

## DEPARTMENT OF VETERANS AFFAIRS

### 38 CFR Part 5

RIN 2900-AL83

### Elections of Improved Pension; Old-Law and Section 306 Pension

**AGENCY:** Department of Veterans Affairs.

**ACTION:** Proposed rule.

**SUMMARY:** The Department of Veterans Affairs (VA) proposes to reorganize and rewrite in plain language its regulations relating to its “old-law” and “section 306” pension programs, as well as its regulations concerning elections of improved pension. These revisions are proposed as part of VA’s reorganization of all of its compensation and pension regulations in a logical, claimant-focused, and user-friendly format. The intended effect of the proposed revisions is to assist readers in locating and understanding these regulations.

**DATES:** Comments must be received by VA on or before February 25, 2005.

**ADDRESSES:** Written comments may be submitted by: mail or hand-delivery to Director, Regulations Management (00REG1), Department of Veterans Affairs, 810 Vermont Avenue, NW., Room 1068, Washington, DC 20420; fax to (202) 273-9026; e-mail to [VAregulations@mail.va.gov](mailto:VAregulations@mail.va.gov); or, through <http://www.Regulations.gov>. Comments should indicate that they are submitted in response to “RIN 2900-AL83.” All comments received will be available for public inspection in the Office of Regulation Policy and Management, Room 1063B, between the hours of 8 a.m. and 4:30 p.m., Monday through Friday (except holidays). Please call (202) 273-9515 for an appointment.

**FOR FURTHER INFORMATION CONTACT:** Bill Russo, Chief, Regulation Rewrite Project (00REG2), Department of Veterans Affairs, 810 Vermont Avenue, NW., Washington, DC 20420, (202) 273-9515.

**SUPPLEMENTARY INFORMATION:** The Secretary of Veterans Affairs has established an Office of Regulation Policy and Management (ORPM) to provide centralized management and coordination of VA’s rulemaking process. One of the major functions of this office is to oversee a Regulation Rewrite Project (the Project) to improve the clarity and consistency of existing VA regulations. The Project responds to a recommendation made in the October 2001 “VA Claims Processing Task Force: Report to the Secretary of Veterans Affairs.” The Task Force recommended that the compensation and pension regulations be rewritten

and reorganized in order to improve VA’s claims adjudication process. Therefore, the Project began its efforts by reviewing, reorganizing and redrafting the regulations in 38 CFR part 3 governing the compensation and pension (C&P) program of the Veterans Benefits Administration (VBA). These regulations are among the most difficult VA regulations for readers to understand and apply.

Once rewritten, the proposed regulations will be published in several portions for public review and comment. This is one such portion. It includes proposed regulations regarding elections of Improved pension benefits as well as regulations concerning two prior pension programs, Old-Law pension and Section 306 pension.

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### Overview of New Part 5 Organization

We plan to remove the compensation and pension benefit regulations from 38 CFR part 3 and relocate them in new part 5. We also plan to reorganize the regulations so that all provisions governing a specific benefit are located in the same subpart, with general provisions pertaining to all compensation and pension benefits also grouped together. We believe this reorganization will allow claimants and their representatives, as well as VA personnel, to find information relating to a specific benefit more quickly.

The first major subdivision would be “Subpart A—General Provisions.” It would include information regarding the scope of the regulations in new part 5, delegations of authority, general definitions, and general policy provisions for this part.

“Subpart B—Service Requirements for Veterans” would include information regarding a veteran’s military service, including the minimum service requirement, types of service, periods of war, and service evidence requirements. This subpart was published as proposed on January 30, 2004. *See* 69 FR 4820.

“Subpart C—Adjudicative Process, General” would inform readers about types of claims and filing procedures, VA’s duties, rights and responsibilities of claimants, general evidence requirements, and general effective dates for new awards, as well as revision of decisions and protection of VA ratings.

“Subpart D—Dependents and Survivors of Veterans” would inform readers how VA determines whether an individual is a dependent or a survivor of a veteran. It would also provide the evidence requirements for these determinations.

“Subpart E—Claims for Service Connection and Disability Compensation” would define service-connected compensation, including direct and secondary service connection. This subpart would inform readers how VA determines entitlement to service connection. The subpart would also contain those provisions governing presumptions related to service connection, rating principles, and effective dates, as well as several special ratings. This subpart will be published as three separate Notices of Proposed Rulemaking (NPRMs) due to its size. The first, concerning presumptions related to service

connection, was published on July 27, 2004. *See* 69 FR 44614.

“Subpart F—Nonservice-Connected Disability Pensions and Death Pensions” would include information regarding the three types of nonservice-connected pension: Improved pension, Old-Law pension, and Section 306 pension. This subpart would also include those provisions that state how to establish entitlement to Improved pension, and the effective dates governing each pension. The portion concerning Old-Law and Section 306 pension and elections of Improved pension is the subject of this document. A subsequent NPRM will cover Improved pension.

“Subpart G—Dependency and Indemnity Compensation, Death Compensation, Accrued Benefits, and Special Rules Applicable Upon Death of a Beneficiary” would contain regulations governing claims for dependency and indemnity compensation (DIC); death compensation; accrued benefits; benefits awarded, but unpaid at death; and various special rules that apply to the disposition of VA benefits, or proceeds of VA benefits, when a beneficiary dies. This subpart would also include related definitions, effective-date rules, and rate-of-payment rules. This subpart will be published as two separate NPRMs due to its size. The portion concerning accrued benefits, special rules applicable upon the death of a beneficiary, and several effective date rules, was published as proposed on October 1, 2004. *See* 69 FR 59072. The portion concerning DIC benefits and general provisions relating to proof of death and service-connected cause of death will be the subject of a separate NPRM.

“Subpart H—Special and Ancillary Benefits for Veterans, Dependents, and Survivors” would pertain to special and ancillary benefits, including benefits for children with various birth defects.

“Subpart I—Benefits for Certain Filipino Veterans and Survivors” would pertain to the various benefits available to Filipino veterans.

“Subpart J—Burial Benefits” would pertain to burial allowances.

“Subpart K—Matters Affecting Receipt of Benefits” would contain provisions regarding bars to benefits, forfeiture of benefits, and renouncement of benefits.

“Subpart L—Payments and Adjustments to Payments” would include general rate-setting rules, several adjustment and resumption regulations, and election-of-benefit rules.

The final subpart, “Subpart M—Apportionments and Payments to Fiduciaries or Incarcerated Beneficiaries” would include regulations governing apportionments, benefits for incarcerated beneficiaries, and guardianship.

Some of the regulations in this NPRM cross-reference other compensation and pension regulations. If those regulations have been published in this or earlier NPRMs for the Project, we cite the proposed part 5 section. We also include, in the relevant portion of the Supplementary Information, the **Federal Register** page where a proposed part 5 section published in an earlier NPRM may be found. However, where a regulation proposed in this NPRM would cross-reference a proposed part 5 regulation that has not yet been published, we cite to the current part 3 regulation that deals with the same subject matter. The current part 3 section we cite may differ from its eventual part 5 replacement in some respects, but we believe this method will assist readers in understanding these proposed regulations where no part 5 replacement has yet been published. If there is no part 3 counterpart to a proposed part 5 regulation that has not yet been published, we have inserted “[regulation that will be published in a future Notice of Proposed Rulemaking]” where the part 5 regulation citation would be placed.

Because of its large size, proposed part 5 will be published in a number of NPRMs, such as this one. VA will not adopt any portion of part 5 as final until all of the NPRMs have been published for public comment.

In connection with this rulemaking, VA will accept comments relating to a prior rulemaking issued as part of the Project, if the matter being commented on relates to both NPRMs. VA will provide a separate opportunity for public comment on each segment of the proposed part 5 regulations before adopting a final version of part 5.

#### Overview of Proposed Subpart F Organization

This NPRM proposes regulations governing elections of Improved pension and the requirements for maintaining entitlement to old-law or section 306 pension. These regulations would be contained in proposed subpart F of new 38 CFR part 5. Although these regulations have been substantially restructured and rewritten for greater clarity and ease of use, most of the basic concepts contained in these proposed regulations are the same as in their existing counterparts in 38 CFR part 3.

In a future NPRM, we will propose regulations concerning the Improved pension program.

#### Table Comparing Current Part 3 Rules With Proposed Part 5 Rules

The following table shows the relationship between the current regulations in part 3 and those proposed or redesignated regulations contained in this NPRM:

Proposed part 5 section or paragraph	Based in whole or in part on 38 CFR part 3 section or paragraph (or “new”)
5.460 .....	3.1(u), (v), (x)
5.461(a) and (b) .....	3.711
5.461(b)(1) through (b)(3) .....	New
5.461(c) .....	3.711
5.461(d) .....	3.960(a)
5.462 .....	3.712(a)
5.463 .....	3.713(a)
5.464 .....	3.700(a)(4)
5.470(a) .....	3.960(b), 3.252(a), (b)
5.470(b) .....	3.960(d)
5.470(c) .....	3.960(c)
5.471 .....	3.28
5.472(a) .....	3.262(b)
5.472(b)(1) and (2) ....	3.252(c); 3.262(a)
5.472(b)(2)(i) and (ii) ..	3.262(h)
5.472(b)(3) .....	3.260(g)
5.472(b)(4) .....	Introduction to 3.260, 3.660(a)(4)
5.472(c)(1) .....	3.262(a)(2), (3)
5.472(c)(2) .....	3.262(j)(4)
5.472(c)(3) .....	3.261(a)(22), 3.262(a)(1)
5.472(d)(1) and (d)(2) ..	3.262(k)(1), (k)(2)
5.472(d)(3) .....	3.262(a)
5.472(d)(4) .....	3.262(k)(1)
5.472(d)(5) .....	3.262(k)(3)
5.472(d)(6) .....	3.262(k)(4)
5.472(d)(7) .....	3.262(k)(5)
5.472(e) .....	3.261(a)(20)
5.472(f)(1) .....	3.262(c)
5.472(f)(2) .....	3.262(r)
5.472(f)(3) .....	3.261(a)(12)
5.472(f)(4) .....	3.261(a)(13)
5.472(f)(5) .....	3.261(a)(31)
5.472(f)(6) .....	3.262(t), (t)(2)
5.472(f)(7) .....	3.261(a)(20)
5.472(f)(8) .....	3.261(a)(7)
5.472(f)(9) .....	3.262(a)(2)
5.472(f)(10) .....	3.261(a)(26)
5.472(f)(11) .....	3.261(a)(22)
5.472(f)(12) .....	3.262(e), (e)(1), (e)(2), (f), (g), (i)(2), (j)(1), (j)(2), (j)(3)
5.472(f)(13) .....	New
5.472(g)(1) .....	3.262(d), (f)
5.472(g)(2) .....	3.262(f)
5.472(g)(3) .....	3.262(k)(1)
5.472(h) .....	3.262(d)
5.473(a) .....	3.262(b)(2)
5.473(b)(1) .....	New
5.473(b)(2) .....	3.262(b)(2)
5.473(c) .....	3.252(e)
5.473(d) .....	3.261(a)(4)
5.474(a) .....	3.960(a)
5.474(b) .....	3.262(l), 3.262(l)(1), (l)(2), (l)(3)
5.474(c) .....	3.262(n), (p)

Proposed part 5 section or paragraph	Based in whole or in part on 38 CFR part 3 section or paragraph (or "new")
5.474(d) .....	3.262(k)(6)
5.475(a) .....	3.260(a), (f)
5.475(b) .....	3.260(f), 3.252(e)(4)
5.475(c) .....	3.252(d)
5.476 .....	3.263
5.477(a) .....	3.660(a)(2)
5.477(b) .....	3.500, 3.501, 3.502, 3.503
5.478(a) .....	3.260(b)
5.478(b) .....	3.660(b)(1)
5.478(c) .....	3.960(d)

Readers who use this table to compare existing regulatory provisions with the proposed provisions, and who observe a substantive difference between them, should consult the text that appears later in this document for an explanation of significant changes in each regulation. Not every paragraph of every current part 3 section affected by these proposed regulations is accounted for in the table. In some instances, other portions of the part 3 sections that are contained in these proposed regulations will appear in subparts of part 5 that are being published separately for public comment. For example, a reader might find a reference to paragraph (a) of a part 3 section in the table, but no reference to paragraph (b) of that section because paragraph (b) will be addressed in a separate NPRM. The table also does not include material from the current sections that will be removed from part 3 and not carried forward to part 5. A listing of material VA proposes to remove from part 3 appears later in this document.

