



## CONGRESSIONAL BUDGET OFFICE COST ESTIMATE

March 29, 2000

### **S. 2003**

### **Keep Our Promise to America's Military Retirees Act**

*As introduced on January 24, 2000*

#### **SUMMARY**

S. 2003 would increase health insurance benefits for certain retirees from the uniformed services and their survivors. Retirees who entered military service before June 7, 1956, and their surviving spouses would be able to use one of the military health insurance programs—Tricare Standard or Extra—and would also be able to enroll in the Federal Employees Health Benefits (FEHB) program. Those enrolling in FEHB would pay no out-of-pocket premiums. The Department of Defense (DoD) would pay the normal government contribution (roughly 70 percent) as well as the remaining share of the premium normally paid by the annuitant.

Retirees who entered military service after June 7, 1956, and their survivors would be eligible for increased insurance coverage regardless of age. They could either enroll in FEHB or continue to use Tricare Standard or Extra, but could not choose both options. All retirees and survivors could continue to receive care at a military treatment facility (MTF) on a space-available basis. For those choosing FEHB, DoD would pay only the normal government contribution and the retiree or survivor would be responsible for the remainder. DoD would also bear costs for those retirees and survivors who choose to continue their use of Tricare Standard or Extra. (Under current law, eligibility to use those programs ends at age 65.)

The bill would result in additional costs for spending on FEHB premiums and increased use of Medicare, but there would be a net decrease in the costs of Tricare. Because the bill would affect direct spending, pay-as-you-go procedures would apply. Allowing for a transition period lasting three years, CBO estimates that the bill would raise direct spending by about \$36 billion over the 2001-2005 period and by about \$92 billion through 2010. The bill would save about \$1.2 billion in discretionary spending over the 2001-2005 period, assuming appropriations are reduced by the estimated amounts.

S. 2003 contains no intergovernmental or private-sector mandates as defined in the Unfunded Mandates Reform Act (UMRA) and would not affect the budgets of state, local, or tribal governments.

## ESTIMATED COST TO THE FEDERAL GOVERNMENT

The estimated budgetary impact of S. 2003 is shown in Table 1. The costs of this legislation fall within budget functions 550 (health), 570 (Medicare), and 050 (national defense).

TABLE 1. ESTIMATED COSTS OF S. 2003

	By Fiscal Year, in Millions of Dollars					
	2000	2001	2002	2003	2004	2005
<b>CHANGES IN DIRECT SPENDING</b>						
Estimated Budget Authority	0	3,000	5,700	8,300	9,400	9,800
Estimated Outlays	0	3,000	5,700	8,300	9,400	9,800
<b>CHANGES IN SPENDING SUBJECT TO APPROPRIATION</b>						
Estimated Authorization Level	0	-120	-240	-320	-300	-260
Estimated Outlays	0	-110	-220	-310	-300	-260

## BASIS OF ESTIMATE

Under current law, military retirees under the age of 65 are eligible either to enroll in Tricare Prime or to use Tricare's insurance programs (Standard or Extra). Those who use Tricare Standard or Extra may also seek care at an MTF on a space-available basis. Once retirees turn age 65, they are no longer eligible to use Tricare, though they may continue to seek care at an MTF when space is available. The same eligibility rules apply to survivors, who are primarily widows and widowers.

S. 2003 would allow greater access to health insurance by allowing retirees and survivors over the age of 64 the added choice of insurance under Tricare and FEHB in addition to their Medicare benefit and any private insurance they already have. Retirees who entered military service before June 7, 1956, and their surviving spouses would be eligible to enroll in FEHB and to use Tricare Standard or Extra. Retirees and survivors who do not meet that test would be able to choose between enrolling in FEHB or using Tricare Standard or Extra regardless

of age. All retirees would continue to be able to use MTFs for health care on a space-available basis.

The bill would result in additional costs for spending on FEHB premiums and increased use of Medicare, but there would be a net decrease in the costs of Tricare. The first step in calculating these costs is estimating the number of eligible beneficiaries.

