Chapter 7
The Civil War and the Revival of the Navy Pension Fund

The regional conflicts over slavery, tariffs, and the western territories ultimately led to the secession of the southern states and the formation of the Confederate States of America. The conflict with the Confederacy over Fort Sumter and the other U.S. possessions within the geographical boundary of the secessionist territories, presented the republic with an unparalleled crisis. However, the war that resulted provided career officers of the "regular" army and navy a once-in-a-lifetime professional opportunity. The nature of the conflict was such that naval officers in particular could expect to enrich themselves through the pursuit of prizes. The Confederacy was not an especially diversified economy by the standards established by the industrial revolution. The southern economy revolved around cotton exports and the importation of industrial goods, and so within twenty years of the liquidation of the navy pension fund in 1842, the nation once again found itself in a war that promised opportunities to capture prizes. This scenario would ultimately yield nearly $30 million in prize money for the officers and men of the U.S. navy, or roughly $300 per capita for the 100,000 or so men who ultimately served in the navy. This was a substantial sum when one considers that per capita income in 1860 was roughly $200 in current dollars. Just as with the earlier prizes, much of the Civil War prize money was ultimately dedicated to navy pensions.

As in the past, armed conflict meant that the number of navy personnel would expand and claims for disability pensions would increase. Facing the secession of its southern states, the Union, as the collection of remaining states was called, expanded its naval forces rapidly. In 1861 alone, the navy nearly tripled in size from less than 10,000 men to roughly 28,000, and this number more than doubled again over the next four years (U.S. Department of Commerce, Bureau of Census 1975). From the outset of the war, a primary component of the Union's military strategy was a blockade of the Confederacy. The commanding general of the Union armies, Winfield Scott, had been a general for a very long time. Having been originally promoted to that august rank in the War of 1812, Scott had been a general for longer than most officers served in the army. Although noted for his love of grand uniforms and the perquisites of his post, Scott had in fact seen as much of war as any man of his generation, and he was not inclined to wage total war on his fellow countrymen, no matter how recalcitrant they seemed at the moment. To bring the Confederate States back into the Union, he proposed to use a joint army-navy force to secure the Mississippi, impose a saltwater blockade of southern ports, and make a frontal assault on Richmond (Ransom 1989). Both the wisdom and the efficacy of this plan, the "Anaconda plan" as it was dubbed by critics, were much disputed at the time and have continued to be a topic of contention among scholars over the years.[1] Whatever its merits on military or political grounds, with the addition of Sherman's campaign through Georgia and the Carolinas, Scott's plan, executed after his retirement, eventually secured victory.

The important role bestowed upon the navy during the Civil War provided both a new cohort of claimants for benefits from the navy pension plan and a large number of potential prizes to finance a new pension fund. By 1863, navy pension payments had reached $159,812 and the prizes sent to prize courts since the start of the war were valued at $13 million (U.S. Navy 1863). At the urging of Secretary of the Navy Gideon Welles, Congress reestablished the navy pension fund in July 1862. In his annual report to Congress, Secretary Welles explained that:

> The moiety of prize money dedicated as a pension fund, and now accumulating, should be made a permanent investment in registered government securities. Were such the case, it is believed that the annual interest would be sufficient to meet all liabilities for naval pensions. At least two million five hundred thousand dollars can now be invested without interfering with the prompt payment of pensions. I recommend that the fund now on hand be made permanent, and that hereafter, whenever the amount shall reach one hundred thousand dollars, at least one-half shall be invested in registered government securities bearing six per cent interest. (U.S. Navy 1863)

The legislation creating the new fund directed the secretary to place half the net proceeds from the sale of prizes into the fund.[2] Welles subsequently purchased $5 million in U.S. government bonds during 1864, which at the time contributed to the war effort as the Treasury was trying desperately to raise funds in the credit market. Although, at its peak, the navy pension fund never purchased more than one percent of the amount of the debt issued in any single calendar year, the use of funds obtained from southern blockade runners to indirectly finance the Union war effort through prize courts was not unlike current U.S. efforts to combat organized crime under the R.I.C.O statute. This law allows federal agencies to confiscate property of criminals and either sell it to finance or employ it directly in subsequent enforcement efforts. This was exactly how the navy prize system worked. Vessels not purchased directly by the navy were sold along with their contraband and the monies went to compensate naval personnel. The result of these transactions was to transfer once again navy pension liabilities at least nominally from the U.S. Treasury to the navy pension fund.