### Background of Prior Pension Programs

"Old-law pension" refers to the nonservice-connected disability and death pension programs that were available to claimants before July 1, 1960. These programs were superseded by the "Veterans' Pension Act of 1959." Public Law 86-211, 73 Stat. 432. However, section 9(b) of that Act protected the right of people receiving pension under the "old law" programs to continue receiving pension under the laws in effect on June 30, 1960.

"Section 306" pension refers to the nonservice-connected disability and death pension programs that were available to claimants on or after July 1, 1960, and through December 31, 1978. Sometimes also referred to as "86-211 pension," or "306 pension," Section 306 pension arose out of Public Law 86-211. VA has adopted the name "Section 306" to refer to these programs because it was section 306 of the "Veterans' and Survivors' Pension Improvement Act of

1978," Public Law 95-588, 92 Stat. 2508, that grandfathered rates paid under both section 306 and old-law pension.

Sections 306(a)(1) and (b)(2) of Public Law 95-588 provide that any person entitled to receive VA pension under the prior pension laws as in effect on December 31, 1978, can elect to receive Improved pension instead. For any individual who is eligible to make an election but does not do so, sections 306(a)(2) and (b)(3) grandfather in the current rates paid by providing that:

[Such] person \* \* \* shall continue to receive pension at the monthly rate being paid to such person on December 31, 1978, subject to all provisions of law applicable to basic eligibility for and payment of pension under [such person's pension program], as in effect on December 31, 1978, [subject to income limits specified for that pension program].

Public Law 95-588, § 306(a)(2). A virtually identical grandfather clause is contained in section 306(b)(3).

Sections 306(a)(3) and (b)(4) go on to provide for automatic increases in the annual income limits and the spousal income exclusion by the same percentage as the automatic cost-of-living adjustments under the Improved pension program.

A claimant cannot establish new entitlement to either Section 306 or Old-Law pension; once a beneficiary loses entitlement under either of these programs, the only pension program for which VA may consider entitlement is Improved pension under Public Law 95-588.

Before 1998, VA required recipients of Section 306 or Old-Law pension to submit annual eligibility verification reports (EVRs) to VA under current 38 CFR 3.256. However, VA no longer requires annual EVRs from this group of beneficiaries. According to VA's Office of Policy, Planning, and Preparedness, as of January 2004, there were 179 veterans receiving Old-Law disability pension, 618 surviving spouses and/or children receiving Old-Law death pension, 13,523 veterans receiving Section 306 disability pension, and 52,832 surviving spouses and/or children receiving Section 306 death pension.

### Overview of Proposed Regulation Changes

Several current regulations from which these proposed regulations are derived apply to more than one need-based program in effect before January 1, 1979. These programs include Old-Law pension, Section 306 pension, and parents' DIC, as well as regulations for establishing the dependency of parents.

Because of the benefit-based structure of proposed part 5, we propose to divide these current part 3 regulations into separate part 5 regulations, each addressing a different type of benefit. This NPRM pertains to Old-Law and Section 306 pension and not to parents' DIC or establishing the dependency of parents. Future NPRMs will address these current part 3 regulations as they pertain to parents' DIC and establishing the dependency of parents.

### Content of Proposed Regulations

#### *Choosing Improved Pension Over Certain Other VA Pension Programs: Veterans and Survivors*

#### 5.460 Definitions of Certain VA Pension Programs

Proposed § 5.460 is based on current § 3.1(u), (v), and (x). The current regulation describes various types of VA pensions in terms of when the pensions were "in effect." Paragraphs (a) and (b) of proposed § 5.460 amend current § 3.1(u) and (v) to describe the VA pensions in terms of the time periods during which those pensions were "available to new claimants." We believe this is clearer because these pensions are still "in effect" in the limited sense that beneficiaries continue to receive them.

Proposed paragraph (c) defines "Spanish-American War death pension" instead of "service pension," which is defined in § 3.1(x), because to our knowledge there are no surviving veterans of the Spanish-American War.

#### 5.461 Electing Improved Pension Instead of Old-Law or Section 306 Pension

Proposed § 5.461 is based on current §§ 3.711 and 3.960(a). Proposed § 5.461 includes a parenthetical reference to the word "choose" immediately after the more technical term "elect" in the heading to proposed paragraph (a) and the first time that the word "elect" appears in the regulation text. The parenthetical reference provides a plain-language synonym for the technical term, "elect."

The first sentence of current § 3.711 states that individuals who are eligible to elect Improved pension may do so "under the provisions of 38 U.S.C. 1521, 1541, or 1542 as in effect on January 1, 1979." We propose to remove this phrase. Instead, proposed § 5.461 simply refers to Improved pension. We believe that removing the phrase makes the proposed regulation clearer. We note that the regulations pertaining to Improved pension would immediately precede the regulations pertaining to

elections of Improved pension in new part 5.

Current § 3.711 provides that unless the provisions of current § 3.714 apply, an election of Improved pension is final when the payee or his or her fiduciary negotiates one check for this benefit. We propose to remove this reference to § 3.714 because we are proposing to remove § 3.714. The proposed removal of § 3.714 is described later in this NPRM. We propose to add three circumstances under which an election may be canceled. All of these circumstances are matters of longstanding VA policy, are reasonable, and are helpful to VA beneficiaries.

First, because the vast majority of VA beneficiaries now receive benefits by direct deposit and the current regulation that states when an election becomes final is based on negotiation of a check, proposed paragraph (b)(1) states that beneficiaries who receive benefits by direct deposit may cancel an election of Improved pension if the beneficiary informs VA of a desire to cancel the election before the financial institution receives the second direct deposit payment.

Second, proposed paragraph (b)(2) states that if VA later determines that the beneficiary was incompetent when he or she elected Improved pension, the election can be canceled if the beneficiary or his or her guardian cancels the election within one year after the date the election became effective.

Finally, proposed paragraph (b)(3) states that a beneficiary can cancel an election within one year after the effective date of the election if he or she elected Improved pension based on erroneous information that VA provided. However, VA must determine, based on the same evidence of record, that it provided the beneficiary with erroneous information. One example of this rule's application would be if VA mistakenly informed the beneficiary that he or she would be entitled to a higher rate upon election of Improved pension and later VA determines that this was not the case, based on the same evidence of record at the time VA mistakenly informed the beneficiary of his or her entitlement to a higher rate.

Proposed § 5.461(d) is based on § 3.960(a), which currently provides that beneficiaries who do not elect Improved pension will continue to receive section 306 or old-law pension at the rate payable on December 31, 1978, unless that rate must be reduced or discontinued as provided in § 3.960(b) and (c). Current paragraph § 3.960(a) is incomplete in implying that the reasons provided in paragraphs (b) and (c) are

the only situations in which a Section 306 pension or Old Law pension rate might be reduced. Current § 3.551, for example, provides for reductions when certain beneficiaries are hospitalized at VA expense. Therefore, proposed § 5.461(d) states that in the absence of an election, the December 31, 1978, rate will continue "unless that rate must be reduced or discontinued under § 5.470 or another regulation in this part."

#### 5.462 Right of Surviving Spouses Receiving Spanish-American War Death Pension to Elect Improved Death Pension

Proposed § 5.462 is derived from current § 3.712(a). Proposed § 5.462 states that the regulations governing finality of election under proposed § 5.461(b) also apply to surviving spouse beneficiaries of Spanish-American War death pension who elect Improved death pension. This is longstanding VA policy. Proposed § 5.461(d) does not apply to surviving spouses of Spanish-American War veterans because Spanish-American War death pension is not based on income or net worth but on the veteran's service only. The proposed regulation states that these surviving spouses who do not elect Improved pension will continue to receive Spanish-American War death pension.

We propose to remove the statutory references to 38 U.S.C. 1536 and 1541, and instead refer to Spanish-American War death pension and Improved death pension. We believe that removing these statutory references makes the regulation easier to understand.

#### 5.463 Effective Dates of Improved Pension Elections

Proposed § 5.463 is derived from current § 3.713(a) and states that an election of Improved pension will be effective on the date that VA receives it.

#### 5.464 Multiple Pension Awards Not Payable

Proposed § 5.464 is derived from § 3.700(a)(4) without any substantive changes.

#### *Continuing Entitlement to Old-Law or Section 306 Pension: Veterans and Survivors*

#### 5.470 Reasons for Discontinuing or Reducing Section 306 or Old-Law Pension

Proposed § 5.470 is derived from current § 3.960(b) through (d). We propose to replace the current word "terminate" and all its iterations with the word "discontinue" and all its iterations. Throughout all of part 5, the Project proposes to use the word

"discontinue" instead of "terminate" in reference to ending VA benefits because we believe the word "terminate" has an adversarial connotation. While one could argue that the word "terminate" better describes the finality of losing entitlement to prior pension than the word "discontinue," we wish to remain consistent in our terminology to the extent possible. More significantly, we note that the word "discontinuance" in reference to ending a beneficiary's entitlement is statutory. See 38 U.S.C. 5112.

Proposed § 5.470(c), based on current § 3.960(c), states that VA will reduce pension based on the loss of a dependent if the dependent was established before January 1, 1979. The regulation need only cover dependents established before that date because section 306 and old-law pension rates are based on calendar year 1978 dependency and income. Pension rates under these programs do not increase when a dependent is established on or after January 1, 1979. Proposed § 5.470(c) clarifies that reductions due to the loss of a dependent are final and such reduced rates do not increase.

#### 5.471 Annual Income Limits and Rates for Section 306 and Old-Law Pension

The proposed regulation, § 5.471, is derived from current § 3.28.

Proposed paragraph (a) informs readers that annual income limits as well as historical pension rates are available on VA's Web site, <http://www.VA.gov>.

Rather than referring to increasing annual income limits "by reason of the provisions of 38 U.S.C. 5312," as current § 3.28 does, proposed § 5.471(b) refers instead to the cost-of-living increase in Social Security benefit amounts. We believe this reference is more familiar to readers and incorporates the provisions of 38 U.S.C. 5312. We note that current § 3.27 refers to the Social Security cost-of-living increase rather than to 38 U.S.C. 5312.

#### 5.472 Evaluation of Income for Section 306 and Old-Law Pension

Current §§ 3.261 and 3.262 provide the regulatory framework VA uses to determine how to calculate income for purposes of section 306 pension, old-law pension, dependency of a parent, and parents' DIC. Because those sections deal with the evaluation of income in different contexts, they are lengthy and complex. As a result, they can be difficult to understand and use. We propose to divide the subject matter addressed by current §§ 3.261 and 3.262 into separate regulations pertaining to these three subjects—dependency of a

parent, parents' DIC, and section 306 and old-law pension. Because income determinations for section 306 and old-law pension are similar in many respects, we propose to continue to combine the regulations for these programs. Proposed § 5.472 deals only with evaluation of income for section 306 and old-law pension. Income regulations for dependency of a parent and parents' DIC will be addressed in other NPRMs.

