

Statement of the Board of Actuaries of the Civil Service Retirement System

This report from the Board of Actuaries (Board) is intended to accompany the September 30, 2016 actuarial valuations included in the Civil Service Retirement and Disability Fund (CSRDF) Annual Report produced by the Office of the Actuaries (OA) of the U.S. Office of Personnel Management (OPM).

BACKGROUND

The Civil Service Retirement System (CSRS) and the Federal Employees Retirement System (FERS) provide defined-benefit retirement, disability and survivor protection to millions of non-military federal employees, retirees and beneficiaries. CSRS is a closed plan that generally covers employees hired prior to 1984, and FERS covers employees hired thereafter.

In the Board's opinion, the systems deliver consistent, predictable income with pooled longevity risk and are, from an actuarial perspective, an effective and appropriate way to provide retirement security to the federal government workforce.

Statutory authority for the Board of Actuaries dates back nearly 100 years. Initially, the Board had direct, hands-on involvement in conducting actuarial valuations of the system. Today, actuarial valuations of the system are conducted by the OA. The Board meets annually to establish the key actuarial assumptions used by the OA and provide guidance on other actuarial issues. The Board's work is done with the support and input from the OA.

The actuarial valuation reflected in the CSRDF Annual Report is intended to estimate the full cost of the system and to allocate the cost over time. The results of the valuation may be used to understand the size of the obligation ultimately borne by U.S. taxpayers.

ACTUARIAL ALLOCATION OF CONTRIBUTIONS

The CSRS and FERS system is funded by contributions from employees and from participating federal agencies plus the Treasury. For FERS, the total annual contributions to the system are intended to cover the actuarially determined normal cost¹ plus a provision to amortize unfunded liabilities. FERS unfunded liabilities are amortized over 30 years while payments for CSRS do not target funding of the full liability over any specific period. In aggregate, these approaches are designed to spread costs smoothly over time. Contributions in excess of the total amount needed to cover benefit payments are held in special-issue U.S. Treasury securities². Annual contributions are required from participating federal agencies using a payroll-based allocation methodology.

¹ Normal cost is the cost of the plan benefits accrued to employees in a single year, as allocated by the actuarial method, without regard to any surplus or deficit in the system.

² Government Account Series securities cannot be traded on public markets.

Annual Contributions to the CSRDF

	Dollars in Billions*	
	10/1/2015 – 9/30/2016	10/1/2014 – 9/30/2015
CSRS	\$34.8	\$35.2
FERS **	\$34.7	\$33.0
Total	\$69.5	\$68.2

*numbers rounded for additive purposes

** totals include amortization payment amounts receivable from the U.S. Postal Service

FINANCIAL OBLIGATION OF U.S. TAXPAYERS

The U.S. taxpayer ultimately pays the cost of the system's promised pension benefits, net of employee contributions. The payment of the pension benefits to beneficiaries is a cash demand that follows a different pattern than the aggregate annual contributions. Much of the cash demand is fulfilled by income and maturing securities from the CSRDF. However, because the CSRDF holds only Treasury securities, the full amount of benefit payments and expenses requires a cash outlay by the government. The actuarial report prepared by the OA includes a projection of benefit payments for the next 75 years, providing an estimate of how this demand on U.S. taxpayers will evolve.

Annual Payments for Beneficiaries

	Dollars in Billions*	
	10/1/2015 – 9/30/2016	10/1/2014 – 9/30/2015
CSRS	\$69.8	\$70.4
FERS	\$12.7	\$11.3
Total	\$82.5	\$81.7

Annual Payments for Beneficiaries, Less Employee Contributions

	Dollars in Billions*	
	10/1/2015 – 9/30/2016	10/1/2014 – 9/30/2015
CSRS	\$69.2	\$69.1
FERS	\$10.1	\$ 9.1
Total	\$79.3	\$78.2

*numbers rounded for additive purposes

PRESENT VALUE OF OBLIGATION

The total value of the system costs accrued to date is referred to as the actuarial liability. The actuarial liability represents the governmental obligation to pay the future CSRS and FERS benefits that have accrued for current plan participants, measured at present value according to

the actuarial methodology and assumptions recommended by the Board and the OA in accordance with statute and regulations.