### **Eligible Population**

S. 2003 differentiates between two groups of beneficiaries. The first group consists of retirees who entered military service before June 7, 1956, and their surviving spouses. This group would be entitled to FEHB insurance without making any out-of-pocket premium payments and could also use Tricare Standard or Extra. Using data from the Department of Defense, CBO estimates that about 1.1 million households would meet the criteria for having their premiums paid in full. Reductions due to mortality will leave this population at a little more than 750,000 in 2010. According to the *1998 Health Care Survey of DoD Beneficiaries*, 10 percent of this population is already enrolled in FEHB. These individuals would also receive their FEHB insurance for free, but only a portion of their premiums would be new costs to the government.

The second group consists of retirees who entered military service after June 7, 1956, and survivors of an individual who entered service after that date. Those people could enroll in FEHB or they could choose to use Tricare Standard or Extra, but they could not use both. Any member of this group choosing to enroll in FEHB would have to make the same out-of-pocket premium payments that current FEHB enrollees make.

CBO expects that the number of beneficiaries age 65 and over who did not enter military service prior to June 7, 1956, is initially low and increases to about 380,000 households by 2010. That number does not reflect those already eligible for FEHB because of civil service employment after their military retirement. (Most current retirees over 64 entered military service before the above cutoff date.) The estimated number of households of retirees and survivors under 65 is relatively constant over the 10-year period. In 2001, an estimated one million households would have a retiree or survivor under 65 and would be eligible for FEHB under the bill. (That figure does not count those already eligible based on current civil service employment.)

## Direct Spending

S. 2003 would increase costs for FEHB and Medicare. These costs would be direct spending and are shown in Table 2.

TABLE 2. ESTIMATED DIRECT SPENDING UNDER S. 2003

	By Fiscal Year, in Millions of Dollars					
	2000	2001	2002	2003	2004	2005
<b>DIRECT SPENDING</b>						
<i>Costs of Premium Payments Under FEHB</i>						
Spending Under Current Law						
Estimated Budget Authority	5,012	5,456	5,906	6,352	6,826	7,338
Estimated Outlays	5,012	5,456	5,906	6,352	6,826	7,338
Proposed Changes						
Retirees Over Age 65						
Estimated Budget Authority	0	2,300	4,300	6,200	6,900	7,100
Estimated Outlays	0	2,300	4,300	6,200	6,900	7,100
Retirees Under Age 65						
Estimated Budget Authority	0	500	1,000	1,500	1,700	1,800
Estimated Outlays	0	500	1,000	1,500	1,700	1,800
Subtotal - Proposed Changes						
Estimated Budget Authority	0	2,800	5,300	7,700	8,600	8,900
Estimated Outlays	0	2,800	5,300	7,700	8,600	8,900
Spending Under S. 2003						
Estimated Budget Authority	5,012	8,256	11,206	14,052	15,426	16,238
Estimated Outlays	5,012	8,256	11,206	14,052	15,426	16,238
<i>Cost Increases in Medicare</i>						
Spending Under Current Law						
Estimated Budget Authority	216,900	234,800	242,500	263,000	282,200	308,500
Estimated Outlays	216,900	234,800	242,500	263,000	282,200	308,500
Proposed Changes						
Estimated Budget Authority	0	200	400	600	800	900
Estimated Outlays	0	200	400	600	800	900
Spending Under S. 2003						
Estimated Budget Authority	216,900	235,000	242,900	263,600	283,000	309,400
Estimated Outlays	216,900	235,000	242,900	263,600	283,000	309,400
<i>Total Proposed Changes</i>						
Estimated Budget Authority	0	3,000	5,700	8,300	9,400	9,800
Estimated Outlays	0	3,000	5,700	8,300	9,400	9,800

**Costs of Premium Payments Under FEHB.** DoD's contribution toward FEHB premiums for beneficiaries under S. 2003 would cost more than \$33 billion over the 2001-2005 period and roughly \$84 billion over the 10-year period ending in 2010. Premiums for retirees who would receive free insurance (those who entered service prior to June 7, 1956) would constitute the majority of these costs. Even in 2010, after significant declines in this population from mortality, the cost of providing free premiums would still make up almost 70 percent of the added FEHB costs—\$7.3 billion out of \$11 billion. (Covering retirees age 65 and over who would pay part of the premium would cost about \$1.1 billion and covering retirees under the age of 65 would cost about \$2.6 billion.) The expected increase in FEHB premiums is greater than the mortality rate, so total costs would continue to increase over the 2001-2010 period.

