CONGRESSIONAL BUDGET OFFICE
COST ESTIMATE

March 31, 1998

H.R. 3249
Federal Retirement Coverage Corrections Act

As ordered reported by the House Committee on Government Reform and Oversight on March 5, 1998.

SUMMARY

H.R. 3249 would alter the procedures for correcting situations where federal employees have been mistakenly placed in the wrong retirement system. Many of these retirement coverage errors occurred between 1984, when the Civil Service Retirement System (CSRS) was closed to new entrants, and 1987, when the Federal Employees' Retirement System (FERS) was created. The bill would also direct the Secretary of State to provide Foreign Service employees with an open season similar to the one scheduled to take place for regular federal employees.

CBO estimates that federal agencies would bear discretionary costs totaling $121 million over the 1998-2003 period, primarily because the bill would increase the size of makeup contributions to the Thrift Savings Plan (TSP). The bill would also increase direct spending by $152 million and be subject to pay-as-you-go procedures. This additional direct spending largely reflects makeup contributions to the TSP and agencies' spending of refunded contributions for misplaced employees who would be allowed to switch their retirement coverage from FERS to the CSRS Offset plan. The bill would not have a significant impact on federal retirement benefits during the next several years because affected employees are generally still in the middle of their careers.

Because the District of Columbia and Gallaudet University would be required to correct instances where employees have been mistakenly enrolled in the wrong retirement system, H.R. 3249 contains both an intergovernmental and a private-sector mandate as defined by the Unfunded Mandates Reform Act of 1995 (UMRA). However, CBO estimates that the cost of these mandates would be minimal.

ESTIMATED COST TO THE FEDERAL GOVERNMENT

The estimated budgetary impact of H.R. 3249 is shown in the following table.

	By Fiscal Year, in Millions of Dollars										
	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008
SPENDING SUBJECT TO APPROPRIATION											
Budget Authority	-5	2	17	22	54	31	3	-11	-16	-22	-28
Outlays	-5	2	17	22	54	31	3	-11	-16	-22	-28
CHANGES IN DIRECT SPENDING											
On-Budget											
Budget Authority	3	57	166	154	54	33	16	17	22	28	34
Outlays	3	56	163	155	56	33	16	17	22	28	34
Off-Budget											
Budget Authority	2	-27	-87	-86	-57	-35	-14	-7	-5	-4	-2
Outlays	2	-27	-87	-86	-57	-35	-14	-7	-5	-4	-2
Total											
Budget Authority	5	30	79	68	-3	-2	2	10	17	24	32
Outlays	5	29	76	69	-1	-2	2	10	17	24	32
CHANGES IN REVENUES											
On-Budget	0	-1	-1	0	1	0	0	0	-1	-1	-1
Off-Budget	0	1	2	5	8	9	9	8	6	4	2
Total	0	0	1	5	9	9	9	8	5	3	1
TOTAL COST											
Direct Spending and	5	29	75	64	-10	-11	-7	2	12	21	31
All Spending and Revenues	0	31	92	86	44	20	-4	-9	-4	-1	3

Note: Components may not sum to totals because of rounding.

The mandatory costs of this legislation fall within budget functions 600 (Income Security), 650 (Social Security), and 950 (Undistributed Offsetting Receipts). Additional costs to employing agencies are discretionary and are funded through appropriations throughout the budget.

BASIS OF ESTIMATE

Title I

H.R. 3249 lays out procedures for correcting a wide variety of retirement coverage errors. CBO estimates that the provisions of Title I would impose discretionary costs on agencies totaling $99 million between 1998 and 2003. In addition, the bill would increase on-budget direct spending by $476 million over the same period. Off-budget direct spending would decrease by $285 million, for a net increase in direct spending of $191 million. This increase in direct spending is partly offset by an increase of $25 million in revenues. These estimates assume that the Postal Service would increase postal rates to fully offset any costs related to the bill. The estimated budgetary impact of Title I is shown in the table below.

Background

There are two main retirement programs for full-time regular federal employees. Most full-time employees hired before 1984 are in the Civil Service Retirement System (CSRS), a defined benefit plan which does not include Social Security. Those hired after 1984 are generally covered by the Federal Employees' Retirement System (FERS), which features Social Security, a more limited defined benefit, and the defined contribution Thrift Savings Plan (TSP). Employees who return to government service after 1987 and have five years of prior service under CSRS may be covered by a hybrid plan known as CSRS Offset that features both CSRS and Social Security benefits.

