FAQs: COLA to Locality Pay Transition

What does the legislation do? The legislation extends locality pay to the nonforeign areas (Alaska, Hawaii, and United States territories and possessions (e.g.; Puerto Rico, Guam, Commonwealth of the Northern Mariana Islands, and American Samoa). Locality pay will be phased in over 3 years beginning in January 2010. The current nonforeign area cost-of-living allowances (COLAs) will be reduced by 65 percent of the locality pay rates. Unlike COLA payments, locality pay is part of basic pay for retirement, life insurance, and Government contributions to employee Thrift Savings Plans.

Who is covered by the provisions of Subtitle B, National Defense Authorization Act for FY 2010 (Public Law 111-84)?

White collar employees who were eligible for the nonforeign cost-of-living allowance (COLA) under 5 CFR 591 are covered by the legislation. Other white collar employees who were paid an amount equivalent to COLA under separate authority by their agency are also covered.

Agencies that have separate authority to set pay rates in a manner similar to pay rates established by OPM under 5 USC 5305 and payable in an allowance area shall be adjusted in accordance with regulations prescribed by the head of the agency that are consistent with the regulations issued by OPM to adjust rates under 5 USC 5305.

What is my locality pay rate?

The legislation phases in locality pay over a 3-year period beginning in January, 2010. The legislation specifies that in 2010, the locality rate in all the nonforeign areas will be set at one third of the Rest of United States (RUS) locality pay rate. The current RUS locality rate is 13.86 percent and one third of that rate would be 4.62 percent. In 2011, the nonforeign areas will receive two thirds of the rate approved by the President for each area, and in 2012, employees will receive the full amount of the rate approved by the President.

What will happen to my COLA rate be 2010?

All COLA rates will be reduced by only 65 percent of an area's applicable locality pay rate. In 2010, the locality rate for all the nonforeign areas will be set at one-third of the RUS locality pay rate The current RUS rate is 13.86 percent which would result in a locality pay rate of 4.62 percent. Sixty-five percent of 4.62 percent is 3.0 percent. Because COLA is calculated on the base General Schedule, the legislation specifies an additional adjustment – dividing the result by one plus the locality pay percentage (or 1.0462).

Example: Current COLA rate of 25 percent and 4.62 percent locality rate:

(25%-65%*4.62%)/(1+.04621) = (25%-3%)/1.0462 = 22%/1.0462 = 21.03%

The adjusted COLA rate is 21.03 percent. This would be applied to the employee's base pay, which includes the base GS schedule pay plus locality pay.

Does the bill affect recent retirees?

No, there are no retroactive provisions in the legislation.

How does this affect U.S. Postal Service employees?

Most postal workers are not eligible for locality pay. The legislation froze COLA rates on October 28, 2009. Postal workers will continue to receive the frozen COLA for their location. When increases in locality pay rates exceed the frozen COLA rate, postal workers will receive the higher amount as their COLA and it will continue to be tax exempt and not included in retirement calculations.

Postal workers who would be eligible for locality pay under 5 USC 5304 in the 48 contiguous states will be covered by the locality pay provisions in the same manner as non-postal employees.

Why is locality pay being phased in over 3 years?

Because locality pay is part of basic pay, agency payroll costs will increase due to higher retirement contributions, Social Security and Medicare payments, and matching Thrift Savings Plan contributions. The 3-year period spreads the impact over several years and gives agencies time to absorb and budget for these costs.

How will pay be set for special rate employees?

In the nonforeign areas (Hawaii, Alaska, Puerto Rico, U.S. Virgin Islands, Guam, and the Commonwealth of the Northern Mariana Islands) the COLA rates are applied to the special rate schedules established under 5 USC 5305. In the contiguous 48 states, special rates are applied to the base General Schedule and employees receive the greater of their special rate or the locality pay rate for their official worksite. This gradually reduces the pay differential between special rates and locality pay. In a number of cases, special rates have been eliminated when locality pay exceeded the special rate.

During the 3-year phase in period, special rates in the nonforeign areas must be increased by at least the dollar amount of locality pay given to non-special rate employees at the same minimum step. This will maintain the existing differences between regular pay and special pay rates during the phase-in period.

Special rates may exceed the Executive Schedule level IV (EX IV) pay cap during the 3-year phase in period. At the end of the 3 years, special rate employees who are above the EX IV pay cap will receive retained pay.

After the 3-year phase in period, special rates in the nonforeign areas will be treated in the same manner as special rates in the contiguous states – employees will receive the higher of their special rate or the locality pay rate for their official worksite.

Agencies will continue to review special rates and may request special rates to be adjusted for recruitment and retention of employees as needed.

Special rates at the Department of Veterans Affairs will be set in a manner consistent with OPM policy.

Some special rate table rates are affected by the EX IV pay cap currently set at $153,200, but COLA does not count against the cap. Does the legislation address the cap?