*Participation Rates.* CBO estimates that by 2003 about 950,000 (90 percent) of retirees and survivors who would be eligible for free FEHB coverage would enroll in FEHB. By 2010, the estimated number of participants would be less than 700,000. Because they would pay no premiums, the overwhelming majority of these people would probably choose to enroll in the most generous and, consequently, expensive plans like the Blue Cross/Blue Shield (BCBS) High option. Under the provisions of S. 2003, such retirees would also be eligible to use Tricare Standard or Extra. Tricare use would likely be limited to covering out-of-pocket medical care costs that beneficiaries would incur using FEHB. Because BCBS High is more generous and has lower catastrophic limits than Tricare, CBO expects that retirees and survivors would choose FEHB as their primary insurance.

In contrast, a much lower percentage of the other retirees and survivors would choose to enroll in FEHB. Using data from the *1998 Health Care Survey of DoD Beneficiaries* and the *Current Population Survey* (March 1997), CBO estimates that roughly 50 percent of military retirees who are working in a second career for the federal government currently choose to pay an out-of-pocket premium to enroll in FEHB. They do this despite being eligible for Tricare Standard or Extra, for which there is no such premium. CBO uses the same estimated participation rate (50 percent) for retirees who would pay part of the premium under S. 2003 because they would face the same choice as current retirees employed by the federal government as civilians.

The estimated participation rate for retirees under age 65 is even lower—about 34 percent of those not already eligible for FEHB. According to data from the *1997 Health Care Survey of DoD Beneficiaries*, almost 25 percent of retirees under age 65 have employer sponsored insurance that requires no out-of-pocket premiums. Because such individuals are unlikely to pay to enroll in FEHB, CBO estimates a lower participation rate in FEHB for this group of retirees and survivors.

Currently, DoD and the Office of Personnel Management (OPM) are conducting a pilot program that allows military retirees age 65 and over to enroll in FEHB for a two-year period. Although enrollment rates have been extremely low, CBO does not believe these rates are representative of what would happen if S. 2003 became law. CBO believes that the temporary nature of the program is the primary reason participation rates are low. According to data from the *1997 Health Care Survey of DoD Beneficiaries*, about 55 percent of retirees and survivors currently purchase some form of medigap insurance. Those who enroll in the FEHB demonstration program may not be aware that they can reacquire their medigap coverage at the end of two years, which would explain why so many are reluctant to enroll in the plan.

*Premium Costs to the Federal Government.* CBO estimates the added per capita FEHB costs by using the premium rates published by OPM for 2000. BCBS High option premiums are \$3,773 for an individual policy and \$8,068 for a family policy. The BCBS Standard option premiums are \$2,831 and \$6,312, while Kaiser Permanente's Mid-Atlantic premiums are \$2,444 and \$6,042. The government pays a fixed amount equal to 72 percent of the average premium (weighted by participation in the various plans), but for expensive plans the actual share is considerably less than 72 percent.

The government's costs would increase significantly under S. 2003 because a large group of beneficiaries would receive health insurance and pay no premiums. In 2001, CBO estimates that the average cost to the federal government for retirees and survivors not paying premiums would be \$3,971 for individuals and \$8,550 for families. In contrast, if the enrollees were to pay their share of the premiums the costs to the federal government would be \$2,177 for individuals and \$4,959 for families. According to data from DoD, 66 percent of retirees age 65 and over have at least one dependent and would likely choose the self-and-family policy.

CBO also estimates that about 80 percent of enrollees who would not receive free insurance would choose a fee-for-service plan like BCBS, and about 20 percent would opt for a managed care plan. These percentages correspond to actual enrollment data for Civil Service retirees who are currently enrolled in FEHB.

S. 2003 would place all new beneficiaries in a separate risk pool, to insulate current FEHB enrollees from any potential increase in premiums. New beneficiaries under S. 2003 would be considerably older than the corresponding pool of federal civilian enrollees. Based on self-reported evaluations, the health status of the potential beneficiaries is somewhat poorer than for current FEHB enrollees. However, CBO believes that these differences will have a small effect on premiums for new beneficiaries.