FERS employees may contribute up to 10 percent of their pay to the TSP. They receive an automatic contribution from their employing agency equal to 1 percent of their pay and may also receive an additional 4 percent in matching contributions. CSRS and CSRS Offset employees may also participate in the TSP, but they may only contribute up to 5 percent of their pay and do not receive any government contributions.

Assumptions about Retirement Coverage Errors

CBO estimated the number of retirement coverage errors that have been made based on discussions with personnel officials in a number of large government agencies, including the Postal Service and the Departments of Defense, Veterans Affairs, and Agriculture. These agencies comprise approximately 70 percent of the federal civilian workforce. On the basis of these discussions, CBO estimates that approximately 18,000 coverage errors have occurred throughout the government, of which approximately 10,000 have already been corrected. The two most common types of coverage errors appear to involve employees who

	By Fiscal Year, Outlays in Millions of Dollars										
	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008
SPENDING SUBJECT TO APPROPRIATION											
Makeup Contributions to TSP	-2	2	6	7	38	24	3	-5	-6	-7	-7
Makeup Payment of Social Security	-1	-4	-4	-4	-4	-5	-5	-5	-5	-5	-6
Makeup Payment of Retirement Contributions	-2	0	10	10	6	-1	-7	-9	-10	-10	-11
Agency Retirement Contributions	0	-1	0	3	5	3	2	0	-2	-5	-7
Employer Social Security Contributions	0	0	1	3	5	5	5	5	3	2	1
Total	-5	-2	13	18	49	26	-2	-15	-20	-25	-30
CHANGES IN DIRECT SPENDING											
On-Budget											
Makeup Contributions to TSP	0	19	56	61	11	0	0	0	0	0	0
Makeup Payment of Retirement Contributions	3	-1	-14	-15	-8	2	10	13	14	16	17
Agency Retirement Contributions	0	1	0	-4	-7	-4	-3	0	3	7	11
Transfers from CSRDF to Social Security	0	32	91	87	55	33	13	7	7	8	9
Spending of Refunds	0	6	32	28	7	4	0	-1	-1	-1	-1
Subtotal	3	58	165	157	58	35	19	19	24	29	35
Off-Budget											
Makeup Payment of Social Security	2	6	6	6	7	7	7	7	8	8	8
Employer Social Security Contributions	0	0	-1	-4	-7	-8	-8	-7	-5	-3	-1
Transfers from CSRDF to Social Security	0	-32	-91	-87	-55	-33	-13	-7	-7	-8	-9
Subtotal	2	-26	-86	-85	-56	-34	-13	-6	-4	-3	-1
Total	5	32	79	71	2	0	6	13	20	26	33
CHANGES IN REVENUES											
On-Budget											
Employee Retirement Contributions	0	0	0	1	2	1	1	1	0	0	0
Off-Budget											
Employee Social Security Taxes	0	0	1	4	7	8	8	7	5	3	1
Total	0	0	1	5	9	10	9	7	5	3	1
TOTAL COST OF TITLE I											
Direct Spending and Revenues	5	33	77	66	-7	-9	-3	6	14	23	33
All Spending and Revenues	0	30	90	84	42	17	-4	-9	-5	-2	2

Note: Components may not sum to totals because of rounding.

should be in FERS but were accidentally put in CSRS, and employees with prior service who returned to government service and were misplaced in either FERS or CSRS Offset.

H.R. 3249 would also affect the speed with which agencies identify and correct retirement coverage errors. CBO assumed that, under current law, agencies would correct coverage errors at a constant annual rate. H.R. 3249 would direct agencies to identify any retirement coverage errors promptly and correct them. Under the bill, agencies would have an incentive to move quickly; they could apply to the Office of Management and Budget (OMB) for assistance for expenses related to correcting coverage errors, but only for those errors identified before January 1, 2002. CBO assumed that agencies would correct most of their retirement coverage errors between 1999 and 2003. Agencies would also stop correcting errors for the remainder of 1998 pending the issuance of final regulations to implement H.R. 3249.

Under current law, coverage errors are usually corrected by converting the employee to the proper retirement system, retroactive to original date of the error. However, some employees who were accidentally placed in FERS are able to remain in FERS by making a retroactive election of FERS coverage. H.R. 3249 would allow most employees affected by coverage errors to choose whether they would like to be placed in the proper retirement system or make their current incorrect coverage permanent. All elections would be irrevocable, and employees who did not make an election would retain their current coverage. Coverage errors lasting less than a year would not be covered by the bill. CBO assumed that 80 percent of the employees whose errors have not yet been corrected would choose to be placed in the proper retirement system.

