CONGRESSIONAL BUDGET OFFICE
COST ESTIMATE

June 18, 2004

S. 2035
Guard and Reserve Readiness and Retention Act of 2004

As introduced on January 28, 2004

SUMMARY

S. 2035 would increase health care benefits for members of the Selected Reserve, including those in the Coast Guard, by allowing them to enroll in TRICARE, the third-party insurance program for the Department of Defense (DoD). In addition, under the bill, DoD would be required to pay the private health insurance premiums for reservists called to active duty, up to the amount it would have to spend on TRICARE insurance for those activated reservists. Allowing reservists to enroll in TRICARE would affect costs in the Federal Employees Health Benefits (FEHB) program. Furthermore, under S. 2035, certain reservists would be eligible to retire earlier than under current law and also would be eligible for health care benefits associated with retirement.

CBO estimates that implementing S. 2035 would result in discretionary spending of about $1.3 billion in 2005 and $8.3 billion over the 2005-2009 period, assuming appropriation of the estimated amounts, primarily for providing health care benefits to both current and retired reservists.

In addition, CBO estimates that enacting S. 2035 would increase direct spending by about $700 million in 2005, $3.5 billion over the 2005-2009 period, and $7.0 billion over the 2005-2014 period. Most of that direct spending—$6.5 billion over the 2005-2014 period—would result from increasing military retirement benefits for members of the reserves.

S. 2035 contains an intergovernmental and private-sector mandate as defined in the Unfunded Mandates Reform Act (UMRA) because it would require both private and public-sector employers to extend the amount of time certain reservists may elect to continue their health insurance after separating from that employment. CBO estimates that the cost of extending that coverage would fall well below the thresholds established for intergovernmental and private-sector mandates ($60 million and $120 million, respectively, in 2004, adjusted annually for inflation).

ESTIMATED COST TO THE FEDERAL GOVERNMENT

The estimated budgetary impact of S. 2035 is shown in Table 1. The costs of this legislation fall within budget functions 050 (national defense), 400 (transportation), 550 (health), and 600 (income security).

TABLE 1. ESTIMATED BUDGETARY IMPACT OF S. 2035

	By Fiscal Year, in Millions of Dollars					
	2004	2005	2006	2007	2008	2009
CHANGES IN SPENDING SUBJECT TO APPROPRIATION						
Estimated Authorization Level	0	1,552	1,534	1,786	1,897	1,969
Estimated Outlays	0	1,312	1,490	1,707	1,841	1,934
CHANGES IN DIRECT SPENDING						
Estimated Budget Authority	0	698	734	718	699	678
Estimated Outlays	0	698	734	718	699	678

BASIS OF ESTIMATE

This estimate assumes that S. 2035 will be enacted before October 1, 2004, and that future appropriations will increase by the estimated amounts.

Spending Subject to Appropriation

S. 2035 would affect spending subject to appropriation by expanding health care benefits for members of the Selected Reserve and by increasing the number of retired reservists who would be eligible for health care benefits. CBO estimates that implementing the bill would cost about $1.3 billion in 2005 and $8.3 billion over the 2005-2009 period, assuming appropriation of the estimated amounts (see Table 2).

TABLE 2. ESTIMATED CHANGES IN SPENDING SUBJECT TO APPROPRIATION

	By Fiscal Year, in Millions of Dollars					
	2004	2005	2006	2007	2008	2009
TRICARE for Reservists						
Estimated Authorization Level	0	240	622	1,070	1,262	1,365
Estimated Outlays	0	193	540	968	1,204	1,329
Payments for Private Health Insurance						
Estimated Authorization Level	0	517	129	0	0	0
Estimated Outlays	0	416	189	30	5	2
TRICARE for Coast Guard Reservists						
Estimated Authorization Level	0	8	8	11	13	14
Estimated Outlays	0	6	8	10	12	14
Federal Employees Health Benefits Program						
Estimated Authorization Level	0	0	-49	-123	-207	-243
Estimated Outlays	0	0	-49	-123	-207	-243
Health Care for Military Retirees						
Estimated Authorization Level	0	462	500	496	487	482
Estimated Outlays	0	372	478	490	485	481
Accrual Payments to Military Retirement Fund						
Estimated Authorization Level	0	325	324	332	342	351
Estimated Outlays	0	325	324	332	342	351
Total Changes						
Estimated Authorization Level	0	1,552	1,534	1,786	1,897	1,969
Estimated Outlays	0	1,312	1,490	1,707	1,841	1,934

