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Testimony

Before the Subcommittee on Military Personnel,
Committee on National Security, House of Representatives

For release on Delivery
Expected at
10:00 a.m., EDT,
Thursday,
May 8, 1997

RESERVE FORCES

Observations on the Ready Reserve Mobilization Income Insurance Program

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Mr. Chairman and Members of the Subcommittee:

I am pleased to be here today to discuss the Ready Reserve Mobilization Income Insurance Program and the Department of Defense Inspector General's (DOD IG) review of that program. Reserve forces are recognized as essential to the nation's defense, as evidenced by the increased use of these forces over the past several years. Because of this increased use, the Congress and DOD have been concerned about the potential adverse impacts of financial losses that some reservists endure when activated and the ability of DOD to continue recruiting and retaining the quantity and quality of people needed to maintain readiness in the reserve components. These concerns led to the development of the insurance program to help protect reservists and their families against financial losses resulting from extended mobilizations.

Let me first provide a short overview of our role and some observations about the program at this time, and then go back to provide more details.

Summary of Our Efforts to Date

As agreed with the Subcommittee, we have not independently reviewed the Ready Reserve Mobilization Income Insurance Program or met with DOD officials to verify the accuracy of the IG's work. Rather, our role has been to help ensure that the IG's examination of the program adequately addressed the Subcommittee's concerns. To that end, we reviewed the IG's audit plan, obtained background information and key documents related to the program, observed several DOD working group meetings where problems in the program were discussed, and obtained two briefings from the IG staff.

The IG staff incorporated several of our suggestions into their audit plan, and we believe that they used a reasonable methodology in their review to address the Subcommittee's concerns. The IG staff briefed us on their preliminary results, and they seem to address the Subcommittee's concerns. However, we also told the IG staff that we could not offer a final opinion until we have had an opportunity to review their report, which they have not yet completed.

Because of our limited work, we can make only a few observations about the program.

- DOD estimated that about 40 percent of the eligible reservists would enroll in the program, but less than 3 percent actually did. The low enrollment

rate raises a key question about the extent of the need for the program. Although previous studies showed that many reservists suffered economic losses and would be interested in an income insurance program, very few actually enrolled when the program was offered. While there is some evidence that DOD did not market the program as effectively as possible, this alone cannot explain the low enrollment rate.

- Because of the low enrollment, which limits the amount of premiums paid into the insurance fund, and because many of those who did enroll suspected, or possibly knew, they would be activated for the ongoing Bosnia operation, the program is not self-sustaining, as intended. Many reservists activated for duty in Bosnia began to receive benefits almost immediately after enrolling in the program. The program is expected to be \$72 million in the red by September 1997. The legislation allows DOD to seek a supplemental appropriation from the Congress to cover funding shortfalls.
- Because enrollment in the program is a one-time opportunity that most reservists have already declined, the existing program cannot significantly improve its viability through increased premium income from new enrollees, at least in the near term.
- The program is not actuarially sound because of the unpredictability of future reserve call-ups, including the frequency of call-ups, their duration, and the number and types of reservists that might be needed.

Our observations tend to support DOD's recent proposal to suspend the program and reexamine the need for it and to consider possible alternatives to meet the needs of reservists and their families.

Background

According to DOD, a survey of a sample of reservists activated during Operation Desert Storm indicated that about two-thirds suffered economic losses. These losses occurred because (1) military pay was less than civilian income, (2) additional expenses were incurred by reservists and their families as a result of the activation, and (3) financial losses continued after release from active duty due to erosion of the reservists' businesses or practices. According to the survey, economic losses were widespread across all pay grades and military occupations. However, health care practitioners, self-employed professionals, and others with relatively high civilian incomes were most likely to have suffered income losses.

Because of concerns over the impact of such losses on reservists and their families, the Congress, in 1996, directed DOD to establish an optional,

self-funded income insurance program for members of the Ready Reserve who are ordered involuntarily to active duty for more than 30 days.¹

DOD implemented the program, called the Ready Reserve Mobilization Income Insurance Program, on October 1, 1996. The program is managed by the Secretary of Defense, and the premiums paid to the Ready Reserve Income Insurance Fund are administered by the Treasury Department. Reservists who elected to enroll in the program during the one-time, 60-day enrollment period could choose monthly coverage options ranging from \$500 to \$5,000 for up to 12 months within an 18-month period. The monthly premium rate is \$12.20 for each \$1,000 of insurance coverage purchased.

