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Reducing Cost-of-Living Adjustments for Military Retirees and the Bipartisan Budget Act: In Brief

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Summary

In addition to raising budget caps in FY2014 and FY2015, the Bipartisan Budget Act (BBA) reduced the cost of living adjustments (COLAs) provided to working-age military retirees under the age of 62 from the full Consumer Price Index (CPI) to the CPI less 1%. Military retirees would then receive a “bump-up” at age 62 that would raise their benefit level to an amount that included full rather than partial CPI adjustments for each year below the age of 62. This new benefit level would then be increased for full CPI adjustments in later years. According to CBO, this change would save the Department of Defense \$6.235 billion over the decade.

This CPI adjustment in the BBA originally applied to nearly all military retirees including those receiving military disability benefits, as well as those receiving survivors benefits. In response to concerns about potential effects, Congress restored full CPI COLA adjustments for disabled military retirees and survivors in the FY2014 Omnibus (H.R. 3547/P.L. 113-76) signed by the President on January 17, 2014. Several bills have recently been introduced that would reverse the COLA decrease for nondisabled military retirees as well. Although the reduced COLAs do not go into effect until December 1, 2015, some Members have called for action sooner.

Many of today’s nondisabled retired military are 62 or older, so the COLA adjustments in the BBA will not affect them. Most nondisability retirees under age 62 would be affected, with the greatest effect on recently retired and future nondisability military retirees, who could face reduced COLAs for 20 years or more. As a point of comparison, had disabled retirees continued to face these adjustments, the effect would have been larger because they tend to retire younger and thus would have faced COLA reductions for more years.

Those calling for a reversal for all retirees argue that retaining the full COLA adjustment is part of a commitment to servicemembers to preserve benefits, including future increases to cover inflation. Those defending the COLA adjustments argue that the effect on most retirees would be small compared to their lifetime benefits, and would moderate the rate of growth in military compensation that has occurred over the past decade.

Based on data published by the Department of Defense (DOD) Actuary about the characteristics of FY2012 military retirees and CBO projections of the CPI, CRS estimates that for the average nondisabled future retiree, lifetime retirement income under the lower COLA would be about

- \$1.67 million rather than \$1.73 million in lifetime retired pay, a \$69,000 or 4.0% reduction for enlisted personnel; and
- \$3.74 million rather than \$3.83 million in lifetime retired pay, an \$87,000 or 2.3% reduction for officers.

Had reduced COLAs been applied to future disabled military retirees, CRS estimates that their lifetime retirement income would have been reduced by \$123,000 or 9.6% for enlisted personnel and \$144,000 or 5.3% for officers.

S. 1963, which would repeal Section 403 of the Bipartisan Budget Act, was introduced on January 27, 2014. The bill does not include any offsets. On February 10, 2014, the Senate invoked cloture on the motion to proceed to S. 1963 by a vote of 94-0.

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Reducing Cost-of-Living Adjustments for Military Retirees¹

One of the offsets for raising the defense and nondefense caps in FY2014 and FY2015 in the Bipartisan Budget Act of 2013 (H.J.Res. 59/P.L. 113-67) was a reduction in the cost-of-living adjustment (COLA) for many current and nearly all future military retirees. Instead of using the full Consumer Price Index (CPI) to adjust retired pay each year, as has been customary in recent years, Section 403 of the Bipartisan Budget Act (BBA) substituted the CPI less 1% for all current and future military retirees under the age of 62 (except those already receiving reduced COLAs under the Redux retirement option).²

At age 62, beneficiaries would receive a bump-up in their benefit level to the amount they would have received had a full COLA adjustment been included each year rather than the lower COLAs. In subsequent years, this new benefit level would be adjusted using the full CPI.³ This change would have affected almost all military retirees below the age of 62, including those collecting disability retirement, as well as individuals receiving survivor benefits. The new formula would take effect on December 1, 2015.⁴ According to CBO, this change would have saved the Department of Defense \$6.235 billion over the decade.⁵

