SUMMARY

In 1972, the Congress enacted the military Survivor Benefit Plan (SBP), a voluntary program for military retirees. Those who elect to cover some or all of their retirement pay under the SBP contribute in the form of a reduction in that pay. In return, their survivors receive lifetime benefits that are adjusted for future increases in the Consumer Price Index (CPI).

Inequities that developed since enactment of the SBP in 1972 caused some retirees to contribute substantially more than their survivors will receive in benefits. Prompted by these inequities, the Congress in 1980 enacted major changes in the SBP, focusing on limits both on the so-called social security offset and on the amount withheld from retirement pay in return for survivor coverage.

This study analyzes the inequities that prompted the changes and examines legislation passed by the Congress to correct them. The study documents analyses presented to the Congress during its debate over the changes.

INEQUITIES IN THE PREVIOUS LAW

Social Security Offsets

Under the law in effect before the recent Congressional changes, most survivors' benefits were reduced by the full amount of any social security benefits they received based on their spouses' earnings during military service. The size of these social security offsets had grown sharply in recent years largely because recent military retirees, who were first covered under social security in 1957, had spent larger portions of their careers under the system. Offsets would have continued to grow, particularly for survivors of officer retirees, mainly because of recent increases in maximum wages subject to social security coverage. As a result of these and other shifts, social security offsets would have completely eliminated benefits for many survivors in future years.

Contribution Formula

Participants in the SBP contribute based on a formula that increases costs per dollar of survivor coverage as retirement pay increases. The "weighted" formula requires that retirees contribute 2.5 percent of their first $300 per month of covered retirement pay and 10 percent of any amount above $300. Under the law in effect before the Congressional changes, each increase in military retirement pay because of growth in the CPI triggered a recalculation of SBP contributions. This recalculation pushed more pay into the 10-percent bracket of the formula and increased the cost per dollar of coverage. Sharp increases in the CPI have already pushed up the costs of coverage over 1972 levels, and costs would have continued to grow in future years. In contrast, the contribution formula for the survivor benefit plan for civil service retirees results in constant costs per dollar of coverage.

Other Inequities

Other possible inequities in the previous law included problems of offsets for widows who are entitled to social security based on their own earnings, offsets for certain part-time reservists, exclusion from the SBP of widows whose spouses died before enactment of the program in 1972, and participation by some disability retirees who would never have received benefits.

Results of Key Inequities

The growing social security offsets, coupled with problems in the contribution formula, meant that, under previous law, military retirees would have contributed considerably more than their survivors would receive in benefits. CBO estimates that an average nondisabled person who retired in 1981 would have contributed three times more than his survivor would receive. By the year 2000, an average retiree would have contributed almost four times more than his survivor would receive. These results are highly sensitive to many detailed assumptions and should be regarded as rough guides. Nonetheless, they suggest that individuals would clearly bear more of the costs than was intended. A Senate committee indicated when it passed the SBP in 1972 that, depending on when they retired, military personnel would bear about 60 percent to 80 percent of the costs of their survivors' benefits.

SENATE ALTERNATIVE (S. 91)

On September 22, 1980, the Congress approved an alternative SBP bill (S. 91) that corrected many of these inequities. S. 91 revises the military contribution formula to conform to the civil service formula and limits the social security offset to no more than 40 percent of survivor benefits. It also makes several other, more minor changes.

The two major changes outlined above mean that an average nondisabled retiree who leaves the military in 1981 will bear about 70 percent of the cost of his survivor's benefits. This is similar to what the Senate envisioned when it passed the SBP in 1972. While reducing costs to the individual, S. 91 will increase the government's costs. The additional costs will amount to about $280 million over the next five years and about $2.6 billion over the next 20 years. (All costs are in constant 1980 dollars.)

ALTERNATIVE PROVISIONS

Before approving S. 91, the Congress considered numerous alternative plans that are analyzed in this study and its appendixes. Included in these alternatives are key provisions that could be debated if further revisions of the SBP are considered.

Open Enrollment

Given the major changes made by S. 91, the Congress could allow those who chose not to participate in the SBP a chance to reconsider and join. Such an "open enrollment" provision could decrease costs over the next five years by a total of $200 million because of the added contributions by those who would elect to join. But costs over the next 20 years would increase by a total of $480 million as survivors of new participants began receiving benefits. The difficulty of estimating the number of new participants under an open enrollment provision makes these cost estimates more uncertain than others in this study.

Indexing

The contribution to SBP on the first $300 of covered retirement pay equals 2.5 percent; the contribution equals 10 percent on amounts above $300. The $300 threshold is fixed in the law and

was not changed by S. 91. This means that, as retirement pay for future retirees increases because of higher military pay, larger and larger portions of retirement pay are included in the 10 percent portion of the formula, which increases costs to participants. Progressive increases in costs could be avoided by "indexing" the $300, which would mean increasing it each time military pay was increased and by the same amount. This would stabilize at today's levels the portion of costs borne by future retirees. Indexing would add a total of $15 million to costs over the next five years and $530 million over the next 20 years.