Proposed § 5.472(b) states the basic rule that VA must count all payments of any kind from any source in determining income. Beginning with this basic rule permits simplification of the proposed regulation because the all-inclusive nature of the basic rule eliminates the need to catalog types of countable income. All income counts unless there is a specific exclusion. Therefore, we propose to remove the first sentence of current § 3.262(j)(2). A discussion of our proposed removal of current § 3.261 and additional removals from § 3.262 are later in this NPRM under "Explanation of Additional Proposed Removals from Part 3."

Proposed § 5.472(b)(3) clarifies that VA rounds down after subtracting deductible expenses from countable income.

Proposed § 5.472(b)(4) incorporates the introductory language of current § 3.260, but clarifies that although VA computes income for the year of receipt, VA does not discontinue benefits based on income that exceeds the income limit until the beginning of the following calendar year.

While VA counts all income except where there is specific authority to exclude it, VA permits deductions from countable income in some instances. That is, the amount of income ultimately counted is the difference between income and certain deductible expenses directly associated with that income. Proposed paragraph (c) lists permitted deductions from particular income sources. Deductions from all income sources for section 306 pension purposes are contained in a separate regulation, proposed § 5.474.

Proposed § 5.472(c)(1) continues a rule in current § 3.262(a)(2) that permits the deduction of expenses incident to the operation of businesses and professions from income from those sources. We propose to clarify that "business" includes the operation of a farm and transactions involving investment property. Because of this definitional change, it is only necessary to state in § 5.472(c)(1) that losses sustained in operating a business or profession may not be deducted from income from any other source. This is

consistent with the rule in current § 3.262(a)(3) that states that "[a] loss sustained in operating a business, profession, or farm or from investments may not be deducted from income derived from any other source." Note also that current § 3.262(a)(3) implies that investment income is counted and that current § 3.262(k)(5) provides, with respect to section 306 pension, that profit from the sale of nonbusiness property is not counted. With respect to investments, VA only counts income when the investment property is sold and does not constantly adjust income based on increases or decreases in the market value of investment property due to market fluctuations. Therefore, VA essentially already treats investment transactions as business transactions.

Proposed § 5.472(c)(2) continues a provision in current § 3.262(j)(4) that permits deduction of related medical, legal, or other expenses from sums recovered under disability, accident, or health insurance. Of course, the same expenses cannot be deducted twice. Therefore, we propose to state in § 5.472(c)(2) that if medical expenses are deducted under that paragraph, they cannot be deducted as unusual medical expenses under § 5.474.

Proposed § 5.472(d) provides the rules VA uses to determine whether income from property is the income of a pension beneficiary (or a veteran's spouse for Section 306 pension purposes). Property ownership is an important indicator of the right to income from that property, but it is not always controlling. In keeping with longstanding VA practice, we propose to state in paragraph (d)(3) that if a beneficiary transfers ownership of income-producing property to another person or legal entity, but retains the right to that income, the income will be counted.

Current § 3.262(k)(1) provides, in part, that "if property is owned jointly each person will be considered as owning a proportionate share." The claimant's share of property held in partnership will be determined on the facts found." Current § 3.262(k)(2) provides, in part, that the claimant's share of "[i]ncome received from real or personal property \* \* \* will be determined in proportion to his right according to the rules of ownership." We propose to combine and simplify these provisions in proposed § 5.472(d)(4) by stating: "[w]here a pension beneficiary owns property jointly with others, including partnership property, each person will be considered as receiving an equal share of the income from that property in the absence of evidence showing otherwise." (Pension beneficiaries may

submit evidence showing that they receive a greater or lesser share of the income.) We believe this will be much easier for beneficiaries to understand.

Proposed paragraph (d)(5), based on applicable portions of current § 3.262(k)(3) and (4), provides an exclusion for an old-law pension beneficiary's net profit from the sale of a principal residence when that profit is used to purchase another principal residence within specified time constraints. Current § 3.262(k)(3), provides in part:

In determining net profit from the sale of property owned prior to the date of entitlement, the value at the date of entitlement will be considered in relation to the selling price. Where payments are received in installments, payments will not be considered income until the claimant has received amounts equal to the value of the property at the date of entitlement.

Because, under the current regulation, the basis for calculating net profit on the sale of a residence is only the value at the date of entitlement if the pension beneficiary owned the property before the date he or she became entitled to pension, the basis for calculating the net profit on the sale of a residence acquired after the date of entitlement would be its cost. We propose to clarify that in the installment sale provision set out in proposed § 5.472(d)(5)(iii).

Proposed § 5.472(e) is an exception to our general guideline that we list only exclusions and not income that counts. Because there are many different VA benefits, most of which are excluded for prior pension purposes, we believe it would be simpler in this instance to list the VA benefits that count rather than those that don't.

Although VA insurance payments are excluded from income under proposed § 5.472(e) because they may be considered VA benefits, proposed paragraph (f)(7) specifically provides that payments under policies of Servicemembers' Group Life Insurance, United States Government Life Insurance, and National Service Life Insurance do not count as income in order to make sure that it is clear that these payments are not considered income for VA purposes.

Most of the income exclusions that apply to both Section 306 and Old-Law pension are listed in proposed § 5.472(f). In proposed paragraph (f)(3), we propose to change the description from "six-months' death gratuity" as it is in current § 3.261(a)(12), to "death gratuity payments under 10 U.S.C. 1475 through 1480." The phrase "six-months' death gratuity" is obsolete. Although the gratuity consisted of six-months' pay when Congress originally authorized VA

to pay this benefit (*see* Public Law 66–99, 41 Stat. 367 (1919)), that is no longer the case. Over the years, these death gratuity payments have evolved into a fixed sum, rather than an amount equal to six-months' pay. *See* 10 U.S.C. 1478.

Current § 3.261(a)(7) states that VA will not count as income, "Rental value of property owned and resided in by claimant." The intent of the regulation is to make it plain that VA will not impute a rental value to a pension beneficiary's own property and count that value as income. However, if a beneficiary resides in a duplex, for example, VA would count any rent that the beneficiary receives. We propose to clarify any potential confusion by stating in proposed § 5.472(f)(8) that the exclusion is for "[t]he rental value of a beneficiary's use of his or her own real property, such as the rental value of the beneficiary's personal residence."

Proposed § 5.472(f)(12) combines all of the various § 3.262 ten percent exclusions in one place. One of these 10-percent exclusions, found at current § 3.262(i)(2), is for certain payments received from the "Bureau of Employees' Compensation." The Bureau of Employees' Compensation was abolished in 1974. *See* 20 CFR 1.5. Its functions are now carried out by the Office of Workers' Compensation Programs of the U.S. Department of Labor. *See* 20 CFR 1.6(b). This change would be reflected in proposed paragraph (f)(12)(iv).

In a future NPRM, we plan to propose a new regulation to be contained in proposed subpart L of proposed new part 5. The new regulation would list all income sources and assets that are statutorily excluded in determining entitlement to all need-based programs that VA administers. This separate regulation is the future regulation mentioned in proposed § 5.472(f)(13).

These broad exclusions that will be addressed in a future NPRM are therefore not specifically listed in proposed § 5.472. These include some of the income exclusions that currently appear in §§ 3.261 and 3.262. These are Agent Orange settlement payments, certain relocation payments, annuity payments elected under the Retired Serviceman's Family Protection Plan, restitution to individuals of Japanese ancestry, income received by American Indian beneficiaries from trust or restricted lands, payments under the Alaska Native Claims Settlement Act, payments from certain volunteer programs, Victims of Crime Act of 1984 payments, and monetary allowances under 38 U.S.C. chapter 18 for certain children of veterans who served in Vietnam and Korea.

#### 5.473 Counting a Dependent's Income for Section 306 and Old-Law Pension

Proposed § 5.473 is derived from those portions of §§ 3.252, 3.261, and 3.262 that pertain to counting income of dependents. Other portions of current § 3.252 no longer apply to section 306 or old-law pension and we propose to remove them. These removals are discussed later in this NPRM under "*Explanation of Additional Proposed Removals from Part 3.*"

Proposed paragraphs (a) and (b) of proposed § 5.473 state that VA excludes the separate income of a veteran's child for both old-law and section 306 pension purposes. This is not a change and is implied in the current regulation, although not explicitly stated. However, because VA's Improved pension program counts children's income as a veteran's or surviving spouse's income in most cases, it is helpful to state explicitly that children's income doesn't count for purposes of calculating income for veterans who are receiving prior pension.

Current § 3.262(b)(2) provides that VA presumes that including a veteran's spouse's income would not cause hardship to the veteran unless there is evidence showing expenses "beyond the usual family requirements." Proposed § 5.473(b)(2)(i)(B) provides two examples of such expenses: special training for a handicapped child and expenses for the prolonged illness of a family member. However, if the spouse's income is excluded because it is needed to pay for unusual medical expenses, those medical expenses cannot be used as deductible medical expenses. This is longstanding VA policy that we propose to include in the regulation.

#### 5.474 Deductible Expenses for Section 306 Pension Only

Proposed § 5.474 is based on the portions of current § 3.262 that pertain to expenses that may be deducted from all countable income. However, these deductions apply only to section 306 pension and not to old-law pension.

Proposed § 5.474(a) states that deductible expenses paid after December 31, 1978, can only be used to continue entitlement to section 306 pension in order to make that fact more clear. They cannot be used to increase pension benefits because Public Law 95–588 provides that rates paid under the prior pension programs cannot increase. *See* current § 3.960(a).

Proposed § 5.474(b)(1)(i) describes a "family member" for Section 306 pension purposes. Currently, § 3.263 cross-references § 3.250 for the

description of a family member, while paragraphs (l)(1) and (2) of § 3.262 use similar language to describe such relatives. We therefore propose to incorporate this description of a "family member" for Section 306 pension purposes as "a relative of the beneficiary who is a member of the beneficiary's household whom the beneficiary has a moral or legal obligation to support. This includes family members who are physically absent from the household for a temporary purpose or for reasons beyond their control."

In a future NPRM, we plan to propose a new regulation pertaining to Section 306 pension to be contained in proposed subpart L of proposed new part 5. This new regulation would provide a comprehensive explanation of what constitutes a "medical expense" for the purpose of all VA-administered need-based benefits. Therefore, we propose to remove the phrase currently found in § 3.262(l), "[h]ealth, accident, sickness and hospitalization insurance premiums will be included as medical expenses \* \* \*." Instead, proposed § 5.474(b)(1)(ii) refers the reader to the new regulation.

Proposed § 5.474(b)(6) is based on the last sentence of current § 3.262(l), which states that VA will estimate future medical expenses and then adjust them, if necessary, upon receipt of an amended estimate or at the end of the year when the beneficiary files an "income questionnaire." The income questionnaire was the method of income reporting before the advent of Eligibility Verification Reports (EVRs) in 1985. However, recipients of Section 306 pension have not been required to complete annual EVRs since the end of calendar year 1997 because on October 6, 1998, VA amended § 3.256(b)(2) so that old-law and section 306 pension beneficiaries are not required to submit EVRs unless VA determines that doing so is necessary to preserve program integrity. 63 FR 53593 (Oct. 6, 1998). Therefore, we propose to remove the reference to the income questionnaire, and instead provide a cross-reference to the regulation that would replace current §§ 3.256 and 3.660(a), which would state that pension beneficiaries must inform VA if there is a change in income.

