



GAO

Accountability * Integrity * Reliability

United States Government Accountability Office
Washington, DC 20548

July 15, 2009

Congressional Committees

Subject: *Coast Guard Retiree Health Care: Coast Guard Contributions to and Payments from the DOD Medicare-Eligible Retiree Health Care Fund (MERHCF)*

This letter formally transmits the enclosed briefing slides in response to 154 Cong. Rec. H9801 (daily ed. Sept. 24, 2008) (Explanatory Statement accompanying H.R. 2638, Consolidated Security, Disaster Assistance, and Continuing Appropriations Act, 2009, Pub. L. No. 110-329, 122 Stat. 3574 (Sept. 30, 2008)). The briefing slides provide information about the process used to determine the amount charged to the Coast Guard for Medicare-eligible retiree health care and amounts paid from the MERHCF for health care benefits provided to Coast Guard retirees for fiscal years 2006 through 2008.

We are sending copies of this report to the appropriate congressional committees. We are also sending copies to the Secretary of Defense, the Assistant Secretary of Defense for Health Affairs, the Secretary of Homeland Security, and the Commandant of the Coast Guard. In addition, the report will be available at no charge on GAO's Web site at <http://www.gao.gov>. Should you or your staff have any questions concerning this report, please contact me at 202-512-9095 or dalykl@gao.gov. Contact points for our Offices of Congressional Relations and Public Affairs may be found on the last page of this report. Key contributors to this report were Kimberly Brooks (Assistant Director), Diane Morris, Donell Ries, and Melanie Swift.

Kay L. Daly
Director
Financial Management and Assurance

Enclosure

List of Congressional Committees

The Honorable Robert C. Byrd
Chairman

The Honorable George V. Voinovich
Ranking Member
Subcommittee on Homeland Security
Committee on Appropriations
United States Senate

The Honorable David E. Price
Chairman

The Honorable Harold Rogers
Ranking Member
Subcommittee on Homeland Security
Committee on Appropriations
House of Representatives



**Coast Guard Contributions to and
Payments from the DOD Medicare-Eligible
Retiree Health Care Fund (MERHCF)**

**Briefing for Staff of the House and Senate
Subcommittees on Homeland Security, Committees
on Appropriations**

June 30, 2009

Overview

- Background
 - Objectives
 - Scope and Methodology
 - Process for Determining Coast Guard's Annual Contribution Amount
 - Determining the Annual Contribution Rate
 - Determining the Annual Contribution Amount
 - Annual Amounts Contributed by Coast Guard and Other Uniformed Services for Fiscal Years 2006-2009
 - Health Care Benefits Paid from MERHCF
-

Background

- MERHCF was established by the Floyd D. Spence National Defense Authorization Act for Fiscal Year 2001 in order to pay for health care benefits received by Medicare-eligible retirees of the uniformed services and their eligible dependents and survivors.
 - Uniformed services refer to both Department of Defense (DOD) uniformed services (Army, Navy, Air Force, Marines) and non-DOD uniformed services (Coast Guard, Public Health Service (PHS), and National Oceanic and Atmospheric Administration (NOAA)).
-

Background

- Health care benefits include
 - Purchased Care—care from civilian providers,
 - Direct Care—care from DOD military treatment facilities, and
 - Uniformed Services Family Health Plan (HMO-like plan).
 - The DOD and non-DOD uniformed services make annual contributions into the MERHCF for the cost of future health care benefits associated with service rendered after October 1, 2002.¹
 - Contribution amounts for all uniformed services are determined by the DOD Office of the Actuary. Funding for the contribution amounts is included in each uniformed service's appropriation.
-

Objectives

We performed this work in response to a mandate related to the Consolidated Security, Disaster Assistance, and Continuing Appropriations Act, 2009, Pub. L. No. 110-329, 122 Stat. 3574 (Sept. 30, 2008).

Our objectives were the following:

1. Describe the process for determining Coast Guard's annual contribution into the MERHCF and report the amounts contributed during fiscal years 2006 through 2009.
 2. Report the amounts paid from the MERHCF for health care benefits provided to Coast Guard Medicare-eligible retirees for fiscal years 2006 through 2008, the last year for which data is available.
-

Scope and Methodology

To address the objectives we

- interviewed knowledgeable agency officials and others from
 - DOD Office of the Actuary,
 - Defense Finance and Accounting Service,
 - DOD's TRICARE Management Activity,
 - Coast Guard, and
 - discussed with the auditors of the MERHCF financial statements their work related to amounts paid from the MERHCF for health care benefits.
-



