Order Code RL30023

CRS Report for Congress

Received through the CRS Web

Federal Employee Retirement Programs: Budget and Trust Fund Issues

Updated May 24, 2004

Patrick J. Purcell
Specialist in Social Legislation
Domestic Social Policy Division

Federal Employee Retirement Programs: Budget and Trust Fund Issues

Summary

Retirement annuities for civilian federal employees are provided mainly through two programs: the *Civil Service Retirement System* (CSRS) and the *Federal Employees Retirement System* (FERS). These annuities are financed through a combination of employee contributions and payments made by the federal government to the civil service retirement trust fund. The federal government makes supplemental payments into the trust fund on behalf of employees covered by CSRS because employee and agency contributions do not meet the full cost of the benefits earned by employees covered by that system.

Civil service retirement annuities are paid from the same trust fund regardless of whether the benefits were accrued under CSRS or FERS. FERS pension benefits are fully funded as they are earned, and the full cost of funding retirement benefits under FERS is recognized in each government agency's annual budget. CSRS is not fully funded, and the full costs of pension benefits earned by workers under CSRS are not accounted for in the budgets of individual federal agencies. Although the two programs are financed differently, the ultimate source of the money from which benefits are paid is the same for both programs: revenue collected by the government through taxes and by borrowing from the public.

In FY2004, the expenditures of the Civil Service Retirement and Disability Fund (CSRDF) are estimated to reach $52.8 billion, composed mostly of annuity payments to retirees and survivors. These expenditures will be 38% as large as the $137.6 billion paid as salary and wages to current employees. Expenditures from the retirement fund will increase over the next several years until they are about 45% as large as the payroll for current federal employees. After 2015, they will fall relative to payroll expenses. By 2050, expenditures from the retirement fund will be less than one-fourth as large as the government's wage and salary payments to current employees. Estimated expenditures from the CSRDF are equal to less than one-half percent of the nation's gross domestic product (GDP) in 2004. Federal pension expenditures are expected to remain steady as a share of GDP for the next 15 years before declining from about 0.43% of GDP in 2020 to 0.20% by 2060.

By law, benefits under FERS must be pre-funded according to their full actuarial cost. CSRS benefits, in contrast, are *not* fully pre-funded. Fully funding the CSRS would require increased contributions from the federal government or employees. If agencies fully funded the costs of the CSRS through increased contributions, they could be required to do so from their current-law appropriations, or they could be granted additional appropriations by Congress. However, because these funds would be used by the CSRDF to purchase Treasury bonds (which is an *intragovernmental transfer* of funds), no additional outlays would occur and there would be no effect on the federal budget. Pre-funding the full costs of the CSRS without giving agencies additional appropriations would reduce the federal budget deficit (or increase the budget surplus), because the outlays of each agency would have to be reduced by the amount of its additional contributions to the CSRDF.

Contents

List of Tables

Federal Employee Retirement Programs: Budget and Trust Fund Issues

Pensions for civilian federal employees are provided through two programs, the Civil Service Retirement System (CSRS) and the Federal Employees Retirement System (FERS). CSRS was authorized by the Civil Service Retirement Act of 1920 (P.L. 66-215) and FERS was established by the Federal Employees' Retirement System Act of 1986 (P.L. 99-335). Under both CSRS and FERS, employees and their employing agencies make contributions to the Civil Service Retirement and Disability Fund (CSRDF), from which pension benefits are paid to retirees and their surviving dependents. Retirement and disability benefits under FERS are fully funded by these contributions and the interest earned by the bonds in which the contributions are invested. The cost of the retirement and disability benefits earned by employees covered by CSRS, on the other hand, are not fully funded by agency and employee contributions and interest income. The federal government therefore makes supplemental payments each year into the civil service trust fund on behalf of employees covered by CSRS. Even with these additional payments into the trust fund, however, CSRS pensions are not fully pre-funded.

Prior to 1984, federal employees did not pay social security payroll taxes and they were not eligible for social security benefits. The Social Security Amendments of 1983 (P.L. 98-21) mandated Social Security coverage for civilian federal employees hired on or after January 1, 1984. This change was made in part because the Social Security system needed additional cash contributions to remain solvent. Enrolling federal workers in both CSRS and Social Security, however, would have required employee contributions equal to more than 13% of workers' salaries. Consequently, Congress directed the development of the Federal Employees' Retirement System (FERS), with Social Security as the cornerstone. The FERS is composed of three elements: (1) Social Security, (2) a defined benefit plan (the FERS basic retirement annuity), and (3) a defined contribution plan (the Thrift Savings Plan).[1] All permanent federal employees initially hired on or after January 1, 1984, are covered under FERS, as are employees who voluntarily switched from CSRS to FERS during "open seasons" held in 1987 and 1998.

Fundamentals of Pension Plan Financing

Retirement programs are classified as either *defined benefit* (DB) plans or *defined contribution* (DC) plans. In a *defined benefit* plan, the retirement benefit typically is based on salary and years of service and is usually paid as a life-long

---

[1] This report describes the financing of CSRS and the FERS basic annuity. For a description of the Thrift Savings Plan, see CRS Report RL30387, *Federal Employees' Retirement System: The Role of the Thrift Savings Plan*.

annuity. A *defined contribution* plan is much like a savings account maintained by the employer on behalf of each participating employee. The employer contributes a specific dollar amount or percentage of pay into the account, which then is invested in assets such as stocks and bonds. In some plans, the amount of the employer contribution depends on how much the employee contributes from his or her pay. When the worker retires, he or she receives the balance in the account, which is the sum of all the contributions that have been made plus interest, dividends, and capital gains (or losses). This is usually paid as a lump-sum, but the employee sometimes has the option to receive benefits as a series of fixed payments over a period of years or in the form of a life-long annuity.[2]

An important difference between defined benefit and defined contribution plans is that the *employer* bears the financial risk in a defined benefit plan, while the *employee* bears the financial risk in a defined contribution plan. In a defined benefit plan, the employer promises to provide retirement benefits equal to a certain dollar amount or a specific percentage of the employee's pay. Under federal law, employers in the private sector are required to pre-fund these benefits by setting aside money in a *pension trust*, which is typically invested in stocks, bonds, and other assets. The employer is *at risk* for the full amount of retirement benefits it has promised to its employees and their survivors. If the value of the pension trust falls below the present value of the benefits that have been accrued under the plan, the employer is required by law to make up this deficit — called an *unfunded liability* — through additional contributions over a period of years.

In a *defined contribution* plan, the employer bears no risk beyond its obligation to make contributions to each employee's retirement account. In a DC plan, it is the *employee* who bears the risk that markets will decline ("market risk") or that the specific investments he or she chooses will fall in value ("investment risk"). If the contributions to the account are inadequate, or if the securities in which the account is invested lose value or increase in value too slowly, the employee risks having an income in retirement that is too small to maintain his or her desired standard of living. If this situation occurs, the worker might find it necessary to delay retirement.

