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Establishing the U.S. Navy Pension Plan

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Chapter 4
Establishing the U.S. Navy Pension Plan

From the earliest days of the American colonies and subsequently the new republic, American naval personnel were promised pension benefits if they were injured in the service of their colony or nation. This chapter begins with a review of the establishment of military pension plans by the Continental Congress for seamen during the war for independence. Next, the analysis focuses on how these early pension plans were then superseded by a pension plan for the regular navy of the new United States. The history of the navy pension plan as explored in this and the following four chapters provides considerable background material for understanding the subsequent evolution of employer pension plans and Social Security in the United States as well as in other countries

Pension Plans for Naval Personnel Before 1800

In November 1775, only months after the onset of the American Revolution, the Continental Congress established a pension plan for naval personnel to be paid out of a fund financed by the sale of "prizes" captured by the Revolutionary navy. These prizes were either ships of war or merchantmen of belligerent states or neutral merchantmen carrying contraband. In theory they constituted legitimate military targets under the generally accepted though unwritten international laws of war and admiralty. As we discussed in the previous chapter, this method of funding the early naval pension plan is quite important in understanding naval compensation in general and naval pensions in particular, and it illustrates how pensions have been used to provide performance incentives. Specifically, because the officers and crews received a share of the value of the prize, the prize system rewarded seamen according to their success in identifying and capturing prizes, and it was this relationship among pension benefits, funding methods, and performance incentives that we seek to highlight throughout much of this volume.

The initial navy pension plan was actually a disability plan. With the exception of the Pennsylvania navy during the Revolution, American seamen were not eligible for retirement pensions until the nineteenth century, though, as will become apparent below, the early disability plans were eventually converted to old-age pensions. The first Continental navy plan paid $400 in a lump sum, roughly one year's salary, to a ship's commander in the event he should be disabled and the same to his widow should he be killed. Subordinate officers and their widows received proportionally smaller amounts.[1] The 1775 pension plan and the fund from which pensions were to be paid did not survive the war. Detailed searches of primary sources have not located any systematic records pertaining to the operation of this initial pension plan, and in any case the 1775 plan was replaced by a new pension plan established by the general pension act of August 1776, which also covered army personnel (see Chapter 8 below).

At least part of the reason the 1775 plan did not survive is that the pension fund from which benefits were to be paid was never properly established in the first place. The legislation that created the navy pension plan specified that officers and seamen were to be paid from prize monies, *even if no prizes were taken during the action in which they were disabled.* Thus, if prizes were taken in the action that produced the disability, some of the monies from the liquidation of prizes and contraband could be set aside for the pensions of deserving seamen. But what if a seaman was disabled in an action that did not produce prizes? Implicitly, the legislation meant that there had to be a reserve fund established to provide funds for the payment to at least some of the men disabled in naval service. Whether the Congress failed to recognize this or whether the fund simply was not established before the pension plan was revised in 1776 has not been determined. In any case, the lack of funding, the relatively high promised benefits, and the pressures of an expanding war soon led to the termination of this initial naval pension plan.

The 1776 plan specified that if an officer, seaman, or marine were completely disabled during an engagement in which no prize was taken, then the individual was to receive one-half of his monthly pay for the term of his disability. If the seaman was not completely disabled but nevertheless could not continue his naval service, he was to receive a reduced pension, with the actual amount of the pension determined by the legislature of the state in which he resided. If the seaman were disabled in an engagement in which a prize was taken, then his share of the prize was subtracted from the value of his pension. Exactly how this was done is not altogether clear. Theoretically, one could calculate the present value of the pension annuity, subtract the seaman's share of the prize or prizes captured during the voyage on which he was disabled, and then reconvert the remainder into an annuity. The few accounts of Revolutionary pensions that can be found in the records of the colonial governments do not suggest that this procedure was used, at least not explicitly. Subsequent legislation in 1778 extended the benefits of the 1776 plan to officers and men disabled prior to the plan's introduction. This expansion in coverage meant that the disability claims under the 1775 plan were honored, at least nominally.

Like its precursor, the 1776 plan ran into problems as a result of the failure of the Continental Congress to provide sufficient funds for benefit payments to claimants. Although the two plans were funded differently, they both collapsed because of inefficient administration and cumbersome administrative structures. The fundamental problem was that, although Congress authorized the plans and payments to veterans, the colonies (or states, as they soon became) were given the responsibility for administering them. Unfortunately, this scheme ran into the same three obstacles that frustrated the new government's financial solvency until the administration of federal public finance was reorganized during the first Washington administration. These general administrative problems were (1) the financial status of the states was as bad as that of the federal government; (2) the various administrative structures overseeing naval affairs were a morass of conflicting lines of authority; and (3) Congressional actions could only be carried out if states passed the necessary enabling legislation.

First, with respect to state finances, the financial condition of the state governments was generally as precarious as that of the federal government, if not more so. Hence any claims against a state were likely to compete for very scarce funds with a host of other military and civil claims. Thus, the federal mandates requiring state spending often went unmet. The inability or unwillingness of the states to pay Continental pensions was partly the result of genuine fiscal distress and partly the result of the reluctance by local legislators to take responsibility for imposing the taxes required to satisfy the political wishes of the federal government, such as it was. None of the colonies was in a position to finance a war with the British empire. Although in theory they might have possessed the tax base to maintain a rebellion, they did not possess the requisite bureaucratic infrastructure for administering the public finances that such a tax base could, again theoretically, support. As a result, a kind of public finance triage occurred in the face of war. Navy pensions did not survive, at least not in their original form.

