CONGRESSIONAL BUDGET OFFICE
COST ESTIMATE

May 22, 2001

H.R. 303
Retired Pay Restoration Act of 2001

As introduced on January 24, 2001, and January 30, 2001, respectively

SUMMARY

S. 170 and H.R. 303 would allow total or partial concurrent payment of retirement annuities together with veterans' disability compensation to retirees from the military, the Coast Guard, the Public Health Service (PHS), and the National Oceanic and Atmospheric Administration (NOAA) who have service-connected disabilities. The legislation also would discontinue special compensation for certain severely disabled uniformed services retirees. As introduced, S. 170 and H.R. 303 are identical.

CBO estimates that enacting this legislation would increase direct spending for retirement payments and veterans' disability compensation by about $3 billion in 2002, $17 billion over the 2002-2006 period, and $41 billion over the 2002-2011 period. In addition, the Department of Defense (DoD) would have to make payments of about $1 billion in 2002, $6 billion over the 2002-2006 period, and $14 billion over the 2002-2011 period to the military retirement trust fund to cover the increase in future liabilities for current military personnel. The increased contributions to the retirement trust fund would come from appropriated funds.

Because the bill would affect direct spending, pay-as-you-go procedures would apply. The legislation contains no intergovernmental or private-sector mandates as defined in the Unfunded Mandates Reform Act (UMRA) and would impose no costs on state, local, or tribal governments.

ESTIMATED COST TO THE FEDERAL GOVERNMENT

The estimated budgetary impact of S. 170 and H.R. 303 is shown in Table 1. This estimate assumes the legislation will be enacted by October 1, 2001, and that the necessary amounts will be appropriated for each fiscal year. The costs of this legislation fall within budget functions 600 (income security), 300 (natural resources and environment), 400 (transportation), 550 (health), 050 (national defense), and 700 (veterans benefits and services).

TABLE 1. ESTIMATED COSTS OF S. 170 and H.R. 303

	By Fiscal Year, in Millions of Dollars					
	2001	2002	2003	2004	2005	2006
CHANGES IN DIRECT SPENDING						
Estimated Budget Authority	0	2,865	3,179	3,464	3,688	3,919
Estimated Outlays	0	2,865	3,179	3,464	3,688	3,919
CHANGES IN SPENDING SUBJECT TO APPROPRIATION						
Estimated Authorization Level	0	994	1,086	1,182	1,284	1,382
Estimated Outlays	0	994	1,086	1,182	1,284	1,382

BASIS OF ESTIMATE

Under current law, disabled veterans who are retired from the military, the Coast Guard, PHS, or NOAA cannot receive both full retirement annuities and disability compensation from the Department of Veterans Affairs (VA). Because of this prohibition on concurrent receipt, such veterans forgo a portion of their retirement annuity equal to the nontaxable veterans' benefit. The bill would allow individuals who have service-connected disabilities and whose retirement annuity is based on their years of service to receive both benefits without the reduction called for in current law. Individuals whose retirement pay is based on their degree of disability would continue to forgo retirement pay equal to the VA compensation payment, but only to the extent that their disability had entitled them to a larger retirement annuity than they would have received based on years of service.

S. 170 and H.R. 303 also would repeal a program that partially compensates certain severely disabled retirees for this reduction in their retirement annuities. This program pays a fixed benefit of $100 to $300 a month, depending on degree of disability.

Direct Spending

CBO estimates that enacting the bill would increase direct spending by about $17 billion over the 2002-2006 period as shown in Table 2.

TABLE 2. ESTIMATED DIRECT SPENDING UNDER S. 170 and H.R. 303

	By Fiscal Year, Outlays in Millions of Dollars					
	2001	2002	2003	2004	2005	2006
RETIREMENT BENEFITS						
Spending Under Current Law	34,072	35,258	36,136	37,184	38,199	39,214
Proposed Changes						
Concurrent Receipt	0	2,908	3,126	3,359	3,603	3,831
Severely Disabled	0	-56	-56	-56	-56	-57
Subtotal - Proposed Changes	0	2,852	3,070	3,303	3,547	3,774
Spending Under S. 170 and H.R. 303	34,072	38,110	39,206	40,487	41,746	42,988
VETERANS' DISABILITY COMPENSATION						
Spending Under Current Law	18,199	21,286	22,329	23,458	26,228	25,068
Proposed Changes	0	0	95	147	126	130
Spending Under S. 170 and H.R. 303	18,199	21,286	22,424	23,605	26,354	25,198
SURVIVOR BENEFIT PLAN OFFSETTING RECEIPTS						
Spending Under Current Law	-17	-17	-17	-17	-17	-17
Proposed Changes	0	13	14	14	15	15
Spending Under S. 170 and H.R. 303	-17	-4	-3	-3	-2	-2
SUMMARY OF CHANGES IN DIRECT SPENDING						
Estimated Outlays	0	2,865	3,179	3,464	3,688	3,919

NOTE: Estimated changes in budget authority would equal estimated changes in outlays.

