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ENLISTMENT AND REENLISTMENT BONUS DEBTS:  
CAN THE GROWTH BE CURBED?

BY

LIEUTENANT COLONEL GEORGE L. SUMRALL, JR.

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ENLISTMENT AND REENLISTMENT BONUS DEBTS:  
CAN THE GROWTH BE CURBED?

AN INDIVIDUAL STUDY PROJECT

by

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7 April 1989

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## ABSTRACT

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ENLISTMENT AND REENLISTMENT BONUS DEBTS:  
CAN THE GROWTH BE CURBED?

CHAPTER I

INTRODUCTION

As the draft-era ended in 1972 and the military services commenced the transition to an all-volunteer force, significant concerns were raised by the Congress and the Department of Defense (DOD) regarding the services' ability, particularly the Army and the Marine Corps, to meet their manpower requirements. Specific fears emerged concerning the combat arms skills, with two-thirds of these requirements in the Army being manned by draftees and Regular Army unassigned personnel.<sup>1</sup> Enlistment and reenlistment bonuses were believed to be necessary to offset the perceived displeasures associated with serving in the combat arms skills, these being reduced transferability to civilian job skills, increased discomforts caused by repetitive field duty, reduced prestige, and increased potential for exposure to combat. Manpower experts felt that regular pay alone would be insufficient to attract and retain the desired quantity and quality of male entrants needed to man the hard-to-fill skills, hence the use of enlistment and reenlistment bonuses was to become pivotal in the services' efforts (particularly within the Army and Marine Corps) to make the all-volunteer force a success.<sup>2</sup>

BONUS HISTORY

The payment of enlistment and reenlistment bonuses was not a phenomenon to the services' efforts to secure necessary

manpower. Enlistment bonuses were paid as early as 1776 with reenlistment bonuses initially appearing in 1791. Enlistment bonuses ceased to be paid after the Civil War, whereas reenlistment bonuses, in one form or another, have continually been in use since their introduction. What was unique in the decades of the 1970's and 1980's however, was the rapid, new growth in the use of enlistment bonuses, a bonus that had not been paid since the Civil War. This growth, combined with the expansion of regular, variable and selective reenlistment bonuses caused a steady rise in the total bonus dollar outlay. Accompanying the expanded use of these bonuses was a corresponding increase in the bonus debt which results when individuals fail to complete their term of obligated service. While reliable records were not kept on the specific amount of "unearned" bonus debt owed to the Army prior to fiscal year (FY) 79, later reports revealed that the cumulative debt from "unearned" enlistment and reenlistment bonuses has steadily increased from \$4.73 million in FY 79 to \$29.64 million at the close of FY 88.3 This study is dedicated to developing a plan to reverse the growth of this "unearned" bonus debt.

#### SCOPE OF THE STUDY

The focus of this study is directed on the Active Army bonus, and the resultant unearned bonus debt problem. While the Reserve Components (RC) of the Total Army utilize enlistment and reenlistment bonuses, and experience similar bonus debts, the RC bonus debt problem is outside the scope of this study. However, some of the recommendations may be adaptable for use by RC debt managers.



Likewise, the bonus debt problem that exists in other services was researched only to the depth necessary to ascertain the essence of their bonus utilization, the size of their unearned bonus debts, and any on-going initiatives aimed at avoiding or reducing such debts. Neither time nor resources permitted an in-depth, comparative analysis between service programs; however, as will be seen in Chapter VI, valuable insights were gained by reviewing the other services' programs.

#### ENDNOTES

1. U.S. Department of Defense, Office of the Secretary of Defense, Fifth Quadrennial Review of Military Compensation, Vol. 3, p. 393.

2. Ibid.

3. Interview with Lois L. Richardson, U.S. Army Finance and Accounting Center, Indianapolis, In., 3 November 1988.

## CHAPTER II

### DEFINITION OF THE PROBLEM

While a \$29.64 million cumulative debt associated with the operation of the Army's bonus programs should, in and of itself warrant concern, because of the bonus programs' importance to Army recruiting and retention efforts, this debt receives only infrequent attention outside of the Army's financial community. This is said with no intent to impugn the fiscal sensitivity of bonus program managers within the Department of the Army, Office of the Deputy Chief of Staff for Personnel (ODCSPER). Faced with an increasingly more competitive recruiting environment, bonus program managers focus on utilizing bonus dollars to achieve the maximum productivity in the recruiting and retention market places. This focus is clearly justified.

With the shrinking manpower pool of service eligible males projected through the mid-1990's, all four military services will be hard-pressed to maintain the favorable recruiting trends accomplished during the 1980's. A glimpse of this environment was seen in the Army's failure to achieve its recruiting goals for the first quarter of FY 89, the first such occurrence since 1980.<sup>1</sup> With this tenuous recruiting environment as a back-drop, one can understand the reluctance of personnel managers to consider adjustments to Army bonus programs which have been such successful ingredients in the Army's recruiting and retention recipes.

#### THE CONFLICT: BONUS PAYMENTS VERSUS BONUS DEBTS

In succeeding chapters it will become increasingly more evident that previously explored solutions to reverse the mounting

unearned bonus debt have conflicted with proven principles of targeting bonus dollars to attract and retain quality soldiers in critical skills. When this has occurred, bonus program managers have resisted such solutions as too risky to implement without jeopardizing recruitment and retention efforts. This friction between sound debt avoidance principles and the necessity to expend significant bonus dollars to remain competitive in today's recruiting environment has placed the Army's bonus program managers and debt managers at odds. This dichotomy is the focus of this study. Attempting to bring together competing interests to forge a common solution remains a most difficult challenge.