Halving the Social Security Offset

This provision, included in an earlier version of S. 91, would halve the social security offset for widows age 62 or older rather than limiting it to no more than 40 percent of total survivor benefits. Cutting the offset in half would be consistent with current provisions regarding social security contributions, which require that individuals pay half the total contribution. Halving the offset would tend to benefit those who retired some years ago, particularly officer retirees, more than did S. 91. Halving the offset, rather than the 40 percent limit enacted by S. 91, would add about $60 million to costs over the next five years and $980 million over the next 20 years.

Eliminating the Mothers' Offset

Under previous law, widows under age 62 receive a social security offset only if they are mothers with one dependent child. (Mothers under age 62 who have more than one dependent child are exempt from any offset, apparently on equity grounds, while young widows who have no children are not eligible for social security and so have no offset.) Under S. 91, the offset for mothers under age 62 who have one dependent child is limited to no more than 40 percent of benefits, as are other offsets. Eliminating this mothers' offset altogether, which was proposed in an earlier version of S. 91, would add $40 million over the next five years and a total of $150 million over the next 20 years.

CHAPTER I. INTRODUCTION

In 1980, the Congress enacted major changes in the military Survivor Benefit Plan (SBP). The Congressional action came after numerous alternatives were proposed and supported by Members of the House and Senate, the Administration, and associations of military retirees and widows. Many of the proposed changes were motivated by inequities in the Survivor Benefit Plan that caused those retiring today to pay substantially more into the plan than their survivors would receive in benefits.

The Congressional Budget Office (CBO) assisted the Congress in considering numerous alternatives to the SBP. CBO calculated changes in outlays under these alternatives as well as the effects of the alternatives on the portion of costs borne by individuals through their contributions to the program. The results of these analyses were presented informally to the Congress during its debate. This study briefly documents these analyses. It begins with a description of the problems in the system in effect before the Congressional changes. Then the study examines the alternative adopted by the Congress. Finally, it briefly examines the numerous other alternatives developed by the Senate Committee on Armed Services and its staff, as well as those developed by House staff members and other groups.

Appendix A of this study contains some of the briefing charts that were presented to the committee staffs during debate over the changes. These provide detail on the costs of the various alternatives and on the fractions of program costs that would be paid by the government and by SBP participants. Appendix B contains a technical description of the methods and data used by CBO to estimate the outlays and cost-sharing ratios.

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CHAPTER II. THE PREVIOUS SURVIVOR BENEFIT PLAN

DESCRIPTION

In September 1972, the Congress established the military Survivor Benefit Plan (SBP). Under this plan, military retirees receive a reduced military pension in return for the guarantee of benefits to their survivors. The retiree can elect whether to participate in the SBP and how much of his retirement pay to "cover" under the plan (subject to a minimum coverage of $300 a month). The election, once made, is irrevocable.

Those who elect coverage contribute 2.5 percent of the first $300 of covered retirement pay plus 10 percent of any amount in excess of $300 a month. The contribution is the same for all types of retirees (nondisability and disability, reserve and active) and usually does not vary with the age of either the retiree or his potential survivor. Under the plan in effect before the recent Congressional changes, the contribution was recalculated each time military retirement pay was adjusted for increases in the Consumer Price Index (CPI).

When the retiree dies, his survivor receives--for the remainder of his or her life--55 percent of the retiree's covered retirement pay as an annuity, less certain social security offsets. The annuity and the offsets are indexed to the CPI. Under the previous plan, social security offsets for those age 62 or older equaled 100 percent of the social security payments based solely on the retiree's military earnings. For survivors under age 62, the offset was required only if the survivor had exactly one dependent child.

The SBP is a complex program with numerous other provisions. These govern coverage of persons other than spouses (this study treats only spouse-coverage provisions); effects of death of spouse, divorce, and remarriage; effects on the offset of reductions in social security; and a host of other provisions. 1/

1/ For more details, see U.S. Department of Defense, Study of the Survivor Benefit Plan for Members of the Uniformed Services (February 1, 1979), Chapter 1. This study includes a history of military survivor benefit programs.

PROBLEMS UNDER THE PREVIOUS LAW

Most of the provisions described above are basic to the SBP and were not changed by the Congress. But several features of the SBP were widely regarded as serious inequities. One had to do with the nature of the contribution. Whenever retirement pay increased, contributions were recalculated. Because the contribution formula was "weighted"--that is, retirees paid 10 percent on covered retirement pay in excess of $300 a month but only 2.5 percent on the first $300--the recalculation resulted in increasing costs per dollar of coverage for most retirees. For example, an enlisted retiree might have covered $400 a month of his retirement pay in 1980. He would then have contributed $17.50 a month toward the program, or about eight cents a month for each dollar of monthly annuity his survivor would eventually receive. (This calculation ignores the social security offsets, which are discussed below.) Ten years from now, if inflation continued at an average of only 6 percent a year, that same retiree would have been contributing about $49 a month, or over 12 cents a month for each dollar of monthly annuity his survivor would eventually receive. This increase in costs per dollar of coverage was viewed as inequitable because it drove up costs of coverage and because the increase, which was tied to future inflation, was difficult to predict when an individual elected coverage. This feature of the previous military SBP also differed from the civil service survivor benefit plan. That plan calculates the contribution at the time the civil servant retires, using the same basic formula as the military. But civil service contributions are then simply increased as the CPI increases, rather than being recalculated.