Over 70 percent of CBO's projected enrollees are over age 64 and eligible for Medicare; about 90 percent enroll in Medicare Part B. When retirees are covered jointly by Medicare and FEHB, Medicare pays first and FEHB acts as a wrap-around policy, which significantly lowers the costs to FEHB. For example, under current law annuitants who are covered by Medicare and active employees cost the federal government about the same per capita amount for FEHB. In absolute terms, annuitants cost a lot more, but since Medicare is first payer the actuarial costs to FEHB are about equal for both groups. This group of potential beneficiaries is somewhat more likely to require health care services than current FEHB enrollees, but since Medicare is first payer the effect on premiums is probably negligible.

However, beneficiaries under 65 would have a slightly larger impact because the population contains few retirees under age 45. The new pool would not have enough younger people to offset the higher average medical costs for those between 45 and 65. Because those already working for the federal government and those with free employer sponsored insurance are not included in the new pool, a relatively higher percentage of new beneficiaries choosing FEHB would be in poor health. But, new beneficiaries would bear any increase in premiums, because the government's contribution is limited to the amount paid in the regular FEHB pool.

**Cost Increases in Medicare.** Allowing military retirees the opportunity to enroll in FEHB plans or to use Tricare insurance would also increase costs to the Medicare program. CBO estimates that S. 2003 would increase Medicare costs by \$2.9 billion over the 2001-2005 period and by almost \$8 billion over the first 10 years. This increase would stem from increased use of health care by those retirees for whom FEHB/Tricare provides better insurance than they currently receive. In addition, some retirees would seek care from private providers instead of an MTF once they have a generous health insurance plan.

Retirees enrolled in Medicare who do not have a medigap plan or employer-sponsored insurance are likely to increase their use of health care, once they receive supplemental insurance. CBO estimates that this group makes up roughly 13 percent of beneficiaries who are over the age of 64 and who do not currently use MTFs for their medical care. The estimate is based on the *1997 Health Care Survey of DoD Beneficiaries*, which provides self-reported data on private insurance coverage. Although Medicare is currently the primary payer for these people, it would have to pay more because more generous insurance encourages more use of health care services. Using data from published research, CBO estimates that Medicare costs for these individuals would rise by about 25 percent as they gain better coverage.

Many retirees seek health care at MTFs, but there is a significant amount of variation in the degree to which those people use MTFs. With the provision of better insurance fewer people would use MTFs and would turn instead to the private sector. This shift in the provision of

care would increase costs to Medicare, which is the first payer under most health insurance policies. CBO estimates that about 6 percent of beneficiaries over age 64 would effectively begin using private health care providers rather than the military health system.

### **Spending Subject to Appropriation**

As shown in Table 3, S. 2003 would lower discretionary spending by DoD, assuming appropriations are decreased by the estimated amounts. The total savings to DoD, after adjusting for changes in use patterns by all retirees and increased use of Tricare Standard or Extra as third payer, would be about \$1.2 billion in outlays over the 2001-2005 period and roughly \$1.7 billion in outlays by the end of 2010.

**Changes in Tricare Caseloads.** Changes in the Tricare caseload result in savings over the 2001-2005 period. The effect of the bill for beneficiaries over age 64 would be savings in each of the first four years but additional costs of \$40 million in 2005. For other retirees under age 65 there would be savings every year, totaling about \$770 million in 2005.

*Retirees Over Age 65.* Retirees who would enroll in FEHB would use the MTFs less frequently. The decline in users would come primarily from those who receive free FEHB insurance. CBO estimates that roughly 30,000 users would leave the military health care system in 2001 and about 75,000 users would leave by 2010. According to DoD estimates, the costs of direct patient care for these beneficiaries averages \$2,340 per person. CBO estimates that outlay savings from reduced use of MTFs by retirees over age 64 would be about \$230 million by 2005.