Most of the employees whose coverage errors have already been corrected would also be given the option of returning to the retirement system in which they were incorrectly placed. However, employees who were mistakenly placed in CSRS and have already been placed in FERS would be able to elect only CSRS Offset coverage. Because employees affected by these errors often have relatively small TSP accounts, CBO assumed that 80 percent of them would elect to join CSRS Offset. CBO also assumed that 20 percent of the employees who were incorrectly put in FERS and have already been placed in CSRS or CSRS Offset will elect FERS coverage.

Effects on Discretionary Spending

Makeup Contributions to TSP. Employees who are incorrectly covered by CSRS rather than FERS are unable to participate fully in the TSP. Under current law, when an individual's coverage is corrected to FERS, the employing agency makes a lump-sum deposit into his TSP account equal to the government contributions and related earnings that would have been made to the employee's previous TSP contributions under FERS rules. If the employee did not have a TSP account, only a deposit for the automatic 1-percent contribution is made. Earnings are calculated using the individual's own fund allocation decisions (if he had a TSP account) or the G Fund rate (otherwise). Employees may provide makeup contributions to their TSP accounts out of future pay. These makeup contributions receive agency matching contributions (up to the 5-percent FERS maximum) and related earnings as if the contributions had been made at the proper time. However, back earnings are paid only on the agency's matching funds, not the employee's makeup contributions.

H.R. 3249 would change the way that makeup TSP contributions are calculated. Under the bill, agencies would make a lump-sum payment to TSP representing past employee contributions, automatic 1-percent agency contributions, and agency matching contributions. The amount representing employee contributions would be calculated using the average contribution rate for FERS employees who participated in TSP, and would be paid whether or not the employee already has a TSP account (subject to the 10-percent annual limit on FERS contributions and the Internal Revenue Service's annual dollar limit on contributions to tax-deferred savings plans). Agencies would also pay past earnings on all three amounts. These earnings would be calculated using the employee's own TSP fund allocation choices. If the employee did not have a TSP account, a composite rate representing the average allocation of all FERS employees contributing to TSP would be used. Based on historical data provided by the Federal Retirement Thrift Investment Board, CBO estimates that these provisions would increase the average TSP makeup payment by $70,000 in 1999. This amount would be higher in later years due to additional foregone returns and contributions.

These makeup TSP contributions could be paid either from agencies' discretionary appropriations or from a new permanent indefinite appropriation. H.R. 3249 would make agencies responsible for the TSP makeup contributions, but would allow agencies to appeal to the OMB Director if these makeup payments would "substantially impair" the agency's operations. If the OMB Director agreed with the agency, some or all of the agency's payments would be made instead from a permanent appropriation. Based on discussions with OMB, CBO has assumed that 90 percent of nonpostal makeup payments prior to the January 2002 deadline would be paid for from the permanent appropriation. CBO estimates that the total cost of TSP makeup contributions will be $222 million, with agencies paying for $75 million from their discretionary appropriations and the remaining $147 million coming from the general fund as direct spending.

Makeup Payment of Social Security Contributions. Agencies are currently responsible for makeup payments of Social Security payroll taxes for employees whose coverage is changed from CSRS to FERS or CSRS Offset. H.R. 3249 would transfer responsibility for past Social Security taxes from agencies to the Civil Service trust fund. As a result, agency spending on makeup Social Security taxes would fall by $22 million during the 1998-2003 period.

Makeup Payment of Retirement Contributions. Under H.R. 3249, any necessary adjustments to past agency contributions to the Civil Service Retirement and Disability Fund (CSRDF) would be completely retroactive, as under current law. CBO estimates that agency makeup payments to the CSRDF would increase by $23 million between 1998 and 2003 under the bill. This increase primarily reflects the impact that the bill would have on speeding up the correction of coverage errors. After 2002, agency makeup payments would be lower than under current law.

Agency Retirement Contributions. The amount that agencies currently contribute towards their employees' retirement would change under H.R. 3249 for two reasons. First, the speeding up of retirement corrections would increase agency contributions in the near term. Second, the decision of many employees whose errors have already been corrected to switch from FERS to CSRS Offset would decrease agency retirement contributions, particularly in later years. These changes would increase agency spending on retirement contributions by $10 million during the 1998-2003 period.