Another possible inequity was the size and nature of the social security offsets. These offsets were based solely on earnings while in the military. Since the military did not come under the social security system until 1957, the offsets under previous law were substantial but not confiscatory for those who retired in the 1960s and later joined the SBP. For a typical person with 20 years of service who retired in 1965, joined the SBP in 1972, and covered the full amount of his retirement pay, the offset for a survivor eligible for social security at age 62 equaled 65 percent for an enlisted retiree's survivor and about 30 percent for the survivor of an officer retiree (see Table 1). But the offsets grew sharply as retirees spent more time under social security. By 1980, the percentages equaled 100 percent--the entire annuity--for the enlisted retirees with 20 years of service and about 60 percent for 20-year officer retirees. By 1990, the percentages for 20-year enlisted and officer retirees would have been about 100 and 80 percent, respectively.

TABLE 1. EFFECTS OF THE SOCIAL SECURITY OFFSET UNDER PREVIOUS LAW

Year of Retirement	Paygrade at Retirement	Years of Service at Retirement	Percentage Reduction in SBP Annuity a/	
			100 Percent of Covered Pay	Minimum Coverage
1965	E-7	20	65	62
	E-9	30	28	60
	O-5	20	31	64
	O-6	30	16	66
1980	E-7	20	100	100
	E-9	30	58	100
	O-5	20	61	100
	O-6	30	33	100
1990	E-7	20	100	100
	E-9	30	66	100
	O-5	20	79	100
	O-6	30	46	100

a/ The offsets assume that the spouse is eligible for social security at age 62 (that is, they equal 82.9 percent of the principal insurance amount attributable to military service). The offsets also assume wage and price growth continuing at 6 percent and 5 percent a year, respectively, until the retiree reaches age 62.

The amount of the offset under previous law also varied widely by officer/enlisted status and by years of service at retirement. As the numbers in Table 1 suggest, the percentage reduction was larger for enlisted retirees than for officers, and for those who retired after 20 rather than 30 years of service. This occurred because the "weighted" nature of the social security formula provided a smaller percentage of benefits, and hence smaller offsets, to those with higher incomes. Officers and senior retirees, who have higher incomes, receive a smaller portion of their income as social security and hence as an offset.

Also, the percentage reduction caused by the offset depended heavily on the amount of retirement pay that was covered. Since the offset under previous law was independent of the percentage of covered pay, those who covered the minimum allowable amount ($300 a month) received a larger percentage reduction--which usually amounted to 100 percent--than those who covered more of their retirement pay.

Nor were the social security offsets easy for the individual to predict when he made an irrevocable decision about whether to participate in the SBP. Most retirees leave the military at ages 40 to 45. But the offsets were not calculated for most persons until at least 20 years later, when the retiree reached age 62. In the interim, the Congress could change the social security law. Also, given the current social security law, offsets were tied partly to the economic changes, such as wage growth, that would occur over this long span of years.

The social security offsets and the contribution formula, while the major problems under previous law, were not the only possible inequities. Persons whose spouses died before 1972, and therefore did not have a chance to participate in the SBP, argued that they should receive added benefits. SBP recipients whose social security was based on their own earnings argued that an offset based on their spouses' earnings was unfair. Part-time reserve personnel who retired and elected SBP coverage argued that their social security offsets were too high because in some cases their pay during part-time military reserve service, when combined with their earnings in full-time civilian jobs, exceeded the maximum income creditable for social security purposes; thus their reserve earnings did not count toward social security benefits but did count toward the offset. Finally, SBP benefits for certain survivors of disabled retirees were reduced by the benefits they could receive from other government programs. This could completely eliminate their SBP benefits. Such persons have argued that they should be able to opt out of the SBP once their disability status is final.

COST SHARING UNDER THE PREVIOUS LAW

Findings

The importance of the problems discussed above are illustrated by estimates of the fraction of the cost of SBP benefits paid by the individual under the previous law. The fractions are

good overall indications of the equity of the program because they reflect not only the provisions of the previous law but also the anticipated mortality of retirees and their survivors, expected economic conditions, economic "discount" rates that indicate preference for benefits now rather than later, and other factors. (See Appendix B for a description of the methods and assumptions used in calculating the fractions.) While the Congress has not recently stated the fraction of the costs it desires to be borne by the individual, the Senate committee report accompanying the 1972 legislation indicated that a person would pay about 60 percent to 80 percent of the cost of his survivor's benefits, depending on when he retired. That same report estimated that civil service retirees who elected their survivor coverage would pay about 60 percent of the total cost. 2/

Table 2 shows the fraction of the cost of benefits paid by the individual under the previous law, assuming the individual covered an amount of his retirement pay similar to the average amount covered by recent SBP participants. The table suggests that the average nondisabled retiree who retired in 1965, and then elected SBP in 1972 when it became available, would have paid about 110 percent of the costs of his survivor's benefits. Thus, the individual contributed slightly more than the cost of the benefits.