In response to concerns raised about the effect on disabled military retirees, who tend to retire younger and have shorter life expectancies, the COLA adjustments in the BBA for disability retirees and survivor benefit recipients were reversed in the FY2014 Consolidated Appropriations Act (H.R. 3547/P.L. 113-76), somewhat reducing the projected CBO savings.⁶ The new formula, as revised by P.L. 113-76, will still take effect for nondisabled retirees on December 1, 2015. Several bills have been introduced that would reverse this action for nondisabled military retirees as well.⁷

Those calling for a reversal argue that retaining the full COLA adjustment is part of a commitment to servicemembers to preserve benefits including future COLAs at the full CPI to

¹ Lawrence Kapp, Specialist in Military Manpower Policy, contributed to this report.

² §403 of H.J.Res. 59/P.L. 113-67, *Bipartisan Budget Act of 2013 and FY2014 Continuing Appropriations Act for COLA minus 1% provision*; H.J.Res. 59 amends Title 10, §1401a(b), which sets COLAs for both military retirement and survivor benefits. The CPI-W tracks price changes for urban consumers; see <http://www.bls.gov/news.release/cpi.nr0.htm>.

³ *Ibid.*

⁴ This provision would not affect “REDUX” military retirees who already receive reduced COLAs of the CPI minus 1% in return for receiving a \$30,000 bonus at 15 years of service.

⁵ CBO, “Bipartisan Budget Act of 2013 as posted on the House Rules Committee website, December 10, 2013,” December 11, 2013; <http://www.cbo.gov/sites/default/files/cbofiles/attachments/Bipartisan%20Budget%20Act%20of%202013.pdf>.

⁶ Division C, Title X, §10001 of H.R. 3547/P.L. 113-67. Savings would be about \$600 million less.

⁷ For proposals to reverse the COLA for all military retirees, see for example, S. 1963, introduced by Senator Pryor on January 27, 2014, S. 1950, introduced by Senator Bernie Sanders on January 1, 2014, H.R. 3804, introduced on December 23, 2013; see also December 2013 press conference on reversing the COLA for all military retirees held by Senators Shaheen, Wicker, and Graham as reported in *Congressional Quarterly*, “Sens. Ayotte, Wicker and Graham Hold News Conference on the Bipartisan Budget Act (H.J.Res. 59) and Military Retirees,” December 17, 2013.

offset inflation. Some servicemembers and advocates also argue that retirement changes should be delayed until the April 2015 report of Military Compensation and Retirement Modernization Commission provides a “holistic” solution.⁸

Those defending the COLA adjustments argue that the effect on most retirees would be small compared to their lifetime benefits. They also argue that the change would help restrain the growth in military compensation over the past decade.⁹ Admiral Winnefeld, Vice-Chair of the Joint Chiefs of Staff, recently suggested that these increases have “more than closed previously existing gaps with the rest of our nation’s workforce.”¹⁰ Some argue further that military retirement benefits are exceptional because servicemembers do not contribute to their basic retirement benefits, and that military personnel have also been insulated from one of the major expenses for older persons, higher health insurance premiums, because premiums for military personnel have been frozen since 1995.¹¹

Reinstating the full COLA might require offsetting savings. Although the reduced COLAs do not go into effect until December 1, 2015, in a recent hearing before the Senate Armed Services Committee, some Members called for action sooner.¹²

S. 1963, which would repeal Section 403 of the Bipartisan Budget Act, was introduced on January 27, 2014. The bill does not include any offsets. On February 10, 2014, the Senate invoked cloture on the motion to proceed to S. 1963 by a vote of 94-0.

CRS and CBO Reports on Military Retirement

For more information on military retirement, see CRS Report RL34751, *Military Retirement: Background and Recent Developments*, by David F. Burrelli and Barbara Salazar Torreon, CRS Report R42087, *Military Retirement Reform: A Review of Proposals and Options for Congress*, by David F. Burrelli, and CBO, *Costs of Military Pay and Benefits in the Defense Budget*, 11-16-12; http://www.cbo.gov/sites/default/files/cbofiles/attachments/11-14-12-MilitaryComp_0.pdf.

