help SSA and State Administrators determine employees' coverage efficiently. We are looking at ways we could enhance our maintenance of these lists across all regions with greater uniformity.

Through our educational presentations, online tools, and recurring conversations, we strive to provide the State Administrators with the information they need to ensure proper implementation of coverage. Through conference participation, annual meetings with NCSSSA leadership, and ongoing conversations with IRS and NCSSSA, we have developed relationships that enable State Administrators to facilitate better and more frequent communication with us when issues arise and to help prevent coverage errors from occurring.

### **Conclusion**

Thank you for the opportunity to describe the history and complexity of Social Security coverage under section 210 and section 218 of the Social Security Act, as well as SSA's role in the coverage and tax withholding compliance process. Our relationship with the State Administrators and with the IRS is a vital one and we are committed to continuing to do our part to strengthen it.