One reason for these high cost-sharing ratios under previous law is that social security offsets largely eliminated survivor benefits for widows over age 62 whose spouses were enlisted personnel. The Senate report in 1972 correctly predicted this effect. 3/ But there are several reasons not anticipated by the report that caused the percentage of costs paid by the individual to be much higher than the 60 percent to 80 percent estimated by the report. One is that the estimates made in the Senate report assumed no future increases in wages or prices. 4/ Price changes, coupled with the contribution formula for the military SBP, have

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2/ Survivor Benefit Plan, S. Rept. 1089, 92:2 (September 6, 1972), pp. 43-45, Tables 15-17. These tables exclude the effects of social security contributions and benefits, which is appropriate for this comparision.

3/ Ibid., p. 44.

4/ Ibid., notes to Tables 14 and 15, pp. 42-43.

pushed up the cost per dollar of coverage under previous law and would have continued to do so. Also, the Congress changed the social security system in 1977. The new method of calculating the social security offsets could have increased the offsets for some personnel, thus cutting down on their benefits and increasing the fraction of costs that they paid. Finally, increases in expected retiree lifespans, which increase contributions while reducing the years during which survivors would receive benefits, may have increased the percentage of costs borne by the individual.

Under previous law, the average retiree in 1965 paid 110 percent of the cost of his survivor's benefits. But Table 2 shows that the average officer retiree paid only about 70 percent of the total cost and so received a subsidy; the average enlisted retiree paid about 120 percent of the total cost. The difference between officer and enlisted retirees reflects the relatively larger impact of the social security offsets on enlisted personnel, as discussed above.

Table 2 also shows that the fractions paid by the individual under previous law would have grown rapidly over time. By 1981, the average retiree would have been paying three times the cost of the benefits his survivors would receive, and the retiree in the year 2000 would have paid almost four times the cost. The rapid growth was due largely to the increasing size of the social security offset as a percentage of SBP benefits. Table 2 does indicate one interesting shift that would have occurred between now and the year 2000. In 1981, officers would have been slightly better off relative to enlisted personnel; but the reverse would have been true by the year 2000. This is because social security offsets for officer personnel will grow rapidly over the next two decades as a result of the increase enacted in 1977 in maximum wages subject to social security taxes. These increases will push up offsets for officers, more of whose pay will be subject to social security in the future, but will not affect enlisted persons, whose pay is already fully covered.

Table 2 provides the major results of CBO's cost-sharing analysis. But two further results are shown in Tables A-7 and A-8 in Appendix A, which give the fractions by paygrades and years of service and give the fractions for maximum amount of covered retirement pay as well as average coverage. First, the previous law was a much better program for those who retired with more than 20 years of service. An average enlisted retiree in 1965 with 20 years of service would have paid about 160 percent of the cost of his survivor's benefits, while one with 30 years of service would

TABLE 2. COSTS OF SBP ALTERNATIVES AND PORTIONS OF COSTS BORNE BY THE INDIVIDUAL

Alternative	Added Costs Above Those Under the Previous Law (millions of constant 1980 dollars with inflated dollars in parentheses) 1981-1985	1981-2000		Fraction of Cost Paid by Nondisability Retiree Who Covers Typical Amount of Retired Pay 1965 retiree	1981 retiree	2000 retiree
Previous Law	--	--	Officer	0.74	2.94	4.62
			Enlisted	1.23	3.21	3.68
			Force-wide	1.10	3.14	3.93
Congressional Changes (S. 91)	280	2,600	Officer	0.64	0.88	1.04
	(380)	(5,950)	Enlisted	0.43	0.64	0.95
			Force-wide	0.49	0.70	0.97
Fleet Reserve Association (FRA)	200	2,830	Officer	0.64	0.84	0.84
	(280)	(6,680)	Enlisted	0.43	0.56	0.56
			Force-wide	0.49	0.64	0.64
Original S. 91	690	5,890	Officer	0.52	0.89	1.20
	(950)	(13,360)	Enlisted	0.43	0.94	1.33
			Force-wide	0.44	0.93	1.29
Retired Officers Association (TROA)	680	6,650	Officer	0.34	0.56	0.66
	(890)	(15,260)	Enlisted	0.38	0.54	0.67
			Force-wide	0.37	0.54	0.67
No Contribution Age 62 or Over	490	3,320	Officer	0.40	1.83	3.18
	(650)	(7,120)	Enlisted	0.70	1.89	2.77
			Force-wide	0.62	1.87	2.88

have paid only 50 percent of the cost. Similar trends hold for officer personnel. The trends reflected the smaller proportion of SBP benefits consumed by the social security offsets for more senior retirees. Second, covering a larger percentage of one's retirement pay generally reduced the fraction of the costs paid by the individual. For example, an average retiree who retired in 1965 and covered an average percentage of his pay contributed three times the amount of benefits that his survivor would receive; a retiree who covered all his pay contributed about 2.5 times his expected future benefits. This difference reflected the smaller percentage of benefits consumed by social security offsets among those who cover more pay.