Far fewer reservists than DOD expected enrolled in the program. On the basis of surveys performed for DOD to assess the need for an income insurance program, DOD had estimated that 40 percent of eligible reservists would enroll in the program. However, less than 3 percent actually enrolled. Moreover, shortly after signing up for the insurance, many of those that did enroll were activated for duty in Bosnia and, therefore, were entitled to almost immediate benefits from the program. According to DOD, 65 percent of the reservists activated for the third rotation to Bosnia purchased the insurance. For these reasons, the program did not have sufficient funds to pay the benefits due to the activated enrollees. Because the program precludes deficit spending from the insurance fund, DOD has to date paid the activated enrollees only about 4 percent of the amount due. DOD estimated that about \$72 million is required to fund full benefit payments through the end of fiscal year 1997.

Request to Review the Program and Our Role

On January 9, 1997, you asked our office to review this program to assess the need for the program, DOD's implementation of the program, and the program's actuarial soundness. As we began planning for the review, we learned that the DOD IG had already begun a detailed examination of the program. In a meeting on January 24 with the Subcommittee's staff, DOD IG representatives, and our office, it was agreed that, to avoid possible duplication, the IG would continue its review and we would participate, to the extent necessary, to ensure that the Subcommittee's concerns were addressed.

¹See section 512, the National Defense Authorization Act for Fiscal Year 1996 (P. L. 104-106, Feb. 10, 1996).

On January 28, we completed a memorandum of agreement with the IG that outlined our respective roles. Basically, the agreement called for the IG to perform the review and for us to review their audit guidelines, receive periodic updates, have access to key documents, attend key meetings with DOD officials, and review the IG's draft report when completed. The essence of the agreement was detailed in a February 10, 1997, letter to you.

We and the IG have complied with the agreement. For example, we reviewed the IG's proposed audit guidelines and found that they represented a reasonable approach to addressing the Subcommittee's concerns. However, we identified a couple of areas where we believed additional audit tasks were needed. For example, we believed that the IG needed to explore further the need for the program, which would include an analysis of recruitment and retention statistics in the reserve components over the past several years. We also believed that they needed to do more work than had been planned to document what went wrong with the program, what were the causes for the problems, and whether DOD could have done anything differently to avoid the problems.

On March 4, we shared our concerns with the IG staff and provided them a copy of our proposed guidelines. On March 10, we discussed the guidelines further, and IG representatives agreed to incorporate our guidelines into their review.

During the review, we met twice with the IG staff to be updated on their progress. Also, we attended several DOD working group meetings where DOD officials debated the continued need for the program and options for making the program more fiscally sound. In addition, the IG staff shared with us key DOD documents related to the program. When the IG's draft report is completed and made available to us, we will review it and provide comments. In keeping with the spirit of our agreement and also to avoid duplication, we did not independently meet with DOD officials or other affected parties to verify any data. As we deemed appropriate, we raised questions to the IG team and relied upon their judgment in pursuing the questions with DOD officials.

Our Observations About the Program

During the course of our ongoing coordination and consultations with the IG staff about the program, we have had opportunities to make the observations that I have already discussed. I would like to offer more support for our observations. For example, two documents we reviewed in particular impressed me not only as warning DOD of the potential for

program problems, but also as summing up key issues that must be addressed as the program's future is debated. These documents were prepared by the DOD Education Benefits Board of Actuaries in August 1995 and August 1996. Minutes of the Board's August 1995 meeting generally discussed and an August 1996 letter specifically expressed the following four concerns about the mobilization income insurance program:

- Benefit payments are caused by mobilizations that are infrequent but that produce large numbers of claims. The program could easily be exhausted by unfavorable experience in the early years despite a premium rate that would be adequate over a longer period.
- Mobilizations depend on the changing world situation and the role of the reserves, which may vary substantially from previous mobilizations that were used to compute premium rates.
- Because of their military specialty or because activation seems likely, reservists who perceive a substantial risk of activation will enroll in greater numbers and buy more insurance.
- The Bosnia call-up appears likely to extend beyond October 1, 1996, when the insurance program begins. Although reservists then on active duty are ineligible for the program, others who replace them can purchase insurance and trigger substantial benefits in fiscal year 1997. Such outlays may immediately endanger the fund.