Proposed § 5.474(c)(1) defines "final expenses" as the amount an individual pays for a deceased individual's last illness and burial. We believe that having a definition makes the regulation clearer. We also propose to state that VA cannot allow the same expense as both a final expense and an unusual medical

expense in order to make this longstanding policy clearer to readers.

#### 5.475 Gaining or Losing a Dependent for Section 306 and Old-Law Pension

Proposed § 5.475 differs from current § 3.260 because most of current § 3.260 no longer applies to pension awards. Paragraphs (a)(2) and (b)(3) of section 306, Public Law 95–588, provide that VA generally continues to pay the December 31, 1978, rate to beneficiaries of section 306 or old-law pension. A future NPRM will address § 3.260 as it applies to parents' DIC.

Paragraphs (a) and (b) of proposed § 5.475 explain the steps VA takes when a section 306 or old-law pension beneficiary gains or loses a dependent. These proposed paragraphs are based on current § 3.260(f), which pertains to rate changes for pension and parents' DIC. However, VA does not generally change section 306 and old-law pension rates unless the beneficiary loses a dependent who was established for VA purposes before January 1, 1979. In such cases, VA reduces, discontinues, or keeps rates the same but does not increase pension rates. (VA must also change pension rates when current § 3.551 pertaining to hospital adjustments applies. Another exception would be a hypothetical case in which VA computed 1978 annual income incorrectly and amended 1978 income to pay a different "protected" rate.)

Proposed § 5.475(a)(2) states that if a veteran beneficiary of section 306 pension gains a spouse, VA will not consider income that the spouse received or deductible expenses paid by or on behalf of the spouse before the date the person became the veteran's spouse for VA purposes. We believe this is fair to claimants and relatively easy to administer, while remaining consistent with statutory provisions that a spouse's income must be counted. We believe that a spouse's income cannot reasonably be assumed to be that of the veteran before the date the person becomes the veteran's spouse for VA purposes. The proposed regulation is also consistent with longstanding VA practice.

Proposed § 5.475(b)(1) clarifies that when a section 306 or old-law pension beneficiary loses his or her last dependent, the annual income limit is lowered. Proposed § 5.475(b)(2) clarifies that if a dependent was established before January 1, 1979, VA must recompute a new "protected" December 31, 1978, rate based on the changed dependency status and recomputed 1978 income. Proposed paragraph (b)(2)(i) also makes it clearer that VA will continue the December 31, 1978,

rate if a recomputed rate based on a dependency change is higher than the previous rate. This could occur if a veteran receiving Section 306 pension lost a spouse who had income or if a surviving spouse pension beneficiary lost a child whose income was counted as the surviving spouse's by virtue of current § 3.252(e)(3).

Proposed § 5.475(c) is based on current § 3.252(d) and pertains to spousal estrangement for Section 306 pension purposes. The current regulation provides that the "rates" provided by 38 U.S.C. 1521(c) may be authorized to certain married veterans who do not live with or are estranged from their spouses. The reference to "38 U.S.C. 1521(c)" is actually to 38 U.S.C. 1521(c) as in effect on December 31, 1978 (when it was numbered 38 U.S.C. 521(c)), or more simply, the "December 31, 1978, rate for a veteran with a spouse." However, it is not only the rates that apply to such married veterans, but also the annual income limits. The proposed regulation would so provide. Proposed § 5.475(c) also clarifies the longstanding VA policy that the spousal income is not included unless the annual income limit for a married veteran applies.

Current paragraphs (c), (d), and (e) of § 3.260, relating to proportional computations, are not included in proposed § 5.477 or elsewhere in these proposed subpart F regulations. We propose to remove these provisions from regulations governing old-law and section 306 pension because they pertain to proportional computations for original or resumed awards. Proportional computations no longer apply to section 306 or old-law pension claims because new claims are not allowed, nor can these benefits be resumed after they have been discontinued, under section 306 of Public Law 95–588. Paragraphs (c) and (d) of current § 3.260, as they apply to proportional computations for parents' DIC, will be addressed in a future NPRM.

#### 5.476 Net Worth for Section 306 Pension Only

Current § 3.263 provides the regulatory authority for evaluating net worth in determining the dependency of a parent as well as entitlement to section 306 pension. Proposed § 5.476 applies only to section 306 pension for reasons previously outlined.

We propose to use the term "net worth" only and remove references to "corpus of estate" because we believe "net worth" to be the more commonly understood term. The terms "net worth" and "corpus of estate" are defined

synonymously in 38 CFR 3.263(b) and 3.275(b) and used interchangeably. Sections 1522 and 1543 of title 38, United States Code, are both titled, "Net worth limitation." However, the term "net worth" is not used in the text of the statutes. Instead, the statutes refer to the "corpus of the estate" of an affected individual. Although the term "net worth" is not used in the text of these statutes, there is no indication that there is any intended difference between the two terms. In VAOCGPREG 64–91, VA's General Counsel confirmed that the terms "corpus of estate" and "net worth" are used interchangeably "[i]n the context of estate valuation for certain need-based veterans' benefits." In order to prevent any misconception that there is a difference between the two terms, we propose to use one term, "net worth."

Proposed § 5.476(a) includes current and longstanding VA policy concerning the evaluation of a "reasonable lot area," as being that which is reflective of lot sizes in the area. This rule is necessarily broad because lot sizes vary from locale to locale. It might be reasonable in some parts of the country to retain significant acreage. In other parts of the country, the same acreage would constitute a sizeable asset and the test of "reasonableness" would dictate disposal for the beneficiary's maintenance.

Proposed § 5.476(c) specifies that the income VA must consider in a net worth determination is income as determined under § 5.472. We propose this specification in order to make it clear that the income VA considers in a net worth determination is the same as income considered for any Section 306 pension purpose. The law (38 U.S.C. 1503 as in effect December 31, 1978 (when it was numbered 38 U.S.C. 503)) defines "annual income under this chapter," as all payments received except for certain kinds of payments specifically excluded or deducted. Therefore, we must conclude that the reference to income in the net worth statute (38 U.S.C. 1522 as in effect December 31, 1978 (when it was numbered 38 U.S.C. 522)) refers to the same definition of income because both provisions are in the same chapter.

At the same time, we propose to state that when VA considers a beneficiary's living expenses, VA cannot consider expenses excluded or deducted in determining income. This statement clarifies that the same expenses cannot be deducted twice. Because we are making this clarification concerning income and because we believe that the phrase "all of the beneficiary's living expenses" sufficiently encompasses



medical expenses, we do not believe it is necessary to specifically mention unusual medical expenses in proposed paragraph (c). Therefore, we propose to remove the reference to unusual medical expenses currently in § 3.263(d).

Proposed § 5.476 does not incorporate the following phrase currently found in § 3.263(d): “whether the property can be readily converted into cash at no substantial sacrifice.” VA has traditionally defined the phrase “substantial sacrifice” as meaning that benefits should not be discontinued for excessive net worth if the beneficiary cannot readily convert other assets into cash. Therefore, proposed paragraph (c)(1), provides for consideration of “[t]he value of liquid assets and the current market value of other property the beneficiary can readily convert into cash.” We believe this wording would be clearer to beneficiaries, as well as consistent with VA practice.

Finally, proposed § 5.476(d) includes a cross-reference to the listing of payment sources that, by statute, VA must exclude from consideration in determining entitlement to need-based benefits. As previously mentioned, we will propose a regulation in a separate NPRM that would list income sources and assets that are statutorily excluded from consideration for all of VA’s need-based programs. Therefore, the following four such sources, currently listed in § 3.263(e) through (h), are not included in proposed § 5.476: “Agent Orange settlement payments”; “Restitution to individuals of Japanese ancestry”; “Monetary allowance under 38 U.S.C. chapter 18 for certain individuals who are children of Vietnam veterans”; and “Victims of Crime Act.”

#### 5.477 Effective Dates for Section 306 and Old-Law Pension Reductions or Discontinuances

Proposed § 5.477(a) is based on the first sentence of current § 3.660(a)(2), which provides:

Where reduction or discontinuance of a running award of [S]ection 306 pension or [O]ld-[L]aw pension is required because dependency of another person ceased due to marriage, annulment, divorce or death, or because of an increase in income, which increase could not reasonably have been anticipated based on the amount actually received from that source the year before, the reduction or discontinuance shall be made effective the end of the year in which the increase occurred.

Proposed § 5.477(a) clarifies the actual effective date that VA pays a reduced rate or discontinues benefits by stating, “If required, VA will pay a reduced

section 306 or old-law pension rate or discontinue benefits effective January 1 of the calendar year immediately following [certain events].” Proposed paragraphs (a)(1) through (a)(3) then go on to specify those events. We believe that stating the effective date in this manner—focusing on the date that the new rate begins rather than on the date that the old rate ends—clarifies the effective-date provisions for reductions and discontinuances. We propose similar wording throughout the Project. VA intends no substantive change by this rewording.

Proposed § 5.477(b) provides that if a reduction or discontinuance is required for any reason other than the events specified in paragraph (a) or in § 5.478(a), VA will apply the general effective-date rules. These are currently found in §§ 3.500 through 3.503. A future NPRM will address §§ 3.500 through 3.503.

#### 5.478 Time Limit To Establish Continuing Entitlement to Section 306 or Old-Law Pension

Proposed § 5.478(a) is based on current § 3.260(b), which provides that “[w]here there is doubt as to the amount of the anticipated income,” VA will make its decision concerning payment for a particular calendar year based on the best income information it has concerning income for that year. If it appears that income exceeds the annual income limit, VA will discontinue the benefit. Proposed § 5.478(a) makes the application of § 3.260(b) to prior pension clearer to readers.

However, proposed § 5.478(b), derived from portions of § 3.660(b)(1), provides that beneficiaries have until the end of the following year to provide evidence to show that income was actually below the limit and thereby establish continuing entitlement to pension. We propose to include an example as an aid to readers.

Proposed § 5.478(c), based on current § 3.960(d), clarifies further that if no income evidence is submitted or if the evidence submitted does not warrant continued benefits, the discontinuance of section 306 or old-law pension is final.

#### Explanation of Additional Proposed Removals From Part 3

Although all of part 3 would be removed and replaced by proposed part 5, we invite public comment concerning rules in current part 3 that we do not propose to transfer to proposed part 5, *i.e.*, that we simply propose to remove. Some of these have already been discussed in this NPRM, but others are discussed below.

We propose to remove § 3.26.

Paragraphs (a) through (c) describe the annual income limits for old-law and section 306 pension. We believe this regulation no longer has value because the statutory provisions are obscure to most readers. More importantly, the cited statutes set forth the January 1, 1979, income limits only. We believe it is more useful to describe how and where to find the current income limits, which we have done in proposed § 5.471. Current § 3.26(d) is redundant of the final sentence of current § 3.28.

We propose to remove § 3.261. This regulation currently contains a table that lists income exclusions and deductions, and applicability of net worth, for VA’s need-based benefits that existed before January 1, 1979: old-law pension, section 306 pension, and parents’ DIC. The § 3.261 table also lists income exclusions and deductions, and applicability of net worth, for VA determinations concerning parents’ dependency. Most of the entries in the table cross-reference § 3.262, where the inclusion or exclusion of a particular type of income is explained in greater detail. We believe that some readers may rely only on the information in the table and fail to refer to the specific provisions of § 3.262. Because it is a bedrock principle of regulatory construction that a specific provision will trump a more general one, we propose to remove all of the paragraphs in § 3.261 that cross-reference § 3.262.

Therefore, when a paragraph from the § 3.261 table has an associated cross-reference in the last column of the table, we have not included that entry in the derivation table at the beginning of this NPRM. For example, § 3.261(a)(6) is not included on the derivation table because it would be removed in favor of the more specific provision it cross references, § 3.262(c).