Both kinds of retirement plan are eligible for favorable treatment under the Internal Revenue Code, provided that they meet the statutory requirements. Plans that meet these requirements are called *tax-qualified* plans. Employers are permitted to deduct contributions to a qualified plan from the firm's income. Contributions and investment earnings are not counted as taxable income to the employee until they are distributed during retirement.

Pre-funding of Pension Benefits in the Private Sector. Private-sector employers are not required to provide retirement plans for their employees, but those that do must comply with the *Employee Retirement Income Security Act of 1974* (P.L.

---

[2] Retirees can also choose a *joint and survivor annuity* in which a surviving spouse continues to receive an annuity after the retired worker's death. Because it is guaranteed for the lifetimes of both spouses, it pays a lower monthly benefit than a single-life annuity.

93-406), popularly known as "ERISA."[3] ERISA sets standards that plans must meet with respect to reporting and disclosure, employee participation, participant vesting, plan funding, and fiduciary standards.

The administration of ERISA is divided among the U.S. Department of Labor (DOL), the Department of the Treasury's Internal Revenue Service (IRS), and the Pension Benefit Guaranty Corporation (PBGC). Title I of ERISA contains rules for reporting and disclosure, vesting, participation, funding, fiduciary conduct, and civil enforcement. Title II of ERISA, amended the Internal Revenue Code to parallel many of the Title I rules. Title III is concerned with jurisdictional matters and with coordination of enforcement and regulatory activities by the DOL and the IRS. Title IV covers the insurance of defined benefit pension plans and is administered by the Pension Benefit Guaranty Corporation (PBGC). DOL has primary responsibility for reporting, disclosure and fiduciary requirements; and the IRS has primary responsibility for participation, vesting and funding issues. However, DOL may intervene in any matters that materially affect the rights of participants, regardless of primary responsibility.

Because employers cannot be certain that their revenues in future years will be sufficient to pay the pension benefits they owe to retired workers, ERISA requires these benefits to be pre-funded. Pre-funding of benefits protects employees who have earned the right to receive pension payments in the event that the firm goes out of business. Employers in the private sector pre-fund their pension liabilities by establishing pension trusts, which are invested in assets such as corporate stocks and bonds and U.S. Treasury bonds. ERISA also established the Pension Benefit Guaranty Corporation, which pays pension benefits (up to certain limits) in the event that a company goes out of business with an underfunded pension plan. The PBGC, which is funded by premiums collected from employers, insures *only* defined benefit plans.

Pre-funding pension benefits is consistent with the principle of *accrual accounting*, in which a firm's assets and liabilities are recognized in its financial records as they accrue, as opposed to waiting until cash is received or paid out. By providing for future pension liabilities as they are incurred, the firm is recognizing that the pension benefits that it must pay in the future are part of the cost of doing business *today*. When an employer fails to set aside enough money each year to pay the retirement benefits accrued by its workers that year, it accumulates an "unfunded liability." An employer that develops an unfunded liability must make additional *deficit reduction payments* over a period of years until the pension plan's assets equal the present value of its liabilities.

Pre-funding of Pension Benefits in the Public Sector. When the Civil Service Retirement System was established in 1920, it was not pre-funded. Benefits paid to retirees and their surviving dependents were paid from current contributions to the plan. This method of financing retirement benefits, called "pay-as-you-go," also has been used in the Social Security system for most of its history. The federal government is not likely to "go out of business," and it could have continued to fund

---

[3] Neither federal nor state and local employee pension plans are subject to ERISA.

its pension obligations to federal employees on a pay-as-you-go basis. Nevertheless, when Congress established the Federal Employees' Retirement System in 1986, it required all pension benefits earned under FERS to be fully pre-funded by employer and employee contributions and the interest earned by the bonds in which these contributions are invested.

In establishing FERS, Congress decided to require pre-funding of federal employee retirement benefits for reasons of equity and efficiency. Many employers would have regarded it as inequitable for Congress to have required pre-funding by private-sector pension plans while not requiring it for federal employees' retirement benefits under FERS. Moreover, pre-funding promotes more efficient allocation of resources between personnel costs and other expenses because it forces agencies to recognize the full cost of retirement benefits when preparing their annual budget requests. Efficient allocation of resources between labor and other inputs can occur only when the price paid for each resource reflects its full *marginal cost* (the cost of one more unit of each resource). Pre-funding employee pensions under FERS promotes efficient allocation of resources by requiring the full marginal cost of employee compensation to be recognized in each agency's budget.

Investment of Trust Fund Assets. The assets in a pension fund represent a "store of wealth" that guarantees that future obligations can be met as they come due. The Civil Service Retirement and Disability Trust Fund, however, is not a store of wealth in the same way as the pension funds of private-sector firms and state and local governments. The civil service trust fund is required by law to invest exclusively in U.S. Treasury bonds. The bonds can be converted to cash only by collecting taxes from the public (or by issuing more Treasury bonds, which merely delays the time at which taxes must be collected.) In short, "pre-funding" federal employee retirement benefits with U.S. Treasury bonds will not obviate the need to raise revenue from the public to pay civil service retirement benefits as those benefits come due.[4] The bonds held by the civil service trust fund assure that the fund has the legal authority to issue pension checks drawn on the Treasury, but they do not reduce future claims against the ultimate guarantor of federal employee pensions, which is the tax-paying public.

If the Civil Service Retirement and Disability Fund held assets that earned a higher average rate of return than U.S. Treasury bonds, some of the future cost of civil service retirement annuities could be paid from these higher investment returns. However, in the short run, allowing the civil service retirement trust fund to invest in private-sector securities such as corporate stocks and bonds would result in higher federal expenditures. The trust fund's two main sources of income are employee contributions and contributions from federal agencies on behalf of their employees. Employee contributions are income both to the federal government and to the trust fund. Agency contributions, however, while they are income to the trust fund, are not income to the federal government. Agency contributions to the trust fund are *intragovernmental transfers* that have no effect on the size of the government's

---

[4] The bonds held by the Civil Service Retirement and Disability Fund represent *budget authority*, which is the legal basis for the Treasury to disburse funds.

annual budget deficit or surplus. *Outlays* from the trust fund occur mainly as benefit payments to annuitants and payment of administrative expenses of the fund.

If the trust fund were to purchase private assets such as corporate stocks and bonds rather than U.S. Treasury bonds, an outlay from the trust fund would be required to purchase the assets. This outlay would consist partly of the employee contributions that are income to both the trust fund and the Treasury and partly of the agency contributions that are income to the trust fund, but are not income to the Treasury. If employee contributions were used to purchase private-sector assets, they would no longer be income to the Treasury, and would increase the federal budget deficit by the amount diverted to purchase private-sector assets. Agency contributions — currently an intragovernmental transfer — would instead be used to purchase private-sector assets, representing an outlay of funds from the Treasury.