Second, the administration of the Continental navy was, to put it politely, cumbersome. For several months after the Revolution began, there was no Continental navy. There were naval forces attached to George Washington's army. These forces, which persisted after the formal establishment of the Continental navy in October of 1775, were thereafter, and appropriately enough, known as "Washington's navy." Shortly after the navy was created, a seven-member Naval Committee was created to administer the assets of the new navy. The members of the committee were appointed by Congress and given the charge of providing nominal oversight of naval affairs. The Marine Committee subsequently replaced, or as one naval historian puts it "absorbed," the Naval Committee. The new committee consisted of one representative from each colony. The Marine Committee created two administrative groups that were intended to simplify the management of naval affairs. Navy Boards were created in the key ports of Boston and Philadelphia, and these boards oversaw the financial transactions of the Marine Committee and subsequent executive committees. In addition, prize agents responsible for the liquidation of prizes captured by the Continental navy or Continental privateers were established to oversee the disbursement of monies that resulted from the prize system. At the same time, various Naval Agents managed the day-to-day operations in American ports, and finally, the Naval Office in Paris largely administered affairs outside the colonies. While in theory these offices were created to more effectively administer the sea war, the Marine Committee was a frequent target of both the Congress and the armed forces, with its cumbersome structure among the main complaints. As a result, the Board of Admiralty, consisting of two members of Congress and three "public members," replaced the committee in October of 1779. In practice, the lines of authority and the relationships between these governmental units were poorly defined, if they were defined at all. Specifically, it was often unclear which unit was primarily responsible for acquiring ships, stores, and men.

Overall, this administrative structure, and the confusion wrought by the winds of war, yielded a public finance morass. After it replaced the Marine Committee in 1779, the Board of Admiralty ordered the naval boards and agents to present naval accounts, receipts, invoices, and other documents for review. However, "Owing to the loose methods of business which obtained during the Revolution, the agents of the Board [of Admiralty] found it in most cases impossible to make such statements" concerning naval finances based on the accounts available (Paullin 1906). Congress recognized that naval finances and accounts were in a state of near hopeless disorder. In an effort to consolidate the management of naval affairs, an attempt was made in February 1781 to appoint a Secretary of Marine to oversee the administrative reforms of naval affairs. The person chosen for this task was Major General Alexander McDougall, who demanded, as a condition of appointment, that he be permitted to maintain his office and rank in the Continental army while serving as secretary. For reasons perhaps having as much to do with the personalities involved as philosophical commitments to a separation of powers, such an arrangement was unacceptable to Congress, and McDougall was dropped from consideration. In the summer of 1781, Robert Morris, then Superintendent of Finance, assumed the financial responsibilities for naval affairs. In September of that year, he was named Agent of Marine, an office he held until November 1784. In this dual capacity, Morris, who earned the sobriquet "Financier of the Revolution," effectively served as minister of finance and secretary of the navy for the nascent republic, at least in an administrative sense. He soon began the thorny process of reorganizing naval finances, including pension liabilities.

The third problem with the pension act of 1776 was related to the fact that it directed the states to pay federal pensions to their seaman serving in the Continental navy. However, before the actual payment of the pension benefits could be made, the states themselves were required to establish an infrastructure for administering Continental navy pensions. Thus, the funding of naval pensions became an issue of dispute between the states and the federal government that had to be resolved before the payment of pensions could begin. These differences were not meaningfully settled until Alexander Hamilton's financial reforms in the 1790s. Actually, the pension accounts were not finally settled for more than a century. As late as 1905, South Carolina and other states were still prosecuting Revolutionary naval claims against the U.S. government (Paullin 1906). Further complicating this administrative structure was the fact that most of the colonies maintained their own naval forces, which were separate from those of the Continental Congress. All of the colonies except Delaware and New Jersey maintained some naval forces. Between May 1777 and June 1782, Connecticut, Pennsylvania, Virginia, and Maryland passed legislation authorizing the payment of naval pensions to officers, marines, and seamen serving in either their navies or to their citizens serving in the Continental navy, or to both. Ultimately, the U.S. Congress assumed responsibility for the payment of the Revolutionary navy's pensions benefits.

Like other Western naval forces over the past millennium or so, a key component of the early Continental navy compensation in general and pensions in particular was the share of the prize that was allocated to the crew. In November 1775, the Continental Congress, attempting to provide "encouragement" to sailors to more efficiently complete their assignment, declared that one-half of all ships of war and one-third of merchantmen and other ships, such as transport and stores vessels, were reserved as compensation for the officers and crews that captured them.[2] A few weeks later the Congress further revised naval regulations (and established the aforementioned pension plan). Among these revisions were the specifications that the man who originally spotted a prize would receive a double share of the prize money, the man who first boarded a prize would receive a treble share, and an additional ten shares were to be divided among those men whom the officers thought most deserving.

The legislation of 1775 also established prize courts, or at least it requested that every colony establish a prize court, with the Congress serving as a court of appeals. It also established sanctioned privateering by the Continental government. As we saw in the previous chapter, privateers had been around for centuries. They were essentially, licensed pirates who in exchange for their license agreed to limit their predatory activities to enemy ships and contraband carried by neutrals. Privateers were to receive

100 percent of the net prize. Since privateers received 100 percent of their prizes, it would at first appear that no one would join the Continental navy when they could be privateers. But there were at least three features of regular naval service that might induce one to join the navy rather than become a privateer. For one thing the navy paid, or at least promised to pay, regular wages on top of the prize share. For another, the privateers were often manned by, shall we say, those at or beyond the fringes of decent society. Among the many features of privateering that might not appeal to everyone was the privateer's reputation for mistreating individuals who fell into their hands. Finally, regular naval forces did not accord captured privateers the same respect and treatment that they extended to their counterparts in the regular navy. Privateers were on occasion hanged from a yardarm with impunity. Taken together, these features suggest that privateering may not have been for everyone.