Scope and Methodology

- We reviewed relevant documents and data such as
 - MERHCF audited financial statements,
 - Office of the Actuary's valuation reports, and
 - DOD's TRICARE Management Activity (TMA) payment schedules and reports.
 - We conducted a reasonableness test of TMA's health care payment data by comparing TMA data to the MERHCF financial statements.
 - We did not independently verify the amounts.
-

Scope and Methodology

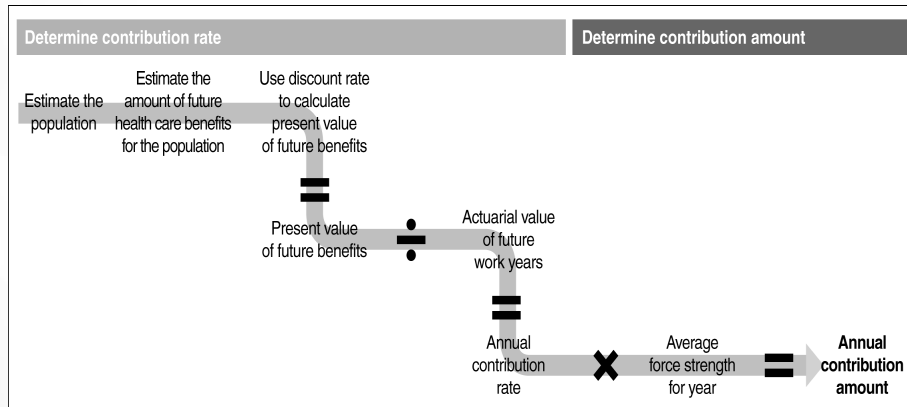
- We conducted our work from March 2009 to June 2009 in accordance with all sections of GAO's Quality Assurance Framework that are relevant to our objectives. The framework requires that we plan and perform the engagement to obtain sufficient and appropriate evidence to meet our stated objectives and to discuss any limitations in our work. We believe that the information and data obtained, and the analysis conducted, provide a reasonable basis for our work.
-



Process for Determining the Coast Guard's Annual Contributions to MERHCF

- DOD actuaries are required by law to use the aggregate entry-age normal cost method to determine annual contribution amounts.²
 - The contribution rate is derived by dividing the present value of future benefits by the actuarial value of future work years. This contribution rate is then multiplied by the average force strength for the year to produce each service's contribution amount.
 - Full-time and part-time rates are determined for active duty and reserves, respectively.
-

Process for Determining the Coast Guard's Annual Contributions to MERHCF



Source: GAO analysis of DOD information.



Determining the Annual Contribution Rate

Contribution Rate = *Present Value of Future Benefits* ÷ *Actuarial Value of Future Work Years*

Determining the present value of future benefits

1. Estimate the population of future Medicare-eligible retirees and their eligible dependents and survivors.
 - The actuaries use an assumed number of new entrants into active duty and the reserves, as required by the aggregate entry-age normal cost method.³
 - The actuaries use a population-projection model that applies various assumptions⁴ over a 100-year period to project the status of the new entrants into the future through their careers into retirement until they and all of their dependents and survivors are deceased.



Determining the Annual Contribution Rate

Contribution Rate = *Present Value of Future Benefits* ÷ *Actuarial Value of Future Work Years*

2. Estimate future health care benefits for the retiree population.
 - The actuaries use historical data on payments from the MERHCF for health care benefits provided to all uniformed services.
 - The payment data⁵ includes purchased care received at civilian health care providers and direct care⁶ received at military treatment facilities for inpatient stays, outpatient visits, and prescription drugs. Also included are amounts paid to Uniformed Services Family Health Plan facilities for Medicare-eligible retirees.

 3. Calculate the present value of the future benefits using the approved discount rate.
-



Determining the Annual Contribution Rate

Contribution Rate = Present Value of Future Benefits ÷ *Actuarial Value of Future Work Years*

- Determining actuarial value of future work years
 - When the status of the new entrants is being projected, the same model also calculates the number of service members remaining on active duty at year-end for each year during the 100-year period.
 - The actuaries use an assumed value of \$1 per work year for the first year of the 100-year period. The \$1 per work year rate increases in subsequent years based on assumed increases in medical costs, mix, and utilization. The stream of future work years valued this way is discounted using the approved discount rate to get the actuarial value of future work years.⁷



Determining Annual Contribution Amount

Contribution Rate × Average Force Strength = Contribution Amount

- The **contribution rates** determined by the actuaries for fiscal years 2006-2009 were
 - fiscal year 2006: full-time rate = \$5,652; part-time rate = \$3,324,
 - fiscal year 2007: full-time rate = \$6,048; part-time rate = \$3,516,
 - fiscal year 2008: full-time rate = \$5,988; part-time rate = \$3,441, and
 - fiscal year 2009: full-time rate = \$5,560; part-time rate = \$3,222.