Demographics of Military Retirees

Based on the profile of the 1.94 million military retirees collecting benefits as of FY2012, about 40% or 750,000 would likely be affected in some way by the lower COLAs that were adopted in

⁸See transcript of hearing before the Senate Armed Services Committee, “Hearing on Changes to the Military Retirement System, Panel 1 and Panel 2,” January 28, 2014. During the hearing, arguments were made that retirement benefits of all current retirees and servicemembers should be “grandfathered,” that is, not changed.

⁹ USA Today, “Paul Ryan: Retirement pay can’t take over defense budget,” December 22, 2013.

¹⁰ For quote, see Admiral Winnefeld’s testimony to the Senate Armed Services Committee, “Hearing on Changes to the Military Retirement System, Panel 1,” January 28, 2014.

¹¹ Servicemembers do not contribute to their basic retirement benefits, which allow an active-duty military member with 20 years of service to receive 50% of their final rate of basic pay or the average of their highest 36 months of basic pay (depending on when they entered military service); see p. 3 and p. 26 in CRS Report RL34751, *Military Retirement: Background and Recent Developments*, by David F. Burrelli and Barbara Salazar Torreon. Servicemembers can also contribute to a Thrift Savings Account, but do not receive matching funds, see p. 17 and 26 in CRS Report R42087, *Military Retirement Reform: A Review of Proposals and Options for Congress*, by David F. Burrelli.

¹² See §403 (c) of H.J.Res. 59/P.L. 113-76.

the BBA and then revised by the FY2014 Consolidated Appropriations Act (which excluded about 95,000 disabled retirees).¹³

To get a picture of the potential effect of reducing the COLA by 1%, the demographic portrait in **Table 1** shows average age, years of service, and retirement benefits, with separate entries for officers and enlisted. While active-duty personnel are eligible for immediate retirement benefits after 20 years of service, reservists generally are not eligible for retirement until age 60, and so would generally be affected by the new COLA minus 1% provision for a year.

Excluding reservists, some 1.6 million military retirees currently receive benefits. For nondisabled military retirees as whole, about half are below the age of 62, and most of those would face reduced COLAs for 1 to 10 years based on DOD Actuary statistics.¹⁴

Nondisabled Retirees

Among the current retiree population, the average disabled retiree retired at age 42 after 22 years of service, receives \$30,550 in retired pay per year, and is now 62 years old. Officers generally are several years older than enlisted personnel, and receive benefits about twice as large as enlisted personnel: an average of \$51,450 vs. \$23,650 in retired pay per year. The table breaks out new FY2012 retirees because the data on them is later used to estimate effects on future retirees.

Table 1. Demographic Characteristics of Military Retirees
Excluding reservists

Category	Nondisability excluding reservists			Disability		
	Officers ^a	Enlisted	Total	Officers ^a	Enlisted	Total
Current beneficiaries as of FY2012						
Number ^b	362,205	1,108,498	1,472,087	17,256	78,619	95,910
Average current age	65.5	61.4	62.4	65.7	53.3	55.5
Average age at retirement	45.2	41.4	42.3	37.1	32.1	33.0
Average years of service	23.2	21.8	22.2	13.7	10.8	11.3
Average annual gross retired pay	\$51,456	\$23,652	\$30,552	\$37,764	\$16,116	\$20,004
No. receiving concurrent receipt ^c	na	na	na	na	na	30,579
New FY2012 Retirees						
Number ^b	9,046	23,517	32,564	625	6,281	6,909
Average current age	47.1	43.2	44.3	40.4	33.3	34.0
Average age at retirement	47.1	43.2	44.3	40.4	33.3	34.0

¹³ CRS calculation based on figures in DOD, Office of the Actuary for the composition of the FY2012 military retired population; excludes reservists, disabled military retirees, and those over the age of 61; see *Statistical Report on the Military Retirement System, Fiscal Year 2012*, p. 50-53, p. 56-57, May 2013; <http://actuary.defense.gov/Portals/15/Documents/statbook12.pdf>.

¹⁴ CRS calculation shows that 427,533 or 57% of those under the age of 62 would face 1-10 years of reduced COLAs based on the age distribution shown in the DOD Actuary, *Statistical Report*.

