

June 20, 2001

Honorable Jim Nussle
Chairman
Committee on the Budget
U.S. House of Representatives
Washington, DC 20515

Dear Mr. Chairman:

Section 314 of the Concurrent Resolution on the Budget for Fiscal Year 2002 (H. Con. Res. 83) expresses the sense of the Congress that the Congressional Budget Office should report “on the risk that provision of full concurrent receipt of military retired pay and disability compensation would reduce the surplus below the level of the Medicare Hospital Insurance (HI) trust fund.” This letter answers that request.

CBO published its most recent baseline budget projections in *An Analysis of the President's Budgetary Proposals for Fiscal Year 2002*, which was issued in May 2001. Assuming that annual appropriations would increase at the rate of inflation and that laws governing revenues and mandatory spending would remain unchanged, CBO estimated that on-budget surpluses would total \$3.1 trillion over the 2002-2011 period. Since that time, the Congress passed and the President signed into law the Economic Growth and Tax Relief Reconciliation Act of 2001 (Public Law 107-16), which is estimated to decrease tax revenues and increase outlays, including increased debt-service costs, by a total of \$1.7 trillion over the 10-year period. After incorporating the effects of the tax bill into the May 2001 baseline, CBO estimates the on-budget surplus for the 2002-2011 period will total \$1.5 trillion (see Table 1). That amount includes an HI trust fund surplus estimated to total \$397 billion over the 2002-2011 period. Thus, under baseline assumptions, CBO estimates the on-budget surplus excluding the HI trust fund will total \$1.1 trillion over the 10-year period.

CBO recently completed its estimate of S. 170 and H.R. 303, identical bills that would allow total or partial concurrent payment of retirement annuities together with veterans' disability compensation to retirees with service-connected disabilities. The bills would apply to retirees from the military, the Coast Guard, the Public Health Service, and the National Oceanic and Atmospheric Administration. The legislation also would discontinue special compensation for certain severely disabled retirees from the uniformed services. CBO estimates that enacting this legislation would increase direct spending for retirement payments and veterans' disability compensation by about \$41 billion over the 2002-2011 period (see Table 2). In addition, the Department of Defense would have to make payments of about \$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 and would represent an intragovernmental transfer to provide for future retirement benefits.

Taken by itself, in the context of CBO's baseline projections, concurrent receipt of military retirement pay and disability compensation, as specified in either S. 170 or H.R. 303, would not reduce the on-budget surplus below the level of the HI trust fund. The legislation would cost \$3 billion to \$5 billion a year, and the projected on-budget surpluses (excluding HI) are \$26 billion or more in every year after 2001.

However, it should be recognized that future legislation could alter the paths of federal spending and revenues, thereby reducing projected on-budget surpluses. In addition, the budget is affected by many economic and technical factors that are difficult to predict. Such developments could result in on-budget deficits or in on-budget surpluses much larger than CBO currently projects.

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I hope this information is helpful to you. If you wish further details on this matter, we will be pleased to provide them. The CBO staff contacts are Sarah T. Jennings for the proposal concerning military retirees and Jeffrey M. Holland for budget projections.

Sincerely,

Dan L. Crippen
Director

Enclosures

cc: Honorable John M. Spratt Jr.
Ranking Democratic Member

Honorable Bob Stump
Chairman, Committee on Armed Services

Honorable Ike Skelton
Ranking Member

Honorable Christopher H. Smith
Chairman, Committee on Veterans' Affairs

Honorable Lane Evans
Ranking Democratic Member

Identical letter sent to Honorable Kent Conrad

TABLE 1. PRELIMINARY ESTIMATE OF THE EFFECT OF THE ECONOMIC GROWTH AND TAX RELIEF RECONCILIATION ACT OF 2001 (PUBLIC LAW 107-16) ON CBO'S BASELINE PROJECTIONS
(By fiscal year, in billions of dollars)

	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	Total 2002- 2011
May 2001 Baseline Surplus Projections												
On-budget	119	132	166	197	215	270	322	366	425	495	553	3,142
Off-budget	<u>156</u>	<u>172</u>	<u>187</u>	<u>202</u>	<u>221</u>	<u>238</u>	<u>256</u>	<u>275</u>	<u>293</u>	<u>311</u>	<u>330</u>	<u>2,487</u>
Total	275	304	353	400	437	508	578	641	718	806	883	5,629
On-Budget Surplus Excluding HI	92	95	125	155	173	225	279	324	385	459	525	2,745
Estimated Effect of Public Law 107-16^a												
Revenue reductions	-70	-31	-84	-101	-100	-126	-142	-151	-158	-176	-117	-1,186
Refundable tax credits (outlays)	4	6	7	7	7	10	10	9	10	11	12	89
Debt service	<u>2</u>	<u>5</u>	<u>8</u>	<u>14</u>	<u>21</u>	<u>29</u>	<u>38</u>	<u>49</u>	<u>61</u>	<u>74</u>	<u>87</u>	<u>385</u>
Total Effect on Surplus	-76	-43	-99	-122	-128	-164	-190	-209	-229	-261	-217	-1,660
May 2001 Baseline Surplus Projections Incorporating Effect of Public Law 107-16												
On-budget	44	90	67	76	88	107	132	157	197	234	336	1,484
Off-budget	<u>156</u>	<u>171</u>	<u>187</u>	<u>202</u>	<u>221</u>	<u>238</u>	<u>256</u>	<u>275</u>	<u>293</u>	<u>311</u>	<u>330</u>	<u>2,484</u>
Total	200	261	255	278	309	345	388	432	489	545	666	3,968
On-Budget Surplus Excluding HI	16	52	26	33	46	62	90	116	157	198	308	1,087
Memorandum:												
HI Surplus	28	38	41	43	42	45	43	42	40	36	28	397

SOURCE: Congressional Budget Office.

NOTE: HI = Hospital Insurance.

a. The Economic Growth and Tax Relief Reconciliation Act of 2001.

TABLE 2. ESTIMATED OUTLAYS FROM S. 170 OR H.R. 303 COMPARED WITH ON-BUDGET SURPLUSES, EXCLUDING HI (By fiscal year, in billions of dollars)

	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	Total 2002- 2011
Estimated additional outlays from S. 170 or H.R. 303	0	3	3	3	4	4	4	4	5	5	5	41
Estimated on-budget surpluses (excluding HI) in the absence of such legislation	16	52	26	33	46	62	90	116	157	198	308	1,087

SOURCE: Congressional Budget Office.

NOTE: HI = Hospital Insurance.