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Limitations

For several reasons discussed below, the former SBP plan could well have been more favorable to the individual than the fractions above suggest. The same caveat applies to Congressional changes and other alternatives discussed in subsequent chapters. One important reason for this caveat is that the cost-sharing fractions discussed above ignore the tax deferral afforded by the SBP. SBP contributions are deducted before reporting retirement income to the government. Hence, the retiree in the SBP does not pay taxes on his contribution. SBP benefits are eventually taxed, but normally during a period of lower tax rates. This tax deferral provides an important advantage that, for typical retirees, could reduce cost-sharing ratios by 5 percent to 15 percent and by more for some officer retirees in high tax brackets. 5/ This study ignored tax effects because they vary widely among individuals.

The cost-sharing ratios in this study also ignore protection against unforeseen price increases. The ratios reflect the effect of future price increases but, for lack of better information, assume a gradually declining annual rate of inflation over the next five years and a constant rate thereafter. If inflation suddenly increases sharply in future years (as has happened in recent years), the full CPI protection of SBP benefits offers protection available in few, if any, private-sector benefit plans.

Moreover, the cost-sharing fractions in this study assume average mortality rates for retirees and survivors. This ignores any "adverse selection" that could prompt those with a high risk of mortality to choose the SBP in disproportionate numbers. Among these high-risk groups, the SBP may be more advantageous than the ratios in this study suggest.

Finally, all the fractions presented in this analysis are for nondisabled retirees from active duty, who constitute the majority of all retirees. The fractions would generally be lower for disabled retirees because of their higher expected mortality, and for retirees from reserve service because they do not begin

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5/ The illustrative calculations here assume that SBP participants are married and file joint returns using standard deductions. No account is taken of possible outside income, which could substantially affect the results.

receiving retirement pay--and hence join the SBP--until they reach age 60. Moreover, the fractions capture the effects only of the contribution formula and social security offsets and not of the more minor liberalizations discussed above.

These factors suggest that the cost-sharing ratios in this study are a conservative estimate. The SBP may be a better deal for individuals than the ratios suggest, both under previous law and the changes discussed in later chapters. Nonetheless, the factors probably do not reverse the conclusion that individuals paid more than the total cost of benefits to their survivors under previous law, since the fractions of costs borne by the individual were substantially greater than one.

While the assumptions noted above could mean that the SBP would be more favorable than the fractions suggest, other assumptions simply cause uncertainty. The mortality and economic assumptions, for example, could be wrong. Cost-sharing ratios are particularly sensitive to assumptions about economic discount rates, which reflect preferences for money now rather than money later. 6/ Other assumptions--such as those about relative ages of retiree and spouse, future remarriage and divorce rates, and other factors--add more minor amounts of uncertainty to the ratios. The cost-sharing fractions also depend critically on estimates of expected social security offsets. These, in turn, depend on numerous detailed assumptions about the complex social security system; the correctness of the assumptions could vary widely among individuals. For all these reasons, the fractions in this study should be used as guides to trends rather than as absolute findings.

In addition to considering inherent uncertainty, the interpretation of fractions presented in this study for those who have already retired requires special caution. The fractions assume that the individual is assessing the SBP at the time of retirement

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6/ This study uses a real discount rate (that is, a rate after adjustment for inflation) equal to 2 percent a year. This is consistent with real returns on long-term government bonds, which may be a reasonable guide to an appropriate discount rate for the government. Higher discount rates would push up the cost-sharing ratios. Lower rates--such as the 1 percent rate recently adopted for these evaluations by the Department of Defense--would push them down.

(or in 1972 for those who retired before that year). This was done to ensure comparable fractions for past and future retirees. But those who have already retired should not use the fractions to judge the desirability of remaining in the SBP. Such an analysis should reflect the actual mortality and health experience of the retiree, and the retiree's actual age.

COSTS UNDER THE PREVIOUS LAW

Government outlays under the previous law followed a pattern resulting from the enactment of the SBP in 1972 and the cost-sharing fractions discussed above. (See Table A-2 for estimates of outlays under the previous law.) Until the mid-1980s, contributions by SBP participants would have exceeded payments to survivors since the previous SBP was a young program that had yet to generate large numbers of benefit payments. Thus, over this period, the government would have "made money" on the SBP. From the mid-1980s until beyond the year 2000, however, payments to survivors would have exceeded contributions, and the government would have "lost money." This reflects the subsidy enjoyed by many nondisabled retirees from 1965 and before and by almost all reserve and disabled retirees from this period. It is retirees from 1965 and before who will reach old age, leave survivors, and influence benefit payments over the next three decades.