Over the long run, however, purchasing private-sector assets would not increase the budget deficit, and it could reduce it. Outlays would be moved from the future — where they would have occurred as benefit payments — to the present, where they would occur as asset purchases. If the net rate of return on private-market securities exceeded the return from Treasury bonds, the extra investment income earned by the trust fund would reduce the amount of tax revenue that would have to be raised from the public in the future to pay pension benefits under CSRS and FERS. This would also be true for any other federal trust fund that purchased higher-yielding private-sector securities, such as the Social Security trust fund.

Financing Retirement Annuities for Federal Employees

The source of the money from which pension annuities are paid is the same for both CSRS and FERS: revenue collected by the government through taxes, employee contributions, and borrowing from the public.[5] Federal agencies "pre-fund" their pension liabilities by deferring some of their budget authority (which represents legal permission to spend money from the Treasury) until it is needed to pay pensions to retired workers. Federal agencies defer this budget authority by transferring it to the Civil Service Retirement and Disability Trust Fund. The Treasury credits the fund with the appropriate amount of budget authority in the form of special-issue bonds that earn interest equal to the average rate on the Treasury's outstanding long-term debt. In the future, when annual outlays for retirement and disability benefits exceed the amount of income from employee and agency contributions, the Civil Service Retirement and Disability Trust Fund will redeem bonds in the amount of the additional budget authority it requires to make benefit payments in that year.

Employee Contributions. Federal employees have mandatory contributions to the Civil Service Retirement and Disability Trust Fund deducted from their paychecks. Employees of the executive branch who are covered by CSRS contribute

---

[5] The contributions to the trust fund from the U.S. Postal Service are derived mainly from the revenue derived by that agency from selling postal services to the public.

7.0% of basic pay, while workers covered by FERS contribute 0.8% of pay.[6] (Members of Congress contribute 8.0% of salary if covered by CSRS and 1.3% if covered by FERS). In addition, workers covered by FERS pay Social Security taxes of 6.2% to the Old-Age, Survivors, and Disability Insurance program (OASDI) on salary up to the annual maximum taxable payroll amount ($87,900 in 2004).[7] Congress made the sum of FERS contributions and OASDI payroll taxes equal to the CSRS contribution rate of 7.0% so that workers with the same salary would have the same take-home pay, regardless of whether they were covered by CSRS or FERS.[8]

Employee contributions to CSRS and FERS do not go into individual accounts, and the pension annuity that a retired employee receives from CSRS or FERS is not directly related to the amount that the employee contributed to the system. Under both CSRS and FERS, the amount of the retirement annuity is based on the employee's years of service and the average of the employee's highest three consecutive years of salary. Workers covered by CSRS accrue benefits equal to 1.5% of pay for their first five years of service, 1.75% for the next five years, and 2.0% of pay for each year beyond the tenth. Employees covered by FERS accrue benefits equal to 1.0% of pay for each year of service. If they have worked for the federal government for 20 or more years and retire at age 62 or older, the accrual rate under FERS is 1.1% for each year of service.

Employer Contributions. Whether a federal employee is covered by CSRS or FERS, his or her employing agency also contributes to the CSRDF. The amount of the contribution differs between CSRS and FERS for employees with the same basic pay. Federal law requires that agency contributions to FERS must be equal to the full cost of FERS, minus employee contributions. The percentage of basic pay contributed by federal employees is set in law at the difference between the CSRS contribution rate (7.0%) and the Social Security payroll tax rate (6.2%). The cost of retirement and disability benefits accrued each year under FERS is currently estimated by the Office of Personnel Management (OPM) to be equal to 11.5% of payroll. Thus, federal agencies contribute an amount equal to 10.7% of their total payroll to the CSRDF for employees covered by FERS.[9] Together, the employee and

---

[6] Under the *Balanced Budget Act of 1997* (P.L. 105-33) employee contribution rates under both CSRS and FERS rose by 0.25% in Jan. 1999, and by a further 0.15% in January 2000. Another 0.1% increase was scheduled for Jan. 2001. Employee contribution rates were to revert to previous levels on Jan. 1, 2003. The increases mandated by the BBA were repealed by P.L. 106-46 (H.R. 4475 of the 106th Congress), effective Jan. 1, 2001.

[7] Retired federal employees are eligible for Medicare at age 65, regardless of whether they were covered by CSRS or FERS, and federal workers in both programs pay the Hospital Insurance (HI) payroll tax of 1.45% on all salary and wages.

[8] Take-home pay is equal for two workers with the same salary whether they are covered by CSRS or FERS only up to the Social Security wage base ($87,900 in 2004). Employees covered by CSRS contribute 7.0% of *all* wage income to CSRS. Employees covered by FERS contribute only 0.8% of pay to FERS on salary above the Social Security wage base.

[9] Because the cost of retirement and disability benefits can vary from year to year based on the age and experience profile of the federal work force, the percentage of pay contributed to FERS by federal agencies on behalf of their employees also can change from year to year.

(continued...)

employer contributions to the CSRDF for employees enrolled in FERS, plus the interest that accrues on those contributions, fully fund the pension benefits earned each year by employees covered by FERS.

Unlike FERS, which by law must be fully pre-funded, the retirement benefits accrued by employees covered by CSRS contributions are *not* fully pre-funded by employee and agency contributions and interest earnings. As a result, retirement and disability benefits under CSRS are paid for in part from the general revenues of the U.S. Treasury. Each year, the Treasury credits the Civil Service Retirement Trust Fund with additional budget authority for this purpose. In FY2004, this transfer amounts to $21.9 billion. (See **Table 1**.)

How the Civil Service Trust Fund Operates

The Civil Service Retirement and Disability Trust Fund is a record of the *budget authority* available to pay retirement and disability benefits. Each year, the trust fund is credited by the Treasury with contributions from current employees and their employing agencies, interest on the securities held by the fund, interest on previous service for which benefits have been accrued but for which budget authority has not yet been provided, and a transfer from the general revenues of the Treasury. Only a small part of this income to the fund — mainly contributions from employees — is in cash, and represents income to both the trust fund and the government as a whole. The remainder of these transactions are *intragovernmental transfers* in which budget authority is transferred from agencies to the trust fund. These intragovernmental transfers have no effect on the size of the government's budget deficit.[10]

The largest sources of income to the trust fund are agency and employee contributions, contributions from the U.S. Postal Service, interest earned by the securities held by the fund, and a transfer of general revenues of the Treasury. The transfers from the Treasury pay part of the actuarial costs of CSRS that are not met by contributions from employees and their employing agencies.[11] The full actuarial cost of the CSRS has been estimated by the Office of Personnel Management to be 24.4% of payroll. Workers covered by CSRS and their employing agencies each contribute an amount equal to 7.0% of payroll to the civil service trust fund.

---

[9] (...continued)
The full cost of the FERS to the federal government also includes the employer share of Social Security taxes and the employer match on employee contributions to the Thrift Saving Plan. These costs are in addition to the 10.7% of payroll contributed for to the civil service trust fund to finance the FERS basic retirement annuity.

