



## CONGRESSIONAL BUDGET OFFICE COST ESTIMATE

February 19, 1999

### **H.R. 416** **Federal Retirement Coverage Corrections Act**

*As ordered reported by the House Committee on Ways and Means  
on February 11, 1999*

#### **SUMMARY**

H.R. 416 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.

CBO estimates that federal agencies would bear discretionary costs totaling \$346 million over the 2000-2004 period, primarily because the bill would increase the size of makeup contributions to the Thrift Savings Plan (TSP). The bill would also decrease direct spending by \$113 million; this drop in direct spending largely reflects makeup contributions to the Social Security trust funds, which are off-budget. The bill would not have a significant impact on federal retirement benefits during the next several years because the affected employees are generally still in the middle of their careers. Because the bill would affect direct spending and receipts, pay-as-you-go procedures would apply.

The bill would require the District of Columbia and Gallaudet University to correct instances where employees have been mistakenly enrolled in the wrong retirement system. This requirement represents 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. 416 is shown in the following table.

TABLE 1. ESTIMATED BUDGETARY EFFECTS OF H.R. 416

	By Fiscal Year, in Millions of Dollars									
	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009
<b>CHANGES IN SPENDING SUBJECT TO APPROPRIATION</b>										
Makeup Contributions to TSP	23	68	66	73	45	31	35	39	-6	-7
Makeup Payments to Social Security	a	1	1	1	1	1	1	1	-2	-2
Makeup Payments to the CSRDF	6	20	17	18	13	11	11	12	-8	-9
Agency Retirement Contributions	- a	- a	- a	-1	-1	-2	-2	-2	-2	-3
Employer TSP Contributions	- a	- a	-1	-1	-2	-2	-2	-2	-2	-3
Employer Social Security Contributions	<u>- a</u>	<u>a</u>	<u>a</u>	<u>1</u>	<u>1</u>	<u>1</u>	<u>1</u>	<u>1</u>	<u>1</u>	<u>1</u>
Total	29	88	83	90	56	40	45	50	-19	-23
<b>CHANGES IN DIRECT SPENDING</b>										
<u>On-Budget</u>										
Makeup Payments to the CSRDF	-9	-30	-25	-27	-19	-16	-17	-19	12	13
Agency Retirement Contributions	a	a	1	2	2	2	2	3	3	4
Transfers from CSRDF to Social Security	<u>10</u>	<u>31</u>	<u>27</u>	<u>28</u>	<u>21</u>	<u>18</u>	<u>19</u>	<u>21</u>	<u>-12</u>	<u>-13</u>
Subtotal	1	2	2	3	4	4	5	5	3	4
<u>Off-Budget</u>										
Makeup Payments to Social Security	- a	-2	-1	-1	-1	-1	-1	-1	3	3
Employer Social Security Contributions	a	- a	-1	-1	-1	-1	-2	-2	-2	-1
Transfers from CSRDF to Social Security	<u>-10</u>	<u>-31</u>	<u>-27</u>	<u>-28</u>	<u>-21</u>	<u>-18</u>	<u>-19</u>	<u>-21</u>	<u>12</u>	<u>13</u>
Subtotal	-10	-33	-28	-30	-23	-20	-22	-24	13	15
Total	-9	-31	-26	-27	-19	-16	-17	-19	16	19
<b>CHANGES IN REVENUES</b>										
<u>On-Budget</u>										
Employee Retirement Contributions	a	- a	-1	-1	-1	-1	-2	-2	-2	-1
<u>Off-Budget</u>										
Employee Social Security Taxes	- a	a	1	1	1	1	2	2	2	1
Total	a	a	a	a	a	a	a	a	a	a
<b>TOTAL COST OF H.R. 416</b>										
Direct Spending and Revenues	-9	-31	-26	-27	-19	-16	-18	-19	16	19
All Spending and Revenues	20	57	56	63	37	24	27	30	-4	-4

a. Less than \$500,000.

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

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

## **BASIS OF ESTIMATE**

H.R. 416 lays out procedures for correcting a wide variety of retirement coverage errors. CBO estimates that the bill would impose discretionary costs on agencies totaling \$346 million over the 2000-2004 period. In addition, the bill would increase on-budget direct spending by \$12 million over the same period. Off-budget direct spending would decrease by \$124 million, for a net decrease in direct spending of \$112 million. H.R. 416 would have little impact on net revenues; on-budget revenues would decrease by \$3 million, while off-budget revenues would increase by \$3 million. The estimate assumes that the Postal Service would increase postal rates to offset its own costs related to the bill. The estimate also assumes that the bill is enacted by October 1, 1999.

## **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 that does not include Social Security. Those hired after 1983 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) with government matching contributions. 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 a combination of 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 11,000 have already been corrected. The two most common types of coverage errors appear to involve employees who 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. 416 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. 416 would direct agencies to identify any retirement coverage errors and correct them by December 31, 2001, but would not impose any penalty on agencies that miss this deadline. CBO assumed that agencies would correct their errors at a 20 percent faster annual rate than under current law, but that some errors would remain undiscovered until 2009. Agencies would also stop correcting errors for the first six months of 2000 pending the issuance of final regulations to implement H.R. 416.

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. 416 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. CBO assumed that 80 percent of these employees would elect to remain in their current 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. 416 would change the way that makeup TSP contributions are calculated, and would apply to employees mistakenly covered by CSRS or CSRS Offset whose coverage is changed to FERS. Employees whose coverage was corrected to FERS prior to the bill's enactment would also be eligible. Under the bill, agencies would make a lump-sum payment to TSP representing past employee contributions as well as the 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 \$85,000 in 2000. Employees whose coverage errors were corrected to FERS in the past would receive smaller payments of about \$35,000. These amounts would be higher in later years due to additional foregone returns and contributions. CBO estimates that the additional cost of TSP makeup contributions would be \$275 million over the 2000-2004 period.