There are currently 13 paragraphs in § 3.261 that do not contain associated § 3.262 cross-references. These are paragraphs (a)(4), (7), (9), (10), (11), (12), (13), (20), (22), (23), (26), (27), and (31). Of these, paragraphs (a)(4), (7), (12), (13), (20), (22), (26), and (31) are included in the derivation table at the beginning of this NPRM as the source of certain proposed part 5 regulations.

The “[a]nnuities” entry in paragraph (a)(14) of § 3.261 does not contain a cross-reference to § 3.262. However, as previously discussed in this NPRM in the discussion of proposed § 5.472, this entry will be included in a future proposed regulation.

We propose to remove paragraphs (a)(9) and (27) of § 3.261 because these paragraphs list included income sources. Under proposed § 5.472, VA



counts all payments unless specifically excluded. For the same reason, we propose to remove the “[r]efund” entry in paragraph (a)(14). We propose to remove paragraph (a)(10), which excludes the “[r]easonable value of allowances to person in service in addition to base pay” for Section 306 child pension beneficiaries. We do not believe there are any remaining beneficiaries to whom this exclusion applies.

We propose to remove paragraph (a)(11) of § 3.261 because authority for mustering-out pay was repealed by Public Law 89–50, 79 Stat. 173.

We propose to remove paragraph (a)(23) of § 3.261, which excludes overtime pay for “Government employees” for old-law veteran pension beneficiaries. We do not believe there are any remaining beneficiaries to whom this exclusion applies.

Current § 3.261(a)(20) lists VA benefits. As previously described in the discussion of proposed § 5.472(e), the portions of § 3.261(a)(20) that pertain to section 306 and old-law pension would be described in proposed § 5.472(e) in terms of those VA benefits that count. We propose to remove the portion of current § 3.261(a)(20) that lists the subsistence allowance under Chapter 31 of 38 U.S.C. as a countable payment because we do not believe that any of the remaining veteran beneficiaries of old-law pension receive these vocational rehabilitation payments. We also propose to remove the portion of § 3.261(a)(20) that lists veterans’ educational assistance under 38 U.S.C. chapter 34 because VA no longer pays this benefit.

We propose to remove the second sentence of § 3.262(j)(3), an income exclusion that applies only to old-law death pension beneficiaries, for payments equaling lump-sum amounts based on the death of a veteran. We believe that all such payments have already been received because the veteran must have died before July 1, 1960, in order for a beneficiary to be receiving old-law death pension.

Current § 3.262(e)(1) provides in part that:

Where the retirement benefit is based on the claimant’s own employment, payments will not be considered income until the amount of the claimant’s personal contribution (as distinguished from amounts contributed by the employer) has been received. Thereafter the 10 percent exclusion will apply.

Similarly, current § 3.262(e)(2) provides in part that:

Where a person was receiving or entitled to receive pension and retirement benefits

based on his or her own employment on December 31, 1964, the retirement payments will not be considered income until the amount of the claimant[’s] personal contribution (as distinguished from amounts contributed by the employer) has been received. Thereafter the 10 percent exclusion will apply.

We propose to remove these two provisions. It is extremely unlikely that an old-law pension beneficiary’s contributions to retirement plans or a Section 306 pension beneficiary’s contributions to retirement plans based on employment on December 31, 1964, were not recovered long ago.

We propose to remove references to the following effective dates in current § 3.262 for exclusion of particular income types: July 1, 1959 (paragraph (g)(2)); January 10, 1962 (paragraph (k)(4)(iii)); January 1, 1965 (paragraphs (e)(1) and (2), (j)(1), and (k)(5)); October 7, 1966 (paragraphs (i)(2), (j)(2), and (j)(4)); and January 1, 1971 (paragraphs (k)(1) and (k)(6)). Although current section 306 and old-law pension rates are based on 1978 income, it is highly unlikely that VA will process a retroactive adjustment to a prior pension award effective more than 30 years in the past; therefore, we believe these effective dates are no longer necessary.

We propose to remove current § 3.262(m), which concerns deducting the veteran’s final expenses and just debts from death pension awards. Current § 3.262(p) specifies that VA allows final expenses as a deduction during the year of the veteran’s last illness and burial or during the year the beneficiary paid the expenses. Because the last date that a surviving spouse or child could establish entitlement to Section 306 pension was December 31, 1978, these claims were made long ago. If a case should arise in which a surviving spouse or child claims to have paid final expenses or just debts many years previously which were claimed but remained unprocessed due to an error, the statute would govern the decision.

From paragraphs (n)(2) and (p) of § 3.262, we propose to remove the references to “spouse” on the same basis as our proposal to remove § 3.262(m). Spouses of veterans who die after December 31, 1978, may only be considered for Improved pension. This is true even if the veteran was in receipt of section 306 or old-law pension.

We propose to remove § 3.270. This regulation currently introduces specific section numbers for regulations that govern entitlement to Section 306 and Old-Law pension and parents’ DIC, and for making dependent parent

determinations. All of the regulations referenced in current § 3.270 are to be moved to various other regulations that are specific to the benefit indicated. Therefore, current § 3.270 would no longer be necessary.

We propose to remove several provisions that pertain to initial entitlement to certain pension programs. First, we propose to remove paragraphs (a)(1), (b)(1), and (b)(2) of current § 3.3. These paragraphs pertain to initial entitlement to Spanish-American War service pension for veterans, Indian war death pension, and Spanish-American War death pension, respectively. Although new claims for these pensions are theoretically possible, they are unlikely in the extreme. As of September 2003, there was one surviving child beneficiary of an Indian war veteran, and there were approximately 400 surviving spouse and child beneficiaries of Spanish-American War veterans. VA RCS 20–0221, September 2002. To our knowledge, no veterans of either war survive. Therefore, we believe removal of these provisions is warranted. In the unlikely event of a new claim, the applicable statute would control. For the same reason, we propose to remove § 3.16, which pertains to computing service for service pension.

Second, we propose to remove current paragraphs (a)(2) and (b)(3) of § 3.3, which pertain to initial entitlement to Section 306 pension. As previously outlined in this NPRM, new entitlement to Section 306 disability or death pension is not possible and has not been possible since January 1, 1979. We note that there are no regulations in current part 3 pertaining to initial entitlement to old-law pension. The governing statutes would control if VA discovers an old claim for Section 306 pension that has not been processed due to error or oversight.

We propose to remove § 3.314, which pertains to basic pension determinations. The provisions in this regulation are either obsolete or redundant of other regulatory provisions. Paragraph (a) pertains to establishing basic eligibility for service pension, which we propose to remove for the reasons stated above in relation to current § 3.3(a)(1) and (b)(2). Paragraph (b) describes when rating decisions are required for nonservice-connected disability pension, which we believe is a procedural matter that should not be included in new part 5. Paragraph (b)(1) is redundant of § 3.3(a)(2)(iii) and (b)(3)(ii). The first sentence of § 3.314(b)(2) is redundant of § 3.342(a). The second sentence of § 3.314(b)(2) pertains to new entitlement

to Section 306 pension, which we are removing for the reasons stated above in relation to current § 3.3(a)(2). Current § 3.314(b)(3) pertains to increased old-law or section 306 pension because of the need for aid and attendance or the housebound rate. This provision is obsolete because section 306 and old-law pension cannot increase; the veteran must have established the need for aid and attendance or eligibility for the housebound rate before January 1, 1979.

We propose to remove § 3.17, which pertains to computing wartime service for nonservice-connected disability and death pension purposes. Because new entitlement cannot be established to section 306 or old-law pension, this regulation no longer pertains to those programs. The regulation still pertains to the Improved pension program; however, it is redundant of current § 3.3(a)(3)(i) through (iv).

We propose to remove § 3.401(i), which is an effective-date provision for an award of increased pension to a veteran who attains the age of 78. With the enactment of Public Law 95–588, 92 Stat. 2497, Congress removed the “age of 78 rule.” This provision does not apply to the Improved pension program. Section 306 pension rates have been frozen since December 31, 1978. They may be reduced or discontinued under limited circumstances, but they cannot increase. In order for the “age of 78 rule” to apply to section 306 pension beneficiaries, the beneficiary must have attained age 78 before January 1, 1979. Current 38 U.S.C. contains no statutory authority for the “age of 78 rule.”

Similarly, we propose to remove current §§ 3.400(j)(2) through (6) and 3.401(f). These are effective-date provisions for Spanish-American War service pension and the other prior pension programs. Because we are proposing to remove the regulations pertaining to new entitlement to Spanish-American War service pension, section 306 pension, and old-law pension, we propose to remove the applicable effective dates.

We propose to remove § 3.712(b) as obsolete. This is a special provision that applies to surviving spouses in receipt of Spanish-American War death pension who require aid and attendance. Current § 3.712(b) provides that these surviving spouses will receive either the Spanish-American War aid and attendance benefit of \$149 monthly or the aid and attendance rate for section 306 death pension, whichever is greater. Current § 3.712(b) further provides that the section 306 death pension rate is based on current income. In the early years following the introduction of improved

pension, it was occasionally the case that section 306 death pension would pay more than Spanish-American War death pension or improved death pension. However, with each passing year, this has become less and less likely as Improved pension maximum annual pension rates increase while section 306 pension rates remain frozen. Now, it is a virtual impossibility. In order for a surviving spouse with no dependents to be entitled to more than \$149 per month under section 306 death pension, the surviving spouse's annual income would have to be less than \$1,900 per year in 2004. If that were the case at this time, such a surviving spouse would almost certainly elect Improved death pension. (A surviving spouse eligible for aid and attendance who has no dependents and an annual income of \$1,900 per year is entitled to \$725 monthly in 2004 under the Improved pension program, unless he or she is in a nursing home and Medicaid is paying for care.) If a case arises in which a surviving spouse beneficiary of Spanish-American War death pension claimed that section 306 death pension should have been paid but was not paid due to error or oversight, the governing statute, 38 U.S.C. 1536(d)(2), would control.

We propose to remove § 3.713(b) as obsolete. Current paragraph (b) creates a special exception to the general effective date in paragraph (a) for beneficiaries who were entitled to receive either section 306 or old-law pension on December 31, 1978, and who elected to receive improved pension before October 1, 1979. (Section 3.713(b) does not apply to Spanish-American War death pension). If a pension beneficiary were to claim entitlement to an earlier effective date based on the filing of an election before October 1, 1979, which VA somehow did not recognize as such at the time, the claim would be processed under section 306(d) of Public Law 95–588, 73 Stat. 432, the governing statute.

We propose to remove § 3.252(e)(1) as obsolete. Current § 3.252(e)(1) provides that if a veteran's child is born after the veteran dies, the surviving spouse cannot claim the child as a dependent until the child is born. Because the last date a surviving spouse could establish eligibility to old-law pension was June 30, 1960, and the last date a surviving spouse could establish eligibility to section 306 pension was December 31, 1978, current § 3.252(e)(1) no longer applies to section 306 or old-law pension.

We propose to remove § 3.252(f), which contains specific provisions for computing a special reduced aid and

attendance allowance under 38 U.S.C. 1521(d)(1) as in effect on December 31, 1978 (when it was numbered 38 U.S.C. 521(d)(1)). We believe there is no longer a need for § 3.252(f). Veterans are not entitled to the special reduced aid and attendance allowance unless they were in need of aid and attendance on or before December 31, 1978. VA publishes the income limits for continued entitlement to this allowance every year as the income limits increase. If there would be a case at some time to which § 3.252(f) would apply (due to error or oversight), the statute would control.