[10] The transaction between the trust fund and the Treasury does not affect the deficit because it occurs *within* the government. Only revenues collected from the public and outlays of federal funds to the public affect the budget deficit.

[11] Part of the actuarial cost of CSRS benefits — the cost of future cost-of-living adjustments (COLAs) paid to retirees — is not covered by contributions from employees, their employing agencies or the Treasury. As a result, the CSRS continues to accrue an unfunded liability.

The civil service trust fund is similar to the Social Security trust fund in that, by law, 100% of its assets are invested in special-issue U.S. Treasury bonds or other bonds backed by the full faith and credit of the United States government. When the trust fund needs cash to pay retirement benefits, it redeems the bonds and the Treasury disburses an equivalent dollar value of payments to civil service annuitants. Because the bonds held by the trust fund are a claim on the U.S. Treasury, they ultimately are paid for by the American taxpayer. According to the U.S. Office of Management and Budget (OMB), balances in the trust fund:

> . . . are available to finance future benefit payments and other trust fund expenditures — but only in a bookkeeping sense. These funds are not set up to be pension funds, like the funds of private pension plans. The holdings of the trust funds are not assets of the government as whole that can be drawn down in the future to fund benefits. Instead, they are claims on the Treasury. When trust fund holdings are redeemed to pay benefits, Treasury will have to finance the expenditure in the same way as any other federal expenditure: out of current receipts, by borrowing from the public, or by reducing benefits or other expenditures. The existence of large trust fund balances, therefore, does not, by itself, increase the government's ability to pay benefits. From an economic standpoint, the Government is able to prefund benefits only by increasing saving and investment in the economy as a whole.[12]

Financial Status of the Civil Service Trust Fund

The Short-Term Picture. The Civil Service Retirement and Disability Fund held a balance of $601.7 billion at the close of FY2003, which represents budget authority that may be used to make payments to annuitants under both CSRS and FERS. Expenditures from the fund totaled $50.4 billion in 2003, and consisted mostly of payments to retired federal employees and their surviving dependents. Annuity payments totaled $50 billion in 2003, and payments to the estates of decedents and to separating employees accounted for another $276 million. Administrative expenses for the fund were $119 million, or 0.2% of total expenditures. (See **Table 1**.) The trust fund currently holds budget authority equal to the estimated outlays from the fund over the next nine years.

Each year, the CSRDF receives payments of two types: *cash transactions* and *intragovernmental transfers*. The largest cash transactions ($4.0 billion in 2003) consist of employee contributions to CSRS and FERS. For executive-branch employees, these contributions are equal to 7.0% of base pay under CSRS and 0.8% of pay under FERS. Smaller cash payments are received from the District of Columbia to finance retirement benefits for its employees, and from additional cash contributions made by federal workers, such as former federal employees who return to government service and repay retirement contributions they had previously withdrawn.

The largest payments to the CSRDF are those it receives from federal agencies and the Postal Service on behalf of their employees, interest payments from the U.S.

[12] U.S. Office of Management and Budget, *Budget of the United States Government, Fiscal Year 2005: Analytical Perspectives* (Washington: GPO, 2004), p. 343.

Treasury on the bonds held by the fund, and a payment from the general fund of the Treasury to make up for the insufficient funding of benefits accrued under CSRS.[13] These payments are not cash transactions. They are intragovernmental transfers that result in an increase in the fund's budget authority as recorded in the accounts of the U.S. Treasury. The fund receives Treasury bonds as a record of this budget authority, which it redeems periodically as annuity payments come due.

In recent years, aggregate employee contributions have declined, while agency contributions have increased. The main reason for this trend is the continuing transition in which more of the federal work force is covered by FERS each year. Employee contributions to the trust fund are a smaller percentage of pay under FERS (0.8% of pay) than under CSRS (7.0% of pay).[14] Agency contributions under FERS must be equal to the full actuarial cost of the program that is not paid for by employee contributions. Agency contributions for employees in FERS are equal to 10.7% of payroll in 2004, compared with 7.0% of payroll for employees in CSRS.

---

[13] Federal law requires that employee and agency contributions to the civil service trust fund, plus the interest paid on securities held by the fund, together must provide sufficient budget authority to pay all of the benefits that federal employees accrue each year under FERS, according to actuarial estimates. Employee and agency contributions to CSRS are not sufficient to fully fund CSRS benefits; consequently, additional budget authority must be transferred each year from the general revenues of the U.S. Treasury to meet benefit obligations under CSRS.

[14] Employees covered by FERS also pay Social Security taxes of 6.2% of pay up to $87,900.

Table 1. Income and Expenditures of the Civil Service Retirement and Disability Fund, 2003-2005
(amounts in millions)

	FY2003	FY2004(est.)	FY2005(est.)
Beginning balance	**$573,738**	**$601,736**	**$631,551**
Income to the fund			
Cash transactions:			
Employee contributions	$4,004	$4,087	$3,990
District of Columbia	$53	$46	$42
Other employee deposits	$518	$543	$569
Intragovernmental transfers:			
Agency contributions	$11,288	$11,566	$12,769
Postal Service (total)	$3,331	$4,364	$4,450
Interest on securities	$37,261	$36,035	$37,926
General fund receipts	$21,878	$25,970	$26,372
Re-employment offset	$33	$34	$36
Total income to the fund	**$78,366**	**$82,645**	**$86,154**
Expenditures from the fund			
Employee annuities	-$42,022	-$44,106	-$45,857
Survivor annuities	-$7,951	-$8,296	-$8,759
Payments to estates	-$153	-$163	-$171
Refunds to separated employees	-$123	-$113	-$104
Administration	-$119	-$152	-$143
Total expenditures from the fund	**-$50,368**	**-$52,830**	**-$55,033**
Ending balance	**$601,736**	**$631,551**	**$662,672**

Source: Office of Management and Budget, *Budget of the United States Government, FY2005.*

The Long-Term Picture. **Table 2** portrays the annual income and expenditures of the CSRDF through the year 2075, as estimated by OPM. The fund receives income from employee contributions, government contributions, and interest income on the securities it holds. The fund's expenses consist mostly of benefit payments. The table also shows the year-end balance of the fund and the estimated amount of the unfunded actuarial liability at the end of the year. The unfunded actuarial liability represents the difference between the present value of the fund's future benefit obligations and the present value of future credits to the fund plus the value of the securities it holds. The final two columns of the table show, respectively, the expenditures of the CSRDF relative to the government's total payroll expenses for employees and CSRDF expenditures relative to the nation's annual gross domestic product (GDP).