Under previous law, the government would have begun "making money" on the SBP again around the year 2010, and continued to make money from then on. This reflects the large social security offsets for those who retired in 1970 and beyond. Such offsets largely eliminated the survivor benefits and ensured that contributions exceeded benefit payments.

As with the fractions of costs discussed in the preceding section, these cost estimates contain important uncertainties, particularly in the years beyond 2000. Key among them are the mortality rates and economic assumptions discussed in the preceding section. In addition, the estimates assume that persons continue participating in the SBP and covering their retirement pay at rates similar to those of the recent past. While better estimates are not available, a shift in participation or coverage could significantly affect costs, especially in the long run.

CHAPTER III. THE CONGRESSIONAL REVISIONS (S. 91)

DESCRIPTION

On September 22, 1980, the Congress enacted a major change in the Survivor Benefit Plan. This change, embodied in Senate Bill 91, is similar to proposals by the Fleet Reserve Association and other groups. S. 91 revises the contribution formula to be consistent with the civil service method. Under this revised method, contributions are calculated on the date of retirement, or on December 1, 1980, for those already retired, and increase after that time by the amount of the increase in the CPI rather than being recalculated after each increase. In addition, S. 91 limits the social security offset to no more than 40 percent of survivor benefits. As Table 1 suggests, this would reduce the social security offset for almost all enlisted retirees and for many officer retirees, particularly those who retire now and in future years. (As an aid to understanding the changes, Table 3 summarizes the effects of this legislation on benefits for selected retirees.)

In addition to these major changes, S. 91 provides benefits to survivors of those who died before September 1972 (when SBP was enacted) while on active duty and eligible for retirement. Spouses of these survivors had no opportunity to elect either SBP or the survivor benefit plan that preceded it. S. 91 eliminates the offsets for those reservists whose reserve military service occurred during periods when their combined reserve and full-time civilian earnings exceeded the maximum wages subject to social security. Finally, S. 91 allows voluntary disenrollment of all totally disabled personnel who are currently in the SBP. Benefits for survivors of these totally disabled personnel are reduced by payments available to them under the Dependency and Indemnity Compensation (DIC) plan, and DIC benefits generally eliminate most or all of the SBP benefits. Thus, these totally disabled personnel are contributing to the SBP, but their survivors will never receive payments (although their survivors will receive a refund of all contributions). The disenrollment provisions were proposed by S. 2463--an earlier bill introduced by Senator Humphrey--and incorporated into S. 91.

TABLE 3. MONTHLY SBP BENEFITS UNDER ALTERNATIVE PROPOSALS FOR A PERSON WHO RETIRES IN 1980 (In 1980 dollars) a/

Alternative	Paygrade at Retirement	Years of Service at Retirement	Monthly SBP Benefit
Previous Law	E-7	20	0
	E-9	30	138
	O-5	20	93
	O-6	30	509
S. 91 Revisions	E-7	20	144
	E-9	30	322
	O-5	20	295
	O-6	30	559
Fleet Reserve Association (FRA)	E-7	20	144
	E-9	30	322
	O-5	20	295
	O-6	30	559
Original S. 91	E-7	20	83
	E-9	30	338
	O-5	20	292
	O-6	30	721
Retired Officers Association (TROA)	E-7	20	149
	E-9	30	447
	O-5	20	400
	O-6	30	841
No Contribution Age 62 or Over	E-7	20	0
	E-9	30	138
	O-5	20	93
	O-6	30	509

a/ Estimates assume that the person is at the median paygrade throughout his military career and retires at fiscal year 1980 pay rates. The retiree is assumed to retire from active duty without disability and to elect average coverage (75 percent of retirement pay for officers and 80 percent for enlisted). The numbers assume social security offsets that reflect real wage growth until the retiree reaches age 62. The offsets also assume that the spouse is eligible and takes social security at age 62. The numbers ignore any special treatment for career widows.

COST SHARING UNDER S. 91

Table 2 shows that these changes guarantee a subsidy for past retirees and for most who will retire over the next two decades. Average retirees in 1981, the first year during which the changes will be in effect, will pay about 70 percent of the cost of their survivor benefits. Given the uncertainties surrounding the estimates of the fractions, this 70 percent would be quite similar to the percentage envisioned by the Senate when the SBP was enacted in 1972. Individuals who retired in 1965, and elected the SBP in 1972, will pay about 50 percent of total costs. 1/ As the discussion in the preceding chapter pointed out, these cost-sharing estimates are conservative; factors not considered in determining the ratios may make the SBP a better deal for many retirees.