In addition to these features of the act, Congress specified that the division of prizes captured by the naval forces of the colonies should be the same as those of the Continental navy. Making the situation even more interesting was the fact that officers could, and did from time to time, "pay out" the more liquid components of prizes before those cases were officially adjudicated. Although typically in violation of both a country's explicit military code of conduct and the unwritten, though in many cases no less explicit, laws of war, officers were known to appease their men with the fruits of a prize before its full value was determined in a prize court. Since the rulings of prize courts were risky and because the disbursement of prize monies could take long periods of time, the seamen's loyalty and effort could often be had at a discount. This type of activity probably occurred much more often than the official records suggest.

In any case, the original plan for distributing prizes was subsequently altered, and prize monies were explicitly reallocated under legislation of January 1776. All prizes accruing to the officers and crew were divided into twenty shares. The commander-in-chief received one-twentieth (or one share), the captains of the fleet two-twentieths, the officers of the ship eight and one-half shares, and the men were to equally divide the remaining eight and one-half shares. In October of that year, Congress increased the shares going to the officers and crews to one-half of merchantmen and 100 percent of ships of war and British privateers. Since merchantmen were less well armed and would be laden with valuable cargo, as opposed to the less valuable sinews of war found upon a ship of the line or enemy sloop, they were preferred pickings among naval forces. Recall Napoleon's characterization of his admirals' preferences. So Congress found it expedient to induce the navy to go after ships of war as opposed to those of commerce.

Eventually, the specifications concerning the allocation of monies from prizes captured by the navies of the colonies were revoked in March 1776. Thereafter, each colony could establish its own rules, and it turned out that there was considerable variation across colonies. For example, Massachusetts returned only one-third of the prize to the officers and men whereas Pennsylvania allowed the crews to keep two-thirds.

As seen earlier, historically naval compensation was based on deferred or backloaded payments and "piecework." The promise of a pension was the deferred component; while the prizes seized by the crew's own efforts represented a form of piecework. Thus, it was only natural that these two features would be combined and that naval pensions would eventually be funded from prize monies. From its inception, the pension plan for U.S. naval personnel was to be funded from assets purchased from the sale of naval prizes. As a result, the flow of prize monies did not always match the pension plan's liabilities. The lack of actuarial assessments linking the inflow of assets to the liabilities, coupled with the political (and financial) pressures faced by Congress and its responses to those pressures, made for a rather colorful history of the post-Revolution U.S. navy pension plan. Furthermore, the experiences of the navy pension plan provide numerous lessons for contemporary pension policy. In the following section and subsequent chapters, this history is described and analyzed in an effort to compare policy choices of the nineteenth century to those of the twenty-first century.

Establishing the Navy Pension Plan

Although the Continental navy eventually went the way of the navy pension plan, after the Constitution was ratified Congress eventually created a U.S. navy. From its earliest days, the United States government authorized separate pension systems for the army and naval forces. Congress created the first pension plan for the "regular" or "standing" *army* in 1790. Between 1794 and the creation of the Department of the Navy in 1798, naval personnel were covered under the U.S. army pension plan. Under this plan, benefits were paid from annual appropriations. The creation of a separate navy department complicated the administration of navy pensions. Since congressional appropriations went to specific departments, in essence, or perhaps it should be said in a bureaucratic sense, the army was asked not only to administer navy pensions but to pay them as well. Given the rivalry and occasional outright hostilities between the services, this arrangement was probably untenable in the long run.

Further complicating matters was the economics of navy compensation during this era. The important role that incentive-based compensation played in ameliorating the incentive to shirk by naval personnel was discussed in Chapter 3. Traditional military pay was not likely to be an efficient method of compensation for an eighteenth-century navy. In March 1799, Congress eased the bureaucratic complications associated with having the army administer navy pensions by establishing a separate administration for the payment of navy pensions. In the following year, Congress addressed the fundamental moral hazard in naval compensation and created a funded navy pension plan that was once again to be funded with the monies from captured prizes.

The revisions to these pension plans in the 1790s maintained the essential features of the original plan: officers' benefits were not to exceed half-pay, while those for seamen and marines were not to exceed $5.00 a month. These were annuities to be paid during the period of disability. When the fund from which these benefits were to be paid actually began disbursing payments in 1801, 18 years after the Treaty of Paris formally ended the Revolutionary War, there were 22 navy pensioners, and the average annual payment per recipient was $72.95. Because of the fundamental reorganization of the republic's finances, which was largely the work of Alexander Hamilton, this navy pension plan was to have a substantially longer life than its antecedents. A growing economy, a funded debt, a sound currency, and a national bank all contributed in various ways to public finances of the United States, and ultimately some combination of these features would be required to ensure the soundness of the navy pension plan. In the short run, however, it was the fortunes of the navy in its quest for prizes that determined the success, such as it was, of the plan.