By the end of 1864, gross proceeds from Civil War prizes exceeded $14 million. After expenses and direct payments to the captors, roughly $6.5 million remained for the navy pension fund. Pension outlays were $189,659 in 1864; counting the $5 million already invested in U.S. bonds, this left approximately $1.3 million in cash in the fund. However, in his 1864 report, Welles proposed to purchase another $2 million in registered securities. One must assume he anticipated either that an additional $700,000 in prize monies would be forwarded to the fund or that the cash position of the fund was substantially larger than $1.3 million because of other, perhaps yet to be adjudicated, prizes not included in the $14 million he had reported up to 1864. In either case, Welles asserted that the $7 million to be invested by early 1865 in 6 percent government bonds would yield $420,000 a year in interest and would be "sufficient for the payment of the entire pension roll . . . without calling upon the national treasury" (U.S. Navy 1864).

In his final report covering the Civil War years, Welles listed the total value of prizes taken during the war as $21,829,543. After accounting for expenses incurred in adjudicating and processing the prizes and after subtracting the captors' shares, prize monies allocated for the navy pension fund amounted to approximately $10,251,000, with several "important cases still before the courts" (U.S. Navy 1864). The Secretary stated that by January 1866 those monies would be fully invested in government bonds; however, at the close of 1865, the fund held only $9 million in bonds. Thus, the plan either maintained a large cash position, which would not have been unreasonable given its perpetual need to pay pensions, or the difference between monies expected from prize courts and that which had been invested in government bonds was held up somewhere along the line. If it were the latter, then such a situation was not unusual.

Prize cases were notorious for the time they took to process and, on occasion, to litigate.[3] Partly, this resulted from the fact that the laws covering prizes were often vague. Statues referred to contraband, for example, without defining it specifically. Furthermore, ships often carried a variety of goods to and from several ports and for many merchants. The prizes were often taken to the ports of nations not a party to the dispute, and regardless of where the prize was taken the practices of the prize courts and agents varied substantially, from time to time and place to place. Finally, the prize agents and lawyers themselves faced a moral hazard in that they often controlled for some period of time the monies involved in prize cases—monies that were often used for other purposes, including occasional speculative ventures. It was not uncommon for prize claimants to be as vexed by their agents as they were by the vagaries of war.

Despite the number of cases still being processed, as the war came to an end, the fund was in good shape relative to its liabilities. During 1865, expenditures from the fund had reached $250,000; so it appeared the plan was indeed solvent for the foreseeable future. The $10 million or so deposited in the navy pension fund, including cash, represented approximately 45 percent of all prize cases settled by, or shortly after, the end of the Civil War. Another $5 million would be added from subsequent prize cases over the next three and a half years. All monies accumulated by the fund added to it only after "expenses" and the captors' shares had been allocated. "Expenses" included the costs of maintaining the prize courts, agents' fees, wharfage, and so forth. During the Civil War, these expenses came to roughly 8 percent of the total value of prizes; the remaining 46 percent ($15 million) had been or was eventually distributed to the officers and crews that had captured the prizes. The exact amount of money that ultimately ended up in the hands of Union officers and seamen remains in dispute. Calculations based on the figures reported above put the figure around $15 million. Contemporary estimates were $13 million. It is possible that that discrepancy results from the uncertainty at any point in time of the disposition of prizes still under litigation

A little arithmetic confirms the potential importance of financial incentives in naval compensation during this era. As noted, roughly 100,000 men served in the U.S. navy during the Civil War. The vast majority never directly participated in the capture of a single prize. During the war, 1,149 prizes were captured by the U.S navy. The average net value of a prize was $13,100. A typical frigate or smaller sloop on blockade duty might have an effective complement of 150 to 200 or more men. Thus, the payout per seaman per prize was $100, roughly 60 percent of a seaman's base wage and 50 percent of per capita income in the United States at that time (or about $17,500 in 2002 dollars), but these figures obscure the most appealing feature of the prize system from the men's perspective—namely, the chance at one or more extremely lucrative prizes. A grand example was the U.S.S. *Aeolus*, a mere gunboat, smaller than a sloop. Late in 1864, she took two blockade runners, netting "$40,000 for her captain, $8,000 to $20,000 for each of her officers, and $3,000 for each seaman" (McPherson 1988, 378). As a share of per capita income, that would be nearly half a million dollars per seaman in today's money.