On the other hand, about 30 percent of those not eligible for free FEHB insurance would choose to use Tricare Standard or Extra. These additions are relatively small in the early years but would become more substantial by 2010. CBO estimates that the number of Tricare users would increase to a little more than 180,000, by 2010. CBO estimates that DoD's cost of providing insurance to these retirees and survivors over the age of 64 would be about 80 percent of the cost of the Blue Cross/Blue Shield High individual premium, or roughly \$3,000 per person. Accordingly, CBO estimates that increased use from this group of beneficiaries would raise DoD's costs by about \$270 million in outlays in 2005.

*Retirees Under Age 65.* Those retirees and survivors under age 65 who would enroll in FEHB would no longer be able to use Tricare Standard or Extra, though they would be able to use the MTFs on a space-available basis. CBO estimates that in a steady state about 330,000 users under the age of 65 would leave the military health care system. According to DoD estimates, the cost of direct patient care and Tricare use for these beneficiaries is

about \$1,708 per person. Thus, CBO estimates that by 2005 savings in Tricare for those under 65 would amount to about \$770 million.

TABLE 3. ESTIMATED SPENDING SUBJECT TO APPROPRIATION UNDER S. 2003

	By Fiscal Year, in Millions of Dollars					
	2000	2001	2002	2003	2004	2005
<b>SPENDING SUBJECT TO APPROPRIATION</b>						
Spending Under Current Law for the Defense Health Program						
Estimated Authorization Level <sup>a</sup>	16,500	16,500	16,500	16,500	16,500	16,500
Estimated Outlays	16,500	16,500	16,500	16,500	16,500	16,500
Proposed Changes						
Changes in Tricare Caseloads						
Retirees Over Age 65						
Estimated Authorization Level	0	-60	-110	-100	-30	50
Estimated Outlays	0	-50	-100	-100	-40	40
Retirees Under Age 65						
Estimated Authorization Level	0	-230	-440	-660	-740	-790
Estimated Outlays	0	-210	-410	-630	-720	-770
Subtotal - Tricare Caseload						
Estimated Authorization Level	0	-290	-550	-760	-770	-740
Estimated Outlays	0	-260	-510	-730	-760	-730
Tricare as Third Payer						
Estimated Authorization Level	0	170	310	440	470	480
Estimated Outlays	0	150	290	420	460	470
Subtotal-Proposed Changes						
Estimated Authorization Level	0	-120	-240	-320	-300	-260
Estimated Outlays	0	-110	-220	-310	-300	-260
Spending Under S. 2003 for the Defense Health Program						
Estimated Authorization Level <sup>a</sup>	16,500	16,380	16,260	16,180	16,200	16,240
Estimated Outlays	16,500	16,390	16,280	16,190	16,200	16,240

a. The 2000 level is the estimated amount appropriated for that year. The current law amounts for the 2001-2005 period assume that appropriations remain at the 2000 level, without adjustment for inflation. If they are adjusted for inflation the base amounts would increase by about \$400 million a year, but the estimated changes would remain as shown under "Proposed Changes."

**Tricare as Third Payer.** Under S. 2003, those eligible for free FEHB benefits can also use Tricare Standard or Extra to offset some of their out-of-pocket costs under FEHB. CBO estimates that in 2000 the average out-of-pocket costs for Medicare-eligible FEHB users would be roughly \$600 for individuals and about \$1,000 for a family of two. CBO estimates that by 2005 the costs to DoD from this benefit would be about \$470 million annually, based on an estimated 1.1 million households that would be eligible for the benefit in 2001.

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

The Balanced Budget and Emergency Deficit Control Act sets up pay-as-you-go procedures for legislation affecting direct spending or receipts. The net changes in outlays that are subject to pay-as-you-go procedures are shown in the following table. For the purposes of enforcing pay-as-you-go procedures, only the effects in the current year, the budget year, and the succeeding four years are counted.

	By Fiscal Year, in Millions of Dollars										
	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010
Changes in outlays	0	3,000	5,700	8,300	9,400	9,800	10,200	10,700	11,200	11,600	12,100
Changes in receipts	Not applicable										

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

S. 2003 contains no intergovernmental or private-sector mandates as defined in UMRA and would not affect the budgets of state, local, or tribal governments.

## **PREVIOUS CBO ESTIMATE**

On March 28, 2000, CBO prepared a cost estimate for H.R. 3573, an identical bill to S. 2003. The CBO cost estimates are also the same.

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