 - Average force strength data is submitted to the DOD Office of the Actuary annually by each uniformed service.

 - Coast Guard's **average force strength** data used to calculate its contribution amount for fiscal years 2006 through 2009 were
 - fiscal year 2006: active duty = 41,332; reserves = 8,100,
 - fiscal year 2007: active duty = 41,373; reserves = 8,100,
 - fiscal year 2008: active duty = 40,788; reserves = 8,100, and
 - fiscal year 2009: active duty = 41,587; reserves = 8,100.
-



Amounts Contributed to MERHCF by the Coast Guard and Other Uniformed Services for Fiscal Years 2006-2009

Service	Contribution amount (thousands)			
	Fiscal year 2006	Fiscal year 2007	Fiscal year 2008	Fiscal year 2009
DOD	\$10,775,392	\$11,230,630	\$11,185,399	\$10,350,593
Coast Guard	260,533	278,704	272,111	257,322
PHS	34,477	36,288	36,647	34,778
NOAA	1,645	1,820	1,802	1,674
Total	\$11,072,047	\$11,547,442	\$11,495,959	\$10,644,367

Source: DOD Office of the Actuary.



Health Care Benefits Paid from MERHCF

- MERHCF payments for purchased care are based on bills submitted by civilian providers and pharmacies.
 - For medical care, claims are filed by the doctor or hospital and sent to a Medicare contractor. The claim is forwarded to TRICARE Management Activity for remaining amounts due after Medicare and any private insurance have paid. MERHCF funds are also used to pay administrative claims-processing fees.
 - For prescriptions from retail pharmacies, claims are filed by the pharmacy and sent to a claims-processing contractor who pays the pharmacy with MERHCF funds. MERHCF funds are also used to pay administrative claims-processing fees.
-



Health Care Benefits Paid from MERHCF

- For prescriptions from the mail-order pharmacy, TRICARE Management Activity uses MERHCF funds to pay the contractor for administrative processing fees and to pay the Defense Logistics Agency, which supplies the drugs.
- MERHCF payments for care obtained from Uniformed Services Family Health Plan providers are made on a monthly basis based on contract-specific capitation rates.⁸



Health Care Benefits Paid from MERHCF

- MERHCF payments for direct care are based on estimates.
 - TRICARE Management Activity (TMA) uses historical workload data to develop estimates of the level of effort at each military treatment facility (MTF) that was devoted to Medicare-eligible members.
 - TMA determines the direct care amounts for MTF operations and maintenance that should be assigned to the inpatient stays, outpatient visits, and prescription drugs for MERHCF beneficiaries and the appropriate portion of amounts for military labor/personnel associated with health care delivered to MERHCF beneficiaries.
 - The MERHCF financial statement auditors have reported weaknesses in the underlying processes used to derive direct care amounts for fiscal years 2006 through 2008. The auditors reported that there is insufficient evidence that adequate controls exist and have been implemented to ensure the completeness, validity, recording, and cut-off of the direct care amounts reported.
-



Amounts Paid from MERHCF
 (dollars in millions)
UNAUDITED

	Fiscal year 2006		Fiscal year 2007		Fiscal year 2008	
	Coast Guard	All services	Coast Guard	All services	Coast Guard	All services
PURCHASED CARE						
Inpatient and outpatient claims	\$30.8	\$2,157.0	\$34.1	\$2,375.7	\$37.6	\$2,543.7
Prescription drugs	40.0	2,706.8	44.2	2,940.5	48.5	3,078.4
US Family Health Plan	19.0	475.0	21.4	527.1	23.7	568.0
Total Purchased Care Payments	\$89.8	\$5,338.8	\$99.7	\$5,843.3	\$109.8	\$6,190.1
DIRECT CARE						
Inpatient and outpatient claims	6.6	962.6	7.8	944.7	7.9	989.5
Prescription drugs	7.5	771.5	7.9	814.3	8.0	810.2
Total Direct Care Payments	\$14.1	\$1,734.1	\$15.7	\$1,759.0	\$15.9	\$1,799.7
TOTAL PAYMENTS FROM MERHCF	\$103.9	\$7,073.9	\$115.4	\$7,602.3	\$125.7	\$7,989.8

Source: DOD TRICARE Management Activity.

Endnotes

¹The MERHCF also receives annual funding from the Department of the Treasury to pay the liability related to the cost of the portion of retiree health care benefits attributable to service rendered prior to October 1, 2002, and to cover any actuarial gains and losses due to changes in assumptions, benefits, and experience since October 1, 2002. This amount comes from the General Fund.