The estimates presented in **Table 2** show the income to the CSRDF rising over the projection period from $78 billion in 2004 to $150 billion in 2025 and to $938 billion in 2075.[15] The total expenses of the fund are projected to rise more slowly, increasing from $53 billion in 2004 to $122 billion in 2025 and to an estimated $494 billion in 2075. Consequently, the assets held by the CSRDF also are projected to increase steadily over the next 70 years, rising from $627 billion in 2004 to more than $1.1 trillion in 2025 and to $10.3 trillion in 2075. According to the estimates prepared by OPM, the unfunded actuarial liability of the CSRS will continue to rise until about the year 2030, when it will peak at $809 billion. From that point onward, as the number of annuitants covered by CSRS steadily declines, the unfunded liability will fall, reaching a projected level of $52 billion in the year 2075.

In FY2004, $53 billion will be expended from the CSRDF, composed mainly of annuity payments to retirees and survivors. The federal government's payroll expense for covered employees in 2004 is approximately $138 billion. Therefore, pension expenditures to former employees and their surviving dependents are equal to about 38.5% of the amount paid as salary and wages to current employees. Pension expenditures are projected to increase relative to payroll expenditures over the next several years, peaking in 2015 at an amount equal to 44.5% of the government's salary and wage expenses for its employees. From that point onward, the expenditures of the CSRDF are projected to fall in comparison with payroll expenses. By 2075, the amount paid to retired workers and their survivors is estimated to be 21% as large as the government's wage and salary payments to its employees.

Annuity payments to retired workers and their survivors are not a component of the government's current payroll expenses. They are a separate, additional category of the government's personnel costs. However, CSRDF expenditures expressed as percentage of payroll are a useful measure of the relative size of pension expenses because of the assumptions underlying OPM's estimates of total payroll expenditures. OPM estimates the government's annual payroll expense under the assumption of a constant number of federal workers from year to year. The ratio of pension outlays to payroll expense provides a measure of the cost of annuities paid to retirees and survivors relative to payroll expenditures for a workforce of constant size. Virtually all of the increase in this ratio through the year 2020 can be attributed to an increase in the number of annuitants relative to the number of currently employed workers. The decline in the ratio of pension outlays to current pay that occurs after 2020, however, does not indicate a declining ratio of annuitants to employees, but rather will occur mainly because more retirees will be receiving smaller pension benefits under FERS than they would have received under CSRS.

Economists often compare the federal budget to the size of the economy (the GDP) to evaluate whether federal spending is absorbing more or less of the nation's resources over time. Individual components of the budget, too, can be compared to GDP to evaluate the proportion of the nation's total economic resources that they consume each year. The final column of **Table 2** shows federal outlays for civil service pensions as a percentage of GDP. Relative to the total economic resources

---

[15] All amounts in **Table 1** and **Table 2** are expressed in nominal dollars.

of the economy, the expenditures of the CSRDF fell throughout the 1990s and are expected to remain steady for the next 15 years before declining dramatically from 2020 to 2075. Federal expenditures for civil service retirement annuities are estimated to equal to 0.46% of GDP in 2004, down slightly from a high of 0.55% in 1991. Between 2004 and 2020, the annual expenditures of the CSRDF are projected to remain at about 0.43% to 0.45% of GDP each year. From that point on, outlays from the CSRDF will fall steadily to about 0.20% of GDP by 2060.

CSRDF expenditures will fall relative to GDP mainly as a result of the decline in the proportion of civil service annuitants who are covered by CSRS and the increase in the number who are covered by FERS. The FERS basic annuity was designed to be much smaller relative to high-3 average pay than a CSRS annuity because FERS annuitants also receive benefits from Social Security and the Thrift Savings Plan. Because the transition from CSRS to FERS is mandated by law, the constant-dollar value of CSRDF outlays per annuitant will decline due to the different benefit formulas between CSRS and FERS. Consequently, outlays for civil service annuities are almost certain to decline relative to GDP, even if GDP grows more slowly than is assumed in the projections displayed in **Table 2**.[16]

The estimates in **Table 2** do not reflect the effects of the *Postal Civil Service Retirement System Funding Reform Act of 2003* (P.L. 108-18, April 23, 2003), which lowers the Postal Service's annual payment for CSRS pensions by over $2.5 billion beginning in FY2003. The legislation was enacted after a study was conducted by the Office of Personnel Management of the Postal Service's estimated remaining financial obligation to the trust fund for service performed by Postal Service employees covered under CSRS. The OPM study concluded that because past Postal Service contributions had earned interest at rates higher than the 5% rate assumed in statute, the Postal Service's remaining obligation to the civil service trust fund for past service performed by employees covered under CSRS was approximately $5 billion, rather than the $30 that had been estimated previously. P.L. 108-18 reduces the future payments from the USPS to the civil service trust fund in recognition of the reduction in the Postal Service's remaining CSRS liabilities.

---

[16] GDP estimates in **Table 2** are taken from the 2004 Annual Report of the Board of Trustees of the Federal Old-Age and Survivors Insurance and Disability Insurance Trust Funds.

Table 2. Past and Projected Flow of Assets of the Civil Service Retirement and Disability Fund, 1990 to 2075

(amounts in billions)

Fiscal Year	Total Income	Total Expenses	Assets at End of Year	Unfunded Actuarial Liability	Expenses as a Percent of Total Payroll	Expenses as a Percent of GDP
Actual						
1990	52.7	-31.4	238.0	568.7	35.8%	0.54%
1991	56.8	-33.2	261.6	593.8	36.0	0.55
1992	60.0	-33.2	288.4	599.7	33.9	0.53
1993	62.9	-35.1	317.4	540.1	35.1	0.53
1994	63.8	-36.5	344.3	540.6	35.5	0.52
1995	66.1	-38.6	371.3	545.8	36.8	0.52
1996	67.7	-39.9	398.9	512.4	37.0	0.51
1997	70.4	-41.8	427.5	505.6	38.3	0.50
1998	72.8	-43.2	457.1	496.1	39.4	0.49
1999	73.7	-44.0	486.8	506.6	38.0	0.48
2000	76.0	-45.2	521.5	509.5	37.4	0.46
2001	77.9	-47.1	548.2	510.9	37.6	0.47
Estimated [a]						
2004	78.1	-53.0	626.6	555.3	38.5	0.46
2005	79.7	-55.4	650.8	571.5	39.2	0.46
2010	94.4	-70.1	768.3	650.1	42.5	0.45
2015	111.0	-88.4	883.7	717.1	44.5	0.45
2020	131.1	-105.6	1,004.7	762.2	43.7	0.43
2025	150.0	-121.8	1,140.2	789.7	41.6	0.40
2030	172.3	-136.2	1,299.7	808.6	38.1	0.36
2035	201.7	-148.9	1,527.5	803.6	33.9	0.32
2040	238.6	-161.3	1,862.0	772.4	29.9	0.28
2045	286.1	-175.4	2,345.0	714.2	26.5	0.25
2050	347.9	-195.2	3,021.3	625.9	23.9	0.22
2055	427.9	-225.2	3,931.6	502.1	22.4	0.21
2060	522.1	-268.6	5,102.9	346.6	21.7	0.20
2065	631.0	-327	6,518.7	212.9	21.5	0.20
2070	767.0	-401.4	8,218.2	114.1	21.4	0.19
2075	937.7	-494.2	10,272.0	51.5	21.4	0.19

Source: U.S. Office of Personnel Management, *Civil Service Retirement and Disability Fund Actuarial Valuation, Fiscal Year 2002*; Council of Economic Advisors, *Economic Report of the President, 2004*; and the 2004 Report of the Social Security Board of Trustees.

a. These estimates do not reflect the effects of the *Postal Civil Service Retirement System Funding Reform Act of 2003* (P.L. 108-18, April 23 2003), which lowers the Postal Service's annual payment for its CSRS obligation by over $2.5 billion beginning in FY2003.

