CONGRESSIONAL BUDGET OFFICE
COST ESTIMATE

September 15, 1998

H.R. 2566
Civil Service Retirement System Actuarial Redeposit Act of 1998

As ordered reported by the House Committee on Government Reform and Oversight on July 23, 1998

SUMMARY

H.R. 2566 would change the way that retirement annuities are calculated for certain federal employees who are covered by the Civil Service Retirement System (CSRS). The bill would affect employees who have received a refund of retirement contributions for a prior period of service that ended after October 1, 1990. Under current law, these employees must repay their contributions with interest in order to have the prior service included in their annuity calculation. H.R. 2566 would allow these employees to take instead an actuarially equivalent reduction in their benefit.

CBO estimates that this bill would increase direct spending by $90 million over the 1999-2003 period due to higher spending on refunds of retirement contributions. The bill would also decrease revenues by $8 million over the same period because fewer employees would make redeposits for retirement contributions that they withdrew in the past. Over the long run, this bill would increase net spending because employees who would not repay their contributions under current law would receive higher benefits under the bill. Because this bill would affect direct spending, pay-as-you-go procedures would apply.

H.R. 2566 contains no intergovernmental or private-sector mandates as defined in the Unfunded Mandates Reform Act of 1995 (UMRA) and would not affect the budgets of state, local, or tribal governments.

ESTIMATED COST TO THE FEDERAL GOVERNMENT

The estimated budgetary impact of H.R. 2566 is shown in Table 1.

TABLE 1. ESTIMATED BUDGETARY EFFECTS OF H.R. 2566

	By Fiscal Year, in Millions of Dollars									
	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008
CHANGES IN DIRECT SPENDING										
Refunds of retirement contributions	12	16	19	21	23	25	23	21	19	16
CSRS retirement benefits	- a	- a	- a	- a	-1	-1	-1	-1	-1	-1
Subtotal	12	16	18	21	23	24	22	20	18	15
CHANGES IN REVENUES										
Employee redeposits for prior service	-1	-1	-2	-2	-2	-3	-3	-4	-4	-4
TOTAL COST										
Direct Spending and Revenues	13	17	20	22	25	26	24	22	19	17

a. Less than $500,000.
This estimate assumes that H.R. 2566 is enacted on October 1, 1998.
Note: Components may not sum to totals because of rounding.

The costs of this legislation fall within budget function 600, Income Security.

BASIS OF ESTIMATE

Most federal employees hired before 1984 are covered by the Civil Service Retirement System, a retirement plan that offers a defined benefit and does not include Social Security. Under CSRS, employees generally contribute 7 percent of their basic pay to the Civil Service trust fund. Employees who leave government service for more than 31 days and are not immediately eligible for retirement benefits can have their retirement contributions refunded to them.

Payment of a refund usually voids the employee's right to any retirement benefits related to that period of service. However, employees who later return to government work may still have the prior service included in their annuity calculation. If the prior service ended *before* October 1, 1990, an employee may get credit for that service by taking an actuarially equivalent reduction in his or her retirement annuity or by redepositing his or her refunded contributions with interest. If the prior service ended *after* October 1, 1990, an employee may receive credit for that service only by redepositing his or her refunded contributions with interest. H.R. 2566 would allow all prior periods of service for current CSRS employees to be credited through the actuarial reduction method.

Direct Spending

Refunds of Retirement Contributions. Under the bill, some employees who would otherwise leave their retirement contributions in the Civil Service trust fund would have greater incentive to take a refund upon leaving government service. This could be particularly true for people who anticipate returning to government service later in their career. Employees who took a refund would receive a significant amount of money (refunds of $10,000 or more are not unusual for CSRS employees). If they later returned to government employment, they would still be able to include this prior service in their annuity calculation in exchange for an actuarial reduction, which for most employees would be less than 10 percent. For example, an employee retiring at age 60 with 20 years of service (10 of which have been refunded) would face a reduction of about 8 percent.

Past experience suggests that federal employees are quite willing to trade a smaller annuity in exchange for an immediate lump-sum payment. Between 1986 and 1990, federal employees could receive an alternative form of annuity (AFA) when they retired. (The AFA has since been limited to employees who are terminally ill.) Retiring employees who chose the AFA received a lump-sum payment equal to the retirement contributions that they had made over their career. In exchange, their retirement annuities were reduced by an actuarially equivalent amount--typically 10 percent to 15 percent. About 80 percent of retiring employees elected the AFA when it was widely available.