S. 2035 would affect discretionary spending by:

- Allowing members of the Selected Reserve, including the Coast Guard, to enroll in TRICARE, even if they have not been called to active duty,
- Paying a portion of the premiums for private health insurance for those members of the reserve who are called to active duty,
- Decreasing spending on the FEHB program for current federal workers,

- Increasing health care spending by DoD by allowing military reservists to retire at a younger age, and

- Increasing accrual charges paid by DoD into the military retirement fund.

TRICARE for Reservists. Section 3 would require DoD to provide expanded health care benefits to members of the Selected Reserve. Members of the Selected Reserve would be able to participate in DoD's TRICARE program with either self-only coverage or self-and-family coverage, even if the reservist has not been called to active duty. Assuming that DoD implements this program in January 2005, CBO estimates that implementing section 3 would cost $193 million in 2005 and $4.2 billion over the 2005-2009 period, assuming appropriation of the estimated amounts.

Under current law, reservists and their families can only participate in TRICARE while the reservist is called to active duty—with one exception. Current law, which expires on December 31, 2004, allows reservists who are unemployed or without employer-sponsored insurance to enroll in TRICARE, provided the reservists pay a premium equal to 28 percent of DoD's expected costs for this benefit. As of the date of this estimate, DoD has not implemented the law allowing such enrollment. Under section 3, any member of the Selected Reserve who is in an inactive status (i.e., not on active duty) would be allowed to enroll in and use TRICARE after paying a premium equal to 28 percent of the total cost of providing the insurance.

Based on data from DoD, CBO estimates that this provision would apply to about 790,000 reservists at any given time during the next five years. Using information from published studies and papers on enrollment in health insurance plans, and comparing the estimated premiums for TRICARE with the premiums in the private sector, CBO estimates that about 45 percent of reservists with dependents and about 40 percent of reservists without dependents would ultimately enroll in TRICARE under this bill. On that basis, we project that enrollment resulting from this bill would gradually increase over the first three years of the program and level off at about 300,000 reservists. Based on data from DoD, CBO estimates that in 2005 the average cost to DoD for those reservists who would purchase self-only coverage would be about $1,600 and the average cost to DoD of self-and-family coverage would be about $5,500. Enrolled reservists would pay about $600 for self-only coverage and $2,200 for self-and-family coverage.

Payments for Private Health Insurance. Section 4 would require DoD to pay a portion of private health insurance premiums for reservists called to active duty who are not enrolled in the TRICARE program. This authority would expire on December 31, 2005, and would only apply to reservists who have dependents (about 50 percent of those reservists).

Reservists without dependents would have no need for this program because reservists themselves are required to use the TRICARE program when they are on active duty. Under this provision, DoD would pay an amount equal to TRICARE's average cost of health care for the reservist and each dependent covered by the private insurance up to the total cost of the reservist's premium. Based on information from DoD, CBO estimates that the average amount DoD would pay towards private premiums would be the same as the total estimated cost of providing TRICARE for self-and-family coverage, or $7,700 in 2005.

CBO estimates that in 2005 the number of reservists called to active duty will average about 160,000 and that about 60,000 of them would receive this benefit. (The others would have no dependents, would be federal employees, or would not have private insurance.) Based on DoD's implementation of similar policies, we assume that this benefit would be paid retroactively to the day of the bill's enactment. Thus, CBO estimates that implementing this provision would cost $416 million in 2005 and $642 million over the 2005-2009 period, assuming appropriation of the estimated amounts. If the number of reservists called to active duty in 2005 differs from this estimate, the cost would change accordingly.

TRICARE for Coast Guard Reservists. The benefits described above—allowing enrollment in TRICARE by reservists who have not been activated and allowing the government to pay private insurance premiums for reservists on active duty—also would apply to the roughly 8,000 Coast Guard reservists. Accordingly, CBO estimates that implementing this benefit would cost the Coast Guard about $6 million in 2005 and $50 million over the 2005-2009 period, assuming appropriation of the estimated amounts.