The Constitution granted Congress the authority "To provide and maintain a navy [and]: To make rules for the government and regulation of the land and naval forces." However, when the Constitution was ratified, the United States had no navy. The last armed vessel of the Continental navy, the frigate *Alliance*, had been sold in 1785 (Paullin 1906). The U.S. Navy was not formally established until 1794, when Congress authorized the construction of six new frigates. At that time, it also began the recruitment of officers and men. The first three frigates, *Constitution*, *Constellation*, and *United States*, were commissioned in 1797. Beginning in 1794, there were 1,856 uniformed personnel in the navy. An additional 83 marines were added the year the ships were launched.[3] In the age of sail, the marines served three purposes: They represented something of a constabulary aboard ship; they aided in firing upon and boarding other ships (and repelling boarders when the situations were reversed); and they could be used in land operations mounted from ships.

The act of 1799, which established a navy pension plan separate from the one controlled by the army, explicitly stated that officers, marines, and seamen injured in the line of duty were entitled to a disability pension. The benefit for officers was not to exceed half-pay while the pension for marines and seamen was not to exceed $5.00 a month. To give the reader a feel for the size of this benefit, consider that in 1812, a captain in the U.S. navy earned $100 per month and "eight rations"—essentially a payment in kind; seamen earned $10 per month. For both types of personnel, the benefit was to be based on the length and extent of the disability. The legislation also authorized the establishment of a separate navy pension *fund* from which pensions were to be paid. The navy pension fund itself was established in 1800. Like the initial Revolutionary navy pension plan of 1775, the navy pension plan began as a disability pension plan; however, it also eventually evolved into a retirement plan. Like the early pension plans for naval personnel, this fund was to be financed by the sale of prizes.

Two additional aspects of the U.S. navy pension fund should be mentioned. First, the monies in the fund were to be used for the exclusive benefit of navy personnel and their families, and second, if these monies were insufficient to provide promised benefits, the U.S. Treasury was to honor the pension liabilities. These points were made clear in the ninth section of the enabling legislation, which stated that:

> all money accruing, or which has already accrued to the United States from the sale of prizes, shall be and remain forever a fund for the payment of pensions and half pay, should the same be hereafter granted to the officers and seamen who may be entitled to receive the same; and if the said fund shall be insufficient for the purpose, the public faith is hereby pledged to make up the deficiency. But, if it should be more than sufficient; the surplus shall be applied to the making of further provision for the comfort of the disabled officers, seamen and marines, and for such as, though not disabled, may merit, by their bravery or long and faithful services, the gratitude of their country. (*American State Papers, Naval Affairs,* 1934, 4: no. 529; hereafter *ASP-NA*)

Note carefully the wording of the legislation. If the pension should experience windfalls, then those could be applied to "further provision for the comfort" of the beneficiaries, but if the fund proved "insufficient for the purpose," then the public—that is, the taxpayers—stood behind the fund's liabilities. The subsequent history of the fund would test the limits of these words.

The basic characterisitics of the naval pension plan are consistent with the economic model of military pensions described in Chapter 2. Furthermore, the emergence of a fund coincided with a period in which opportunities for seizing prizes were expanding because of rising tensions with the French, which marked a transition from revolutionary times. Under the doctrine that the enemy of an enemy is a friend, the ancien régime in France had supported the colonists in the American Revolution. Unfortunately for the champions of that policy, financing the American fight for independence drove the French crown to the brink of insolvency. The French had not yet adopted the principle of the separation of crown and state finances, the efficacy of which the British had discovered during their own civil war more than a century earlier. As a result, attempts at fiscal reform by the crown accelerated the political forces that ultimately produced the French Revolution.

As the Convention was deposing Louis XVI, and as France was engaged in a war with Britain, Prussia, Austria, Spain and the Dutch Republic (the War of the First Coalition), the administration of George Washington was repairing its rocky relationship with the British. Since neither the French nor the British had any desire to land troops on U.S. soil, these conflicts were largely played out on the high seas by both naval forces and privateers. Most of the disputes between the United States and Great Britain were settled, or at least temporarily papered over, by Jay's Treaty of 1794, which ushered in a brief period of U.S.-British amity. Although this goodwill proved to be rather short lived, it was too much for the French Revolutionary regime and a de facto naval war between France and the United States ensued. Thus, the U.S. navy and its pension plans were born as much out of political and military expediency as economic efficiency.

The disability plan almost became a true retirement plan as early as 1801. With the change in administrations from Adams's to Jefferson's, the navy was subjected to a severe reduction in funds. Only 45 officers above the rank of midshipman were kept on active duty (Miller 1997, p. 45). Secretary of the Navy Benjamin Stoddert proposed creating a "half-pay" retirement system like that of the royal navy (see Chapter 3 above). The proposal was soundly rejected by the Jefferson administration, and instead the discharged officers were given only four months' pay. It would be several decades before a "regular" navy pension plan along the lines of Stoddert's proposal became law.

The dismemberment of the navy proved to be shortsighted. Reversing the political realignment of the 1790s, American policy eventually became strongly anti-British. This policy reflected national sentiment and the fact the British had waged a particularly nasty and aggressive naval war against France, her allies, and anyone doing business with either. These tensions culminated in the War of 1812. The war provided numerous opportunities for the seizure of prizes and the U.S. navy proved to be rather efficient in this activity. As a result, the assets in the navy pension fund expanded. As the fund grew, the commissioners found the pension system increasingly difficult to manage through three federal departments (Navy, Treasury, and War). Consequently, they requested that Congress place the pension fund under a single department; however, it was not until 1832 that the Secretary of the Navy was made the sole manager of the pension fund.