While S. 91 offers a subsidy for those who retire today or who retired in past years, the fraction of costs borne by the individual will grow in coming years (though the fractions always remain less than under the previous law). By the year 2000, average retirees will be paying almost the entire cost of the program. The growth is caused by the nature of the revised contribution formula, which would still require that retirees pay 2.5 percent of the first $300 of their covered retirement pay and 10 percent above that amount. The revision in the formula under S. 91 ensures that costs per dollar of coverage stay constant once a person has retired, as under the civil service survivor benefit system. But--again like civil service--the revision leaves the $300 fixed in nominal terms, which means that the smaller, 2.5 percent part of the contribution formula gradually becomes less important as pay raises push up retirement pay for future retirees. Thus for future retirees, the cost of each dollar of coverage grows, as does the fraction of costs paid by the individual. (The proposal of the Fleet

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1/ In addition to reducing fractions of costs paid by individuals well below their levels under the previous law, S. 91 also alters some patterns that existed under previous law. The SBP no longer costs senior enlisted retirees substantially less, though it does cost senior officer retirees less. Nor is the new plan a better deal for those who cover all their retirement pay rather than only part of it, as under the previous law. (See Tables A-7 and A-8, as well as Table 2, for results underlying these conclusions.)

Reserve Association, which is discussed in the next chapter, would arrest this growth.)

COSTS

One effect of the changes in S. 91 is to increase outlays over those under the previous law. CBO estimates that, in constant 1980 dollars, S. 91 will add $280 million to total outlays over the next five years and $2.6 billion over the next 20 years. (Table 2 also shows, in parentheses, added outlays assuming continued inflation. While not discussed in this study, these inflated-dollar estimates were widely used during debate over changes to the SBP.) The details of the costs in Table A-4 show that, over the next five years, the change in the contribution formula accounts for more than half the added costs, with the added benefits for certain survivors of pre-1972 personnel accounting for another 25 percent. Over the next 20 years, the change in the contribution formula still accounts for half the costs, with the social security offset now accounting for another 40 percent. 2/

At the request of some of its clients, CBO also estimated the cost changes caused by S. 91 over the next 50 years. These long-run costs are subject to substantial uncertainties which suggest that they be used at most to judge patterns of change. The estimates show that S. 91 will add a total of about $17 billion to costs over the next 50 years.

2/ Some of these added costs, namely the added $60 million over the next 20 years for voluntary disenrollment of totally disabled personnel, are caused primarily by the 20-year period chosen by CBO for this study. The voluntary disenrollment provisions of S. 91 allow totally disabled personnel to withdraw immediately from the SBP and cease contributing. Under the previous law, these persons continued contributing, but their survivors eventually received a refund of all contributions. Voluntary disenrollment thus adds costs now because contributions cease, but will eventually result in lower costs of refunds.

CHAPTER IV. OTHER ALTERNATIVES

During its extensive consideration of possible changes to the SBP, the Congress considered numerous alternatives other than the one finally selected, including several proposed by retiree associations. Table A-1 details the provisions of the major alternatives, while subsequent tables in Appendi A show effects on cost sharing and outlays. Table 3 summarizes the effects these proposals have on benefits for survivors of selected retirees.

This chapter does not attempt to discuss every detail of the proposals, but rather indicates how they differ from S. 91. The alternatives are discussed in order of similarity to S. 91, beginning with the most similar. The chapter concludes with a summary of key provisions in these proposals that could be considered in any future debate over the SBP.

THE FLEET RESERVE ASSOCIATION (FRA) PROPOSAL

Much of S. 91 is similar to the FRA proposal. The FRA suggested revising the contribution formula and providing the 40 percent limit on social security offsets, the two key provisions of S. 91. The major difference from S. 91 was the "indexing" of the $300 limit in the contribution formula included in the FRA proposal. This indexing would have increased that $300 each time military pay was increased, and by the same amount. The effect would have been to hold constant the cost per dollar of coverage for future retirees, and thus hold the fraction of costs borne by the individual at approximately the 1981 level. Over the next 20 years, however, this indexing would have added $530 million more to costs than will S. 91. (See estimates of costs of FRA proposal in Table A-4 for details.)

THE ORIGINAL S. 91

The original version of S. 91, which had been proposed by Senator Thurmond and others for several years, differed more sharply from the enacted version of S. 91 than did the FRA proposal. The original S. 91 would have made the same revision to the contribution formula as the enacted S. 91, but would have

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simply reduced most social security offsets by one-half rather than limiting the offsets to no more than 40 percent of benefits. (Offsets of mothers with one dependent child would have been eliminated altogether.) The original version of S. 91 would generally have been more advantageous for those who retired some years ago. Many of those who retired some years ago, however, were already receiving some subsidy even under the previous law. (For details, see cost-sharing ratios for 1965 retirees in Table 2 and Tables A-7 and A-8.)

The reduced offsets under the original S. 91, both for those over age 62 and for mothers with one dependent child, also would have increased costs over the next 20 years by $2.2 billion above those under the previous law, compared to $1.1 billion under the enacted version of S. 91 (Table A-4). Higher costs would have occurred mostly because of the improved benefits noted above for those who retired some years ago. These persons will reach old age and leave survivors over the next 20 years.