#### KEY PRINCIPLES IN CONFLICT

Chapters III through V address distinct elements of the unearned bonus debt issue--enlistment bonuses, reenlistment bonuses, methods of payment of these bonuses, and recoupment of the unearned portion of these bonuses once a soldier has been discharged. As one reads these chapters it is beneficial to focus on the following key principles which are woven throughout the bonus debt mosaic:

- Personnel managers argue that bonus dollars are most effective when front-loaded in lump sum payments.
- Front-loading bonus payments results in larger dollar amounts to be recouped from soldiers who are discharged owing bonus debts.
- Soldiers separated prior to completion of their obligated service are normally released under adverse conditions for

character and behavior disorders or for disciplinary reasons. Their civilian employment opportunities often fail to produce sufficient funds to repay these debts, resulting in write-offs.

- The cost effectiveness of collecting unearned bonus debts from soldiers who have been discharged from active duty is questionable. An average of only "24¢ on the dollar is recovered by the government," with many accounts being written-off as uncollectible.<sup>2</sup>

#### ENDNOTES

1. George C. Wilson, "Army's Recruiting Falters as Manpower Pool Shrinks," Washington Post, 14 February 1989, p.A5.
2. Interview with Lois L. Richardson, U.S. Army Finance and Accounting Center, Indianapolis, In., 28 February 1989.

## CHAPTER III

### ENLISTMENT BONUSES

#### BACKGROUND

As introduced in Chapter I, enlistment bonuses (EB) have been used to induce persons to serve in the enlisted corps of the military since before the formation of the United States. Although abandoned after the Civil War, in 1973 EB's were seen as critical to the continued viability of our armed forces since the services depended upon sufficient numbers of high-quality recruits to flow smoothly into critical occupational specialties. Since the inception of the all-volunteer force, the services have not faced an outright shortage of people, indeed volume requirements have consistently been met. The problem has been attracting "high-quality" recruits. The Army defines a "high-quality" recruit as one who is a high school diploma graduate and has scored in the upper 50 percentile on the Armed Forces Qualification Test (AFQT).

Enlistment bonuses are extremely effective policy options for efficiently managing the recruiting process and for channeling high-quality individuals into military specialties (primarily the combat arms) that have historically been the most difficult to fill. Cash bonuses in general (and enlistment bonuses in specific) are very flexible policy tools for personnel managers to use in shaping the desired skill mix in the force.

The military compensation package is complex and difficult to adjust, consisting of basic pay, allowances for food and housing, health care, retirement and other fringe benefits that are closely regulated by law and only changed by Congress. Cash bonuses

represent one area where personnel managers have fairly wide latitude in adjusting compensation. Bonuses provide flexibility since they can be quickly added or deleted without affecting other elements of the future or current compensation package. They also cost less than across-the-board pay increases since they are paid only to persons in hard-to-fill specialties, principally in infantry, armor and artillery skills.<sup>1</sup>

#### DUAL MARKET CONCEPT

When the Army begins to screen potential recruits it subscribes to what has become known as the dual market concept. That is, the Army believes there are two major sub-markets within the eligible youth population. Individuals recently graduating from high school will either be employment oriented or college oriented. The Army has historically done well in the employment oriented segment; however, inter-service competition for high-quality youth in this market segment is intensifying. Combined with the fact that youth demographics are shrinking through the mid-1990's, the Army has had to rely more heavily on the college-bound market segment to achieve its quality requirements. These two market segments respond to different incentives:

- Employment oriented youth respond to bonuses for specific skills, guaranteed skill training, job security, and the need for immediate employment offering a competitive pay package.
- College oriented youth are more interested in educational benefits such as the Army College Fund or Montgomery G.I. bill, patriotism, service to country, adventure and independence.<sup>2</sup>

Over-reliance on either bonuses or educational benefits could skew

the recruit population toward one or the other of these market segments, resulting in an uneven flow through the accession/separation stream. Conversely, a melding of bonus takers and those drawn to educational benefits balances the flow. Hence, it is important to understand the complementary role bonuses and educational benefits play in the recruiting game.

The most recent and perhaps most comprehensive study into the effects bonuses have on the enlistment decision was completed by the Rand Corporation in April 1986.<sup>3</sup> This nation-wide experiment, directed by the Congress and sponsored by the DOD, spanned the period of July 1982-June 1984. Utilizing the Army as the test service, three cells were established to test two new bonus programs against the control program (a \$5,000 bonus for a four-year enlistment--which was the maximum enlistment bonus at that time). The other test cells provided a cash bonus of \$8,000 for a four-year enlistment; and a cash bonus of \$8,000 for a four-year enlistment or a \$4,000 bonus for a three-year enlistment. This oft referenced and statistically sound experiment revealed that cash bonuses "were extremely effective at channeling high-quality individuals into occupations and that bonuses had the ability to move people from two-year to three-year obligations".<sup>4</sup> What was noteworthy is that bonuses have only a "modest market expansion effect increasing the total number of high-quality recruits".<sup>5</sup> In sum, bonuses play a significant role in recruiting high-quality youth into critical, hard-to-fill skills and in lengthening the period of their initial commitment; however, as an inducement to draw additional recruits into the force, bonuses play only a modest role.<sup>6</sup>