	Nondisability excluding reservists			Disability		
Average years of service	24.2	22.6	23	12.4	9.4	9.7
Average annual gross retired pay ^c	\$59,340	\$27,996	\$36,708	\$42,516	\$19,140	\$21,264

Sources: CRS calculations based on DOD data. See tables on pp. 50-,54, 57- 59 for average age at retirement; p. 83, 84 and 123 for average years of service; pp. 98, 99, 101, 138, and 139 for gross retired pay; and pp. 144, 154 for concurrent receipt; Department of Defense, Office of the Actuary, *Statistical Report on the Military Retirement System, Fiscal Year 2012, May 2013*; <http://actuary.defense.gov/Portals/15/Documents/statbook12.pdf>.

Notes:

- a. Includes regular and warrant officers.
- b. Total may not add because of small number of "unknowns."
- c. Includes those receiving both DOD military disability retirement and VA disability benefits because of a VA disability rating over 50% or a combat-related injury.

Based on the most recent DOD Actuary data, those servicemembers who retired in FY2012 were, on average, slightly older than those who retired in earlier years (age 44 vs. 42), with one additional year of service, and received somewhat higher average retired pay (\$37,700 vs. \$30,550) (**Table 1**). Higher average pay for the latest group may reflect a variety of factors, including pay raises above the Economic Cost Index (ECI) received in the past decade.¹⁵

Future retirees would be more affected by the lower COLAs than the current beneficiary population because they are generally younger, so the reduced COLAs would affect them for a longer period of time. The benefits of today’s older retirees would only be reduced for those under the age of 62.

Disabled Retirees

As a point of comparison, and to illustrate the effect of the original BBA, **Table 1** shows that today’s disabled retirees generally retire at 33-34 with 10-11 years of service with lower benefits. Compared to nondisabled retirees, disabled retirees generally retire some 10 years earlier, with roughly half the number of years of service, and over \$10,000 less in annual retired pay. Those retiring in FY2012 show similar characteristics (see **Table 1**).

The congressional decision to exempt disabled retirees from the lower COLAs may reflect, in part, the fact that disabled retirees generally retire at younger ages, meaning that lower COLAs would affect them for a longer period of time, and that their benefits are lower as well. In addition, the life expectancy for disabled retirees is about 8 years below that of nondisabled retirees, meaning that there would have been fewer years after 62 with full COLA benefits had the original BBA remained in effect.¹⁶ Because of these two factors, disabled retirees would have experienced a greater loss of retirement income than nondisabled retirees.

These demographic factors help explain why lower COLAs would be expected to have greater effects on disabled retirees. In addition, enlisted disabled personnel would have been more

¹⁵ CRS Report RL33446, *Military Pay and Benefits: Key Questions and Answers*, by Lawrence Kapp; see p. 6ff or history of military pay raises since 1993; military pay raises in FY2000-2010 generally exceeded the Economic Cost Index (ECI) by ½% or more.

¹⁶ Life expectancy table for disabled retirees was provided by DOD Actuary, January 2014.

affected than disabled officers in percentage reductions to their income, because their retirement income is considerably lower (see **Table 1**).

Potential Effects on Military Retirees

If FY2012 retirees are representative of future retirees, then those currently retired would be less affected than future retirees because of the demographic characteristics described above.¹⁷ Similarly, disabled retirees would have been more affected than nondisabled retirees had the original BBA remained in effect. To estimate the effects on both current and future retirees, CRS used DOD Actuary data about average age, retirement income, and life expectancy for nondisabled and disabled military and CBO's projections of the CPI. To project the effect on future retirees, CRS used DOD Actuary statistics about those who retired in FY2012, the most recent data available.

Current Nondisabled Retirees

On average, lifetime retirement benefits for the current retiree population are about \$590,000 for enlisted personnel and \$1.37 million for officers based on DOD Actuary figures and CBO projections of Consumer Price Index (CPI).¹⁸ The average age of nondisabled current retirees is 61 for enlisted and 66 for officers, suggesting that many retirees would not be affected by reduced COLAs or would be subject to lower COLAs for fewer years than future retirees.