The various laws establishing the navy pension plan and the fund from which benefits were to be paid also specified the fund's administrative structure and management as well as eligibility conditions for receipt of pension benefits. The 1800 legislation "An Act for the Better Government of the Navy of the United States" also specified that the commissioners of the pension fund must provide annual reports to Congress concerning the operations of the fund. Many of these reports have survived as official government records and provide considerable information on the activities of the pension fund. These original reports are a primary source of information and data employed in this volume.

The 1800 act revised the pension benefit formula so that "every officer, seaman and marine, disabled in the line of his duty, shall be entitled to receive for life, or during his disability, a pension from the United States, according to the nature and degree of his disability, not exceeding one-half of his monthly pay" (*ASP-NA*, 4: no. 529). The monthly pay of a seaman in the U.S. navy in the early nineteenth century was in the neighborhood of $12; lieutenants earned $40 a month and captains $100 plus "rations" (Lebergott 1964; *ASP-NA*, 1).[4]

To receive a disability pension, a claimant had to complete an application indicating the circumstances of the injury, when it occurred, the extent of the injury, and the extent of the disability that resulted from the injury. The application had to be signed by the company surgeon and commanding officer. Injuries could result in a partial or total disability and the amount of the pension depended on the extent of the disability. Table 4.1 indicates the relationship between various disabilities and the level of benefits paid by the navy pension plan. Such a schedule was on the books over a very long period of time. The schedule shown in Table 4.1 is for two checkpoint dates, showing the changes in the absolute and relative amounts for various injuries over time. The basic concept of the disability pensions is that the amount of the pension is related to the extent of the injury. Pensions were forfeited if the veteran was convicted of a felony (*ASP-NA*, 4: 427).

Table 4.2 contains a listing of the number of beneficiaries, the total amount of annual benefits paid, and the average benefit per recipient for each year between 1800 and 1842.[5] The figures show that the number of beneficiaries, the total cost associated with their pensions, and per capita expenditures generally increased during the life of the pension fund. There were 22 pensioners in 1801 receiving annual benefits of $1,605 for an average of $72.95 per recipient. By 1842, the number of beneficiaries had increased to 946 and annual outlays were $107,129 or an average of $113.24 per recipient for "ordinary" benefits. Including "extraordinary" payments, the payment per beneficiary was $232.60, and a total of $220,053 was paid in benefits during the year.

The estimates of extraordinary payments are largely compensation for "back" benefits, as required by subsequent legislation. To assist readers in assessing the value of benefits and earnings, Appendix A provides a consistent price index from 1800 to 1999. Multiplying the dollar values shown in Table 4.2 by the factors for the corresponding year in Appendix Table A.1 produces an estimate of benefits and assets in December 1999 dollars.

In its first decade of operation, the assets of the pension fund seemed to be sufficient to pay promised liabilities for many years in the future. In addition, the steady infusion of prize monies produced considerable growth in the size of the fund. With an investment of almost $30,000, interest income comfortably exceeded any immediate payouts. The value of the fund itself increased from 1800 through 1807 due to, among other things, the delayed receipt of the sale of prizes from earlier naval conflicts with Britain and France, as well as the excess of investment returns over outlays. During the War of 1812, prizes became more abundant, the value of the fund

TABLE 4.1. Statutory Rates for Permanent Specific Disabilities for Military Pensions as of 1872 and 1904

Disabilities	*1872*	*1904*
Loss of both hands	$31.25	$100.00
Loss of both feet	31.25	100.00
Loss of sight of both eyes	31.25	100.00
Loss of sight of one eye, the sight of the other having been lost before enlistment	31.25	100.00
Loss of one hand and one foot	24.00	60.00
Loss of a hand or a foot	18.00	40.00
Loss of an arm at or above the elbow or a leg at or above the knee	18.00	46.00
Loss of either a leg at the hip joint or an arm at the shoulder joint, or so near as to prevent the use of an artificial limb	—	55.00
Loss of a leg at hip joint	24.00	55.00
Loss of an arm at shoulder joint	18.00	55.00
Total disability in both hands	31.25	31.25
Total disability in both feet	31.25	31.25
Total disability in one hand and one foot	24.00	60.00
Total disability in one hand or one foot	18.00	40.00
Total disability in arm or leg	18.00	46.00
Disability equivalent to the loss of a hand or a foot (third grade)	18.00	24.00
Incapacity to perform manual labor (second grade)	24.00	30.00
Regular aid and attendance (second grade)	31.25	72.00
Frequent and periodical, not constant, aid and attendance (intermediate grade)	—	50.00
Total deafness	13.00	40.00

Source: Edited from Glasson (1918, 133) based on *Laws of the United States Governing the Granting of Army and Navy Pensions,* compiled under the direction of the Commissioner of Pensions, 1916 edition, 110.

TABLE 4.2. History of the U.S. Navy Pension Plan, 1800–1842

Year	*Pensioners*	*Annual*[a] *outlays*	*Per capita outlays*
1800	—	—	—
1801	22	$1,605	$72.95
1802	—	—	—
1803	37	3,567	96.40
1804	37	3,261	88.13
1805	49	4,413	90.06
1806	65	5,298	85.51
1807	78	6,396	82.00
1808	85	6,863	80.74
1809	90	6,671	74.12
1810	93	7,043	75.73
1811	107	8,045	75.19
1812	122	9,287	76.12
1813	148	11,273	76.17
1814	176	13,667	77.65
1815	252	20,547	81.54
1816	327	27,627	84.49
1817	358	32,036	89.49
1818	—	34,970	—
1819	438	39,340	89.82
1820	480	43,863	91.38
1821	491	44,488	90.61
1822	431	38,772	89.96
1823	423	37,248	88.06
1824	524	—	—
1825	524	—	—
1826	533	49,653	93.16
1827	534	—	—
1828	570	—	—
1829	596	—	—
1830	536	31,938	59.58
1831	536	—	—
1832	—	—	—
1833	—	—	—
1834	—	—	—
1835	442	54,083	122.36
1836	466	58,009	124.48
1837	678	200,689	296.00
1838	847	216,042	255.06
1839	901	223,045	247.55
1840	914	221,675	242.53
1841	959	226,825	236.52
1842	946	220,053	232.61

Source: Authors' calculations based on Clark et al. (1999a, b) and original sources cited therein.

