Congressional Research Service

Memorandum March 20, 2002

SUBJECT: **Federal Employee Retirement Funds and the Public Debt Limit**

FROM: Retirement and Income Security Section
Domestic Social Policy Division
Congressional Research Service

When the federal government's expenditures exceed its income from tax collections, the Treasury may borrow funds by selling bonds to the public. The Treasury also issues bonds that are held by federal trust funds, including the Civil Service Retirement and Disability Fund (CSRDF). All of the bonds issued by the Treasury, whether held by the public or by federal trust funds, comprise the public debt of the United States. The total amount of this debt can be no greater than the maximum that has been authorized in law by Congress. When the amount of outstanding debt approaches the statutory maximum, Congress must act either to reduce the public debt or to authorize an increase in the debt limit.

Congress last raised the public debt limit in 1997.[1] During fiscal years 1998 through 2001, the federal government's revenues exceeded its outlays, but the public debt continued to rise, mainly because of growing surpluses in the Social Security trust funds.[2] In February 2002, the Treasury announced that its cash requirements would cause the public debt to reach the currently authorized limit of $5.95 trillion by the end of March.[3] The Secretary of the Treasury has requested that Congress raise the public debt limit (also called the "debt ceiling") by $750 billion so that the Treasury will be able to borrow additional funds from the public. Without legal authority to issue new bonds, the government would have insufficient cash income to finance its normal day-to-day operations while continuing to make timely payments of interest and principal to holders of U.S. Treasury securities.

Statutory authority of the Secretary. In order to avert a shutdown of government operations whenever the national debt approaches the legally authorized maximum, Congress has granted to the Secretary of the Treasury the authority to take certain actions that allow the Treasury temporarily to continue borrowing cash from the public without increasing the public debt. The Secretary is authorized to take these actions, which effectively reduce the

[1] P.L. 105-33. The debt limit is defined in statute at 31 U.S.C. § 3101(b).

[2] Although the total debt rose, the debt held by the public declined from $3.8 trillion to $3.3 trillion.

[3] "Future of U.S. Leadership and U.S. Economy Require an Immediate Permanent Increase in the Debt Limit," Office of Public Affairs, United States Treasury, PO-1049, February 27, 2002.

obligations of the government that are counted toward the public debt ceiling, only during a "debt-issuance suspension period." This is defined in statute as any period for which the Secretary determines that issuing additional obligations of the United States would breach the public debt limit.[4] In these circumstances, the Secretary of the Treasury is authorized to

- suspend the investment of amounts in the Civil Service Retirement and Disability Fund that normally would be invested in interest-bearing Treasury securities;
- sell or redeem Treasury securities held by the CSRDF prior to maturity; and
- suspend the issuance of interest-bearing Treasury securities to the "G" fund of the Thrift Savings Plan.

Federal law requires the Secretary to reinvest these funds in interest-bearing Treasury securities when the debt-issuance suspension period has ended, and to credit both the CSRDF and the "G" fund with the interest that was foregone when the funds were invested in non-interest-bearing accounts. *Consequently, neither the Civil Service Retirement and Disability Fund nor the "G" fund of the TSP can suffer any reduction in assets or loss of interest income as a result of the actions taken by the Secretary of the Treasury under the authority of sections 8348 and 8438 of title 5, United States Code.*

The Civil Service Retirement and Disability Fund. The Civil Service Retirement and Disability Fund is a federal trust fund established under the authority of 5 U.S.C. § 8348 to finance benefit payments under the Civil Service Retirement System (CSRS) and the basic retirement annuity of the Federal Employees' Retirement System (FERS). The fund holds mainly nonmarketable, interest-bearing securities issued by the U.S. Treasury. The bonds held by the CSRDF are part of the national debt, and count toward the total public debt limit authorized by Congress. The Treasury bonds held by the CSRDF represent *budget authority* that can be used to pay pension benefits under CSRS and FERS. These bonds represent an obligation of the Treasury to the Civil Service Trust Fund that the CSRDF can redeem, as necessary, to make annuity payments to retired federal employees and their surviving dependents. When the CSRDF redeems the bonds, the Treasury makes the required outlays to retirees and survivors who have earned benefits under CSRS and FERS. The Treasury makes these outlays from its general revenues in the year the outlays occur.

At the end of fiscal year 2001, the Civil Service Retirement and Disability Fund had a balance of $538.5 billion. During FY2002, the fund will take in an estimated $80 billion in cash receipts and intragovernmental transfers and it will disburse an estimated $50 billion in retirement and disability benefits. Thus, the fund's income will exceed its expenditures, and by the end of FY2002, the balance of the CSRDF will have increased to approximately $568 billion.[5] Most of the income of the CSRDF (approximately 94% in 2002) is received as *intragovernmental transfers* representing agencies' contributions toward their employees' retirement benefits under CSRS and FERS, interest on bonds held by the fund, and transfers from the general revenues of the Treasury. The remainder of the fund's income (6% in 2002) is cash, representing mainly payroll deductions from federal employees.

Suspension of additional investments. The income of the CSRDF is invested in interest-bearing securities issued by the Treasury, which are counted against the public debt limit. Under the authority of 5 U.S.C. § 8348(j), the Secretary of the Treasury "may suspend

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[4] See 5 U.S.C. §8348(j)(5)(B) and 5 U.S.C. §8438(g)(6)(B).