Interestingly, in contrast to the result for those who retired in past years, the enacted version of S. 91 actually offers lower fractions to some current and future retirees (particularly enlisted retirees) than did the original version (see Tables A-7 and A-8). This occurs because the large size of many future social security offsets means that the 40 percent limit is more generous than simply cutting the offset in half.

In addition to the major difference in the proposed social security offset, the original version of S. 91 offered an open enrollment that would have allowed those not now participating in the SBP to join. It would have reduced or eliminated offsets for some "career" widows; that is, widows entitled to social security benefits based on their own earnings. It also provided added benefits not only for those survivors whose spouses died before September 1972 while on active duty and eligible for retirement, but also for all those who died in retirement before September 1972. All these differences together meant that the original S. 91 would have increased costs by $5.9 billion over the next 20 years relative to costs under the previous law, compared to $2.6 billion under the enacted version of S. 91 (see Table A-4).

RETIRED OFFICERS ASSOCIATION (TROA) PROPOSAL

The TROA proposal, differing still more from S. 91, would not only have revised the contribution formula as in S. 91 but would

have provided a one-time recalculation of contributions so that, on and after enactment, contributions would equal their level had the revised contribution formula been in effect since 1972. In addition, the TROA proposal would have provided a flat dollar offset to survivor benefits, equal for officers and enlisted, not directly tied to social security. The offset would have been substantially smaller than the social security offsets under previous law for most retirees, particularly officer retirees. TROA would have also made several other important changes not in S. 91 (see Table A-1). The total added costs of this proposal would have amounted to $6.7 billion above those under the previous law, the largest costs of any of the proposals (Table A-4). But, among all the alternatives examined in this study, the TROA proposal would have also provided the lowest overall fraction of costs borne by the individual, about 54 percent for an average retiree in 1981.

NO CONTRIBUTION AGE 62 OR OVER

This proposal differed most radically of all from S. 91. It would have made no change at all in the social security offset and hence in survivor benefits. This would have been consistent with the notion of the SBP as "gap" coverage that provides benefits before the survivor becomes eligible for social security; after age 62, the SBP would have provided little or no benefits for most survivors. The numbers in the 1972 Senate report suggest that the Senate intended such a philosophy of gap coverage. Estimates in that report show substantial survivor benefits for widows before age 62, but small payments to some widows thereafter. 1/

The proposal recognized, however, that individuals would be paying substantially more than the value of this gap coverage. In response, it would have revised the contribution formula as did S. 91, but would also have eliminated all contributions when the survivor reached age 62 or older and so passed the gap years. The proposal would have added $3.3 billion to total costs over the next 20 years above those under the previous law, an increase similar in size to that for S. 91. But it would have left the typical retiree now and in the future paying more than the full

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1/ Survivor Benefit Plan, S. Rept. 1089, 92:2 (September 6, 1972), Table 16, p. 44.

cost of his survivor's benefits. Moreover, cost sharing would have varied widely depending on years of service at retirement, with much lower ratios for more senior retirees. (See Tables 2, A-7, and A-8 for details.)

EFFECTS OF KEY PROVISIONS ON S. 91

The proposals discussed above contain several provisions that could be debated in any future consideration of the SBP. The effects of these provisions are discussed above. In some cases, however, the costs of the provisions differ when added to S. 91 rather than their original bill. Hence this section indicates how much each would add to the costs of S. 91. Table A-5 in Appendix A shows the details of the costs.

Both the original S. 91 and the TROA proposals allowed an open enrollment period during which those who had not previously joined the SBP could do so. An open enrollment attached to the enacted S. 91 would save about $40 million in 1981 because of contributions by new participants but would add a total of $480 million over the next 20 years. The long-run costs of open enrollment could be reduced by requiring that the survivors of those who elected to participate under the open enrollment, but who died within one year of election, would receive a refund of contributions but would not receive any survivor benefits. This would avoid the costs of "death-bed" elections. An open enrollment with such a one-year delay provision would save about $40 million in 1981 and add a total of $290 million over the next 20 years. The one-year delay significantly affects costs and savings over the next 20 years because CBO assumed that some participants under the open enrollment would be "death-bed" elections who would have very short lifespans (see Appendix B). This assumption, and the others connected with estimating costs of open enrollment, are highly uncertain and make these cost estimates less reliable than others in this study.

Future debates could also consider adding indexing to S. 91. Indexing of the $300 threshold was discussed above in connection with the FRA proposal. Indexing the $300 threshold to military wages, beginning with the wage increase in fiscal year 1981, would add negligibly to costs in 1981 but would add a total of $530 million to costs over the next 20 years. The $300 threshold could also be indexed to the CPI. This would not hold cost-sharing fractions constant, as would indexing to military wages (see discussion of the FRA proposal above), but would be more consistent with other military retirement provisions that are tied