### METHOD OF PAYMENT

The Rand experiment above showed that cash bonuses play a key role in channeling high-quality youth into the right skills in the force. Further studies have asserted that these dollars can be maximized by developing the best method of payment. The Congress currently authorizes the services to pay enlistment bonuses in the following manner:

- Up to \$5,000 upon completion of skill training
- Remainder (for skills with bonuses exceeding \$5,000) in four equal installments commencing three months from payment of initial \$5,000 and every three months thereafter.<sup>7</sup>

Paying enlistment bonuses in this manner is at the heart of a long-standing argument between financial managers, personnel managers, economists and behavioral scientists. Contemporary research performed by economists and behavioral scientists addresses what has become known as an individual discount rate. A potential recruit's individual discount rate can be equated to be the value one places on dollars received immediately versus deferred dollars. Several organizations have performed such studies for DOD; namely the 5th Quadrennial Review of Military Compensation (November 1983), the Army Research Institute, and the Office of Economic and Manpower Analysis, U.S. Military Academy during the development of the YAGSTAN model. These researchers agreed that the real individual discount rate fell between 15% and 20% but fluctuated based on a person's age and the economic situation. Given a 20% discount rate, a potential recruit would value as equal an \$80 bonus paid today versus a \$100 bonus paid one year from now. As might be anticipated, personnel



managers and economists who adhere to the individual discount rate theory argue that front-loading cash bonuses maximizes their drawing power making them more cost effective than deferring payments.

Financial managers take a contrary view asserting that paying significant amounts of front-loaded bonuses to untested recruits is not a sound investment and results in a larger than necessary unearned bonus debt (the Army's cumulative enlistment bonus debt for FY 79-88 is \$20.4 million). Further, deferring payments to occur throughout the soldier's term of service would provide additional cash incentives for the soldier to complete the full contract plus reducing the soldier's unearned bonus debt should separation occur early.<sup>8</sup>

#### POINTS DESERVING EMPHASIS

Before moving to the next chapter on reenlistment bonuses, it is important to review several key points regarding enlistment bonuses:

- Enlistment bonuses are especially useful to channel employment oriented youth toward hard-to-fill skills and to increase manyears per accession. Enlistment bonuses have only a modest effect on market expansion.<sup>9</sup>
- Only 5.2% of new recruits give "earning money" as a major reason for enlisting. This ranks fifth among the reasons young people join.<sup>10</sup>
- The method of paying bonuses (front-loaded versus deferred) affects the draw of the bonus and the unearned bonus debt. The optimal method of paying enlistment bonuses has not been empirically determined. Research regarding individual discount

rates noted in this chapter did not focus on enlistment bonuses but rather on the broad spectrum of all cash payments. The most thorough empirical work on paying bonuses was done by the Rand Corporation in 1985; however, it looked only at reenlistment bonuses.<sup>11</sup> This report will be addressed in detail in the following chapter.

- Bonuses and educational benefits are two tools in the recruiting arsenal--changes to either require a well-reasoned approach. Mistakes could have far-reaching consequences.<sup>12</sup>

#### ENDNOTES

1. U.S. Department of Defense, Office of the Secretary of Defense, Fifth Quadrennial Review of Military Compensation, Vol. 3, pp. 389-390.

2. U.S. Department of the Army, Office of the Deputy Chief of Staff for Personnel, Recruiting, Retention and Quality in Today's Army, p.20.

3. James N. Dertouzos, J. Michael Polich and S. James Press, The Enlistment Bonus Experiment, p.v.

4. Ibid., p.49.

5. Ibid.

6. Ibid.

7. U.S. Department of the Army, Army Regulation 601-210, p.97.

8. Interview with Jerry Lipka, U.S. Army Finance and Accounting Center, Indianapolis, In., 24 October 1988.

9. U.S. Department of the Army, Office of the Deputy Chief of Staff for Personnel, Recruiting, Retention and Quality in Today's Army, p.viii.

10. Ibid., p.21.

11. James R. Hosek and Christine E. Peterson, Reenlistment Bonuses and Retention Behavior.

12. Recruiting, Retention and Quality in Today's Army, p. x.

## CHAPTER IV

### REENLISTMENT BONUSES

#### BACKGROUND

Since the first Congress in 1791 authorized the payment of reenlistment "bounties", reenlistment bonuses have been paid continuously except for 1933-1939. Reenlistment bonuses have been called by many different names but most recently known as regular reenlistment bonus, variable reenlistment bonus and currently as selective reenlistment bonus. Despite the title, reenlistment bonuses have always been designed to "maintain an adequate level of experienced and qualified personnel in the peacetime forces".<sup>1</sup>

The purpose of today's Selective Reenlistment Bonus (SRB) is best defined in the DOD directive prescribing its implementation policies: "the SRB is to serve as a retention incentive paid to enlisted members serving in certain selected military specialties to reenlist for additional obligated service. The bonus is intended to generate additional reenlistments in critical military specialties characterized by retention levels insufficient to sustain the career force at an adequate level".<sup>2</sup> Inherent in this purpose statement are two key phrases that distinguish the SRB from previous reenlistment bonuses. SRB's are focused on selected military specialties with chronic and persistent shortages in total career manning. Skills meeting the established criteria are nominated by the services and selectively approved for payment by the Office of the Secretary of Defense. Soldiers serving in skills not covered by SRB's

receive no monetary incentive to reenlist. Computations used to determine the level of bonus to be paid were developed to generate additional reenlistments by paying increasingly higher bonuses for additional manyears of obligated service above the minimum three-year term required to draw an SRB. The specific method used to calculate an SRB is contained in AR 601-280, Total Army Retention Program.<sup>3</sup> A total SRB cannot exceed \$20,000 for Army members, while certain nuclear trained sailors can receive up to \$30,000.