²This is an actuarial cost method designed to fund a member's total health care benefits over the course of his or her career. Entry age is the earliest age at which a member begins to accrue health care benefits. In most cases, this is assumed to be the date of hire or entry.

Endnotes

³The assumed number of new entrants used by the actuaries is 100,000 for active duty and 20,912 for the reserves. The 100,000 is an arbitrary number that, according to the DOD actuaries, is large enough to produce reasonable results when projecting the status of the new entrants throughout their career and into retirement. The actuaries have used 100,000 since the establishment of the MERHCF. The assumed number of new entrants into the reserves--20,912--is derived based on the 100,000 active duty new entrants.

⁴Assumptions based on historical data about changes in DOD active duty and retiree populations, both enlisted and officers, represent probabilities of a new entrant leaving a category of military service for a specific cause such as active duty and retiree deaths, temporary or permanent disability retirements, nondisability retirements, withdrawals, and transfers between enlisted and officer status.

Endnotes

⁵The actuaries use 3 years of payment data to determine expected average family benefit payment amounts for a given year per retiree, by retiree age and category. The retiree categories are (1) retired, nondisabled, active duty, enlisted; (2) retired, nondisabled, active duty, officer; (3) retired, disabled, active duty, enlisted; (4) retired, disabled, active duty, officer; (5) retired, nondisabled, reserve, enlisted; (6) retired, nondisabled, reserve, officer; (7) survivor of active duty enlisted; (8) survivor of active duty officers; (9) survivor of reserve enlisted; and (10) survivor of reserve officer.

⁶The MERHCF financial statement auditors have reported weaknesses in the underlying process used to derive direct care costs; existing cost accounting systems do not have the capacity to record or generate cost data for each patient and the processes used to identify costs at the patient level could not be verified.

Endnotes

⁷The actuaries assume a normal cost based on a contribution starting at \$1 per work year and increasing thereafter with medical trends. This assumption is made to assign a monetary value to the work years so that the value of future work years can be expressed in present value the same as the future benefits. This enables the actuaries to calculate a normal cost rate each year that covers a portion of the future health benefits for each group of new entrants.

⁸Capitation is a payment method for health care services. The physician, hospital or other health care provider is paid a contracted rate for each member assigned, regardless of the number or nature of services provided.



GAO Contacts and Staff Acknowledgments

GAO Contact Kay Daly, (202) 512-9095

Acknowledgments In addition to the contact named above, staff members who made key contributions to this report include Kimberly Brooks (Assistant Director), Diane Morris, Donell Ries, and Melanie Swift.

(195144)

This is a work of the U.S. government and is not subject to copyright protection in the United States. The published product may be reproduced and distributed in its entirety without further permission from GAO. However, because this work may contain copyrighted images or other material, permission from the copyright holder may be necessary if you wish to reproduce this material separately.

GAO's Mission

The Government Accountability Office, the audit, evaluation, and investigative arm of Congress, exists to support Congress in meeting its constitutional responsibilities and to help improve the performance and accountability of the federal government for the American people. GAO examines the use of public funds; evaluates federal programs and policies; and provides analyses, recommendations, and other assistance to help Congress make informed oversight, policy, and funding decisions. GAO's commitment to good government is reflected in its core values of accountability, integrity, and reliability.

Obtaining Copies of GAO Reports and Testimony

The fastest and easiest way to obtain copies of GAO documents at no cost is through GAO's Web site (www.gao.gov). Each weekday afternoon, GAO posts on its Web site newly released reports, testimony, and correspondence. To have GAO e-mail you a list of newly posted products, go to www.gao.gov and select "E-mail Updates."

Order by Phone

The price of each GAO publication reflects GAO's actual cost of production and distribution and depends on the number of pages in the publication and whether the publication is printed in color or black and white. Pricing and ordering information is posted on GAO's Web site, <http://www.gao.gov/ordering.htm>.

Place orders by calling (202) 512-6000, toll free (866) 801-7077, or TDD (202) 512-2537.

Orders may be paid for using American Express, Discover Card, MasterCard, Visa, check, or money order. Call for additional information.

To Report Fraud, Waste, and Abuse in Federal Programs

Contact:

Web site: www.gao.gov/fraudnet/fraudnet.htm

E-mail: fraudnet@gao.gov

Automated answering system: (800) 424-5454 or (202) 512-7470

Congressional Relations

Ralph Dawn, Managing Director, dawnr@gao.gov, (202) 512-4400
U.S. Government Accountability Office, 441 G Street NW, Room 7125
Washington, DC 20548

Public Affairs

Chuck Young, Managing Director, youngc1@gao.gov, (202) 512-4800
U.S. Government Accountability Office, 441 G Street NW, Room 7149
Washington, DC 20548