We propose to remove current § 3.257 as obsolete. This regulation states that if old-law or section 306 pension is not payable to a surviving spouse because his or her annual income exceeds the income limit, VA will make payments to children as if there were no surviving spouse. Because new entitlement to old-law or section 306 pension cannot be established, VA cannot establish new entitlement to either old-law or section 306 pension for a child if a surviving spouse's income exceeds the income limit for either of these pensions. Removal of this regulation would not affect current pension awards to children.

We propose to remove current § 3.714 as obsolete. Current § 3.714 implemented the Adoption and Child Welfare Act of 1980, Public Law 96–272 § 310(b), 94 Stat. 500, which provided that certain beneficiaries who had once been in receipt of prior pensions had the right to disaffirm an election of improved pension, thereby restoring their right to prior pension. The primary purpose of the law was to restore Medicaid eligibility to those who lost it because they were required to elect improved pension under the regulations that previously governed eligibility to receive public assistance. Under section 310(b), VA was required to obtain from every affected pension beneficiary an informed decision regarding whether he or she wish to continue to receive improved pension or disaffirm the earlier election. VA long ago complied with these notification provisions.

Current § 3.714 also provides for a special informed election process for those pension beneficiaries who reside in states in which Medicaid eligibility is based on public assistance. However, section 114(a) of the Personal Responsibility and Work Opportunity Reconciliation Act of 1996, Public Law 104–193, 110 Stat. 2105, provides that eligibility for Medicaid is no longer linked to the receipt of public assistance. In other words, there is no longer any state to which the first sentence of current § 3.714(b) applies.

### Endnote Regarding Removals From Part 3

For the reasons shown in the preceding supplementary information, the amendments proposed in this document would, if adopted, result in removal of current §§ 3.16, 3.17, 3.26, 3.28, 3.252, 3.257, 3.261, 3.270, 3.314, 3.711, 3.712, 3.713, and 3.714, and removal of portions of §§ 3.1, 3.3, 3.260, 3.262, 3.263, 3.400, 3.401, 3.660, 3.700, and 3.960. This would be the case because those part 3 sections, or portions of sections, would be replaced by new part 5 sections or they would be removed entirely. Readers are invited to comment both on these part 5 removals and on the proposed new part 5 rules at this time.

NPRMs frequently include formal “amendatory language” listing the sections, or portions of sections, that would be removed if the proposed amendments are adopted. However, we have not included such “amendatory language” in this NPRM because of the nature of this Project. Because of the very large scope of the Project, we are publishing proposed amendments in several NPRMs. Then, after public comments in response to all of the NPRMs making up the Project have been reviewed and considered, VA will propose to remove all of part 3, concurrent with the implementation of part 5.

### Paperwork Reduction Act

Although this document contains a provision constituting a collection of information in proposed 38 CFR 5.478(b), under the provisions of the Paperwork Reduction Act (44 U.S.C. 3501–3521), no new or proposed revised collection of information is associated with this proposed rule. The information collection requirement for proposed §§ 5.474 and 5.478(b) are currently approved by the Office of Management and Budget (OMB) and have been assigned OMB control numbers 2900–0624 and 2900–0101.

### Regulatory Flexibility Act

The Secretary hereby certifies that this proposed regulatory amendment will not have a significant economic impact on a substantial number of small entities as they are defined in the Regulatory Flexibility Act, 5 U.S.C. 601–612. This proposed amendment would not affect any small entities. Only VA beneficiaries could be directly affected. Therefore, pursuant to 5 U.S.C. 605(b), this proposed amendment is exempt from the initial and final regulatory flexibility analysis requirements of sections 603 and 604.

### Executive Order 12866

This document has been reviewed by the Office of Management and Budget under Executive Order 12866.

### Unfunded Mandates

The Unfunded Mandates Reform Act requires, at 2 U.S.C. 1532, that agencies prepare an assessment of anticipated costs and benefits before developing any rule that may result in an expenditure by State, local, or tribal governments, in the aggregate, or by the private sector of \$100 million or more in any given year. This proposed rule would have no such effect on State, local, or tribal governments, or the private sector.

### Catalog of Federal Domestic Assistance Numbers

The Catalog of Federal Domestic Assistance program numbers for this proposal are 64.100–102, 64.104–110, 64.115, and 64.127.

### List of Subjects in 38 CFR Part 5

Administrative practice and procedure, Claims, Disability benefits, Pensions, Veterans.

Approved: October 14, 2004.

Anthony J. Principi,

Secretary of Veterans Affairs.

For the reasons set forth in the preamble, VA proposes to amend 38 CFR chapter I as set forth below:

## PART 5—COMPENSATION, PENSION, BURIAL, AND RELATED BENEFITS

Part 5, as proposed to be added at 69 FR 4832, January 30, 2004, is further amended by adding subpart F to read as follows:

### Subpart F—Nonservice-Connected Disability Pensions and Death Pensions

*Choosing Improved Pension Over Certain Other VA Pension Programs: Veterans and Survivors*

Sec.

- 5.460 Definitions of certain VA pension programs.
- 5.461 Electing improved pension instead of Old-Law or Section 306 pension.
- 5.462 Right of surviving spouses receiving Spanish-American War death pension to elect improved death pension.
- 5.463 Effective dates of improved pension elections.
- 5.464 Multiple pension awards not payable.
- 5.465–5.469 [Reserved]

*Continuing Entitlement to Old-Law or Section 306 Pension: Veterans and Survivors*

- 5.470 Reasons for discontinuing or reducing section 306 or old-law pension.
- 5.471 Annual income limits and rates for section 306 and old-law pension.
- 5.472 Evaluation of income for section 306 and old-law pension.
- 5.473 Counting a dependent's income for section 306 and old-law pension.

- 5.474 Deductible expenses for section 306 pension only.
- 5.475 Gaining or losing a dependent for section 306 and old-law pension.
- 5.476 Net worth for section 306 pension only.
- 5.477 Effective dates for section 306 and old-law pension reductions or discontinuances.
- 5.478 Time limit to establish continuing entitlement to section 306 or old-law pension.
- 5.479–5.499 [Reserved]

**Authority:** 38 U.S.C. 501(a) and as noted in specific sections.

### Subpart F—Nonservice-Connected Disability Pensions and Death Pensions

#### Choosing Improved Pension Over Certain Other VA Pension Programs: Veterans and Survivors

##### § 5.460 Definitions of certain VA pension programs.

(a) *Section 306 pension* means the nonservice-connected disability and death pension programs available to new claimants during the period beginning on July 1, 1960, and ending on December 31, 1978.

(b) *Old-Law pension* means the nonservice-connected disability and death pension programs available to new claimants before July 1, 1960.

(c) *Spanish-American War death pension* means pension payable to a surviving spouse or child of a veteran who served in the Spanish-American War. Entitlement is based solely on the veteran's service in the Spanish-American war without regard to disability, income, or net worth.

(Authority 38 U.S.C. 501(a)).

##### § 5.461 Electing improved pension instead of old-law or section 306 pension.

(a) *Right to elect (choose) Improved pension.* Unless this section states otherwise, a pension beneficiary who was entitled to receive old-law pension or section 306 pension on December 31, 1978, may instead elect (choose) to receive improved pension.

(b) *Finality of election.* Unless one of the following exceptions applies, an election of Improved pension is final when a beneficiary negotiates a check for a payment of Improved pension. Once the election is final, the beneficiary cannot receive old-law or section 306 pension. An election may be canceled according to the following exceptions:

(1) *The beneficiary receives benefits by direct deposit or electronic funds transfer (DD/EFT).* If the beneficiary receives a payment of improved pension benefits by direct deposit or electronic

funds transfer, the beneficiary must cancel the election of improved pension before the financial institution receives the second Improved pension payment. Once the financial institution receives a second payment, the election is final.

(2) *The beneficiary is incompetent.* If VA finds that a beneficiary was mentally incompetent when he or she elected Improved pension, the beneficiary (or guardian) may cancel that election. VA must receive the request to cancel the election within one year from the date the election became effective.

(3) *Beneficiary based election on erroneous VA information.* A beneficiary who elected improved pension based on erroneous information provided by VA may cancel the election within one year after the date the election became effective. For this paragraph (b)(3) to apply, VA must determine that it previously provided erroneous information and that determination must be based on the same evidence that VA used when it previously provided the erroneous information.

(c) *If a veteran's spouse is also a veteran eligible to elect Improved pension.* If a veteran who is eligible to elect Improved pension has a spouse who is also a veteran who is eligible to elect Improved pension, neither veteran may receive Improved pension unless both elect to receive it.

(d) *If a beneficiary does not elect Improved pension.* If a pension beneficiary who is eligible to elect Improved pension does not do so, VA will continue to pay that beneficiary old-law pension or section 306 pension at the monthly rate in effect on December 31, 1978, unless that rate must be reduced or discontinued under § 5.470 or another regulation in this part.

(Authority: Sec. 306(a) and (b), Pub. L. 95-588, 92 Stat. 2508)

**§ 5.462 Right of surviving spouses receiving Spanish-American War death pension to elect improved death pension.**

A surviving spouse who is receiving Spanish-American War death pension may elect to receive Improved death pension instead. Paragraph (b) of § 5.461, concerning finality of elections, applies to surviving spouses of Spanish-American War veterans. Once the election is final, the surviving spouse has no right to receive Spanish-American War death pension again. Surviving spouse beneficiaries of Spanish-American War death pension who do not elect Improved pension will continue to receive Spanish-American War death pension.

(Authority: 38 U.S.C. 1536).

**§ 5.463 Effective dates of improved pension elections.**

An election to receive improved pension will be effective the date VA receives the election.

(Authority: Sec. 306(d), Pub. L. 95-588, 92 Stat. 2508)

**§ 5.464 Multiple pension awards not payable.**

If a veteran is entitled to improved pension on the basis of his or her own service and is also entitled to pension under any other VA pension program based on another person's service, VA will pay only the greater benefit.

(Authority: 38 U.S.C. 1521(i)).

**§§ 5.465 through 5.469 [Reserved]**

**Continuing Entitlement to Old-Law or Section 306 Pension: Veterans and Survivors**

**§ 5.470 Reasons for discontinuing or reducing section 306 or old-law pension.**

(a) *Discontinuances.* Section 306 or old-law pension will be discontinued for any one of the following reasons:

(1) A veteran pension beneficiary ceases to be permanently and totally disabled.

(2) A surviving spouse pension beneficiary no longer meets the definition of "surviving spouse" as provided in § 3.50 of this chapter.

(3) A child pension beneficiary no longer meets the definition of "child," as provided in § 3.57 of this chapter.

(4) A pension beneficiary's income exceeds the annual income limit.

(5) A section 306 pension beneficiary has a net worth of such value that it is reasonable that some part of it be consumed for the beneficiary's maintenance. Evaluation of net worth will be made under § 5.476, "Net worth for section 306 pension only."

(b) *Finality of discontinuance.* Discontinuance of section 306 or old-law pension for one of the reasons listed in paragraph (a) of this section means that a pension beneficiary is no longer entitled to receive section 306 or old-law pension benefits. Any new entitlement that may be established would be to improved pension.

(c) *Reduction and finality of reduction.* If a beneficiary of section 306 or old-law pension loses a dependent who was established before December 31, 1978, VA must reduce such pension by the additional amount payable based on the existence of the dependent. Such reductions are final and rates do not increase. VA must discontinue pension as provided in paragraph (a)(4) of this

section if a veteran or surviving spouse no longer has any dependents and his or her annual income exceeds the annual income limit for a veteran or surviving spouse alone.