#### REENLISTMENT BONUSES AND RETENTION BEHAVIOR

As with enlistment bonuses, reenlistment bonuses are a "powerful tool for controlling retention in targeted occupations and increase not only the rate of retention but also the number of man-years per reenlistment".<sup>4</sup> An in-depth study completed by the Rand Corporation in March 1985, highlighted the effects of bonuses on retention behavior.<sup>5</sup> For the purposes of this study, particular attention was given to the method of payment of these bonuses (i.e. lump sum, front-loaded versus deferred or installment payments) and was thus extremely beneficial.

Before focusing on the method of payment, it is of benefit to review the Rand study as to the effects cash bonuses have on reenlistment:

- "Reenlistment bonuses are a potent, versatile component of compensation. Bonuses may be turned on or off rapidly and targeted on critical skills".<sup>6</sup>
- Bonuses increase the retention rate by inducing personnel to reenlist rather than extend; thus manyears are increased.
- Bonuses, because they can be rapidly targeted, help alleviate unexpected personnel shortages in critical skills.

- Higher bonuses can offset the migration of soldiers out of the force during times of low civilian unemployment.

This extensive study by a firm widely recognized for its expertise in military personnel and compensation analysis has had significant influence on personnel policy analysts both within and outside DOD.

#### METHODS OF PAYMENT

Personnel managers throughout the uniformed services have unanimously favored returning to the lump sum (front-loaded) method of paying reenlistment bonuses which ended in January 1982. The current method of payment, 50% of total bonus paid immediately with the remainder paid in equal, annual installments, is a blend of the lump sum and deferred payment method. Personnel managers would agree with the Rand findings that indicate that due to the individual discount rate, "installment bonuses (are) worth less to a person than its nominal lump sum equivalent".<sup>7</sup> Further, the Rand study found that despite the need to recoup greater dollar amounts caused by lump sum payments, the lump sum method was still more cost effective because of its ability to:

- Increase expected manyears by shifting personnel from extensions to reenlistment.
- Increase the proportion of personnel choosing to stay in their current specialty thus decreasing retraining costs.
- Increase the reenlistment rate to a higher degree than an installment bonus of the same nominal value.

In a separate but related study, the DOD 5th Quadrennial Review of Military Compensation (5th QRMC) found that due to the individual discount rate "typical reenlistment bonuses can be reduced by about 15% before any reduction in reenlistment rates occur....,provided bonuses were paid in lump sum instead of by the present method".<sup>8</sup> The 5th QRMC report also noted that the "services must continually monitor recoupment, termination, and utilization issues related to bonus management, but a switch to lump sum would have a miniscule impact on these concerns relative to the substantial gains to be made".<sup>9</sup>

Despite the virtues of lump sum payments noted in these two studies, SRB's continue to be paid by "blending" the lump sum and installment methods. Although the DOD recommended a return to the lump sum method through the 5th QRMC report, the Congress has failed to act positively on the change. Reverting to lump sum has also been side-tracked by more stringent Defense budgets which could not support the up-front outlay of lump sum payments while continuing to pay prior year installment obligations.

#### POINTS DESERVING EMPHASIS

Prior to closing this chapter, a reemphasis of a few points is in order:

- SRB's, in concert with educational benefits and enlistment bonuses, are the three main monetary tools used to attract and distribute high-quality soldiers.

- Replacing soldiers who decided against reenlistment incurs significant recruitment and training costs. Personnel managers seek the most cost effective bonus program possible.

- Recent studies support the hypothesis that lump sum payment of SRB's is more cost effective than the current method and would be far more cost effective than a purely deferred method paid in equal annual installments.
- The Army has experienced a healthy retention climate throughout the 1980's due in some measure to its successful SRB program. Reenlistment goals have been met and in recent years at lower costs than originally programmed (in FY 87 \$20 million of SRB funds was reprogrammed with an anticipated FY 88 expenditure of less than the reduced FY 87 level).
- Lump sum payments of SRB's are more cost effective even when considering higher recoupment costs and the negative effects of a growing unearned bonus debt.

#### ENDNOTES

1. U.S. Department of Defense, Office of the Secretary of Defense, Military Compensation Background Papers, p.321.

2. U.S. Department of Defense, Office of the Secretary of Defense, DOD Directive 1304.21: Award of Enlisted Personnel Bonuses and Proficiency Pay.

3. U.S. Department of the Army, Army Regulation 601-280, p.32.

4. U.S. Department of the Army, Office of the Deputy Chief of Staff for Personnel, Recruiting, Retention and Quality in Today's Army, p.48.