After the war, Welles remained optimistic concerning the financial status of the plan, noting that income from the plan would "if rightly husbanded, be ample to meet the requirements of the government for the payment of naval pensions, without any tax upon the people" (U.S. Navy 1865). Welles made repeated assurances that the navy pension plan would not impose any new burden on the taxpayers. His often stated assessment of the financial status of the fund leads one to suspect that he was aware of the history of the navy pension fund in the first half of the nineteenth century. His protestations may well have been addressed to those, perhaps in Congress, who were also aware of that history and who for that or other reasons were skeptical of the navy's plan. If Welles was in fact concerned that the fund's history might be used as a pretense for altering the navy pension plan, then he was prescient.

The prizes still being adjudicated in 1865 plus the plan's net earnings (interest less expenses) after that date yielded another $5 million that were added to the balance in the fund. Net earnings (interest less outlays) plus new revenues during the years immediately after the war were $2.75 million in 1866, $1.25 million in 1867, and $1 million in 1868. These monies were also invested in government bonds. By the end of 1868, the total (par) value of the plan's holdings of U.S. Treasury liabilities was $14 million, all of which paid 6 percent interest per year. It appears the plan maintained a small cash position as well. The navy reports do not offer any detailed accounting as to exactly what securities the fund held, the price at which they were acquired, or whether the bonds had been bought directly from the Treasury or on the open market. It can be surmised that the bonds were some combination of the "Sixes of 1868," "Sixes of 1881," and the "Sixes 5-20s of 1865." According to Homer and Sylla (1991) and bond price quotations in the *Financial Review* (1876–1921), all of these bonds were selling at a premium to par value.

The growth in the plan's portfolio corresponded with an upward trend in annual outlays for pension benefits. Payments were approximately $270,000 in 1866, $320,000 in 1867, and $391,000 in 1868. There is no evidence in the Navy Secretary's reports that the securities held by the reconstituted pension fund were ever purchased or valued at anything other than par. Although these reports do not offer a detailed accounting of exactly what securities the fund held, it is likely that the fund held some combination of the 6 percent bonds mentioned above.[4] The fund's ability to purchase the bonds from the Treasury at par when they traded on the open market at a premium implies that the government was giving a subsidy to the pension fund, albeit a relatively small one.

Although the number of beneficiaries was rising, under the current rules for eligibility, it would not continue to do so indefinitely, and indeed, given the irrefutable arithmetic of the life table, at some point it would begin to decline. So by the late 1860s, the plan seemed solvent under any reasonable set of actuarial assumptions. With nearly 100 percent of the plan's portfolio invested in U.S. government bonds paying a 6 percent coupon, the plan generated sufficient annual income to pay current benefits based on existing coverage, eligibility, and benefit standards. Even a fairly substantial increase in the number of beneficiaries added to the pension rolls would not have put the fund's long-run viability in jeopardy. Welles must have agreed with that assessment because he formally requested both an increase in benefits and an expansion in the number of persons covered by the plan, writing in 1866: "Further legislation is therefore required in order that 'the surplus shall be applied to the making of further provision for the comfort of disabled officers, seamen and marines'" (U.S. Navy 1866). A year later he added:

> I recommend, therefore, that the pension laws applicable to the navy be revised, and such an increase in the rates of pension be authorized as the fund will warrant. The entire principal of the fund was earned by the officers and men of the navy . . . It may also be well to consider whether the family of a person dying in the navy after a specified time of service should benefit from this surplus fund, even though the death should not have occurred in the strict "line of duty." (U.S. Navy 1867)

In July 1868, Congress granted half of Welles's request. It did revise the pension laws as they applied to the navy pension plan, but rather than increase pensions or expand coverage, as Welles suggested, Congress changed the way in which navy pensions were funded. The legislation altered the character of the assets held by the plan and in so doing lowered returns from these assets. This legislation fundamentally transformed the navy pension plan forever.