Since the enactment of the mobilization insurance program, all of the Board's concerns have been realized. Based upon discussions with the IG staff, we understand that they also believe that because of the unpredictability of the size and frequency of future reserve component mobilizations, designing an actuarially sound program may not be possible. The IG staff also said that because of the way the program was structured, there was little, if anything, DOD could have done to change the adverse outcome.

We agree that once the program was initiated in October 1996, there was little DOD could have done to change the outcome. However, it appears that the concerns noted in the Board's letters were not fully addressed. In view of the Board's concerns, we believe DOD could have discussed the issues with the Congress prior to program implementation to determine whether the implementation date or other provisions in the program needed to be modified. However, to our knowledge, this step was not taken.

As the future of the program is debated, I think several issues need to be addressed. One issue is the extent to which the program is needed. The information currently available is contradictory. On one hand, earlier studies indicated a significant need for a program to address the economic hardships many reservists endure when called to active duty. Previous surveys performed for DOD showed that the majority of reservists that served in Desert Storm endured economic losses and were interested in purchasing mobilization income insurance if such a program were available. For example, in one survey, 77 percent indicated that they either were interested or might be interested in paying for such insurance, even at a cost of \$10 monthly for each \$1,000 of coverage. Also, DOD was concerned after Desert Storm that many reservists would leave the military because of the income losses endured during extended mobilizations.

On the other hand, when the program was offered during the fall of 1996, less than 3 percent of the eligible reservists purchased the insurance, and many enrolled because they believed, or possibly knew, that they would be activated for Bosnia and receive almost immediate benefits from the program. Furthermore, according to DOD officials, reserve component recruiting and retention rates have remained stable since the Persian Gulf War. Further, the military services have not voiced strong support for a mobilization income insurance program.

Assuming there is sufficient reason to have a program addressing the loss of income for many activated reservists, a second issue is whether improved marketing of the program can significantly increase enrollment. There is some evidence that DOD did not market the program as effectively as possible. For example, in telephone surveys recently done by RAND, as many as 27 percent of the reservists contacted stated that they were never informed of the program. An additional 16 percent stated that they were informed of the program but did not have sufficient detailed information or time to make an informed decision about program enrollment.

With better marketing, more of these reservists might have enrolled in the program. However, there is uncertainty that more effective marketing would result in a sufficient level of voluntary participation for the program to be self-sustaining. For example, the RAND survey data can also be interpreted to indicate that the majority (57 percent) of eligible reservists were aware of the program. Yet, for reasons that have not been determined, only a small percentage of these individuals—much lower than the 40-percent estimated—actually enrolled. To increase

participation, DOD has discussed options to make at least a portion of the program mandatory. However, such a step would involve a significant policy decision, one in which the pros and cons would need to be weighed very carefully.

Another issue is whether a mobilization income insurance program can be actuarially sound. To be actuarially sound, an insurance program must contain a large number of enrollees and assurance that a predictable majority of these enrollees will not incur the losses that they insure against. Yet, the current program does not include a large number of enrollees, and DOD's increased reliance on reserve component forces in a changing and unpredictable world situation makes projections of the frequency, duration, and size of future call-ups exceedingly difficult. It is also our understanding that primarily for these reasons, private insurers have stated that they would not be interested in underwriting the program.

In conclusion, although we have not done an independent review of the program, I think it is fair to say that the program is not self-sustaining under its current design and with its current low enrollment. Thus, it seems prudent to suspend the program while DOD reexamines the need for and possible alternatives to the program.

This concludes my prepared remarks. I would be happy to respond to any questions the Subcommittee might have.

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