5. James R. Hosek and Christine E. Peterson, Reenlistment Bonuses and Retention Behavior, p.iii.

6. Ibid., p.54.

7. Ibid., p.7.

8. U.S. Department of Defense, Office of the Secretary of Defense, Fifth Quadrennial Review of Military Compensation, Vol 3, p.656

9. Ibid., p.658.

## CHAPTER V

### RECOUPMENT OF THE UNEARNED BONUS DEBT

#### BACKGROUND

In October, 1978, the General Accounting Office (GAO) began releasing a series of reports highlighting the necessity for improving the way the Federal government administered its credit management and debt collection programs. Stimulated by these reports, the Office of Management and Budget (OMB) created a Federal Debt Collection Project in August 1979. This committee, comprised of representatives of 24 federal agencies, was tasked to determine the breadth of the debt problem, to identify government-wide impediments to agency collection efforts and to provide recommendations to solve the debt collection dilemma. The results of the OMB project revealed that the U.S. domestic debt was \$126 billion as of 30 September 1979. Of this, \$25 billion was identified as delinquent.

Under the guidance of President Reagan and his Director of OMB, Mr. David Stockman, intensive efforts were begun within the Federal government to identify and implement initiatives necessary to reduce this debt. DOD began to develop systems to more accurately account for and manage their debt portfolios. Although precise amounts were unavailable, the Army's initial unearned bonus debt was estimated to be \$4.7 million--\$3.5 million due to unearned enlistment bonuses, and \$1.2 million from unearned reenlistment bonuses. Through the ensuing years since this initial report was issued, the methods for tracking these debt



accounts have been automated and collection systems improved, resulting in what is believed to be a much more accurate assessment.

Throughout the early 1980's, agencies of the Federal government were hindered in their debt collection efforts by bureaucratic and legal impediments. With the enactment of the Debt Collection Act of 1982 and the Debt Reduction Act of 1984, federal agencies were provided the tools necessary to significantly improve their debt collection efforts. New provisions permitted federal agencies, except the Internal Revenue Service (IRS): (1) to contract with private debt collection agencies, (2) allowed IRS addresses to be provided to private debt collectors under contract to the Federal government, (3) authorized the IRS to disclose to federal agencies the tax liability status of an applicant for a government loan, (4) required charging interest and penalties on overdue debts, (5) permitted salary off-sets of government employees in order to repay overdue government debts, (6) authorized a pilot program under the Justice Department to contract with private lawyers to litigate cases to collect debts owed the Federal government, and (7) authorized the off-set of federal income tax refunds to repay delinquent federal debts.

Financial managers in the U.S. Army Finance and Accounting Center were quick to capitalize on these new debt collection capabilities and implemented an aggressive collection program. Despite these efforts, the rapid growth of bonus dollar expenditures, matched by the growth of bonus debtors, pushed the unearned bonus debt steadily upward. In 1982 the cumulative

enlistment bonus (EB) debt stood at \$5.5 million with the SRB debt at \$2.8 million. Three years later at the end of FY 85 these debts had almost tripled to an EB debt of \$14.8 million and a SRB debt of \$7.8 million. At the end of FY 88 the cumulative debt in these respective accounts had reached \$20.3 million and \$9.3 million.<sup>1</sup>

#### INITIATIVES TO REDUCE UNEARNED BONUS DEBT

To this point my work has focused on the creation and growth of the unearned bonus debt and the challenges faced in trying to "avoid" that debt by looking at alternative methods of paying cash bonuses. In a sense, earlier chapters have concentrated on debt avoidance. This chapter and Chapter VI focus on debt collection.

There are two categories of recoupable bonuses that must be addressed when considering repayment of unearned bonuses. The first category occurs when a soldier remains in the service but becomes ineligible for the bonus due to skill or qualification changes. Relatively minor difficulties are encountered in recouping these debts since the individual is still drawing military pay and a viable repayment schedule can be enforced. The second category includes those who leave the service before completing the bonus obligation. In these cases the local finance and accounting office attempts to recoup as much as is legally possible prior to the individual's separation. Often these soldiers are separated under derogatory circumstances leaving only minimal pay and allowances due at separation. When this

occurs, establishment of an out-of-service debt collection schedule is negotiated. Experience has shown that soldiers separated under these conditions often have difficulty in securing suitable civilian employment and frequently renege on all or part of their government debt. Army debt collection analysts indicate that only 24¢ on the dollar can expect to be recovered through out-of-service collections, although in recent years this rate has increased because of the addition of IRS refund off-set provisions.<sup>2</sup> While debt collection is certainly important to demonstrate sound fiscal management of government funds, recoupment efforts alone cannot stunt the growth of the unearned bonus debt. An aggressive debt avoidance effort, combined with tough debt collection procedures must be pursued.

In February 1984, the Comptroller of the Army (COA), LTG Peixotto, proposed to the Deputy Chief of Staff for Personnel, LTG Elton, three alternatives to assist in eliminating the unearned bonus debt. The alternatives consisted of the following:

- Change the law to allow bonus debts to be counted as a direct expense of recruiting and retention--a simple "cost of doing business" option.
- Pay bonuses monthly, as earned--a deferred payment method in monthly installments.
- Pay bonuses at the end of each enlistment year or end of each reenlistment period--a deferred payment method in annual installments.

Interesting in these alternatives is the realization that to make major progress at reducing the debt requires an adjustment

to the method of payment. Debt collection efforts, no matter how successful, are only "chipping" at the margins. This appears to have been at the center of the finance community's argument from the outset.