All special rates are capped at level IV of the Executive Schedule (EX-IV), per 5 U.S.C. 5305(a)(1). The legislation allows special rate employees to exceed the EX IV cap during the 3-year phase-in period. At the end of the 3-year period, employees whose pay (including locality pay) exceeds the EX IV cap will receive retained pay until increases in the cap exceeds the employees' pay. Employees would continue to receive the gradually reducing COLA like other employees.

What happens to COLA after the 3-year phase-in period?

The law was enacted on October 27, 2009. At that time all COLA rates were "frozen." The law specifies that COLA rates are reduced by 65 percent of the locality pay rate. At the end of the 3-year phase-in period, the full locality pay rate will have been implemented but a reduced COLA will still be in effect. Each year, the "frozen" COLA rate will be reduced by 65 percent of the applicable locality pay rate. OPM cannot accurately determine how long this will take, but the table below shows the locality rate needed to reduce the applicable COLA rates to zero.

Location	"Frozen" COLA Rates	Locality Pay Rate Needed to Reduce COLA to Zero
Alaska: Anchorage, Fairbanks, and Juneau	23%	35%
Rest of Alaska	25%	38%
Hawaii: Counties of Honolulu, Kauai, and Maui	25%	38%
Hawaii County	18%	28%
Guam and CNMI	25%	38%
Puerto Rico	14%	22%
US Virgin Islands	25%	38%

Will post differentials be affected?

Post differentials are based on conditions of environment which differ substantially from the continental United States and warrant an allowance as a recruitment incentive. The differentials are paid only to non-local hires. Post differentials have been approved for Guam and the Commonwealth of the Northern Mariana Islands (CNMI), American Samoa, and Johnston, Midway, and Wake Atolls. Guam and CNMI have a 20 percent post differential. The other areas are authorized 25 percent.

The legislation does not address post differentials. An employee can be paid both COLA and post differential, but the total of the two cannot exceed 25 percent.

Post differentials are calculated on base pay and where applicable, will be calculated on an employee's base pay plus the applicable locality pay rate.

Can I choose to continue to receive an unreduced COLA and not receive locality pay?

No, all employees receiving COLA will be covered by the legislation.

I plan to retire in a few years. Can I have my COLA count towards my "high 3" pay?

The law allows you elect to have COLA count for retirement – but only up to the locality pay you would have received if it were not being phased in, and you must retire by December 31, 2012. For example, in 2010, covered employees will receive 1/3rd of the Rest of U.S. locality pay rate. Using the 2009 rate of 13.86 percent as an example, you would have a locality rate of 4.62 percent (1/3rd of 13.86 percent). In year 2, assuming no other changes, your locality pay rate would be 9.24 percent (or 2/3rd's of 13.86 percent). In the third year, you would get the full 13.86 percent. The "opt-in" provision would let you have your retirement "high-3" calculated as if you had received the full locality rate of 13.86 percent for all 3 years.

At the time you retire, you can elect to pay the retirement contributions you would have made over the 3-year period as if you have had received the full locality rate for the 3-year period. Most employees under the Civil Service Retirement System (CSRS) would be required to pay 7 percent while most employees under the Federal Employees Retirement System (FERS) would need to pay 0.8 perent. (Certain employees such as firefighters and air traffic controllers would be required to pay 7.5 percent or 1.3 percent, depending on their retirement system.) You will also be required to pay interest. The current interest rate for these payments is 3.875 percent. Most employees should recoup their payments with their higher retirement pay within 6 to10 months.

If I die during the transition period, can my survivor elect to have my COLA count toward my "high 3" pay in computing a survivor annuity?

Under the provisions of the law, an election can only be made by an employee who retires. An individual who dies in service does not meet these requirements, so even if an employee had completed an election form but died before separating for retirement, the election could not be honored. There is also no provision permitting anyone else to make an election regardless of circumstances. Thus, there is no basis for any non-foreign COLA payments to be treated as basic pay for retirement except in the case on an employee who has retired and filed an election.

How will SES, SL and ST employees be affected by the bill?

Senior Executive Service, Senior Level, and Scientific and Professional positions (established under 5 USC 3104) are not authorized to receive locality pay in the continental United States. The legislation does provide that locality pay may be extended to employees in these pay plans whose official worksite is in one of the nonforeign areas on the day before the first pay period beginning on or after January 1, 2010. Employees in these pay plans who are assigned to positions in the nonforeign areas after the date of enactment are not eligible for locality payments. They will remain eligible for the offset COLA rate in effect for their official worksite.

Additionally, the legislation specifies that if an SES, SL, or ST employee's rate of basic pay with the addition of locality pay would exceed the EX-III pay cap (or EX-II for employees in certified plans), the employee must continue to receive any applicable locality payment which is not in excess of the maximum rate set in 5 U.S.C. 5304 in addition to a reduced COLA payment equal to the rate computed using the 65 percent offset less the amount of locality pay received until the employee leaves the nonforeign area or pay system, or until the EX caps are increased so as to allow the employee to be entitled to receive basic pay and locality pay at a higher rate without hitting or exceeding the appropriate EX pay cap.