Federal Employees Health Benefits Program. CBO estimates that about 120,000 reservists are also employees of the federal government and are thus eligible to participate in the FEHB program. Under S. 2035, those reservists would be able to enroll in TRICARE if they paid 28 percent of the total cost of providing their health care. Based on information from DoD and the Office of Personnel Management (OPM), CBO estimates that TRICARE premiums would be about 50 percent of FEHB premiums for self-only plans and about 75 percent of FEHB premiums for self-and-family policies. TRICARE premiums cost less because medical costs are highly correlated with age—the average reservist is age 34 while the average age for enrollees in the FEHB program (including retirees) is closer to age 60. Based on those premium differences, CBO estimates that about 13,000 reservists would switch to TRICARE in 2006; that number would grow to more than 40,000 by 2008. (CBO does not expect any reservists to switch in 2005, because it would take DoD some time to implement the new TRICARE program.)

Because the estimated health care costs for reservists switching to TRICARE are likely to be lower than the average per capita costs for all other enrollees in the FEHB program, average costs for the FEHB program would rise, even though its total costs would decline. Thus, CBO expects premiums for the remaining enrollees in the FEHB program would rise to cover the higher average cost. Based on information from OPM, CBO estimates that the average premium for remaining enrollees would rise, on average, by about $14 in 2006. (The increased premiums also would increase direct spending associated with the FEHB program, which is discussed below under the heading "Direct Spending.") CBO estimates that federal agencies would pay about 72 percent of this additional cost for an estimated 1.5 million active workers. However, those additional costs would be more than offset by savings of about $6,000 in 2006 for every reservist who would switch from the FEHB program to TRICARE. Thus, CBO estimates that implementing section 3 would, on net, lower federal spending on the FEHB program by $622 million over the 2006-2009 period.

Health Care for Military Retirees. Under S. 2035, some reservists would benefit from early retirement, and those reservists would be eligible for health care benefits offered by DoD and paid from the department's appropriation. As discussed in more detail below under the heading "Direct Spending," CBO estimates that 51,000 additional reservists from the military would retire in 2005, and that, on average, an additional 42,000 reservists a year would retire through 2014. Based on information from DoD, CBO estimates that the health care for those additional retirees and their dependents would cost an average of about $9,000 per retiree in 2005. Thus, CBO estimates that this proposal would cost $372 million in fiscal year 2005 and about $2.3 billion over the 2005-2009 period, assuming appropriation of the estimated amounts.

Accrual Payments to the Military Retirement Fund. The military retirement system is financed in part by an annual payment from appropriated funds to the military retirement fund, based on an estimate of the system's accruing liabilities. Section 2 would allow some reservists to begin receiving retirement annuities at an earlier age than under current law. If this provision were enacted, the yearly contribution to the military retirement 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 implementing this provision would increase such payments by $325 million in 2005 and $1.7 billion over the 2005-2009 period. CBO estimates that there also would be direct spending of about $6.5 billion over the 2005-2014 period for increased retirement benefits paid from the fund. (CBO's estimate of those costs is discussed below under the heading of "Direct Spending.")

Direct Spending

S. 2035 would allow certain reservists in the military and the Coast Guard to retire earlier than under current law and would allow those reservists and their dependents to receive the associated health care benefits for retirees. Retirement benefits are considered direct spending, as are health care expenditures for retirees from the Coast Guard. Health care expenditures for military retirees affected by this bill are funded with discretionary appropriations. Finally, as discussed above, allowing reservists to enroll in TRICARE would slightly increase direct spending for the FEHB program because premiums for retirees would rise. Taken together, CBO estimates that enacting S. 2035, would increase direct spending by about $700 million in 2005, $3.5 billion over the 2005-2009 period, and $7 billion over the 2005-2014 period (see Table 3).