As might have been predicted, after exchanges of correspondence and thorough review, the DCSPER could not support the COA's proposals. LTG Elton sensed that the idea to identify a debt as the cost of doing recruiting business would send the wrong signal to Congress. Further, the proposals to defer bonus payments would jeopardize recruiting and retention efforts. As an alternative, LTG Elton proposed that the Army develop a sound argument that "unearned bonuses are not much (when) compared to the overall program performance".<sup>3</sup> The DCSPER's response cited as its source the 5th QRMC recommendation to pay SRB's in lump sum payments versus deferred payments, the same assertion later made in the Reenlistment Bonuses and Retention Behavior study done by the Rand Corporation.<sup>4</sup> This approach to deal with the unearned bonus debt issue resulted in no visible policy shift.

In 1985, Senator Proxmire (D-Wis) was highly critical of the Army's failure to collect \$65 million worth of out-of-service debts owed to the Federal government. As a result a thorough review of the out-processing system was made to ensure complete audits of soldiers' pay accounts were conducted prior to their separation. The Vice Chief of Staff of the Army, General Thurman, sent a personal message to each major commander directing that soldiers' separation dates would not

be expedited no matter the urgency, so that a thorough review of their pay accounts could be conducted. Additionally, he directed commanders to consider debt implications when making their final decision to discharge a soldier prior to the normal expiration of the term of service. Shortly following General Thurman's message, Mr. Jeffcoat, the Assistant Comptroller of the Army for Finance and Accounting, dispatched a follow-up message stressing to local Finance and Accounting Officer's (FAO) the need to improve separation procedures and internal controls in order to prevent errors. FAO's were also challenged to ensure sufficient time was provided to perform thorough final audits, even if the soldier's separation date was delayed. While initial reaction to these messages certainly caused procedural reviews, long-term improvements in the coordination of out-processing activities to identify existing debts have not been totally successful.

Although two attempts have been undertaken to bring together the personnel and finance communities on the unearned bonus debt issue, substantive policy changes aimed at enhancing debt avoidance and debt collection measures have not materialized.

#### POINTS DESERVING EMPHASIS

Key points worth remembering in this chapter are:

- Debt managers have developed the tools necessary to identify the cause and the full extent of the Army's unearned bonus debt. Accurate identification however, has not led to debt reduction.
- Army debt managers cannot attack the bonus debt problem in isolation. A coalition must be forged with the personnel

policy decision makers. Solutions which threaten the viability of the Army's recruiting and retention programs will routinely be resisted by personnel managers.

- Intermittent periods of intense efforts focused on debt avoidance and collection measures have not resulted in reversing the growth of the unearned bonus debt. Perhaps a coordinated, long-term action plan might provide more favorable results.

#### ENDNOTES

1. Interview with Lois L. Richardson, U.S. Army Finance and Accounting Center, Indianapolis, In., 3 Nov 1988.

2. Ibid.

3. Robert E. Elton, LTG, Deputy Chief of Staff for Personnel, Letter to Comptroller of the Army, 5 March 1984.

4. James R. Hosek and Christine E. Peterson, Reenlistment Bonuses and Retention Behavior.

## CHAPTER VI

### UNEARNED BONUS DEBT: POLICIES AND INITIATIVES IN THE NAVY AND AIR FORCE

#### BACKGROUND

The Navy and the Air Force utilize enlistment and reenlistment bonuses in a similar propensity as does the Army. Noticeable differences are that the Air Force has only a limited enlistment bonus program, but uses reenlistment bonuses at a slightly higher rate than does the Army. The Navy is the heaviest user of reenlistment bonuses of all the services and ranks near the Army in use of enlistment bonuses. As a general rule, the Navy has historically relied on bonuses and incentive pays to compensate for extended periods of arduous sea duty. On the other hand, the Air Force and the Army use enlistment and reenlistment bonuses in their traditional attraction and retention roles. Since both the Navy and the Air Force use EB and SRB bonuses, each faces the unearned bonus debt dilemma. A review of their programs to avoid and collect these outstanding debts revealed certain initiatives worthy of Army consideration.

#### THE AIR FORCE UNEARNED BONUS DEBT PROGRAM

Air Force financial analysts paid little attention to their debt portfolios in general, and the unearned bonus debt in specific, until February 1987. Only approximate figures on the size of the debt were available in FY 82; however, the out-of-service debt account grew from \$4.2 million in that year to \$12.2 million in FY 86. The unearned bonus debt was not

specifically identifiable prior to February 1987, but it was placed at \$1.01 million at the end of FY 87 (this figure includes only the months of Feb-Sep 87). During FY 88 the bonus debt grew by \$1.1 million but this trend appears to be reversing in FY 89 as projections after four months of operation expect the debt to increase by only \$.88 million.<sup>1</sup>

In January 1987, the Commander, Air Force Accounting and Finance Center began to attack the issue of "separation indebtedness". At that time statistics revealed that 22% of the airmen discharged in FY 86 left the service owing a total of \$12.3 million to the government. A series of policy changes and procedural revisions were initiated. However, more importantly the support of the chain of command was energized. Specific initiatives undertaken to accomplish this are summarized below:

- In March 1987, a monthly report began to be provided to each major commander and local finance officer depicting the command's debt analysis. Specific amounts and causes of debts were identified in order to pinpoint whether the finance office or another agency was impacting on debts.
- A public information effort was undertaken using the Air Force Times and the Air Force Comptroller Magazine to warn airmen of the tough approach being taken to collect debts. Also, these articles were aimed at alerting the chain of command and local FAO's to the importance of debt collection.
- Enlistment and reenlistment forms were modified to secure the airman's consent to initiate recoupment of unearned



bonus payments. This recoupment action could begin if the airman was "flagged" for certain offenses leading to a derogatory discharge.