(Authority: Sec. 306, Pub. L. 95-588, 92 Stat. 2508)

**§ 5.471 Annual income limits and rates for section 306 and old-law pension.**

(a) *Where to find the annual income limits and pension rates.* When annual income limits are adjusted as provided in paragraph (b) of this section, VA will publish the new limits in the "Notices" section of the **Federal Register**. Current and historical annual income limits and historical pension rates for old-law and section 306 pension can be found on the Internet at <http://www.va.gov> or are available from any Veterans' Service Center.

(b) *When annual income limits are adjusted.* Whenever there is a cost-of-living increase in Social Security benefit amounts under the Federal Old-Age, Survivors, and Disability Insurance Benefits section of the Social Security Act (42 U.S.C. 415(i)), VA will increase the following by the same percentage effective the same date:

(1) The annual income limits applicable to continued receipt of section 306 and old-law pension.

(2) The dollar amount of a veteran's spouse's income that may be excluded in determining the income of a veteran for section 306 pension purposes.

(Authority: Sec. 306, Pub. L. 95-588, 92 Stat. 2508)

**§ 5.472 Evaluation of income for section 306 and old-law pension.**

(a) *Purpose and scope.* This section provides rules for determining how to count income for section 306 and old-law pension purposes. This section also applies to counting spousal income for section 306 pension purposes when spousal income is included as the veteran's income.

(b) *Countable income.* (1) *All payments included.* VA counts all payments of any kind from any source in determining the income of a pension beneficiary, except payments that are not counted under an exclusion provided in this section or § 5.473.

(2) *"Payments" defined.* For purposes of this section, "payments" are cash and cash equivalents (such as goods and other negotiable instruments) and include the fair market value of personal services, goods, or room and board a beneficiary receives in lieu of other forms of payment.

(i) For section 306 pension purposes, VA counts as income retirement benefits

(pension or retirement payments) that have been waived.

(ii) For old-law pension purposes, "payments" do not include retirement benefits from the following sources that have been waived pursuant to Federal statutes:

(A) Civil Service Retirement and Disability Fund.

(B) Railroad Retirement Board.

(C) District of Columbia (paid to firemen, policemen, or public school teachers).

(D) Former United States Lighthouse Service.

(3) *Countable income is rounded down.* VA rounds countable income down to the nearest whole dollar. For section 306 pension, VA rounds down after subtracting any authorized deductible expenses specified in § 5.474.

(4) *Income considered for year of receipt.* VA computes income for the calendar year in which it is received and considers income for the full calendar year. However, when VA discontinues section 306 or old-law pension awards based on income that exceeds the limit, it does so effective January 1 of the following calendar year as provided in § 5.477.

(c) *Deductions from specific income sources.* (1) *Expenses of a business or profession.* Necessary business operating expenses such as the cost of goods sold and payments for rent, taxes, upkeep, repairs, and replacements are deductible from income from a business or profession. Depreciation is not a deductible expense. Losses sustained in operating a business or profession may not be deducted from income from any other source. For purposes of this section, "business" includes the operation of a farm and transactions involving investment property.

(2) *Expenses associated with disability, accident, or health insurance recoveries.* Medical, legal, or other expenses incident to the insured injury or illness are deductible from sums recovered under disability, accident, or health insurance. However, the same medical expenses cannot then be deducted as unusual medical expenses under § 5.474.

(3) *Salary deductions and employer contributions.* Income from a salary is not determined by "take-home" pay. The salary counted as income is the gross salary without any deductions. An employer's contributions to health and hospitalization plans are not included in gross salary.

(d) *Income-producing property and income from property sales.* (1) *Scope.* This paragraph (d) provides rules for determining whether income from

income-producing property and property sales should be counted as a pension beneficiary's income. The provisions of this paragraph (d) apply to all property, real or personal, in which a pension beneficiary has an interest, whether acquired through purchase, bequest, or inheritance.

(2) *Proof of ownership.* In determining whether to count income from real or personal property or property sales, VA will consider the terms of the recorded deed or other evidence of title. In the absence of evidence showing otherwise, VA will accept the beneficiary's statement as proof of the terms of ownership.

(3) *Transfer of ownership with retention of income.* If a pension beneficiary transfers ownership of property to another person or legal entity, but retains the right to income, the income will be counted.

(4) *Income from jointly-owned property.* If a pension beneficiary owns property jointly with others, including partnership property, each person will be considered as receiving an equal share of the income from that property in the absence of evidence showing otherwise.

(5) *Property sales for old-law pension.*

(i) Unless it is the beneficiary's principal residence, net profit from the sale of real or personal property counts as income for old-law pension.

(ii) In determining net profit from the sale of property owned prior to the date of entitlement, VA will compare the value of the property at the time entitlement began with the selling price.

(iii) If payments are received in installments, the entire amount of installment payments received (including principal and interest) will be excluded until the total of installments received is equal to the cost of the residence, or if paragraph (d)(5)(ii) of this section applies, equal to the value of the property on the date pension entitlement was established. The entire amount of any installment received thereafter will be counted as income.

(6) *Profit from sale of principal residence for old-law pension.* (i) Net profit realized from the sale of an old-law pension beneficiary's principal residence is not counted to the extent that it is applied to the purchase price of a subsequent principal residence for the beneficiary in either the calendar year of the sale or the following year.

(ii) This exclusion does not apply where the net profit is applied to the price of a home purchased earlier than the calendar year preceding the calendar year of the sale of the old residence.

(iii) To qualify for this exclusion, the application of the net profit from the sale of the old residence to the purchase of the replacement residence must be reported to VA within one year following the date it was so applied.

(7) *Profit from sale of non-business property for section 306 pension.* Profit realized from the disposition of real or personal property other than in the course of a business does not count for section 306 pension. However, amounts received in excess of the sales price, such as interest payments, count as income. If payments are received in installments, the entire amount of installment payments (including principal and interest) are excluded until the total amount received equals the sales price. The entire amount of any installment received thereafter counts as income.

(e) *VA benefits.* (1) *Old-law pension.* All VA benefits are excluded for old-law pension.

(2) *Section 306 pension.* Only the following VA benefits count as income for section 306 pension:

(i) Subsistence allowance (38 U.S.C. Ch. 31).

(ii) Special allowance under 38 U.S.C. 1312(a).

(iii) Accrued benefits, unless paid as a reimbursement.

(iv) World War I adjusted compensation.

(f) *Income exclusions for section 306 or old-law pension.* VA will not count payments from the sources listed in this paragraph (f) when calculating income for section 306 or old-law pension. Paragraph (g) of this section provides additional exclusions for section 306 pension.

(1) *Maintenance.* The value of maintenance furnished by a relative, friend, or a civic or governmental charitable organization, including money paid to an institution for the care of the beneficiary due to impaired health or advanced age. However, if the maintenance is paid to the beneficiary and excluded under this provision, VA cannot also deduct it as an unusual medical expense under § 5.474.

(2) *Survivor benefit annuity.* Annuities paid by the Department of Defense under the authority of section 653, Public Law 100-456, 102 Stat. 1991, to qualified surviving spouses of veterans who died before November 1, 1953.

(3) *Death gratuity.* Death gratuity payments under 10 U.S.C. 1475 through 1480.

(4) *State service bonuses.* Payments of a bonus or similar cash gratuity by any State based upon service in the Armed Forces.

(5) *Payment for civic obligations.* Payments received for performance of jury duty or other obligatory civic duties.

(6) *Fire loss reimbursement.* Proceeds from fire insurance.

(7) *Certain life insurance payments.* Payments under policies of Servicemembers' Group Life Insurance, United States Government Life Insurance, Veterans' Group Life Insurance, or National Service Life Insurance.

(8) *Rental value of beneficiary's property.* The rental value of a beneficiary's use of his or her own real property, such as the rental value of the beneficiary's personal residence.

(9) *Increased inventory value of a business.* The value of an increase of stock inventory of a business.

(10) *Commercial insurance dividends.* Dividends from commercial insurance.

(11) *Employer contributions for retired employees.* Contributions a public or private employer makes to either of the following:

(i) Public or private health or hospitalization plan for a retired employee.

(ii) Retired employee as reimbursement for premiums for supplementary medical insurance benefits under the Social Security program.

(12) *Income from retirement plans and similar plans and programs.* Ten percent of the amount of payments under public or private retirement, annuity, endowment, or similar plans. This includes, but is not limited to, payments under or for any of the following:

(i) Annuities or endowments paid under a Federal, State, municipal, or private business or industrial plan.

(ii) Old age and survivor's insurance and disability insurance under title II of the Social Security Act.

(iii) Retirement benefits received from the Railroad Retirement Board. However, if the beneficiary is a veteran receiving old-law pension, payments from this source do not count at all.

(iv) Payments for permanent and total disability or death received from the Office of Workers' Compensation Programs of the United States Department of Labor, the Social Security Administration, or the Railroad Retirement Board, or pursuant to any worker's compensation or employer's liability statute, including damages collected incident to a tort suit under an employer's liability law of the United States or a political subdivision of the United States. This 10-percent exclusion applies after the income from the specified payments is reduced by the

deductions described in paragraph (c)(3) of this section.

(v) The proceeds of commercial annuity, endowment, or life insurance.

(vi) The proceeds of disability, accident, or health insurance. This 10-percent exclusion applies after the income from the specified payments is reduced by the deductions described in paragraph (c)(3) of this section.

(13) *Other payments.* Other payments listed in [regulation that will be published in a future Notice of Proposed Rulemaking].

(g) *Additional income exclusions for section 306 pension.* In addition to the payments listed in paragraph (f) of this section, VA will exclude payments from the following sources as income for section 306 pension:

(1) *Donations received.* Donations from public or private relief or welfare organizations, including benefits received under noncontributory programs such as Supplemental Security Income payments.

(2) *Social Security death payments.* Lump sum death payments under title II of the Social Security Act.

(3) *Money acquired from joint accounts because of death.* Money that a death pension beneficiary acquires because of the death of a co-owner of a joint account in a bank or similar institution.

(h) *Donations received for old-law pension.* If an old-law pension beneficiary receives additional donations from public or private relief organizations for members of his or her family, these additional allowances may not be divided per member of the family in determining the pension beneficiary's income. The entire payment is counted as income.

(Authority: Sec. 306, Pub. L. 95-588, 92 Stat. 2508)

#### **§ 5.473 Counting a dependent's income for section 306 and old-law pension.**

(a) *Veteran awards for old-law pension.* VA excludes the separate income of a veteran's spouse or child in computing income for veteran old-law pension beneficiaries.

(b) *Veteran awards for section 306 pension.* (1) *Child's income.* VA excludes the separate income of a veteran's child in computing income for veteran section 306 pension beneficiaries.

(2) *Spousal income.* (i) VA *presumptions concerning spousal income.* For section 306 pension purposes, if a veteran and his or her spouse live together, VA presumes—

(A) That the spouse's income is available to the veteran. The veteran may rebut this presumption by

submitting evidence showing that all or part of the spouse's income is not available.

(B) That counting the spouse's income would not cause the veteran hardship. The veteran may rebut this presumption by submitting evidence showing that there are expenses beyond the usual family requirements. Examples of such expenses include special training for a handicapped child and expenses for the prolonged illness of a family member. However, if the spouse's income is excluded because it is needed to pay for unusual medical expenses, the same medical expenses cannot be deducted as unusual medical expenses under § 5.474(b).

(ii) *Spousal income exclusions.* Unless excluded under paragraph (b)(2)(i) of this section, the veteran's income includes his or her spouse's income for section 306 pension purposes. However, VA will exclude from the veteran's income the greater of the following two amounts:

(A) The amount of the spousal income exclusion specified in Public Law 95-588, section 306(a)(2)(B) (as increased by amounts published in the "Notices" section of the **Federal Register**).