The details of the pension act of 1868 revolve around the personalities at the epicenter of national politics and some rather arcane aspects of public finance. Let us turn to the financial aspects first. The act authorized the Treasury to exercise an implicit call option on the $14 million in Treasury bonds held by the navy pension fund, 100 percent of the fund's noncash assets at that time. None of the 6 percent bonds issued during the period in which the navy was purchasing them (and hence in all probability those held by the fund) were redeemable before five years from their date of issue (Homer and Sylla 1991). The fund only began purchasing securities on a large scale in 1864. There is no record that those or subsequent purchases were traded for earlier issues. Thus, the earliest date at which the bonds were called should have been 1869.

After calling the 6 percent bonds from the fund's portfolio, Congress replaced them with a special issue of nonnegotiable 3 percent Treasury liabilities. There is no evidence that these bonds ever existed except on the ledgers of Treasury and Navy Department accounts. Thus, the bonds resemble the current government securities held by the Social Security trust fund in that they were special-issue, nontradable bonds. This observation and the fact that the bonds were redeemed at par while they were trading at a premium suggests that the fund experienced a substantial capital loss as a result of congressional action. It should also be recalled that the Treasury issued the bonds to the pension fund at par when they were trading at a premium.

Any type of dollar value or interest yield over the period is suspect depending on whether the values are in terms of currency or gold. Specie payments had been suspended in February 1862. The government issued paper liabilities (including currency in the form of so-called "greenbacks") that depreciated over time; however, a market existed between currency and gold. Wesley Mitchell (1908) reconstructed the record of the daily high, low, and market closing prices of gold over the period 1862 and 1878. Thus, there are two sets of prices for this period. These prices relate to financial assets as well as commodities, like the Sixes of 1881 that were probably held by the fund. This asset, which was paying 6 percent of par interest, is used as an example of the ambiguities and confusions between prices and yield during this 15-year period. The Sixes of 1881 were issued in two phases. The initial issue was for $18.4 million sold at 89 percent of par for a yield of 6.73 percent. The second issue was for $50 million sold at 89.25 percent of par for a yield of 6.70 percent (Homer and Sylla 1991). At the beginning of the suspension of specie payments, the government declared that the interest on bonds, as opposed to shorter notes, would be paid in gold. However, there was uncertainty as to whether the redemption of par upon maturity would be paid in greenbacks or gold. Currency depreciated and the greenback price of gold reached a ratio of 2.6 dollars of greenbacks for one dollar of gold (at the presuspension price) in July 1864. The relative price of the currency began increasing and the ratio of greenbacks to gold declined to a ratio of 1.4 in 1868 and 1.1 in 1870, and it reached approximate par early in 1871 (Mitchell 1908).

The greenback price of the Sixes of 1881 went from their originally issued discount price to a premium. However, in terms of gold, that price was at a discount from par. In July 1864, the premium price in terms of greenbacks was around 50 percent of par value in gold and the gold yield was almost 15 percent. In 1868, the gold price was about $82 with a greenback-gold ratio of 1.4. The opposite was true of yields, from the 6 percent par value yield, the greenback premium of 15 percent caused a yield of less than 6 percent. However, in terms of gold, the yield was in excess of 6 percent; actually these bonds had a yield of over 8 percent. As this example shows, as a result of the postwar appreciation of the greenback, the meaning of yields and the interpretation of bond prices and portfolio values during the period illustrate the potential for honest confusion. During the war expectations regarding the future exchange rate between currency and gold, along with fluctuating yields, moved up or down depending on successes or failures of Union troops on the battlefield (Macaulay 1938; Roll 1972). After the war, speculation on the eventual return to gold drove the exchange rate.

With the currency market as a backdrop, the legislation altering the navy pension fund's assets was passed only after a lengthy and acrimonious debate. Indeed the section of the act covering the navy pension fund was attached to the main corpus of a bill that appropriated $33.3 million dollars to cover *army* pension benefits. Representative Frederick Pike, a

Republican from Maine, was a staunch defender of the (pro-navy) status quo and, as Chairman of the House Committee on Naval Affairs, a close ally of Secretary Welles. Pike called the navy pension fund, as it was constituted during the war, a "contract on behalf of the United States" and labeled the legislation altering it "a breach of faith on the part of the Government" (*Congressional Globe* 1868). This statement was followed by a lengthy and well-informed recitation of the history of the antebellum navy pension fund by the bill's sponsor, Representative Benjamin Butler from Massachusetts.