**Makeup Payments to Social Security.** Agencies are currently responsible for paying makeup Social Security payroll taxes covering the last 3 years, 3 months, and 15 days for

employees whose coverage is changed from CSRS to FERS or CSRS Offset. CBO estimates that these makeup payments would increase by \$4 million during the 2000-2004 period. This rise primarily reflects the impact that the bill would have on speeding up the correction of coverage errors.

**Makeup Payments to the Civil Service Retirement and Disability Fund (CSRDF).** Under H.R. 416, any necessary adjustments to past agency retirement contributions to the CSRDF would be completely retroactive, as under current law. Agencies would also have to reimburse the CSRDF for certain transfers from the CSRDF to the Social Security trust funds. As noted earlier, agencies are responsible for makeup Social Security payroll taxes covering the last 3 years, 3 months, and 15 days. If an employee was erroneously covered for a longer period of time, H.R. 416 would require the CSRDF to transfer to the Social Security trust funds an amount equal to the agency's payroll taxes for that additional period that should have gone to Social Security but went instead to the CSRDF. The agency would then be required to reimburse the CSRDF for the makeup employer taxes transferred to Social Security. CBO estimates that agency makeup payments to the CSRDF would increase by \$74 million between 2000 and 2004 under the bill.

**Agency Retirement Contributions.** The amount that agencies contribute towards their employees' retirement would decrease slightly because, relative to current law, the bill would shift some employees out of FERS into CSRS Offset, which requires lower agency retirement contributions.

**Employer TSP Contributions.** The additional employees who would shift out of FERS into CSRS Offset under H.R. 416 would no longer be eligible for the automatic and matching TSP contributions available under FERS, lowering agency spending on TSP contributions by \$4 million over the 2000-2004 period.

**Employer Social Security Contributions.** Employer contributions to Social Security would increase by \$2 million between 2000 and 2004 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 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 \$110 million between 2000 and 2004. The increase in receipts is larger than the increase in

agency makeup payments because the receipts figure includes payments by the Postal Service.

**Agency Retirement Contributions.** The increase in agency retirement contributions under the bill would decrease CSRDF receipts by \$5 million over the 2000-2004 period. The decrease in receipts is larger than the decrease in agency retirement contributions because the receipts figure includes payments by the Postal Service.

**Transfers from the Civil Service Trust Fund to Social Security.** Under H.R. 416, the CSRDF would make payments to the Social Security trust funds for certain back payroll taxes. CSRDF would be required to transfer amounts equal to any employee payroll taxes and employer payroll taxes beyond the current statute of limitations of 3 years, 3 months, and 15 days that should have gone to Social Security but instead went to the CSRDF. As noted above, agencies would reimburse the CSRDF for transfers of employer payroll taxes. CBO estimates that transfers from the CSRDF to the Social Security trust funds would total \$117 million over the 2000-2004 period. Although these transfers are intragovernmental, the payments would be on-budget, and the receipt of these funds by Social Security would be off-budget.

### **Effects on Direct Spending (Off-Budget)**

H.R. 416 would affect offsetting receipts to the Social Security trust funds in three ways. First, agency makeup payments would be slightly accelerated, increasing receipts by \$5 million between 2000 and 2004. Second, receipts from employer Social Security contributions would rise by \$3 million during this period. In both of these instances, the increase in receipts is larger than the increase in discretionary spending because the receipts figure includes payments by the Postal Service. Finally, transfers from the Civil Service trust fund for back taxes would increase receipts by \$117 million during the 2000-2004 period.

### **Effects on Revenues**

**Employee Retirement Contributions.** Because of the speeding up of retirement corrections, employee retirement contributions would decrease by \$3 million over the 2000-2004 period. Employees would be moved more rapidly out of CSRS, which requires 7 percent employee contributions, and into CSRS Offset or FERS, which both require 0.8 percent employee contributions.

**Employee Social Security Taxes.** By moving from CSRS to CSRS Offset or FERS, employees would also become covered by Social Security. The speeding up of retirement

corrections thus would increase receipts of employee Social Security taxes by \$3 million between 1999 and 2003.

## **PAY-AS-YOU-GO CONSIDERATIONS**

The provisions of H.R. 416 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 Table 2.

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TABLE 2. SUMMARY OF PAY-AS-YOU-GO EFFECTS

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	By Fiscal Year, in Millions of Dollars									
	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009
Change in outlays	1	2	2	3	4	4	5	5	3	4
Change in receipts	0	0	-1	-1	-1	-1	-2	-2	-2	-1

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## **INTERGOVERNMENTAL AND PRIVATE-SECTOR IMPACT**

H.R. 416 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**

An identical version of H.R. 416 was reported by the House Committee on Government Reform on February 3, 1999.

H.R. 416 is similar to H.R. 3249, which was approved by the House of Representatives in the 105th Congress. The only major difference between the two bills is that H.R. 3249 also included a provision authorizing an open season for federal employees covered by the Foreign Service Retirement and Disability System to switch into the newer Foreign Service Pension System.

CBO estimated that H.R. 3249 would impose discretionary costs on agencies totaling \$443 million and reduce direct spending by \$135 million over the 1999-2003 period. The main reason that the discretionary impact of H.R. 416 is lower than that for H.R. 3249 is that CBO lowered its estimate of the additional TSP makeup contributions that would be paid to employees whose coverage had already been corrected to FERS prior to the bill's enactment.

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