Actuarial Liability

	Dollars in Billions	
	9/30/2016	9/30/2015
CSRS	\$1,084.2	\$1,056.4
FERS	\$ 715.7	\$ 606.5
Total	\$1,799.9	\$1,662.9

CURRENT ISSUES

The Board looks at some issues every year and takes up other issues when appropriate. The issues under current consideration are described below.

System financing

Significant unfunded actuarial liabilities exist for previously accrued costs under the closed CSRS plan. The current statutory contribution provisions do not target paying off these legacy CSRS unfunded liabilities over a specific period. Because both the funded and unfunded liabilities are obligations of the federal government, the Board is not concerned that benefit security for participants is impacted by this approach.

There are other policy considerations, that the Board does not opine on, with regard to the appropriate allocation of costs over time. These include:

- Are federal agency budgets being appropriately charged for amortization costs?
- Is there an appropriate balance between explicit federal debt (the U.S. Treasury securities held in the CSRDF) and implicit federal debt (the system’s unfunded liability which is not yet denominated as U.S. Treasury debt) to be achieved?

Economic assumptions

Some of the actuarial assumptions upon which the OA valuations are based are considered economic assumptions. Plan costs allocated to federal agencies are highly dependent on the economic assumptions, as is the estimated value of the taxpayers’ obligation. One key assumption is the interest rate used to discount projected future cash flows.

The economic assumptions are reviewed annually by the Board. The interest assumption is based on a judgment associated with the expected “rate of return” on U.S. Treasury securities both now and in the future. The Board reduced the interest rate assumption to 4.50% from 5.25% beginning with this actuarial valuation as of September 30, 2016. This reflects a reduction in both the assumed overall rate of inflation from 3.00% to 2.50% and the assumed real rate of return on Treasury securities from 2.25% to 2.00%. Additional changes were made to lower the assumption for future cost-of-living adjustments for FERS annuitants and the general salary increase assumption. The Board is continuing to consider its approach for determining the

economic assumptions in light of the current economic environment with historically low interest and inflation rates.

Demographic assumptions

This actuarial valuation as of September 30, 2016 incorporates revised demographic assumptions which reflect the results of an experience study completed by the staff at the OA in 2017. The Board reviewed the results of the study and approved the system-wide assumptions produced by the OA.

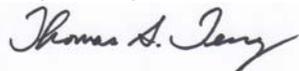
Contribution allocations for the U.S. Postal Service (USPS)

As noted above, actuarial assumptions used in the development of federal agency contributions have historically been based on actuarial valuations using the same assumptions for all agencies. The USPS has formally questioned whether this approach is appropriate going forward for FERS given their contention that there are non-trivial differences in demographic experience (e.g. salary increases and rates of retirement) between the USPS and the other federal agencies. The Board has considered the USPS requests and recommended that OPM explore amending its regulatory provisions, and OPM published revised regulations in October 2017. The Board will carefully review these new regulations and will provide guidance to OPM with regard to any potential changes in assumptions used in the annual actuarial valuation.

Borrowing from the pension trust

The Board is aware that the CSRS and FERS trust fund securities are, from time to time, used to finance U.S. Government activities that would otherwise have to be curtailed due to the imposition of statutory limits on explicit debt. Each time this has happened in the past, the fund has been made whole after the debt ceiling has been raised. The Board feels strongly that the retirement system trust fund should be made whole as soon as practical after these events in order to avoid confusion about the financial status of the system.

Respectfully submitted,



Thomas S. Terry
Chairperson, Board of Actuaries
April 2, 2018