As a point of comparison, had the COLA adjustment for current disabled military retirees in the BBA remained in effect, the average enlisted disabled retiree, with an average age of 53, would have received \$13,000 or 3% less in lifetime benefits of \$390,000. For disabled officers, with an average age of 66, few would experience reductions in lifetime benefits of \$440,000.¹⁹ Disabled retirees who are younger than this average would have been affected by larger amounts and those older by lesser amounts.

Future Nondisabled Retirees

Future military retirees would be more affected than current retirees. Generally in their early 40s, the average future retiree would receive reduced COLAs for about 18 years until the age of 62. To estimate the effect on future nondisabled military retirees, CRS calculated average lifetime retirement income for enlisted and officer retirees with a full CPI adjustment and with the CPI less 1% as set in the Bipartisan Budget Act.

CRS based its calculations of the effect on future nondisabled retirees using the DOD Actuary's data on the characteristics of those who retired in FY2012—average age, retirement income, and life expectancy—and CBO's projections of the CPI. These estimates exclude reservists and

¹⁷ FY2012 retirees are likely to be more representative of future retirees than the current retiree population, which is generally older and receives somewhat higher retirement income (see **Table 1**).

¹⁸ Retirement benefits are often referred to as "retired pay."

¹⁹ CRS calculation based on DOD, Office of the Actuary, *Statistical Report on the Military Retirement System*, p. 56-59 and p. 144 and CBO, *The Long-term Budget Outlook*, FY2013-FY2023, 9-17-13; <http://www.cbo.gov/publication/44521>.

reflect the bump-up to full-COLA retired benefits at age 62 and full CPI adjustments for the remainder of a retiree’s life as provided in current law.²⁰

Under these assumptions, the average nondisabled military retiree could be affected by the lower COLAs as follows.

- Enlisted personnel would receive a total of about \$1.67 million rather than \$1.73 million in lifetime retirement benefits, a \$69,000 or 4.0% reduction in a 36-year period;
- Officers would receive a total of \$3.74 million rather than \$3.83 million in lifetime retired pay, an \$87,000 or 2.3% reduction in a 36-year period (see **Table 2**).²¹

For nondisabled enlisted retirees, the estimate reflects an average where servicemembers joined the military at age 21, retired at age 43, and would receive reduced COLAs for 18 years when they would reach the age of 62 in FY2034, and then full COLAs for the rest of their lives. DOD Actuary figures project a life-expectancy of 79 for these nondisabled, enlisted military retirees (see **Table 2** below).

For nondisabled officer retirees, the average reflects servicemembers who joined the military at age 23, retired at 47, reached the age of 62 in FY2030, and received full COLAs for the rest of their lives. The DOD Actuary projects a life expectancy of 84 for the average officer.

Table 2. Estimated Effect of Reduced COLA on Average Lifetime Retirement of Future Military Retirees:

Nondisability and Disability, Officers and Enlisted, Excluding Reservists

Category	Nondisability excluding reservists	Disability
Enlisted^a		
Lifetime retirement at full CPI for COLA	\$1.73 million	\$1.29 million
Effect of CPI less 1% till age 62 COLA in \$	-\$69,000	-\$123,000
Lifetime retirement at CPI minus 1% till age 62 in \$	\$-1.67 million	\$1.16 million
Effect of reduced COLA as % of total	-4.0%	-9.6%
Officers^b		
Lifetime retirement at full CPI	\$3.83 million	\$2.74 million
Effect of CPI less 1% till age 62 COLA in \$	-\$87,000	-\$144,000
Lifetime retirement at CPI minus 1% till age 62 in \$	\$3.74 million	\$2.60 million
Effect of reduced COLA as % of total	-2.3%	-5.3%

Sources: For average age at retirement, average pay, and life expectancy for military retirees, enlisted and officers for those retiring in FY2012, see tables on pp. 83, 84, 149, and p. 175 in DOD, Office of the Actuary, *Statistical Report on the Military Retirement System, Fiscal Year 2012*; <http://actuary.defense.gov/Portals/15/Documents/statbook12.pdf>. For Consumer Price Index projections, see

²⁰ See Table 2 for sources and notes.