[a] The figures from 1837 through 1842 include two extraordinary treasury remittances resulting from the act of 1837. These remittances appear to have been passed "straight through" a cash position to beneficiaries.

increased, and by 1831, the fund had assets of one million dollars. The lack of synchronization of the increase in the value of the fund due to prizes relative to the war years was due to the difficulty in getting the purveyors of the prizes in various ports to remit their sales receipts to the fund. This problem was a pervasive feature of the prize system since its inception and in all belligerent countries. Indeed, it was just such disputes associated with the disbursement of prize money from the war with Spain that, among other things, led Congress to finally abolish the whole system in 1899 (Oliver 1946).

With respect to the navy pension plan, subsequent actions to extend coverage and to increase benefits seem to have been taken without regard for the actuarial conditions facing the fund. For example, in 1813, benefits were extended to the widows of navy personnel who died as a result of a wound received in the line of duty. These benefits were equal to half the monthly pay of the deceased and were to be paid for a five-year term. Payments could be renewed for additional terms of five years each. If no surviving widow existed, these survivors' benefits could be paid to children under 16 years of age. In addition, in the annual report filed in January 1816, the commissioners concluded that limiting the benefit to half-pay:

> proved inadequate to the maintenance of disabled seamen and marines, particularly the latter, which cannot exceed three dollars per month. The extension of the law, so as to vest in the commissioners a discretionary power to allow, in extreme cases, to the full amount of monthly pay, or otherwise to provide for the necessary subsistence of those who are totally unable to take care of themselves, would, it is believed, obviate causes of complaint, and reflect honor upon the liberality and justice of the National Legislature. (*ASP-NA*, 1).

As requested, in April 1816, the commissioners were given the ability to provide benefits in excess of half-pay in cases of exceptional hardship. This expansion of benefits and the extension of benefits to widows and orphans, along with the growth of naval personnel during the War of 1812, dramatically increased the total annual outlay of pension benefits.

Furthermore, adding widows and orphans to the pension rolls involved more than just increasing the number of pensioners at the time. An added actuarial complexity was the longevity of the obligation. As an example, consider that "in 1906, 123 years after the close of the Revolution, there still remained one widow of a Revolutionary soldier on the pension list, Esther S. Damon of Plymouth Union, Vt., 92 years of age" (Glasson 1918). There also remained "a few aged daughters of Revolutionary soldiers who had been pensioned by special acts of Congress." The navy pension fund also had a problem with keeping track of the list of pensioners on the rolls. In response to an audit request from Congress, in January 1836, without irony, the navy admitted that "some of the names on this list may be dead" (*ASP-NA*, 4).

In 1816, payments of $27,627 were paid to 327 veterans, widows, and orphans. In 1817, benefits to widows and orphans were expanded to include those whose husband or father had died "*in consequence* of disease contracted or of casualties or injuries received" (emphasis added). If a veteran's dependents could show that his eventual death was in some way connected to his previous service, then they would be eligible for benefits. This extension sharply increased expenditures, and by 1823, annual expenditures totaling $37,248 were paid to 423 beneficiaries. In 1824, this provision, along with that for widows and orphans, was repealed because of the now obvious drain on the pension fund. Persons already receiving benefits were allowed to continue receiving payments; however, the act stipulated that no future pensions would be awarded to widows or orphans. Despite this change, the total number of beneficiaries continued to increase, reaching 596 in 1829. Even with the increased expenditures associated with this growth, the fund continued to grow, reaching $950,675 in the same year.

By the early 1830s, the fund's assets approached one million dollars. At the same time, the number of pensioners was stabilizing. Thus, the pension system appeared to be in excellent financial condition, with sufficient assets to pay promised benefits for years to come. With the pension fund in such sound financial condition, Congress was unable to resist the temptation to expand the coverage of the pension plan. In June 1834, Congress restored the provisions for widow and orphan benefits that existed between 1817 and 1824. The legislation also extended benefits to widows of officers, seamen, and marines who had died since 1824. These actions substantially increased plan liabilities with no additional funding.

The official account of this episode in the *American State Papers* makes the case that the fund could adequately support this expansion of benefits (*ASP*-NA, 4). Given the lack of new monies resulting from prizes and the aging of the veterans of the War of 1812, it is difficult to support such a claim with any plausible actuarial scenarios. Whether the official account simply reflects political opportunism or ignorance of financial arithmetic is unclear. In either case, and not surprisingly, this extension of benefits resulted in "a heavy charge [being] made upon the fund" (*ASP-NA*, 4). The magnitude of the financial impact on the pension system is revealed by noting the size of the awards to the new beneficiaries. Only 56 widows had been granted a pension benefit under the terms of all previous acts. This new legislation added 80 widows to the rolls at an annual sum of $20,031, an amount equal to nearly 40 percent of the whole of navy pensions (*ASP-NA*, 4). The aging of the veterans of the War of 1812 only compounded this problem, both directly through their disabilities and indirectly through their deaths.