Concurrent Receipt. Since the proposed legislation would treat retirees differently based on their type of retirement—nondisability or disability, the potential costs of the legislation depend on the number of beneficiaries, their type of retirement, their disability levels, and the benefit amounts.

Nondisability Retirees. A nondisability retirement is granted based on length of service—usually 20 or more years. S.170 and H.R. 303 would allow these retirees to receive full retirement annuities and veterans' disability benefits with no offset. Data from the uniformed services indicate that in 2000 the prohibition on paying both benefits concurrently caused about $2.2 billion to be withheld from annuity payments to about 493,000 DoD retirees with nondisability retirements, and about 5,180 Coast Guard, 880 PHS, and 50 NOAA retirees that fall into the nondisability category. Using current rates of net growth in the population of new beneficiaries, CBO estimates this caseload would rise to about 530,000 nondisability retirees in 2002, and 640,000 by 2011. Assuming that future benefit payments increase according to current rates of growth in average disability levels and increase from cost-of-living adjustments, CBO estimates that implementing the legislation would increase spending on DoD nondisability retirement annuities by $2.6 billion in 2002, $15.2 billion over the 2002-2006 period, and $36.4 billion over the 2002-2011 period. We estimate the cost to the other uniformed services to be $35 million in 2002, about $200 million over the 2002-2006 period, and about $450 million over the 2002-2011 period.

Enacting S. 170 or H.R. 303 may also increase direct spending for VA disability compensation. About 1.2 million nondisability retirees of the uniformed services do not currently receive VA disability benefits. Some of these retirees may be eligible for VA disability benefits. Under current law, retirees receiving veterans' disability benefits exchange taxable retired pay for nontaxable VA benefits. In those cases where the VA benefit is small, or where the retirees' income is such that they do not pay income taxes, the ability to exchange taxable income for tax-free income may not provide a sufficient incentive to cause all those eligible to apply for disability benefits. Consequently, CBO expects that enacting the bill would cause some of these retirees to apply for VA disability benefits. However, we do not have sufficient information to estimate their number or degree of disability at this time.

Disability Retirees. Servicemembers who are found to be unable to perform their duties because of service-related disabilities may be granted a disability retirement. S. 170 and H.R. 303 would allow disability retirees to receive retirement annuities based on their years of service and veterans' disability benefits with no offset. CBO estimates that the additional spending for disability retirees would total $1.9 billion over the 2002-2006 period and $4.2 billion over the 2002-2011 period.

A disability retirement annuity is usually the product of basic pay and degree of disability. However, if the individual has 20 or more years of service and thus is also eligible for a nondisability retirement, the disability annuity may be calculated based on years of service, if that yields a greater annuity. Under the proposed legislation, retirees whose disability annuity is greater than the amount they are entitled to receive based on years of service would continue to have that portion of their annuity tied solely to their disability reduced dollar-for-dollar by the amount of their VA disability benefit. Disability retirees whose annuities are based solely on their disability (i.e., those retirees with less than 20 years of service) would continue to have their full annuities subject to reduction by the amount of VA disability benefit.

According to DoD, 146,000 disability retirees had their annuities reduced by $1.1 billion in fiscal year 2000 because of VA disability payments. Of those, almost 23,000 retirees who would be eligible for partial concurrent receipt under S. 170 and H.R. 303 had their annuities reduced by $247 million. An analysis of retiree records by DoD indicates that, under criteria set forth in the legislation, these retirees would be eligible to receive about 95 percent of their retirement annuity concurrently with their VA disability benefit. Assuming continuation of current trends in population and benefit growth, CBO estimates that, of the disability retirees who would be receiving VA disability benefits in fiscal year 2002, about 23,000 would be entitled to an additional $253 million in retirement annuities. CBO estimates the cost of partial concurrent receipt to be $1.3 billion over the 2002-2006 period and $2.9 billion over the 2002-2011 period. In addition, approximately 850 disability retirees from the other uniformed services would be entitled to an additional $11 million in 2002, $60 million over the 2002-2006 period, and $120 million over the 2002-2011 period.

Veterans Disability Compensation. Data from DoD indicates that an additional 15,000 uniformed services disability retirees—14,500 from DoD and about 600 from the other uniformed services—do not currently receive VA disability benefits that the vast majority are entitled to receive. Since many disability retirees are not taxed on their annuities, there is no incentive under current law for these retirees to apply for the tax-free VA benefits, as they will be offset, dollar-for-dollar, against their retirement annuities. Enacting S. 170 or H.R. 303 would provide a significant incentive for these individuals to apply for VA disability benefits. Because many of these retirees are both disabled and quite elderly, CBO expects that only about half would become informed of this improved benefit and successfully complete the application process. Based on their DoD-assessed degree of disability, CBO estimates that outlays for VA disability benefits would increase by $95 million in 2003, $500 million over the 2003-2006 period, and $1.2 billion over the 2003-2011 period. Due to the time needed for individuals to prepare and submit their applications and the current VA backlog in processing applications, CBO estimates that enacting this legislation would not increase VA outlays in 2002.