About 67 percent of CSRS employees who quit without being eligible for an immediate annuity get a refund of their retirement contributions. CBO assumed that under the bill this figure would increase to 70 percent in 1999 and then gradually rise to 75 percent over the following five years. CBO estimates that the number of additional people who would take refunds under the bill would be less than 4,000. This increase would raise spending on refunds by $91 million over the 1999-2003 period.

CSRS Retirement Benefits. Under the bill, retirement benefits for individual employees could either rise or fall, depending on whether or not the employees would make a redeposit for their prior service under current law. Benefits would decline for employees who would have made a redeposit but decide instead under the bill to take an actuarial reduction in their annuity. In contrast, benefits for employees who had no intention of making a redeposit would rise, because they would be allowed to include additional service in their annuity calculation.

The bill would affect the benefits of only a small fraction of the approximately 1.2 million employees covered by CSRS. According to the Office of Personnel Management (OPM), about 17,200 CSRS employees have a prior period of service and were rehired after October 1, 1990. However, many of these employees completed their prior service before that date and would not be affected by the bill. CBO assumed that about one-third of the 17,200 employees, or 5,700, have a prior period of service that ended after October 1, 1990. OPM information indicates that about two-thirds of CSRS employees who quit withdraw their retirement contributions. CBO thus estimated that about 3,800 current employees would be affected by the bill. The bill would also affect about an additional 4,300 people with prior CSRS service who will be rehired over the 1999-2003 period.

CBO assumed that affected employees who would retire during the 1999-2003 period have an average of six years of current service. CSRS allows employees to retire at age 55 with a minimum of 30 years of service, at age 60 with at least 20 years of service, or at age 62 with at least five years of service. Since employees with a break in service usually have less total service than career government employees, many affected employees would be retiring under the age 60/20 years option. They would thus have a significant amount, perhaps 15 years or more, of prior refunded service. At a minimum, since CSRS-covered employees were first hired no later than 1982, affected employees would have at least eight years of prior service. For some employees, the refund received from the prior service could be about $25,000.

CBO assumed that 70 percent of the employees affected by the bill would have made a redeposit but decide instead to take an actuarial reduction. For employees with this much prior refunded service, the reduction would be approximately 10 percent, or $125 a month.

In contrast, CBO assumed that this bill would increase benefits for about 10 percent of the affected employees. The amount of the increase would be substantial, since prior service for affected employees would represent more than half of their total service. Furthermore, CSRS retirement benefits equal 1.5 percent of average pay for each of the first five years of service, 1.75 percent of pay for each of the next five years of service, and 2 percent for each additional year beyond that. As a result, the additional service would often be credited at a higher rate than the employee's current service, making it even more valuable. CBO estimates that monthly benefits for these employees would rise by about $600.

Overall, CBO estimates that retirement benefits for the employees affected by the bill would decrease by about 2.5 percent, lowering spending on CSRS retirement benefits by $1 million over the 1999-2003 period.

Revenues

The redeposits that employees make to receive credit for prior service would decrease under the bill because most employees affected by the bill would opt for the reduced annuity. CBO assumed that under the bill the number of employees who elect to make a redeposit would drop by 80 percent. This figure is consistent with the percentage of federal employees who chose the AFA option back in the late 1980s. This drop would reduce redeposits, which are treated as revenues, by $8 million over the 1999-2003 period.

PAY-AS-YOU-GO CONSIDERATIONS

Section 252 of the Balanced Budget and Emergency Deficit Control Act sets up pay-as-you-go procedures for legislation affecting direct spending or receipts. The net changes in outlays and governmental receipts that are subject to pay-as-you-go procedures are shown in Table 2. For the purposes of enforcing the pay-as-you-go procedures, only the effects in the current year, the budget year, and the succeeding four years are counted.

TABLE 2. SUMMARY OF PAY-AS-YOU-GO EFFECTS OF H.R. 2566

	By Fiscal Year, in Millions of Dollars									
	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008
Change in outlays	12	16	18	21	23	24	22	20	18	15
Change in receipts	-1	-1	-2	-2	-2	-3	-3	-4	-4	-4

INTERGOVERNMENTAL AND PRIVATE-SECTOR IMPACT

H.R. 2566 contains no intergovernmental or private-sector mandates as defined in the Unfunded Mandates Reform Act of 1995 (UMRA) and would not affect the budgets of state, local, or tribal governments.

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