The problem faced by the fund was one of imbalance between its assets and it liabilities. The assets were the accumulated monies from prizes and any interest in excess of outlays that remained in the fund. Congress could have refrained from increased liabilities, or it could have created another source of revenue for the fund. The conflicts with the Indians on the American frontier were never going to replenish the fund. The natives had no navy from which prizes could be extracted.

Despite the changes, in November 1835, the fund still possessed assets of $1,160,262 and the income for 1835 was $66,083. Expenses totaled $23,842 paid to 306 disabled veterans and $30,241 paid to 136 widows and orphans. In assessing the implications of the 1834 legislation, the commissioners, who were also the trustees of the fund, lamented Congress's improvident expansion of benefits, writing:

> It will be perceived that, by the act of 1834, a pension is allowed to the widow of every person who may die in the naval service by reason of disease contracted while in his line of duty; a phrase than which nothing can be more vague or more liable to abuse, and which is nearly tantamount to authorizing a pension to be granted to the widow of every person who may die in the naval service. To such an extension of the pension system, the committee are decidedly opposed. (*ASP-NA*, 4)

Yet, by March 1837, the fund stood at $1,115,330, and interest and dividends exceeded $50,000. Despite the recent increase in claimants and outlays and, importantly, without reference to future claims that would ultimately result as more of the War of 1812 veterans died, Congress once again expanded benefits enacting the "Act for the More Equitable Administration of the Navy Pension Fund" (the Jarvis Act). This legislation required the fund to pay pensions to widows and orphans *from the dates of the veteran's death.* In addition, the act stipulated that pensions granted to veterans be paid from the time that they were disabled, not the date at which their disability was confirmed by the navy; thus creating substantial liabilities resulting from the nonpayment of such benefits prior to the act's passage. In other words, the act created substantial new liabilities without creating any new source of funds.

Although the passage of the Jarvis Act smacks of fiscal irresponsibility, it was perhaps not a coincidence that it corresponded with a dramatic expansion of naval personnel, a 50 percent increase in 1837 alone (U.S. Department of Commerce, Bureau of the Census, 1975). At the time, the United States was once more embroiled in a territorial dispute with a European power. This time it was the northeastern boundary with Canada that provided the source of the tension. In response to the international crisis, the United States began to expand its navy by increasing enlistments. The buildup of naval forces began during the peak of the business cycle. A wage series for "able-bodied seamen" indicates that real earnings peaked in 1836 (Lebergott 1964; see also Appendix A). Thus, the pension improvements may have been an attempt by Congress to increase the total compensation of naval personnel in order to recruit new seamen. If true, this action reflects a basic understanding of the value of pension plans by both government officials and potential recruits. If Congress increased pension benefits in an effort to entice young men to enter the service, the panic and subsequent recession of 1837, which began two months after the act was passed, made higher compensation to seamen unnecessary as wages throughout the private sector dropped substantially thereafter (Thorp 1926).

The commissioners of the pension fund opposed this expansion of benefits and especially the payment of back pension benefits (required by the Jarvis Act), which ran as high as $6,000 to $8,000 *per beneficiary*. These payments were apparently for long-ago injuries that eventually resulted in disability or death. Each of these lump sum awards represented approximately 5 to 9 percent of the total annual outlay prior to this legislation. The annual number of pensioners was raised to 847 and annual expenditures rose to $103,120. "Arrears payments soon consumed nearly $600,000. Between March 3, 1837, and October 1, 1838, about $725,000 of the invested capital of the fund was sold, and the proceeds, with the interest and dividend on the capital were applied to payment of pensions and arrears" (Glasson 1918).

The sharp reduction in the size of the pension fund reduced annual income while the increased number of beneficiaries sharply increased expenditures, resulting in the further decline of the fund. Complaining about the financial pressures imposed on the fund by Congress, the Secretary of the Navy reported that the provisions of the act of 1837 "involving arrearage commencing many years anterior to its passage" had severely damaged the long-run viability of the fund. Primarily, this was due to the first section of the act, which provided that pensions to widows and orphans "shall be paid from the date of the demise of the husband or fathers. The only condition is, that the demise shall have happened in the naval service" (U.S. Senate 1839). The Secretary concluded that "Arrearage of pensions for more than thirty-seven years, in one instance involving the payment of more than $20,000, have been paid under this section which has mainly caused the rapid diminution of a fund originally constituted for the sole purpose of providing for officers and seamen only, disabled in naval service" (U.S. Senate 1839). The 1839 report of the Secretary of the Navy also noted that the second section of the act of 1837 contributed to the increase in expenditures of the fund:

> The section of the same act provides, that "pensions which have been granted, or which shall here after be granted to officers, seamen, and marines, in the naval service, disabled by wounds or injuries received in the line of their duty, shall commence from the time when they were disabled." (U.S. Senate 1839)

Previously, pensions had been paid from the time they were *approved*. The lag between the purported onset of disability and initial payment was what the act attempted to address. Following the passage of this act, the fund declined in two years from $1,115,330 to $253,139. In summary, the

Secretary concluded that "the primary source of the decline of the navy pension fund is the act of 1837," and he went on to note:

> It is therefore certain that at the end of two years, at the farthest, the navy pension fund will be exhausted. Under the existing laws there is not the least prospect of any decrease in the number of pensioners or the amount of their pensions; and consequently, Congress will be called upon to . . . make good any deficiency in the navy pension fund arising out of its own legislation. (U.S. Senate 1839)

Just as the Secretary predicted, two years later, with the pension fund facing total liquidation, Congress passed new legislation in August of 1841 appropriating $139,666 to provide for the continued payment of pensions to current beneficiaries until the close of the next session of Congress. Benefits would not be paid to widows and orphans of men who died after the passage of this act. In 1842, Congress appropriated another $84,951 and formally repealed the (arrears) act of 1837. In 1843, Congress began the practice of passing authorization for the payment of two years worth of benefits from general tax revenues (Glasson 1918). The navy pension fund was dead.

