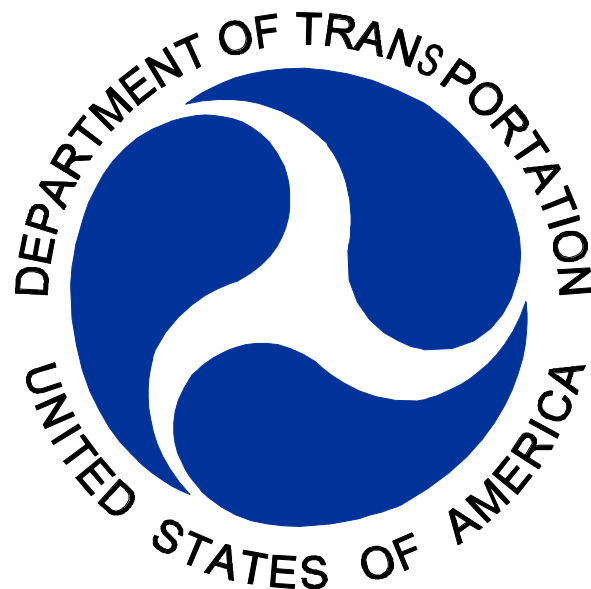

Office of Inspector General

*Management Advisory Memorandum on
Actuarial Estimates for U.S. Coast Guard
Retired Pay and Health Care Cost*

Report Number: AD-CG-7-003

Date Issued: April 4, 1997

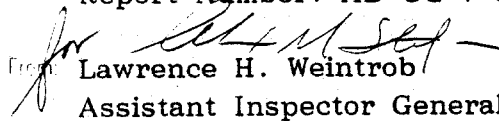




Memorandum

U.S. Department of
Transportation
Office of the Secretary
of Transportation
Office of Inspector General

Subject: INFORMATION/ACTION: Management Advisory Date: April 4, 1997
Memorandum on Actuarial Estimates for U.S.
Coast Guard Retired Pay and Health Care Cost
Report Number: AD-CG-7-003

For: 
Lawrence H. Weintrob
Assistant Inspector General for Auditing

Reply To:
Attn Of: JA-20:x61496

To: Chief of Staff
United States Coast Guard

This management advisory memorandum is to provide you the study results of the United States Coast Guard (USCG) actuarial model for estimating liabilities for retired pay (attachment). This study was conducted by Hay/Huggins Company under contract with the Office of Inspector General as part of our audit of the Department of Transportation's (DOT) Fiscal Year (FY) 1996 Consolidated Financial Statement. The principal objective of the study was to determine whether the methodology used by the USCG contractor to calculate liabilities and annual actuarial activity of the USCG military retirement system was reasonable and reliable as of September 30, 1995.

Overstated Liabilities - Retired Pay

The Hay/Huggins study showed USCG reported actuarial liability for military retired pay was overstated by about \$1 billion. This variance occurred because the USCG contractor did not update its actuarial model to reflect changes in key assumptions upon which the model was based.

Understated Liabilities - Health Care

The requirement for reflecting an actuarial estimate for retired health care cost on the FY 1996 Consolidated Financial Statement was not clearly defined in the Office of Management and Budget guidance for preparing FY 1996 financial statements. The USCG thought this actuarial estimate was not required until FY 1997 when Statement of Federal Financial Accounting Standards Number 5 becomes effective, and was not aware a similar requirement was contained in Statement of

Standards Number 106. Therefore, USCG did not obtain a separate actuarial estimate for retired health care cost.

The estimated understatement for retired health care cost could be at least \$3.5 billion. This estimate was based on a ratio of USCG active and retired military personnel to the Department of Defense (DoD) active and retired military personnel. This ratio was applied to the DoD actuarial estimate.

We are making five recommendations based on the Hay/Huggins Company report, and the need to recognize liabilities for retired health care cost.

Recommendations

We recommend the Coast Guard Chief of Staff:

1. Review all actuarial assumptions including a comparison of the active and retired populations to the DoD military active and retired populations.
2. Recognize all offsets to retired benefit payments and the liability for former spouse benefits.
3. Change the economic and mortality assumptions to those used by DoD for the USCG FY 1997 actuarial estimate.
4. Change the salary growth assumptions to more closely represent the actual promotion and merit increases for active duty members.
5. Ensure the FY 1996 Consolidated Financial Statement includes an estimate for retired health care cost and that a valid actuarial estimate for retired health care cost is completed in FY 1997.

Management Response

We discussed the results of the actuarial study with USCG officials on March 10, 1997. The USCG concurred with the recommendations and said the necessary actions would be taken for the FY 1997 actuarial estimates. The USCG also revised the FY 1996 Consolidated Financial Statement to reflect a net increase of \$2.5 billion in the line items "Pensions and Other Actuarial Liabilities" and "Future Funding Requirements," and made a note disclosure on how the health care cost estimate was derived.

Office of Inspector General Comments

The USCG action to reflect the health care cost estimate on the FY 1996 Consolidated Financial Statement was appropriate, and resulted in a more accurate presentation of future cost for retired pay and health care cost.

In accordance with DOT Order 8000.1C, please provide your written comments within 60 days identifying the specific corrective actions taken or planned, and estimated target completion dates for each recommendation.

I sincerely appreciate the cooperation of USCG officials. If you have any questions, please call me at x61992, or James Childers at x66120.

Attachment

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