It would have been difficult to imagine a more cagey and dangerous opponent than Representative Butler, who was one of the most colorful political figures of an age marked by such characters. After using his political influence to secure an appointment as a general in the Union army, he outraged southerners by confiscating slaves on the grounds that they were "contraband" and employing them in support of the Union war effort. Later he commanded the ground troops that accompanied flag officer, later Admiral, David Farragut's famous capture of New Orleans. Butler eventually became the military governor of the city, earning the name "Beast" Butler for his harsh and uncompromising rule. After being recalled to Washington, he commanded a series of military disasters, most notably the failure to capture Fort Fisher, North Carolina in 1864. He spent various parts of his political career in both the Democratic and Republican parties before eventually ended up as the Populist candidate for president in 1884. At the time of the navy pension fund debates, Butler was a leader of the Radical Republicans in Congress. As an anti-slavery New Englander who had ruthlessly pursued the death of the Confederacy and the subjugation of the South, Butler might have been expected to be Welles's ally, but he had more than one axe to grind when it came to Welles and the administration.

Welles and Butler had crossed paths many times in their careers. At various times, Welles considered Butler an incompetent general, a political opportunist, and an outright criminal. These assessments of Butler's character were held by many other leaders; however, Welles also recognized that Butler was a fearless proponent of the Union, and Welles had explicitly defended Butler's administration of New Orleans to President Lincoln (West 1943). Furthermore, Welles recognized that Butler had a first-class legal mind, and eventually Welles supported—unsuccessfully, as it turned out—the nomination of Butler as the prosecutor in the trial of Jefferson Davis (Nash 1969).

An even more portentous case, which Butler *did* prosecute, led to the permanent estrangement of the two men. The year before his attack on the navy pension fund Butler had led the prosecution in the impeachment trial of Andrew Johnson. Welles, who had remained loyal to the administration after Lincoln's assassination, came to consider Butler's role in the proceedings to be dishonorable at best and, to the extent Butler suborned perjury from at least one potential witness, probably criminal (Niven 1973). Despite Welles's occasional defense of Butler during the Civil War, their battle over the navy pension fund had its roots in the dispensation of booty from that conflict.

Disputes between the various branches of the armed services go back centuries. In comparing the glorious performance of the U.S. navy with that of the army during the War of 1812, future assistant navy secretary (and army colonel) Theodore Roosevelt wrote that "the war on land for us had been full of humiliation . . . the militiamen, a partially armed mob, ran like sheep whenever brought into the field. The regulars were not much better . . . [and] the generals were as bad as the armies they commanded" (1882).

For their part, the soldiers in the trenches often resented what they considered to be a more pampered existence in the navy, and army officers in particular were acutely aware of the potential for enrichment offered by prizes. Such opportunities were generally unavailable, at least legally, to soldiers. Nathaniel Greene, a general in the Continental army, noted that his ill-fed and poorly clad troops were "distressed" at news of the financial success of their naval colleagues resulting from the liquidation of prizes. Similarly, Napoleon was perpetually confounded by his admirals' hunger for prizes, which he felt was matched only by their distaste for engaging British ships of the line. He complained that when it came to fighting a man-of-war his admirals "saw double," though they were all to eager to scoop up unescorted merchantmen.

The dispute between Welles and Butler had more than a touch of interservice rivalry. Welles, a Connecticut Yankee, had once been a Jacksonian Democrat but had eventually abandoned the party over slavery. He was by all accounts deliberate, temperate, and decorous, characteristics not typically attributed to Butler. In every post Butler held during the war, he was accused of corruption. Although Welles himself was not aloof from such accusations, his biographer summarized Welles's opinion of Butler's management of the Norfolk area (after Butler's recall from New Orleans) as "scandalous." In his diaries, Welles was typically a bit more decorous, but nonetheless considered Butler a man of less than sterling character.

For his part, Butler's opinion of Welles was no more charitable, but unlike Welles, Butler displayed no restraint in saying exactly what he disliked and why. No Civil War general was more blatantly outspoken in his criticism of the navy's prize system than Butler. He was particularly incensed by the navy's selection of targets entering southern ports. He thought navy officers were letting inbound blockade runners carrying weapons, ammunition, and supplies sneak through to safe harbors while they concentrated on stopping outward bound ships in order to confiscate their more remunerative cargoes of cotton. He all but accused Welles of complicity in this scheme.