The Civil Service Retirement and Disability Fund in the Federal Budget

In FY2003, the total receipts of the CSRDF were approximately $78 billion, and disbursements from the fund were about $50 billion. The data displayed in **Table 1** show that only a small part of the revenues to the fund ($4.0 billion) were *cash receipts*. The remainder consisted of budget authority transferred from other federal agencies.[17] The cash receipts of the fund come primarily from the contributions of federal and Postal Service employees toward their future retirement benefits. Other cash income to the fund comes from payments made by the District of Columbia on behalf of its employees covered by CSRS or FERS, and a small amount of supplemental contributions made by federal employees. All of the cash payments into the CSRDF are income to *both* the U.S. government and to the trust fund. These cash receipts reduce the government's budget deficit (or increase its surplus). Benefit payments to retirees and survivors are cash outlays of the federal government.

Most of the payments into the CSRDF — $74 billion in 2004 — are *intragovernmental transfers*. These transactions are income to the fund, but they are *not* income to the U.S. government. Agencies of the federal government do business not only with the public, but also with *each other*. These intragovernmental transactions rarely involve cash and they *never* affect the government's budget deficit or surplus because no funds either come into or go out of the government. Cash is rarely involved in intragovernmental transfers because individual government agencies, in general, have no cash to spend.[18] What the Congress appropriates to federal agencies each year is not cash, but *budget authority*. Budget authority is *legal permission for an agency to spend money from the accounts of the U.S. Treasury*. The Treasury takes in money from the public by collecting taxes and by borrowing (issuing bonds), and in most cases it is only the Treasury that disburses cash.

Only transactions in which the government either *collects* money from the public or *pays* money to the public affect the federal budget surplus or deficit. (The "public" includes federal employees, who are paid salaries and who make mandatory contributions to the civil service trust fund.) Intragovernmental transfers merely move budget authority from one agency's account with the Treasury to the account of another agency. Income to the trust fund that comes from the public also is income to the government. Income to the trust fund that is transferred from another government agency is income only to the trust fund, and not to the government. Agencies pre-fund their employees' pension benefits by transferring budget authority to the civil service trust fund. When the income of the trust fund exceeds the amount it needs to pay benefits, it "saves" this budget authority for the future by purchasing

---

[17] "Cash" in this context refers to money deposited in a bank, not just notes and coins.

[18] Some federal agencies collect "user fees" or other payments from the public, but the cash receipts of federal agencies are trivial in comparison to the size of the federal budget. The majority of the government's cash transactions with the public — collecting taxes, purchasing goods and services, paying federal employee salaries, and disbursing Social Security benefits, government pensions, and cash welfare — are conducted by the U.S. Treasury.

bonds from the U.S. Treasury. The CSRDF can pay retirement benefits up to the amount of budget authority it holds in its account at the Treasury.

It has been suggested from time to time that the Civil Service Retirement and Disability Fund should be taken "off budget," as has already been done with the Social Security Trust Fund. Some observers have noted that Congress has on occasion sought budgetary savings from CSRS and FERS that were not sought from Social Security.[19] Of course, it cannot be known with certainty whether any special consideration that might have been given to Social Security in the Congress's annual budget deliberations was due to its being "off budget" or to the much larger number of beneficiaries who would be affected. Whether taking the civil service retirement programs off-budget would protect them from future budget cuts is uncertain.

Taking an account "off budget" means that its income, outgo, and year-end balance are not included in calculations of the government's annual budget surplus or deficit. Off-budget accounts are portrayed separately in the budget documents prepared by the Office of Management and Budget and the Congressional Budget Office (CBO). However, both OMB and CBO also publish *unified budget accounts* that include Social Security and other programs that are "off budget." This is done because taking an account off budget does not end the activity or remove its effects from the U.S. economy. Whether Social Security — or civil service retirement — is on-budget or off-budget, it still collects revenues from the public, pays benefits to the public, and affects the nation's financial markets by influencing the amount of private capital that is absorbed by government borrowing.

Taking the civil service trust fund off-budget would not affect the government's revenues or outlays in the *unified budget accounts*, but it would affect the size of the budget deficit or surplus as portrayed in any budget documents that excluded the CSRDF. For example, employee contributions to CSRS and FERS that are now counted as revenue to the Treasury would not be treated as revenue if they were paid to an "off-budget" CSRDF. The money that federal agencies now send to the trust fund in the form of intragovernmental transfers would instead be recorded as outlays, and would therefore increase the government's budget deficit or reduce the budget surplus in the year that the transfer occurs rather than in the future when benefits are paid. The outlays made by the fund to pay civil service annuitants would not appear at all in the federal budget. The net effect of these changes if the CSRDF had been off-budget in 2003 would have been an increase of $28 billion in the government's reported budget deficit, even though the amount of money collected from the public and the amount of money paid to civil service annuitants would have been no different than under current law.

One of the purposes of the federal budget is to show whether the government's revenues and outlays are in balance or out of balance. Therefore, taking *any* account off-budget distorts the picture of the government's fiscal condition. It is for this reason that financial analysts and economists focus almost exclusively on the *unified budget* totals when evaluating the effect of the federal budget on the nation's

[19] For example, in 1994, 1995, and 1996, cost-of-living adjustments (COLAs) for CSRS and FERS were delayed from Jan. to Apr., but Social Security COLAs were not delayed.

financial markets. If "outlays" were to include amounts not actually paid from the Treasury in the current year (as would be the case if the CSRDF were off-budget), then no revenue from the public would be needed in that year to pay for them. In years of budget deficits, some of the "deficit" would require borrowing from the public, and some of it would not. In years of modest budget surplus, there might *appear* to be a deficit because transfers to an off-budget account would be recorded as outlays, even though they do not involve payments from the Treasury to the public. For these reasons, taking the CSRDF off-budget might lead to greater confusion about the size of the "real" budget deficit or surplus, as has been the case with the off-budget status of Social Security.[20]

Civil Service Retirement: Funding and Accounting Issues

Accounting for Pension Costs Under CSRS and FERS. Actuaries use a concept called "normal cost" to estimate the amount of money that must be set aside each year from employer and employee contributions to pre-fund pension benefits. Normal cost is usually expressed as a percentage of payroll. There are two measures of normal cost: *static* and *dynamic*.