²¹ This estimate assumes lifetime expectancy of 77 for enlisted and 84 for officers based on DOD Actuary data.

supplementary material in CBO, *The FY2013 Long-Term Budget Outlook*, 9-17-13; <http://www.cbo.gov/publication/44521>.

Notes: CRS assumed that life expectancy for military disability retirees was 10 years below nondisabled retirees as shown in the DOD Actuary report for FY2012.

- a. For nondisabled enlisted retirees, the average reflects servicemembers who joined the military at age 21, retired at age 43, receive reduced COLAs for 18 years until the age 62 in FY2034. At age 62, retirees would then receive a bump-up to retirement pay reflecting full COLA adjustments in earlier years and then full COLAs thereafter, and lived until age 79. For disabled enlisted retirees, the average reflects servicemembers who enlisted at 24, retired at 33 after 9 years of service, reached 62 in FY2044, and live until age 71, or 8 years less than nondisabled retirees. All these figures reflect DOD Actuary figures for those who retired in FY2012.
- b. For nondisabled officers, the average reflects servicemembers who joined the military at age 23, retired at 47, reached 62 in FY2030, received a bump-up to retired pay reflecting full COLA adjustments in earlier years, and then full COLAs thereafter, and live till age 84. For disabled officers, the average reflects servicemembers who joined at age 28, retired at 40 after 12 years of service, reached 62 in FY2037, and live until age 77, 8 years less than nondisabled retirees. All these figures reflect DOD Actuary figures for those who retired in FY2012.

Current Disabled Retirees

As a point of comparison, had the lower COLAs been applied to disabled retirees as originally required by the BBA, the effect on these retirees would have been greater than for nondisabled retirees because disabled servicemembers tend to retire at younger ages resulting in more years with a reduced COLA. In addition, with an average life expectancy of eight years less than nondisabled retirees, disabled retirees would have had fewer years with full-COLA benefits (**Table 1**). Because the average disabled retiree is 55 rather than 62, the majority of currently disabled retirees would have experienced several years of reduced COLAs had the original BBA remained in effect.

Future Disabled Retirees

As a point of comparison and to illustrate the effect of the original BBA, CRS used DOD Actuary estimates of the effect on future disabled retirees. Based on those data, CRS estimated that lifetime retired benefits for the average disabled military retiree would have been affected as follows if the reduced COLAs had remained in effect.

- Enlisted personnel would have received about \$1.16 million rather than \$1.29 million, a reduction of \$123,000 or 9.6% in lifetime benefits received over a 37-year period;
- Officer personnel would have received about \$2.60 million rather than \$2.74 million, a decrease of \$144,000 or 5.3% in lifetime benefits received over a 38-year period (see **Table 2**).²²

Reflecting DOD Actuary data, the estimate above reflects an average disabled enlisted retiree who joined the military at 24, retired at 33 after 9 years of service, and lived until the age of 71.

²² This estimate assumes that life expectancy for disabled military retirees is eight years less than for nondisabled retirees based on a table provided by the DOD Actuary, and higher life expectancy for officers than enlisted.

The comparable average disabled officer retiree would have begun service at the age of 28, retired at 40 after 12 years of service, and lived until the age of 77.

These estimates suggest that had disabled military retirees been subject to the reduced COLAs in the original BBA, the potential effect would have been about double that faced by nondisabled retirees (**Table 2**). These estimates, however, do not include income that about one-third of disabled retirees would receive in additional Combat Related Special Compensation (SRSC) or Veterans Administration (VA) disability benefits. Under concurrent receipt, certain disabled military retirees can receive CRSC or VA disability benefits in addition to their DOD retirement benefits if their disability was combat-related or assessed as 50% or greater.²³

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²³ The DOD Actuary report indicates that a total of 30, 579 of the 95, 610 disability retirees receive both military retired pay and VA disability benefits because of a disability rating of 50% or more or a combat-related injury which makes them eligible for combat related special compensation (see table on p. 192).