TABLE 3. ESTIMATED CHANGES IN DIRECT SPENDING UNDER S. 2035

	By Fiscal Year, in Millions of Dollars									
	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014
Earlier Retirement for Reservists										
Estimated Budget Authority	693	718	686	648	618	602	602	609	625	658
Estimated Outlays	693	718	686	648	618	602	602	609	625	658
Health Care for Coast Guard Retirees										
Estimated Budget Authority	5	5	5	5	5	5	5	5	6	6
Estimated Outlays	5	5	5	5	5	5	5	5	6	6
Federal Employees Health Benefits Program										
Estimated Budget Authority	0	11	27	46	55	59	62	66	71	75
Estimated Outlays	0	11	27	46	55	59	62	66	71	75
Total Changes										
Estimated Budget Authority	698	734	718	699	678	666	669	680	702	739
Estimated Outlays	698	734	718	699	678	666	669	680	702	739

Earlier Retirement for Reservists. Under current law, military and Coast Guard reservists are eligible to receive retirement benefits when they have completed 20 qualifying years of service (a qualifying year, or good year, is one in which a member earned at least 50 points by participating in such activities as weekend drills, active duty and training assignments), and have reached the age of 60. Section 2 of the bill would create a sliding scale of age and years of service that would allow retirement at a younger age for reservists who attain more than 21 good years. Reservists who stopped actively participating in the reserves after completing 20 or 21 years would remain eligible for retirement benefits at age 60. However, reservists who continued to drill would be eligible to retire one year earlier for each additional two years served, up to a maximum of 14 additional years. Thus, under section 2, reservists who served for 34 qualifying years would be eligible for full retirement benefits as early as age 53.

Based on information from DoD on the distribution of years of service by age for reservists and on DoD's projections of retirement eligibility, CBO estimates that, if section 2 were enacted, 52,000 additional reservists would retire and receive retirement benefits in 2005, and, on average, an additional 43,000 reservists a year would receive retirement benefits through 2014. Reserve annuities are calculated as a percent of pay, based on the total number of points earned during a career. Annuities increase over time as the basic pay of each new cohort of retirees increases and with cost-of-living adjustments (COLAs) for those already retired. Taking both pay increases and COLA adjustments into account, CBO estimates these reservists would receive an average annual annuity that would increase from $13,500 in 2005 to $17,500 in 2014. Thus, CBO estimates that enacting the legislation would increase direct spending on retirement annuities for military and Coast Guard reservists by $693 million in 2005, $3.4 billion over the 2005-2009 period, and $6.6 billion over the 2005-2014 period.

Health Care for Coast Guard Retirees. Some of the reservists who would benefit from early retirement are members of the Coast Guard. CBO estimates that 500 additional reservists would retire in 2005, and, on average, an additional 400 reservists a year would retire from the Coast Guard through 2014. The health care costs for retirees from the Coast Guard are direct spending. Based on information from DoD, CBO estimates that health care for additional retirees and their dependents would cost an average of $9,000 per retiree in 2005, increasing to about $16,000 per retiree in 2014. Thus, CBO estimates that this proposal would increase direct spending for health care for retirees of the Coast Guard reserves by about $5 million a year. (The cost of health care for military retirees is discussed above in the section "Spending Subject to Appropriation.")

Federal Employees Health Benefits Program. As discussed above under the heading "Spending Subject to Appropriation," CBO estimates about 13,000 reservists would switch to TRICARE in 2006, with that number leveling off at more than 40,000 a year by 2008, and that the average premium for remaining enrollees in the FEHB program would rise, on average, by about $14 in 2006. The government's share of a retiree's premium (about 72 percent) is considered direct spending, and that increase would affect about 1.5 million retirees. Thus, CBO estimates that direct spending for FEHB premiums for retirees would increase by $139 million over the 2006-2009 period and $472 million over the 2006-2014 period.

INTERGOVERNMENTAL AND PRIVATE-SECTOR IMPACT

S. 2035 contains an intergovernmental and private-sector mandate as defined in UMRA. Under current law, the Consolidated Omnibus Budget Act of 1985 (COBRA) imposes a mandate on public and private-sector employers by requiring them to continue to provide health insurance coverage to certain workers who are separated from employment. Although those workers can be required to pay the employer 102 percent of the average cost of the insurance, research suggests that the actual cost of providing that coverage generally is greater than that amount.

S. 2035 would increase the amount of time those reservists who are mobilized are eligible to continue their COBRA coverage. That extension would effectively increase the cost of the existing mandate on employers to provide continued coverage. However, CBO estimates that few workers would participate and the total direct cost of that mandate to employers would be less than $5 million annually, well below the threshold established in UMRA for both intergovernmental and private-sector mandates ($60 million for intergovernmental mandates and $120 million for private-sector mandates, both adjusted annually for inflation).

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