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April 27, 1995

The Honorable John McCain
United States Senate

The Honorable Jon Kyl
United States Senate

Current law requires a career military service member who retires and is disabled to offset his or her retirement pay by any disability compensation the member receives from the Department of Veterans Affairs (VA). Over the past several years, several members of the Congress have proposed bills to allow concurrent receipt of Department of Defense (DOD) longevity[1] retirement and VA disability compensation. To provide information the Congress could use in its deliberations on this matter, the National Defense Authorization Act for Fiscal Year 1993 (P.L. 102-484) required DOD to report on the cost of concurrent receipt of military retirement pay and VA disability compensation. In December 1993, DOD reported, "If full concurrent receipt were enacted, it would add $50.8 billion in present value of unfunded government liabilities."[2] In March 1994, DOD revised this estimate to $53.5 billion.[3]

Because of your concerns with the accuracy of DOD's estimate, you asked us (1) to assess the methodology DOD used in preparing its report about full concurrent receipt and (2) to provide estimates of the 1-year outlays for allowing

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[1]Military personnel are generally eligible for longevity retirement upon completion of 20 or more years of qualifying service. Service members who become physically unfit to perform their military duties are eligible for disability retirement under certain conditions and may retire with less than 20 years of service.

[2]Unfunded liability is the total amount of liability attributable to past service for which no assets have been set aside.

[3]DOD's unfunded liability estimate was revised to reflect costs associated with partial offsets for active duty personnel projected to retire.

concurrent receipt for a limited group of retirees, namely, longevity retirees with 20 or more years of service[4] who had varying levels of disability or were unable to secure substantially gainful employment (a group VA describes as "unemployable veterans").[5]

To assess the methodology DOD used to estimate the increase in unfunded liability that would result from implementation of concurrent receipt, we performed an actuarial review of specific assumptions and factors used in DOD's calculations. To develop estimates of concurrent receipt costs for longevity retirees with 20 or more years of service who had varying levels of disability or were considered to be unemployable, we obtained fiscal year 1994 data on these retirees from DOD. We did not independently verify the data. We interviewed officials from DOD and VA to discuss estimates of concurrent receipt costs under various options. Our work was conducted in accordance with generally accepted government auditing standards. We performed our work between February 1995 and April 1995.

DOD'S UNFUNDED LIABILITY ESTIMATE

We reviewed the methodology DOD used to calculate the revised estimate of a $53.5 billion increase in unfunded liability. We found that DOD generally applied reasonable assumptions and factors in developing this estimate. However, we also found that DOD incorrectly applied one assumption and as a result, may have overstated the unfunded liability estimate by up to $3 billion.

In calculating the unfunded liability for full concurrent receipt, DOD included all veterans who were receiving VA disability compensation, regardless of the number of years of service or level of disability. In fiscal year 1992, the year

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[4]As agreed with your staff, because of the lack of reliable data on combat-related disabilities, we did not estimate the cost to allow concurrent receipt for veterans with 20 or more years of service who are 100-percent disabled and have combat-related disabilities.

[5]Unemployable veterans are veterans who have disability ratings less than 100 percent (usually between 60 and 90 percent) but are compensated at the 100-percent disability rate.

on which data were based to calculate the increased unfunded liability, a total of 496,000 veterans fell into this category. Included were those who retired on longevity or disability, those on temporary disability, and those who were considered unemployable.

To estimate the increase in unfunded liability, DOD computed the present value of the annual outlays for both the current retirees and active duty personnel pension benefits. Adjustments were made for such factors as (1) pay increases, (2) percentage of personnel who will retire and when they will retire, (3) percentage of pay that is offset at retirement because of disability or other factors, (4) increases in the veterans' compensation as a result of higher disability ratings and increased numbers of current retirees who receive veterans' compensation, (5) cost of living increases, and (6) mortality.