> Thus our system of prize money was in fact a bribe to every one of our blockading vessels of many, many dollars to let all blockade runners in with their supplies and catch them when they came out with their cargo of cotton. Yet our Secretary of the Navy [Welles] never waked up [sic] during the four years of the war. (Butler 1892)

This accusation comes from Butler's memoirs, published years later. However, Butler's remarks on the prize system, delivered on the floor of the House during the pension fund debate, express the same sentiments. They dripped with sarcasm. Noting that only half of the (net) prize money had been deposited in the pension fund, Butler added:

> Now then, the other half has been distributed to the officers and the men of the Navy, over thirteen million dollars, as their own, which they have gone away with. I do not know that it is germane to this subject to enter into any discussion of that distribution. . . . The soldier who has not had any prize money, the soldier who has not had any comfortable ship to sleep in all the time, but has slept in the muddy trenches must look to the general Treasury for his pension, and I think the sailor and seaman . . . should look to the same source for his pension. (*Congressional Globe* 1868)

Butler demonstrated at least a rudimentary understanding of the principles of "the currency question" when he discussed the relationship between the pension fund and the U.S. Treasury. He argued that in the unified accounts of the U.S. government, the navy pension fund's $13 million in assets was balanced on the other side of the ledger by a debt obligation that was the responsibility of the U.S. Treasury. The Treasury was collecting "$319,878.25 [in currency or greenbacks], while the interest of that fund is $780,000 in gold" (*Congressional Globe* 1868). Although this assertion stretched the truth a little in terms of the then current greenback-to-gold ratio, the essence of the argument rang true, and it was effective in the debate.

For his part, Secretary Welles made no attempt to conceal his outrage at what he perceived to be a gross breach of faith. In his 1868 report, he reminded Congress that the original legislation had pledged:

> that the money arising from the sale of prizes shall be and forever remain a fund for the payment of naval pensions and for the investment in registered bonds bearing interest in gold. It is difficult to reconcile the act of July last, which reduces the interest to three per cent in currency, with the pledge faith previously given, . . . had not the income been reduced over fifty per cent by the act of July last, the rate of naval pensions might be increased, and I should have felt it my duty to renew my recommendation for a revision of the naval pension laws for that purpose. (U.S. Navy 1868)

The exact value of the loss imposed on the plan's assets by the action of Congress is difficult to determine. Dollar value or interest yield comparisons between 1862 and 1868 are suspect depending on whether references are to greenbacks or gold. Confusion concerning the dollar value and yields of securities played a role in the congressional debate in 1868 that led to the loss of autonomy of the navy pension plan in the management of its portfolio.

The fact that the fund's assets paid in gold was not the only or perhaps not even the principal complaint against the fund. Another factor that weighed heavily in Butler's attack on the fund involved the so-called "sinking fund" of the United States. As noted earlier, Alexander Hamilton, in his plan for the consolidation and origination of the U.S. debt, set up a scheme to repay any indebtedness incurred by the government. That plan proved to be effective in nearly paying off the debt by 1832, and despite its subsequent reappearance, at the beginning of the Civil War the federal debt stood at only $50 million. Over the next four years, the national debt rose to $2.4 billion (Sylla and Wilson 1999). Butler's argument was that the excess of the navy pension plan's receipts over its obligations should revert to the Treasury for debt reduction. This scenario could be compared to the use of Social Security to support other (that is, non-Social Security) government expenditures or the use of Social Security surpluses to repurchase outstanding government debt. Although a less than outstanding field general, Butler was by all accounts a clever politician, and he ultimately carried the day. The bill passed, ending forever the U.S. navy's early experiment in both the funding of its pension plan and the investment in private equities as part of its financing strategy.

The value of navy pension funds confiscated by the Treasury in 1868 was between $13 and $14 million in terms of greenbacks, but it had a gold value of only about $9.5 million. The 3 percent interest remitted to the fund by the Treasury was certainly less than the higher greenback coupon rate of 6 percent or the considerably higher gold yield at the time. However, nominal interest yields on government bonds following the Civil War until the first World War ranged between 3.5 percent and 4.5 percent (Wilson and Jones 1997). In any case, the change in funding scheme eliminated any extraordinary surpluses from the fund and ameliorated any tendency to expand coverage or benefits. As a result of these actions, the navy pension fund finally came to an end, almost.