[5] Figures are from the *Budget of the United States Government, Fiscal Year 2003*.

additional investment of amounts in the Fund if such additional investment could not be made without causing the public debt of the United States to exceed the public debt limit."[6] In such cases, the income of the fund is temporarily credited to non-interest-bearing accounts in the Treasury. Because only interest-bearing accounts are counted against the debt limit, crediting income of the CSRDF to non-interest-bearing accounts temporarily prevents the public debt from increasing by the amount of the credit. The law requires the Secretary to reinvest these funds in interest-bearing securities "as soon as such investments can be made without exceeding the public debt limit," and to credit the fund with the amount of interest that would have been credited if the fund had remained invested in interest-bearing securities during the debt-issuance suspension period.

Early redemption of investments. Section 8348(k) of title 5 permits the Secretary of the Treasury to "sell or redeem securities, obligations, or other invested assets of the Fund before maturity in order to prevent the public debt of the United States from exceeding the public debt limit," but only in an amount equal to the benefit payments from the fund during the debt-issuance suspension period.[7] The Treasury can then borrow from the public an amount equal to the funds that have been moved into non-interest-bearing accounts. The law does not require the cash generated by the sale or redemption of these securities to be used to make benefit payments under CSRS or FERS, but it limits the amount of the sale or redemption to no more than the amount of benefits that are expected to be paid during the debt-issuance suspension period.[8] Both the diversion of trust fund income to non-interest-bearing accounts and the early redemption of securities allow the Secretary to "make room" under the debt ceiling by temporarily placing funds from the CSRDF in accounts at the Treasury that do not count toward the debt limit.

The Thrift Savings Fund. The Thrift Savings Fund is *not* a federal trust fund. Like employer-sponsored "401(k)" plans in the private sector, the Thrift Savings Plan (TSP) consists of individual accounts that are owned by the employees and former employees who participate in the plan.[9] Employees' contributions to the TSP and contributions made by their employing agencies are credited to a deposit fund in the Treasury. From this Treasury account, the monies are deposited in one of five investment options, as elected by the employee. Only one of these funds – the "G" fund – is invested in interest-bearing Treasury securities that comprise part of the public debt. Because the individual employees and retirees who participate in the TSP own their account balances, including the amounts that they have elected to invest in Treasury securities through the "G" fund, TSP participants have the same property rights in these accounts as do any other holders of U.S. Treasury bonds. The other TSP investment funds are:

- the "F" fund, consisting of bonds issued by businesses in the private sector;
- the "C" fund, comprising the stock of corporations represented in the Standard & Poor's 500 Index;
- The "S" fund, which invests in stocks of small and medium-sized corporations represented in the Wilshire 4500 index; and,

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[6] This section was added to title 5 by P.L. 99-509 (October 21, 1986).

[7] This section was added to title 5 by P.L. 99-509 (October 21, 1986).

[8] Because money is fungible – one dollar is a perfect substitute for another – such a restriction on the specific use of funds derived from the CSRDF would have little or no effect in practice .

[9] The term "401(k)" refers to the section of the Internal Revenue Code that authorizes these plans.

- The "I" fund, which invests in foreign corporations represented in Morgan Stanley Capital International's EAFE Index of firms in Europe, Australia, and the Far East.

As of September 30, 2001, the Thrift Savings Fund held assets totaling $93.3 billion. Of this total, $45.3 billion (48.6%) was invested in the "C" fund; $39.2 billion (42.0%) was invested in the "G" fund; $8.0 billion (8.6%) was invested in the "F" fund; $0.6 billion was invested in the "S" fund; and $0.2 billion was invested in the "I" fund.

The Secretary cannot sell or redeem Treasury bonds held by TSP participants, but he or she may, under the authority of 5 U.S.C. § 8438(g), "suspend the issuance of additional amounts of obligations of the United States, if such issuance could not be made without causing the public debt of the United States to exceed the public debt limit."[10] The "G" fund matures and is reinvested daily. During a debt-issuance suspension period, rather than reinvesting the full balance of the "G" fund, the Secretary can credit some or all of the balance of the fund to non-interest-bearing accounts in the Treasury. These non-interest-bearing accounts do not count against the public debt limit. The law requires the Secretary to move these funds back into interest-bearing Treasury securities as soon as the securities can be issued without exceeding the public debt limit. The accounts of the "G" fund must also at that time be credited with the interest that would have been credited during the debt-issuance suspension period. Consequently, no one who has invested TSP contributions in the "G" fund can suffer any reduction in assets or loss of interest income as a result of the actions taken by the Secretary of the Treasury under the authority of section 8438 of title 5.

Previous actions by the Secretary under 5 U.S.C. § 8348 and § 8438. The Secretary last used the authority granted under sections 8348 and 8438 of title 5 from November 1995 through March 1996. In November 1995, the Secretary of the Treasury announced that issuance of further debt obligations of the U.S. government would result in the public debt exceeding the statutory limit. Over the next four months – until Congress acted to raise the public debt limit – the Secretary redeemed approximately $46 billion of Treasury securities held by the CSRDF prior to maturity, suspended investment of about $14 billion in income of the CSRDF, and periodically credited up to $18 billion in TSP "G" fund securities to non-interest-bearing accounts. The Treasury subsequently reinvested all of these amounts in Treasury securities and credited the funds with the interest earnings that would have been credited if the funds had been fully invested in interest-bearing Treasury securities at all times. According to the General Accounting Office, the Secretary's actions were "in accordance with statutory authority" provided by the Congress.[11] Both funds were made whole, as required by law, and neither the CSRDF nor individual investors in the "G" fund of the TSP suffered any financial losses, delays in payment of monies owed to them, or restrictions on account activity during the debt-issuance suspension period.

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[10] This language was added to title 5 by P.L. 100-43 (May 22, 1987).

[11] *Debt Ceiling: Analysis of Actions During the 1995-1996 Crisis*, AIMD-96-130, U.S. General Accounting Office, Washington, DC, August 1996.