- *Static normal cost* is the estimated percentage of payroll that must be set aside each year to fund pension benefits based on current employee pay with no future pay increases, no future COLAs for retiree annuities, and a fixed rate of interest.

- *Dynamic normal cost* is the estimated percentage of payroll that must be set aside each year to fully fund pension benefits for workers who will continue to accrue new benefits, including the effects of employee pay raises, post-retirement COLAs, and changes in the rate of interest.[21]

By law, the basic FERS annuity must be pre-funded according to its *dynamic normal cost*. Every year, OPM estimates the dynamic normal cost of FERS pension annuities for employees entering the federal work force that year. Of course, some employees will never collect a FERS annuity, so for each group of new employees, OPM must estimate average job tenure, turnover, career-long salaries, age at retirement, rates of disability, death rates, and the number of annuitants who will leave surviving dependents. OPM's periodic re-estimates of the dynamic normal cost of FERS reflect anticipated changes in interest rates, inflation, and employee and retiree demographic characteristics.

---

[20] For further discussion, see CRS Report 98-422, *Social Security and the Federal Budget: What Does Social Security's Being "Off Budget" Mean?*.

[21] Interest rates must be projected because the normal cost is computed as a "present value." Expressed in absolute terms, rather than as a percentage of payroll, the normal cost of a pension plan is the amount of money that would have to be invested at a given rate of return to pay future pension obligations, including increases in pension costs that will result from employee pay raises and retiree cost-of-living adjustments (COLAs).

OPM has estimated the normal cost of the FERS basic retirement annuity at 11.5% of payroll. Employee contributions were set in law at 0.8% of pay, so the contributions of federal agencies are equal to 10.7% of basic pay. If the assumptions underlying these cost estimates prove to be accurate, FERS will be "fully funded."[22] OPM has estimated the dynamic normal cost of CSRS, using the same economic assumptions used in FERS, at 24.4% of payroll. The financing of CSRS has at times been a topic of controversy, however, because it is *not* funded according to its dynamic normal cost. CSRS is funded through a combination of employee and agency contributions that together are equal to the static cost of CSRS, along with contributions from the general fund of the U.S. Treasury that make up some of the difference between the static normal cost of CSRS and its dynamic normal cost.

Why Are CSRS Revenues Less Than the Present Value of Benefits? At the time that Congress established the CSRS in 1920, it set up a trust fund from which benefits would be paid. From the beginning, however, CSRS was funded on a *pay-as-you-go* basis. The trust fund was used to pay benefits to already-retired workers, rather than to pre-fund the pension benefits of current workers. Initially, only employees made regular payroll contributions to the fund. Regularly scheduled agency contributions were not mandated until the 1950s. For many years, there were so few retirees that the fund was able to meet its financial obligations to beneficiaries from employee contributions alone.

In 1956, Congress passed P.L. 84-854 which required federal agencies to make contributions to the Civil Service Retirement Trust Fund on behalf of their eligible employees. The contributions made by federal agencies were equal in amount to the money paid into the fund by their employees, and were made from appropriations that agencies received specifically for this purpose. Even with regular contributions from the employing agencies, however, the CSRS was still being funded on a pay-as-you-go basis. Contributions to the fund were sufficient to meet *current* benefit obligations but not to *pre-fund* the future retirement benefits of federal employees.

As the federal civil service pension system matured (that is, as the ratio of annuitants to workers began to rise), it became necessary to establish a formal system of accounting for the pension obligations that had been incurred by the federal government but for which funds had not yet been set aside. In response to this need, Congress enacted P.L. 91-93 in 1969. This law set the employee contribution to CSRS at 7.0% of pay and required an equal amount to be contributed from funds appropriated to federal agencies. This amount (equal to 14.0% of payroll) represented the total contribution required in 1969 to pay the costs of pension liabilities accrued by federal employees, using "static" assumptions: no future pay increases, no COLAs, and a 5.0% annual rate of return on the securities in the Civil Service Retirement and Disability Fund. Agency and employee contributions under CSRS have remained at the same percentage of payroll since this law was passed.

---

[22] If the amount set aside each year proves to be insufficient (due to inaccurate assumptions about pay raises, interest rates, the rate of inflation, or other variables) the shortfall would be made up from the general revenues of the U.S. Treasury. See 5 U.S.C. §8423(a)(4).

P.L. 91-93 also requires three types of payments to be made annually from the general revenues of the U.S. Treasury into the CSRDF. These payments, which are made by the Treasury each year, are

- The amount necessary to amortize (pay off with interest) over a 30-year period any increase in pension liability that results from pay increases (but not retiree COLAs) or from bringing newly covered groups of workers into the CSRS;

- the amount of the employer's share of the cost of benefits attributable to military service; and

- interest, fixed at a rate of 5%, on the estimated amount of the previously accrued liabilities of the CSRS for which contributions have not yet been made to the fund.[23]

Thus, while the *static* costs of the CSRS were shared equally between federal employees and their employing agencies, the government assumed the full responsibility for pension liabilities that are not captured by measuring only static normal costs. By including the 30-year amortized cost of pay raises in the annual transfer from the general fund, the federal government explicitly assumed the additional pension expenses that result from pay raises.[24] All costs of the CSRS that are not paid by employee and agency contributions or through the transfers to the CSRDF mandated by P.L. 91-93 ultimately will be paid from the general revenues of the Treasury. The costs of retiree COLAs, which also are not part of the static normal cost of the CSRS, are not included in the annual transfer from the Treasury to the CSRDF, and ultimately will be paid from the general fund of the Treasury.

Employee and government contributions under both CSRS and FERS are paid into the CSRDF, and pension benefits are paid to annuitants under both programs from this fund. Because the full costs of CSRS are not met by the combined total of employee contributions, agency contributions, and the supplemental payments from the Treasury, some future CSRS benefits will of necessity be paid from contributions that were made to the fund on behalf of employees who are covered by FERS. This will create an unfunded liability for FERS. This liability will be paid off through a new series of 30-year amortization payments from the general fund of the Treasury to the CSRDF. As stated by OPM:

> CSRS benefit payments [will] begin to exceed total CSRS income in the year 2007, and the assets attributable to CSRS [will be] depleted by the year 2026.

---

[23] Although this law mandated interest payments on the accrued CSRS liability to be made from the Treasury to the CSRDF at the fixed rate of 5%, it did not provide for amortizing ("paying off") the accumulated liability.

[24] Pay raises affect pension costs because the CSRS annuity is based on a worker's high-3 average pay. The effect of pay raises on future CSRS pension costs is met by amortizing them over a 30-year period with payments to the from the U.S. Treasury. Because the cost of COLAs is not accounted for in the payments to the trust fund mandated by the 1969 law, the CSRS continues to accumulate an unfunded liability attributable to retiree COLAs.