(B) All of the spouse's earned income.

(c) *Surviving spouse awards for section 306 or old-law pension.* (1) *Veteran's child not in surviving spouse's custody.* For section 306 or old-law pension purposes, if a deceased veteran is survived by a spouse and a child, the annual income limits for a surviving spouse and child apply even if the child is not the surviving spouse's child and not in the surviving spouse's legal custody.

(2) *When a child's separate income is excluded.* (i) VA will not count a child's or children's separate income as part of the surviving spouse's income if it is paid to the child, regardless of who has legal custody of the child.

(ii) If the child's income is paid or given to the surviving spouse, VA will only count as much of the child's income as remains after deducting the child's living expenses.

(d) *Child awards.* (1) *Old-law pension.* Earned income of child beneficiaries counts as income for old-law pension.

(2) *Section 306 pension.* Earned income of child beneficiaries is excluded for section 306 pension.

(Authority: Sec. 306, Pub. L. 95-588, 92 Stat. 2508)

#### **§ 5.474 Deductible expenses for section 306 pension only.**

(a) *Scope.* This section applies to section 306 pension only. Because section 306 pension rates cannot increase, deductible expenses paid after

December 31, 1978, can only be deducted from a pension beneficiary's income to keep the income within the annual income limit and continue entitlement to section 306 pension.

(b) *Unusual medical expenses.* (1) *Application.* (i) *Family members.* For section 306 pension purposes, a family member is a relative of the beneficiary who is a member of the beneficiary's household whom the beneficiary has a moral or legal obligation to support. This includes relatives who are physically absent from the household for a temporary purpose or for reasons beyond their control.

(ii) *Unusual medical expenses.* For purposes of this section, "unusual medical expenses" means unreimbursed medical expenses above 5 percent of annual income. However, if annual income includes retirement plan income, VA will calculate the 5 percent before applying the 10 percent exclusion under § 5.472(f)(11). For medical expenses that VA will deduct, see [regulation that will be published in a future Notice of Proposed Rulemaking].

(2) *Veteran or surviving spouse awards.* VA will deduct amounts paid by a veteran or surviving spouse for the veteran's or surviving spouse's own unusual medical expenses and those of family members.

(3) *Child awards.* VA will deduct amounts paid by a child pension beneficiary for his or her own unusual medical expenses and those of the child's parent, brothers, and sisters.

(4) *When expenses are deducted.* VA will deduct unusual medical expenses from income for the calendar year in which they were paid regardless of when the expenses were incurred.

(5) *Proof of expenses.* VA will accept the pension beneficiary's statement as proof of the amount and nature of such medical expenses, the date of payment, and the identity of the creditor, unless circumstances create doubt as to the statement's credibility.

(6) *Estimates of expenses for future benefit periods.* VA will project anticipated medical expenses based on a clear and reasonable expectation that they will continue. See § 3.660(a) of this chapter (concerning the beneficiary's responsibility to inform VA concerning income changes).

(c) *Final expenses.* (1) *Definition.* Final expenses are amounts paid for the expenses of a deceased person's last illness and burial. The same expense cannot be deducted as both a final expense and an unusual medical expense under paragraph (a) of this section.

(2) *Final expenses paid by the veteran.* VA will deduct from a veteran's income the final expenses the veteran pays for his or her spouse or child.

(3) *Final expenses paid by a surviving spouse.* VA will deduct from a surviving spouse's income the final expenses the surviving spouse pays for the veteran's child.

(4) *Proof of expenses.* VA will accept as proof of expenses deductible under paragraph (c) of this section the pension beneficiary's statement as to the amount and nature of each expense, the date of payment, and identity of the creditor unless the circumstances create doubt as to the credibility of the statement.

(5) *When expenses are deducted.* Expenses deductible under paragraph (c) of this section are deductible for the year in which they were paid. However, if such expenses were paid during the year following the year the spouse, surviving spouse, or child died, the expenses may be deducted for the year the expenses were paid or the year of death, whichever is to the beneficiary's advantage.

(d) *Prepayment on real property mortgage after death of spouse.* (1) *Section 306 veteran pension beneficiaries only.* If a veteran who is receiving section 306 pension makes a pre-payment on a mortgage or similar type security instrument on real property after the death of his or her spouse, VA will deduct the amount of the pre-payment from the veteran's income. The real property must have been the principal residence of the veteran and spouse, and the mortgage or security instrument must have existed when the veteran's spouse died.

(2) *Time limit of pre-payment.* The pre-payment described in paragraph (d)(1) of this section must be made after the spouse's death but before the end of the year following the year of death. VA will deduct the amount of the pre-payment from the veteran's income for the year of death or the year after death, whichever is to the veteran's advantage.

(Authority: Sec. 306, Pub. L. 95-588, 92 Stat. 2508)

#### **§ 5.475 Gaining or losing a dependent for section 306 and old-law pension.**

(a) *Pension beneficiary gains a dependent.* (1) *Section 306 or old-law pension.* If a section 306 or old-law pension beneficiary gains a dependent, VA will determine if a higher annual income limit applies. A higher limit applies if the beneficiary previously had no dependents.

(2) *Veteran receiving section 306 pension gains a spouse who has income.* If a veteran beneficiary of section 306

pension gains a spouse who has countable income, VA will recompute the veteran's income for the year in which the person became the veteran's spouse. VA will then determine if the veteran is entitled to continued pension benefits or whether the recomputed income exceeds the annual income limit. VA makes the determination based on calendar-year income. However, VA will not count income that the spouse received or deduct any of the spouse's expenses paid before the date the person became the veteran's spouse for VA purposes.

(b) *Pension beneficiary loses dependent.* (1) *Loss of last dependent.* When section 306 or old-law pension beneficiaries lose their last dependent, their annual income limit is lowered. When this occurs, VA must determine if the beneficiary is still entitled to pension based on the lowered income limit and recalculated income for the calendar year that the dependent was lost.

(2) *Computation of new rate if a dependent established on or before December 31, 1978.* If a pension beneficiary loses a dependent and that dependent was established on or before December 31, 1978, VA will calculate a new pension rate. Because section 306 and old-law pension rates are based on 1978 income and number of dependents, VA calculates the new rate by removing the dependent and the dependent's 1978 income, if any, and using the remaining 1978 income to determine the new rate.

(i) If the recomputed rate is higher than the previous rate, VA will continue the previous rate.

(ii) If the rate payable to a surviving spouse with one child is less than the rate payable for a child alone, the surviving spouse will be paid the child's rate unless paragraph (b)(2)(i) of this section applies.

(c) *Section 306 pension and dependency of spouse.* For section 306 pension purposes, the December 31, 1978, rates for a veteran with a spouse and the annual income limit for a veteran with a spouse apply as long as the veteran and spouse live together or if not living together, are not estranged. If they are estranged, the married rates and the annual income limit for a veteran with a spouse apply if the veteran is reasonably contributing to the spouse's support. VA counts spousal income only if the annual income limit for a veteran with a spouse applies. VA bases its determination of "reasonable" contribution on all of the circumstances of the case, including a consideration of the veteran's income and net worth and the spouse's separate income and net



worth. VA automatically considers the requirement of “reasonable” contribution met without further review if the spouse is receiving an apportionment under § 3.451 of this chapter.

(Authority: Sec. 306, Pub. L. 95–588, 92 Stat. 2508)

**§ 5.476 Net worth for section 306 pension only.**

(a) *Definition.* For purposes of determining continuing entitlement to section 306 pension, net worth means the market value, minus mortgages or other encumbrances, of all real and personal property the beneficiary owns. VA excludes the beneficiary’s dwelling (single-family unit), which also includes a reasonable lot area, and personal effects suitable to and consistent with the beneficiary’s reasonable mode of life. VA will evaluate a “reasonable lot area” by considering the typical size of lots in the area. If the person lives on a farm, VA will exclude the value of a reasonable lot area, including the residence area, and consider the rest of the farm as part of net worth.

(b) *General.* VA only considers the net worth of the veteran, surviving spouse, or child beneficiary. In determining whether property belongs to a pension beneficiary, VA will consider the terms of the recorded deed or other evidence of title. In the absence of such evidence, VA will accept the beneficiary’s statement as proof of the terms of ownership.

(c) *How VA evaluates net worth.* In determining whether some part of a beneficiary’s net worth should be used for his or her maintenance, VA considers the beneficiary’s income as determined under § 5.472, “Evaluation of income for section 306 and old-law pension,” along with all of the beneficiary’s living expenses. However, in considering the beneficiary’s living expenses, VA cannot consider expenses it excluded or deducted in determining income. In addition to these income and expense factors, VA will also consider the following factors:

(1) The value of liquid assets and the value of other property the beneficiary can readily convert into cash.

(2) The ability of the beneficiary to dispose of property if limited by community property laws.

(3) The number of family members (as described in § 5.474(b)(1)(i)) who depend on the beneficiary for support.

(4) The beneficiary’s average life expectancy, and the potential rate of depletion of the beneficiary’s net worth.

(d) *Statutory exclusions from net worth.* Resources excluded by statute will not be considered part of the beneficiary’s net worth. For the list of resources excluded by statute, see [regulation that will be published in a future Notice of Proposed Rulemaking].

(Authority: Sec. 306, Pub. L. 95–588, 92 Stat. 2508)

**§ 5.477 Effective dates for section 306 and old-law pension reductions or discontinuances.**

(a) *Reductions or discontinuances based on certain events.* If required, VA will pay a reduced section 306 or old-law pension rate or discontinue benefits effective January 1 of the calendar year immediately following any of these events:

(1) *Marriage, annulment, divorce, or death.* A beneficiary loses a dependent due to marriage, annulment, divorce, or death.

(2) *Increased income.* The beneficiary receives increased income that could not reasonably have been anticipated based on the amount actually received from that source the previous year.

(3) *Increased net worth.* The beneficiary’s net worth increases to the extent benefits must be discontinued (section 306 pension only).

(b) *General effective dates apply for other reasons.* VA will use the general effective dates in §§ 3.500 through 3.503 of this chapter for a discontinuance or reduction for any reason other than those stated in paragraph (a) of this section or in § 5.478(a).

(Authority: Sec. 306, Pub. L. 95–588, 92 Stat. 2508)

**§ 5.478 Time limit to establish continuing entitlement to section 306 or old-law pension.**

(a) *Anticipated income appears to exceed income limit.* If it appears that a section 306 or old-law pension beneficiary’s income for a calendar year will be higher than the annual income limit, VA will discontinue pension benefits for that year effective January 1 of the following year, subject to paragraph (b) of this section.

(b) *Time limit for continuing entitlement.* If VA discontinues pension benefits as described in paragraph (a) of this section because of the beneficiary’s anticipated income for a calendar year, the beneficiary can establish continuing entitlement by submitting evidence showing that income for the calendar year was below the annual income limit. The beneficiary must submit the evidence before the end of the calendar year that follows the year for which VA determined the income exceeded the limit. For example, if VA determines that a beneficiary’s income for 2005 exceeds the income limit and discontinues pension benefits effective January 1, 2006, the beneficiary has up to and including December 31, 2006, to submit evidence such as deductible medical expenses or other information showing that 2005 income was within the 2005 income limit.

(c) *Finality of discontinuance.* If a beneficiary does not submit income evidence as described in paragraph (b) of this section or if such evidence does not warrant continued benefits, the discontinuance described in paragraph (a) of this section is final. This means that the beneficiary is no longer entitled to receive section 306 or old-law pension benefits. Any new entitlement that may be established would be to Improved pension.

(Authority: 38 U.S.C. 5110(h))

**§§ 5.479 through 5.499 [Reserved]**

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