Survivor Benefit Plan Offsetting Receipts. Many retirees have a Survivor Benefit Plan (SBP) premium payment deducted from their retirement annuity. The SBP was established in Public Law 92-425 to create an opportunity for military retirees to provide annuities for their survivors. Those retirees who are not receiving a paycheck from DoD because their retirement annuity is totally offset by their VA disability benefit may still participate in the SBP by paying the monthly premium to the U.S. Treasury. According to DoD, approximately 31,000 military retirees paid $19 million in SBP premiums to the Treasury in 2000. About $13 million of that was paid by the 15,000 of these retirees who would begin to receive annuity checks under S. 170 or H.R. 303. These payments are recorded as offsetting receipts to DoD. The increase in retirement outlays estimated above assumes the premiums of retirees who benefit from the legislation would be deducted from the retirees' annuities, and their payments to the Treasury would cease. Assuming continuation of current trends in population and benefit growth, CBO estimates these receipts would decrease by about $13 million in 2002, $70 million over the 2002-2006 period, and $150 million over the 2002-2011 period.

Severely Disabled Retirees. S. 170 and H.R. 303 also would repeal a special compensation program that currently pays a fixed benefit of $100 to $300 a month to uniformed service, nondisability retirees who were determined to be 70 percent to 100 percent disabled within four years of their retirement. Beginning in fiscal year 2002, the benefit will also be available to similarly disabled individuals receiving disability retirements. Based on information from DoD and assuming the population growth trends continue, CBO estimates that about 20,000 DoD retirees and about 330 retirees of the other uniformed services will receive an average monthly benefit of $228 in 2002. Savings from repealing this program would be $56 million in 2002, about $280 million over the 2002-2006 period, and about $570 million over the 2002-2011 period.

Spending Subject to Appropriation

The military retirement system is financed in part by an annual payment from appropriated funds to the military retirement trust fund, based on an estimate of the system's accruing liabilities. If S. 170 or H.R. 303 is enacted, the yearly contribution to the military retirement trust fund (an outlay in budget function 050) would increase to reflect the added liability from the expected increase in annuities to future retirees. Using information from DoD, CBO estimates that enacting this legislation would increase such payments by about $1 billion in 2002, and $6 billion over the 2002-2006 period, assuming appropriation of the necessary amounts (see Table 3).

DoD reports that, in recent years, these annual accrual payments have not fully recognized the extent to which retirement outlays have been reduced as a result of the ban on concurrent receipt. The accrual payments have been too large as a result. If S. 170 or H.R. 303 is enacted before DoD has made the necessary technical corrections, then the actual increase in accrual payments that would be needed to fund the increased future annuities would be significantly less than we have estimated.

TABLE 3. ESTIMATED SPENDING SUBJECT TO APPROPRIATION FOR S. 170 and H.R. 303

	By Fiscal Year, in Millions of Dollars					
	2001	2002	2003	2004	2005	2006
DoD Payment to Military Retirement Trust Fund for Accrual Costs						
Spending Under Current Law						
Estimated Authorization Level [a]	11,430	12,230	12,737	13,270	13,797	14,328
Estimated Outlays	11,430	12,230	12,737	13,270	13,797	14,328
Proposed Changes						
Estimated Authorization Level	0	994	1,086	1,182	1,284	1,382
Estimated Outlays	0	994	1,086	1,182	1,284	1,382
Spending Under S. 170 and H.R. 303						
Estimated Authorization Level	11,430	13,224	13,823	14,452	15,081	15,710
Estimated Outlays	11,430	13,224	13,823	14,452	15,081	15,710

a. The 2001 level is the actual payment for that year; the 2002 is the estimated appropriation for that year.

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 and governmental receipts that are subject to pay-as-you-go procedures are shown in Table 4. 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.

TABLE 4. ESTIMATED IMPACT OF S. 170 and H.R. 303 ON DIRECT SPENDING AND RECEIPTS

	By Fiscal Year, in Millions of Dollars										
	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011
Changes in outlays	0	2,865	3,179	3,464	3,688	3,919	4,166	4,428	4,687	4,961	5,251
Changes in receipts	Not applicable										

INTERGOVERNMENTAL AND PRIVATE-SECTOR IMPACT

S. 170 and H.R. 303 contain no intergovernmental or private-sector mandates as defined in UMRA and would impose no costs on state, local, or tribal governments.

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