> Since the CSRS benefits continue to be paid from the assets of the CSRDF, the assets attributable to FERS will be reduced each year by the amount that the CSRS benefits exceed the CSRS contributions. This will cause an increase in the supplemental liability under FERS each year, which must then be amortized by a new series of 30-year payments under FERS.[25]

Current law specifies that funds that were paid into the CSRDF on behalf of employees covered by FERS will be used to pay the unfunded liability of CSRS. FERS will then be reimbursed by a series of payments with interest from the general fund of the Treasury to the CSRDF.

Accounting Issues Raised by the Way CSRS Benefits Are Financed. Actuarial estimates indicate that the unfunded liability of the CSRS does not pose a threat to the solvency of the Civil Service Retirement and Disability Trust Fund. In its annual report, OPM has stated that "the total assets of the CSRDF continue to grow throughout the [75-year] term of the projection, and ultimately reach a level of about 4.4 times payroll, or 21 times the level of annual benefit outlays." Nevertheless, the current method of funding the CSRS has in recent years been a source of debate for at least two reasons:

> (1) Because employee and government contributions do not account for the full actuarial cost of CSRS pension obligations as they accrue each year, the CSRS continues to accumulate additional unfunded liabilities. Consequently, some of the pension costs that are incurred each year will not be reflected in the government's budget until those benefits are paid at some time in the future. Some budget experts argue that these costs should be accounted for in each agency's budget *as they accrue*, just as is done in the FERS program.
>
> (2) The supplemental payments to the trust fund that are required by the 1969 law come from the general revenues of the Treasury rather from the budgets of the various federal agencies where these costs are incurred. As a result, the amount of employee compensation for which agencies must account in their budgets each year understates the *full costs* of employment.[26] Critics say that this contributes to an inefficient allocation of resources in the federal government by making labor costs appear lower than they really are.

If federal law were amended so that agencies were required to fully fund the current and future costs of the CSRS through increased contributions, agencies could do so from their current-law appropriations or they could be granted additional budget authority for this purpose. The two approaches would have different effects on the federal budget. For agencies to be held harmless for the increased contributions, they would have to receive additional appropriations to their salary and

---

[25] U.S. Office of Personnel Management, *Civil Service Retirement and Disability Fund, Report for the Fiscal Year Ended September 30, 2002* (Washington: GPO, 2003).

[26] This transfer of funds to the CSRDF from the Treasury is included in the federal budget in the account for OPM.

expense accounts.[27] Because agencies would transfer the appropriated funds to the CSRDF, which would in turn use them to purchase Treasury bonds, no additional outlays would occur as a result of these appropriations, and they would not effect the federal budget deficit or surplus. The outlays would occur in the future when retired employees collect their CSRS annuities, just as under current law.

An alternative means of fully financing the normal cost of the CSRS would be to require agencies to increase their contributions to the CSRDF *without* receiving any additional appropriations to their salary and expense accounts.[28] Pre-funding the full costs of the CSRS in this way would reduce the federal budget deficit (or increase the surplus), because the outlays of each agency would have to be cut by the amount of its additional transfers to the CSRDF. Outlays to CSRS annuitants would, of course, still occur in the future just as under current law. However, these future outlays would be *offset* by a reduction in current outlays so that the future payments to CSRS annuitants could be fully pre-funded. The reduction in resources available for current spending, however, could force some agencies to cut back on the services they provide to the public, or possibly to reduce the number of people they employ.

Paying the full normal cost of CSRS through employee and agency contributions would prevent the system from accruing additional unfunded liabilities, but it would not reduce the previously accumulated liability of the CSRS. Under current law, this liability will be paid off eventually through a series of 30-year amortization payments from the general fund of the Treasury to the CSRDF. Some observers favor starting these amortization payments sooner. They note that private-sector employers are required by ERISA to begin paying down accumulated liabilities soon after they occur. Others advocate paying down the liability now as a way to forestall proposals calling for reduced pension benefits or increased employee contributions in the future.

The *Budget of the United States* for FY1997 included a proposal to reduce previously accumulated CSRS liabilities through a series of amortization payments from the Treasury to the CSRDF.[29] In this proposal, which was not enacted by Congress, the three payments to the CSRDF required by P.L. 91-93 would be replaced with a single, slightly larger annual payment over a period of 40 years. The payment would have been classified by OMB as mandatory spending and therefore would not have required an increase in any limits placed on discretionary spending. The payments to the CSRDF would have been an "intra-governmental transfer" which would not have resulted in additional outlays and, therefore, would not have increased the government's budget deficit (or reduced the surplus). For the same reason, however, reducing the accumulated liability of the CSRDF would not reduce the government's future outlays for CSRS annuities.

---

[27] This was proposed in the *Budget of the United States, FY1996*, but was not enacted.

[28] This was proposed in the FY1997 *Budget of the United States*, but was not enacted by Congress.

[29] The accumulated CSRS liability also could be funded by payments from individual agency budgets. The allocation of fixed costs, however, is always somewhat arbitrary.

Conclusion. Congressional interest in the civil service retirement programs in recent years has tended to focus on the "under-funding" of retirement annuities in CSRS. Proposals to pre-fund CSRS in the same manner as required under FERS have foundered either on the question of whether additional budget authority should be granted to federal agencies, or whether they should make higher contributions from their current budget authority. Finding the means to accelerate paying off the accumulated liability under CSRS under current budget rules also has contributed to the difficulty in resolving the under-funded status of CSRS. Recently, however, another issue has been introduced into the debate: some observers have suggested that investing the civil service trust fund entirely in U.S. Treasury bonds does not represent true "pre-funding" because these bonds are merely a claim held by the government against its own future revenues. These critics suggest that at least part of the trust fund's assets should be invested in private-sector stocks and bonds where they could earn a higher rate of return than is available from U.S. Treasury securities (albeit at greater risk). In addition to issues of risk and investment policies, however, this proposal faces another significant obstacle in the budgetary "scoring" rules that would count the purchase of private sector assets as an outlay of federal funds, which would raise the budget deficit (or lower the budget surplus).

Many policymakers believe that greater pre-funding of CSRS retirement annuities would lead to improved accounting of personnel costs among federal agencies. There also appears to be some interest in the possibility of investing some of the assets of the Civil Service Retirement and Disability Fund in private-sector stocks and bonds. Obstacles to these proposed changes include differing political philosophies about the role of government in private financial markets, the effect of such changes on the budgetary resources of federal agencies and on the federal budget deficit or surplus, and the continued preference of some policymakers for financing federal employee retirement benefits on a pay-as-you-go basis. At present, there is no looming financial crisis facing either CSRS or FERS. According to the actuaries of the Office of Personnel Management, both programs will have sufficient budget authority to meet their obligations for the indefinite future. This will provide the Congress with adequate time to consider fully the benefits and drawbacks that could arise under various reform proposals.