- Procedures were established to require commanders to advise the local finance office upon "flagging" an airman for an offense which can lead to a derogatory separation. When notified, the finance officer could begin to withhold or suspend the individual's pay in order to satisfy the debt, and suspend any further bonus payments that might be due.

- Several proposals to change DOD policies have been drafted to bolster debt avoidance efforts. Authority has been sought to deny paying the remainder of bonuses to individuals who cannot perform in their bonus specialty due to an approved hardship discharge, medical reclassification (not due to own misconduct), and pregnancy reclassification.

Because of these initiatives and the increased emphasis being placed on lowering the separation debt, FY 87 "realized a sharp decline in both the number of former members who separated in debt and the dollar value of these debts".<sup>2</sup> Only 17% of the airmen separated in FY 87 owed the government money, with the total indebtedness being \$9.2 million.

In addition to the above actions, the Air Force Inspector General is conducting a systems review of the "separation indebtedness" problem. Preliminary findings reveal that finance officers are complying with the procedures calling for suspension and withholding of pay and bonus payments and that

debt payments at separation have increased proportionately. No incidences have been noted wherein the finance officer's authority to withhold has been challenged. Indeed, his role in protecting the interests of the government has been upheld in a Comptroller General decision. The most notable problems were in educating the chain of command and defeating parochialism amongst base agencies.<sup>3</sup>

#### NAVY UNEARNED BONUS DEBT PROGRAM

In comparison to the debt avoidance and collection programs in the Air Force and the Army, my view is that the Navy has not yet "awakened" to the issue. Contact with the personnel manager of enlistment and reenlistment bonus programs revealed an absence of sensitivity to the unearned bonus debt.<sup>4</sup> Part of this could be caused by the lack of capability in their finance center to accurately display the amount of the unearned bonus debt. This results because all bonuses are accounted for under the same debt code, thus enlistment and reenlistment bonus debts are immersed with doctor bonuses, officer bonuses, nuclear bonuses, etc. The personnel program manager provided a cumulative unearned bonus debt of \$18.7 million spanning FY 85-88.5 The financial analyst who manages debt accounts at the Navy Finance Center indicated that the Navy's debt portfolio at the close of FY 88 was \$37.0 million, of which 40%, or approximately \$14.8 million, was "believed" to be bonus debt.<sup>6</sup> As can be seen these figures differ and reconciling them is not possible as bonus debt tapes older than FY 87 were destroyed when the center changed to a new computer system.<sup>7</sup>

Responses to questions regarding Navy programs to avoid and collect unearned bonus debts revealed no notable on-going initiatives. The Navy collects debts using the normal collection methods available to federal agencies. My impression was that unearned bonus debts were viewed as the "costs of a viable recruiting and retention effort".

#### ENDNOTES

1. Interview with Bill Dunn, U.S. Air Force Accounting and Finance Center, Denver, Colorado, 22 February 1989.

2. Bill Dunn, "USAF Separation Debts Slowly Waning", The Air Force Comptroller Magazine, Vol. 22-2, April 1988, p. 15.

3. Interview with James Bennett, LTC, Office of the Air Force Inspector General, Norton, AFB, California, 1 March 1989.

4. Interview with S.A. Gillette, CDR, Office of Navy Personnel Programs, Washington, D.C., 9 February 1989.

5. Ibid.

6. Interview with Marilyn Mayka, U.S. Navy Finance Center, Cleveland, Ohio, 14 February 1989.

7. Ibid.

## CHAPTER VII

### CONCLUSIONS

To reduce the Army's enlistment and reenlistment bonus debt, the personnel and finance communities must converge and develop mutually agreeable solutions. Nowhere is this more evident than over the issue of lump sum payments of EB and SRB bonuses. To please one community, the other must be slighted. Similarly in the area of recoupment, FAO's must rely on the local personnel office to provide sufficient out-processing time to conduct thorough, pre-separation audits. At literally every juncture, finance officers and personnel managers are inextricably linked if progress is to be made. For ease of reading, this chapter has been subdivided into debt avoidance, debt collection and action plan packages. However, to be effective the conclusions and recommendations should be treated as a single entity comprised of uniquely different, yet closely linked elements.

#### DEBT AVOIDANCE

Developing mutually agreeable debt avoidance options is most difficult. Chapters II, III, and IV are replete with references to the conflict between paying "up-front", lump sum bonuses and the resultant increase in unearned bonus debt. The Rand retention behavior study documents the cost effectiveness of lump sum payments over deferred, installment payments. In my view, the Army would be unwise to move closer to an

installment method of paying SRB's, as the current "blend" in itself is not optimal. Should any shift occur, it should be made toward the lump sum option.