From 1869 until World War I, with the inexplicable exception of 1891, the U.S. Treasury annually credited the navy pension plan with an interest payment of $420,000 (3 percent of $14 million). Indeed, the essential features of the navy pension plan continued until it was abolished by Congress in 1935. When annual expenditures exceeded $420,000, benefits were paid from other naval accounts. When expenditures were less than the credited interest payment, the navy reallocated the surplus to other items. In essence, the legislation of 1868 converted the navy pension plan from a funded pension system to a pay-as-you-go pension plan. Interestingly, the country's decision about funding the Social Security trust fund in the twentieth century was directly counter to that of the navy pension. Apparently, a majority of the members of Congress (in 1868) reflected on the navy's antebellum experiences and decided public assets were the best match for public liabilities.

Retirement Pensions

Each of the navy pension plans and/or funds discussed so far was originally intended to be a disability plan for the seamen and a life insurance plan for their dependents. However, all of these early plans, including the Revolutionary pensions, the War of 1812 pensions, and the antebellum and Civil War pension plans, eventually became what today would be called retirement plans. Although nominally a symbol of the republic's gratitude for military service, the stipends essentially served as old-age pensions with half-pay and later full-pay for life in the case of veterans of the Revolution and of the War of 1812, and eight dollars a month for Mexican War veterans. Interestingly, these pensions were originally created only for army veterans (the navy, as we have seen, having its own plan), but when they were converted to life annuities, navy personnel were covered as well.

Perhaps even more interesting is the fact that the "regular" navy established retirement pensions, in the modern sense of that term, before any other institution, public or private, in the United States. In 1855, Congress passed "An Act to Promote the Efficiency of the Navy." It created a review board composed of five officers from each of the following ranks: captain, commander, and lieutenant. The board was to recommend to the Secretary of the Navy that superannuated officers or those generally found to be unfit be placed on the reserve rolls at half-pay subject to the approval of the President. This act was passed during the absence of the navy pension fund, and because the officers were subject to recall, the pensions were paid from navy personnel appropriations. Before it had any noticeable effect on either the efficiency of the navy or the history of pensions, the South Carolina militia fired on Fort Sumter.

With the onset of the Civil War, the Lincoln administration sought to ease a number of superannuated senior military personnel into retirement and to prevent the future accumulation of such individuals in the army and navy. In August of 1861, Congress established a formal retirement plan for U.S. naval officers. The essential features of this plan were to remain in effect throughout the rest of the century. Retirement could occur in one of two ways: either a retirement board could find the officer incapable of continuing on active duty, or after 40 years of service an officer could apply for retirement. In either case, officers on the retired list remained subject to recall, were entitled to wear their uniforms, were subject to the Articles of War and courts-martial, and received 75 percent of their base pay; however, certain constraints on the length of the retired list limited the effectiveness of the act (see below). In July 1862, marine officers aged 63 or over with more than 45 years of service could be retired at the President's discretion. Interestingly, naval officers were not subject to this act.

The acts of 1861 and 1862 applied to officers only. However, prior to the demise of the navy pension fund in 1867, Congress authorized the retirement of seamen and marines who had served 20 or more years and who had become infirm as a result of old-age. These veterans would receive one-half their base pay for life. These pensions were nominally payment in lieu of residence at the Naval Home, but because the home was hopelessly oversubscribed and would continue to be indefinitely, the stipends became in essence old-age pensions. In addition, the act allowed any seaman or marine who had served 10 or more years and subsequently become disabled to apply to the Secretary of the Navy for a "suitable amount of relief" up to one-half base pay from the navy pension fund. Thus, the United States navy established a defined benefit retirement plan (accompanied by a disability plan) for all of its uniformed personnel by 1868. It was soon to be followed by a number of other institutions, public and private.

Notes

1. See, for example, the sources cited in Wise, Holcombe, and Foster (1996).
2. The material in this section pertains to the payment of pensions to Union personnel only. Some of the states in the Confederacy paid extremely small pensions to their veterans. These Confederate pensions are not considered in this volume.
3. See, for example, some of the cases cited in Scott (1923).
4. For details concerning the names of U.S. government debt instruments, see Chapter 5.