Employer Social Security Contributions. Employer contributions to Social Security would increase by $14 million between 1998 and 2003 due to the speeding up of retirement corrections. These contributions would not be affected by the decision of some employees to switch from FERS to CSRS Offset since both types of coverage include Social Security.

Effects on Direct Spending (On-Budget)

Makeup Contributions to TSP. H.R. 3249 would allow some agency makeup payments to TSP to be made from a new permanent appropriation. CBO estimates that the portion of makeup contributions to the TSP that would be funded from this permanent appropriation would be $147 million during the 1998-2003 period.

Makeup Payment of Retirement Contributions. The increase in agency makeup payments to the CSRDF would be reflected in the budget both as additional agency outlays and as offsetting receipts to the CSRDF. As a result, receipts to the trust fund would increase by $33 million between 1998 and 2003.

Agency Retirement Contributions. The increase in agency retirement contributions under the bill would increase CSRDF receipts by $14 million during the 1998-2003 period.

Transfers from the Civil Service Trust Fund to Social Security. Under H.R. 3249, the CSRDF would be responsible for the payment of back Social Security payroll taxes for any future retirement corrections. Unlike current law, these corrections would be completely retroactive and would not be affected by the current limit of 3 years, 3 months, and 15 days.

CBO estimates that transfers from the CSRDF to the Social Security trust fund would total $298 million during the 1998-2003 period. Although these transfers are intragovernmental, the payments would be on-budget and the receipt of these transfers of funds by Social Security would be off-budget.

Refunds from CSRDF to Agencies. Agencies would receive a partial refund of their retirement contributions for employees who have already been restored to FERS but elect to be covered by CSRS Offset under H.R. 3249. Agencies currently contribute 10.7 percent of employee pay for retirement under FERS rules but only 8.51 percent under CSRS Offset. The difference of 2.2 percent would be refunded to the agency. These refunds from the CSRDF to the agencies would amount to $77 million over the 1998-2003 period and would be available to the agencies to be spent for future CSRDF contributions.

Effects on Direct Spending (Off-Budget)

H.R. 3249 would affect offsetting receipts to the Social Security trust fund in three ways. First, agencies would no longer be responsible for making back payments of Social Security payroll taxes when correcting coverage errors. This change would reduce receipts by $34 million between 1998 and 2003. Second, transfers from the Civil Service trust fund for back taxes on future corrections of coverage errors will increase receipts by $298 million between 1998 and 2003. These transfers would include the $34 million that agencies would be responsible for under current law. Finally, receipts from ongoing employer Social Security taxes would increase by $20 million over the same period.

Effects on Revenues

Employee Retirement Contributions. As with current agency retirement contributions, current employee retirement contributions would also be affected by the speeding up of retirement coverage errors corrections and the new retirement coverage elections under H.R. 3249. The net impact of these effects will decrease employee contributions to the CSRDF, which are considered receipts, by $4 million during the 1998-2003 period.

Employee Social Security Taxes. Primarily due to the speeding up of retirement coverage corrections under H.R. 3249, receipts from employee Social Security taxes would increase by $20 million between 1998 and 2003.

Title III

Section 304 of H.R. 3249 would direct the Secretary of State to provide employees in the Foreign Service Retirement and Disability System (FSRDS) with an opportunity to switch into the newer Foreign Service Pension System (FSPS). This open season would be similar to that currently scheduled to take place starting in July 1998 for employees in CSRS who would like to join FERS. The estimated budgetary impact of Section 304 is shown in the table below.

FSRDS employees had a previous opportunity to switch to FSPS during a six-month open season in 1987. About 17 percent of the FSRDS employees switched to FSPS during this first open season. CBO estimates that approximately 325 people--between eight and nine percent of all FSRDS employees--would switch to FSPS during a second open season. This estimate reflects the assumptions that those employees most interested in switching to FSRDS did so during the 1987 open season, and that current FSRDS employees switch at half the rate seen in 1987.

Discretionary Spending. Employer contributions would increase for those employees who switch to FSPS. Agencies' retirement contributions for Foreign Service employees are currently 8.51 percent for FSRDS workers and 18 percent for FSPS workers, so agencies would contribute an additional 9.5 percent of pay to the Foreign Service trust fund for employees who switch. In addition, employees who switch to FSPS would become covered by Social Security, so agencies would have to contribute 6.2 percent of an employee's pay (up to the maximum taxable salary) to the Social Security trust funds. Overall, employer retirement contributions would increase by $16 million between 1998 and 2003.