A Pension Plan for Privateers

The navy pension fund was not the only such fund in existence for U.S. seamen during the antebellum era. As noted, Jay's Treaty eased tensions between the United States and Great Britain for nearly a decade; however, by 1807, circumstances had changed. The British blockade of the European continent and related circumstances, including the impressment of American seamen, led to Jefferson's embargo. Although the Embargo Act was subsequently repealed, there was no easy way to continue a profitable Atlantic trade and simultaneously steer clear of the maritime war among the European powers. Napoleon had shut off the continent to the British; while the British had shut off Napoleon from the rest of world. As a result of these efforts, relations between the United States and both Britain and France had deteriorated during the naval war between the two European powers; however, the British had pursued a more aggressive and effective naval policy against the United States. Last minute French diplomatic efforts swayed U.S. policy toward Napoleon, and so in June 1812, war was declared on Britain.

At the time war was declared, the U.S. navy was quite small by British standards; however, as noted in Chapter 3, privateers played an important role in western naval warfare until the mid-nineteenth century. Indeed, most of the prize cases that eventually found their way into the federal courts in the late eighteenth and early nineteenth centuries involved the questionable practices of privateers or those who claimed to be privateers. During the War of 1812, Congress began once again commissioning privateers for the sea war against the British. The U.S. privateers of the War of 1812 proved to be a colorful and effective force. Following the economic logic discussed in the previous chapter, in the same month that war was declared, Congress created a pension fund for privateers. It proved to be money well spent. In a report to the U.S. House of Representatives in 1830 on a review of the history and operation of their pension fund, a group of surviving privateers reported "the interesting fact that our private armed ships captured more British seamen, during the last war, than the whole of our gallant navy" (*ASP-NA,* 4: no. 185).

Unlike the navy pension fund, the privateer pension fund was supervised solely by the Secretary of the Navy. Congress directed that 2 percent of all U.S. prize monies collected from the privateer's actions be allocated to this fund. By 1820, the fund had a balance of $213,535 and was paying $20,700 annually to 254 privateers, widows, and orphans. Like the rules governing eligibility for a navy pension, the privateer's fund eventually covered seamen and their widows and orphans who died or were disabled "in consequence" of accidents or casualties in the line of duty. The fund's assets were invested in 6-percent treasury bonds. By 1829, the balance in the fund had fallen to $63,272, yielding only $4,210 in interest annually. The latter amount was substantially below that required to pay annual pensions. By 1830, the fund had declined to $53,115 and was earning no interest "as the stock in which it was invested has been redeemed" (*ASP-NA*,1830, 3: 496). In other words, as part of the general reduction in the federal debt during the 1820s and early 1830s, the treasury had redeemed the bonds held by the fund and replaced them with a cash balance. Not surprisingly, the fund eventually went bankrupt in 1837. Interestingly, unlike the annuitants covered by the U.S. navy pension plan, Congress did not immediately make whole the 36 privateers who were still receiving $2,900 in pension payments annually. However, in 1844, Congress reinstated pension payments from annual appropriations and granted back pension payments dating from July 1, 1837.

Assessment of the Naval Pension Plan

Between 1800 and 1840, the U.S. government operated a separate pension plan for the navy, and the plan was separate from the other accounts of the federal government. While the benefits and coverage of this plan were similar to those of the army plan, the funding was considerably different. Instead of using general revenues or employee contributions, this pension plan was funded from the sale of prizes captured by the navy. Of course, this made funding highly variable from year to year and only tangentially related to expected benefits. At the time, the unique aspect of this pension system was that the government was managing a pension portfolio in the early nineteenth century and that the trustees of the plan were allowed to invest these monies in private equities as well as government securities. In addition, Congress created a pension plan for U.S. privateers, and in some key respects, the history of that plan followed that of the navy's plan.

The history of the legislation covering navy pensions before the Civil War shows that in general Congress could not resist the temptation to expand coverage and benefits when the trust fund seemed to be large and growing—regardless of the fund's future liabilities. Congress continually pushed benefits beyond the fund's actuarial capacity to support promised benefits from the monies held in trust. The actions of Congress along with poor investment decisions by the trustees ultimately resulted in a shift of pension liability from the trust fund itself to taxpayers in general. The details of the management of the pension fund, actions by Congress, and investment choices are reported in Chapters 5 through 7.

Notes

1. The material in this section relies heavily on the accounts of Paullin (1906).
2. The history of the Continental Navy is from Miller (1997) and Paullin (1906).
3. The figures on the size of the early navy are estimates (U.S. Bureau of the Census 1975).
4. Appendix A to this volume provides both a historical price index and reproduces Lebergott's wage index so that the interested reader can evaluate the real value of these wages and benefits.
5. Through 1836 these data are from the various annual reports by the commissioners of the navy pension fund; thereafter, the figures are from the annual reports of the Secretary of the Navy, which were required by Congress.