One of the assumptions DOD made in calculating the $53.5 billion increased unfunded liability caused the estimate to be overstated. DOD assumed that the entire offset at the time of retirement was attributable to veterans' compensation when a significant portion of the offsets was attributable to other factors, such as civil service salary. Military retirement pay is subject to reductions as a result of federal civilian employment depending on the status of the retired member, the federal civilian salary, and the dates of employment. Therefore, if concurrent receipt of military retirement pay and VA compensation were allowed for this group of individuals, DOD would not incur the additional expense of the entire military retirement pay because all or part of it would be reduced by the retiree's civil service salary. For this reason, DOD's unfunded liability estimate of $53.5 billion is overstated and could be reduced by a maximum of $3 billion. Therefore, the revised unfunded liability estimate would be $50.5 billion, closer to DOD's original estimate of $50.8 billion. DOD officials agreed and told us that when they recompute the increase in unfunded liability, they will modify their assumptions to reflect the potential effects of reductions to military retirement pay as a result of civil service salaries.

We also found that the unfunded liability for full concurrent receipt may be slightly lower for fiscal year 1994 because of changes in actuarial assumptions and the number of retirees. The interest rate, cost of living adjustment, and salary assumptions have decreased since fiscal year 1992, the period on which the $53.5 billion estimate was based. The number of eligible retirees for full concurrent receipt has increased from 496,000 in fiscal year 1992 to about 520,000 in fiscal year 1994. DOD plans to recompute the unfunded liability based on the fiscal year 1994 assumptions and data in the near future. The new unfunded liability for full concurrent receipt will probably be slightly lower--between $45 billion and $49 billion.

COST ESTIMATES FOR LIMITED CONCURRENT RECEIPT

Table 1 shows the estimated cost of concurrent receipt at various disability levels for longevity retirees with 20 or more years of service.

Table 1: Concurrent Receipt Costs for Retirees With 20 or More Years' Service, Fiscal Year 1994

VA disability rating	Number of eligible retirees	Concurrent receipt cost[a] (in millions)
100%	7,493	$119.0
90	1,734	25.7
80	4,343	58.9
70	7,488	90.0
60	15,128	139.8
50	15,381	105.0
40	39,305	189.6
30	56,240	191.0
20	77,636	155.6
10	139,992	146.2
0	715	2.3
Total (0 - 100%)	365,455	$1,223.1

Note: Veterans who receive military disability retirement are not included.

[a]Additional outlays for military retirement pay that would be required in fiscal year 1994 if concurrent receipt was allowed for this group of veterans.

Table 2 shows the estimated cost of concurrent receipt at various disability levels for longevity retirees who have 20 or more years of service and are considered to be unemployable or 100-percent disabled.

Table 2: Concurrent Receipt Costs for Unemployable or 100-Percent Disabled Retirees With 20 or More Years' Service, Fiscal Year 1994

VA disability rating	Number of eligible retirees	Concurrent receipt cost[a] (in millions)
100%	7,493	$119.0
90	1,042	16.6
80	1,962	30.3
70	2,250	34.5
60	1,837	26.6
0 - 50	12	0.2
Total (0 - 100%)	14,596	$227.0

Note: Veterans who receive military disability retirement are not included.

[a]Additional outlays for military retirement pay that would be required in fiscal year 1994 if concurrent receipt was allowed for this group of veterans. Numbers do not add to total shown because of rounding.

During our efforts to obtain data on the costs of options for limited concurrent receipt, DOD and VA officials noted that while limiting concurrent receipt to a smaller universe would reduce the budgetary impact, the costs incurred under these options would likely be higher than estimated. The officials expect that allowance of concurrent receipt would encourage some veterans who are not currently listed as disabled to apply for disability benefits. Also, they believe that some veterans already receiving disability benefits would reapply for a higher disability rating. This would result in additional payments of benefits to veterans. In addition, VA officials believe that they will incur additional administrative costs in processing applications for new or revised disability ratings and benefits. Neither DOD nor VA has estimated these expected additional costs.

We discussed this letter with DOD and VA officials, and they generally agreed with its contents. We have incorporated their comments where appropriate.

As arranged with your offices, unless you publicly announce its contents earlier, we will make no further distribution of this correspondence until 7 days after the date of this letter. At that time, we will send copies to the Secretary of Veterans Affairs, the Secretary of Defense, and other interested parties.

We hope this information is useful to you. This correspondence was prepared by Irene Chu, Assistant Director; Shelia Drake; and Mark Trapani, under the direction of Carlotta Joyner, Associate Director, Federal Health Care Delivery Issues. Please contact me at (202) 512-7101 if you have any questions.

Sincerely yours,

David P. Baine

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Director, Federal Health Care
Delivery Issues

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