Like FERS employees, FSPS workers may contribute up to 10 percent of their pay to TSP and receive up to 5 percent in matching government contributions. CBO assumed that employees would switch to FSPS in part to take fuller advantage of TSP and that their average TSP contribution would rise from 4 percent (the current average for employees in the similar CSRS system) to 7 percent. As a result, switching employees would receive the full 5-percent government match. These matching contributions would cost $5 million during the 1998-2003 period.

	By Fiscal Year, Outlays in Millions of Dollars									
	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008
SPENDING SUBJECT TO APPROPRIATION										
Agency Retirement Contributions	3	3	3	3	4	4	3	3	2	2
Agency Thrift Savings Plan Contributions	1	1	1	1	1	1	1	1	1	1
Total	4	4	4	5	5	5	4	4	3	2
CHANGES IN DIRECT SPENDING										
On-Budget										
Agency Retirement Contributions	-2	-2	-2	-2	-2	-3	-2	-2	-1	-1
Off-Budget										
Employer Social Security Taxes	-1	-1	-1	-1	-1	-1	-1	-1	-1	-1
Total	-3	-3	-3	-3	-4	-4	-3	-3	-2	-2
CHANGES IN REVENUES										
On-Budget										
Employee Retirement Contributions	-1	-1	-1	-1	-1	-1	-1	-1	-1	-1
Off-Budget										
Employee Social Security Taxes	1	1	1	1	1	1	1	1	1	1
Total	0	0	0	0	0	0	0	0	0	0
TOTAL COST OF TITLE III										
Direct Spending and Revenues	-3	-3	-3	-3	-4	-4	-3	-3	-2	-2
All Spending and Revenues	1	1	1	1	1	1	1	1	1	1

Note: Components may not sum to totals because of rounding.

Direct Spending. The increases in agency retirement contributions--with the exception of TSP contributions--would be reflected in the budget both as additional agency outlays and as offsetting receipts to the retirement trust funds. CBO estimates that receipts to the Foreign Service Retirement and Disability Fund would increase $10 million over the next five years, and that receipts to the Social Security trust funds would rise by $5 million over the same period. CBO estimated that the impact of switching employees on Foreign Service and Social Security benefit outlays would be insignificant between 1998 and 2003.

Revenues. FSRDS employees who switch to FSPS would contribute 7.5 percent of their pay towards retirement on earnings up to the Social Security maximum wage level ($68,400 in 1998) and 1.3 percent on earnings over that level. This rate is slightly higher than the rate for FSRDS, where employees contribute 7 percent of pay. The allocation of contributions would also change since 6.2 percentage points (of the 7.5) would go to Social Security instead of the Foreign Service trust fund. This change would shift revenues from one fund to the other but would have no significant net budgetary impact.

PAY-AS-YOU-GO CONSIDERATIONS

The provisions of H.R. 3249 would affect on-budget direct spending and revenues and therefore be subject to pay-as-you-go procedures. The pay-as-you-go procedures cover only the current year, budget year, and the succeeding four years. The pay-as-you-go effects of the bill are shown in the following table.

Summary of Pay-As-You-Go Effects

	By Fiscal Year, in Millions of Dollars										
	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008
Change in outlays	3	56	163	155	56	33	16	17	22	28	34
Change in receipts	0	-1	-1	0	1	0	0	0	-1	-1	-1

INTERGOVERNMENTAL AND PRIVATE-SECTOR IMPACT

H.R. 3249 would require the government of the District of Columbia and Gallaudet University to correct errors associated with the incorrect enrollment of employees in certain retirement plans. This requirement is both an intergovernmental and a private-sector mandate as defined by UMRA. However, costs associated with those corrections would be minimal, and only a small number of employees of the District of Columbia and Gallaudet University have been affected by the errors addressed by the bill. Consequently, CBO estimates that the total cost of the mandates would be minimal.

COMPARISON WITH OTHER ESTIMATES

In October 1997, CBO issued a pay-as-you-go estimate of the open season provision for CSRS employees contained in the Treasury and General Government Appropriations Act for 1998. CBO's estimate of the effects of the proposed open season for Foreign Service employees is based on assumptions similar to the ones used in that estimate. Specifically, CBO assumed in each instance that employees would switch retirement systems at half the rate seen in the 1987 open season and that switching employees would increase their TSP participation by similar amounts.

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