However, the method of paying enlistment bonuses may offer some opportunity for debt avoidance. An exhaustive search for an empirical study dealing with the optimal method of paying enlistment bonuses revealed that none has been conducted since the inception of the all-volunteer force. It is not sound to assume that behavior of a potential recruit toward a lump sum enlistment bonus is closely related to the behavior of a soldier making a reenlistment decision. Research dealing with the individual discount rate, while certainly relevant, must be expanded to consider economic factors, the recruiting environment and the costs of recouping unearned bonuses. This idea is particularly true when one considers that Army personnel managers point out that enlistment bonuses are "distribution, skill-channeling tools" and only 5.2% of potential recruits list "earning money" as their primary reason for joining the Army.<sup>1</sup> It is realized that the shrinking manpower pool will certainly complicate any decision to shift payment methods, but the potential reduction to the unearned bonus debt mitigates that an alternative be studied. Furthermore, the enlistment bonus debt is more than twice as large as the SRB debt, providing an excellent opportunity for more than "marginal" savings.

## DEBT COLLECTION

Army programs to collect out-of-service debts are equal to, if not better, than all of the other services. While these positive programs are sustained, efforts should be focused on recovering the maximum amount prior to the soldier's separation. In this area much can be learned from the Air Force. The Army has made one step in the right direction by ensuring that commanders making discharge decisions consider the indebtedness of the soldier. In this regard, the commander's interface with the personnel and finance offices is essential if the commander is to receive the entire indebtedness picture. Efforts to energize the chain of command behind debt collection must be continuous. Providing major commanders and local FAO's with a "score card" that makes them sensitive to the effectiveness of their separation indebtedness program has merit. Similarly, JUMPS validation team inspection visits might also be used to check the implementation of certain key elements of debt collection.

Further, the withholding and suspension of pay in certain cases where the individual is "flagged" pending a derogatory discharge appears to be benefiting Air Force collection systems. Expansion of Army FAO's authority in this area might result in increased pre-separation collections.

Army Regulation 635-200, Personnel Separations, provides the procedures to be followed in order to discharge enlisted soldiers from the Army. Derogatory discharges must be submitted on a standardized format with positive responses required to a series of leadline elements. Adding to these formats, information that

shows the indebtedness status of a soldier being considered for discharge, would ensure that commanders reviewed and considered the soldier's debts.

#### UNEARNED BONUS DEBT ACTION PLAN

Reversing the upward growth of the unearned bonus debt is a complex, multi-faceted challenge requiring long-range planning and sustained execution. In my view, one specific office such as the Director of Centralized Pay Operations should be designated as the responsible agent for all debt management actions within the Finance and Accounting Center. In this role the director must become conversant in every aspect of the debt mosaic--from studies being conducted to determine how bonuses should be paid, to the collection of out-of-service debts. Any issue that arises across the spectrum of bonus debts should activate the involvement of this director. Early on a principal function of this director would be to develop an Action Plan that focuses the necessary attention and resources on reducing the bonus debt. Specific critical elements must be identified and closely monitored. One essential ingredient to the success of this plan is a public information effort designed to keep the Army's bonus debt clearly in the minds of commanders, personnel managers, local FAO's and potential debtors. While it is unclear if the Air Force has such a plan, evidence of an active public information effort certainly exists.

#### ENDNOTES

1. U.S. Department of the Army, Office of the Deputy Chief of Staff for Personnel, Recruiting , Retention and Quality in Today's Army, p.21.

## CHAPTER VIII

### RECOMMENDATIONS

1. Recommend that the Assistant Secretary of the Army for Financial Management (ASA(FM)) request the DCSPER to revise enlistment and reenlistment contracts to specify that recoupment action may begin when the soldier is "flagged" for an offense which could lead to a derogatory discharge.

2. Recommend that the ASA(FM) develop and subsequently provide a periodic report to major commanders and local FAO's which shows the effectiveness of their separation indebtedness program.

3. Recommend that the ASA(FM) provide expanded authority to local FAO's to withhold and suspend pay in certain cases of soldiers being "flagged" pending derogatory discharges who upon separation will be indebted to the government.

4. Recommend that the ASA(FM) request that the DCSPER revise AR 635-200, Personnel Separations, to incorporate the soldier's indebtedness status into standard formats for requesting separations and discharges.

5. Recommend that the DCSPER and the ASA(FM) jointly sponsor a test to empirically measure the cost effectiveness of the current method of paying enlistment bonuses, ensuring the costs of recoupment and the costs of out-of-service collections are fully considered. Because of their demonstrated expertise in closely related work, the Rand Corporation should be given careful consideration to perform this test.

6. Recommend that the ASA(FM) develop and coordinate with the DCSPER a long-range Action Plan to combat the Army's unearned



bonus debt. Initially, as a minimum, these two elements should be included:

- Appoint one directorate to oversee the entire bonus debt issue. This directorate would possess the authority to bridge functional lines to seek policy changes necessary to reduce the debt.
- Develop a pro-active public information campaign and marketing strategy aimed at focusing the chain of command on their debt reduction responsibilities.

As has been mentioned earlier, the finance community cannot on its own effectively reduce the Army's unearned bonus debt. A coordinated, concerted effort between the finance and personnel communities is essential. This theme should be clear when one reviews the above recommendations. The overarching challenge facing the ASA(FM) is to heighten the DCSPER's sensitivity to the bonus debt to a level that would accept a change in the method of paying EB's despite the associated risk. Failing to do this relegates debt reduction efforts to a unilateral option--debt collection. To date this approach has been unable to reverse the upward growth.

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