



Linking Military Compensation to Retention

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One Congressional Concern

Will the recruiting and retention problems of 2005 be repeated:

- As the economy improves?
- With the surge in Afghanistan?



Congress Authorizes

- Basic pay increase,
 - 3.4% for 2010, 0.5% above ECI
- Payment of selected reenlistment and other retention bonuses
 - Congress appropriates total funding
 - Rates of pay per service member set by law for some other special and incentive pays (sea pay, family separation)
- Retirement, education benefits, medical benefits to non-active-duty
 - Jurisdiction split among various committees
 - DOD may have statutory authority under current law but Congress may override (e.g. TRICARE cost sharing)



Indicators of the Adequacy of Pay as a Retention Tool

- Military-civilian comparisons
 - Military-civilian pay gap
 - Comparing cumulative increases over time in civilian wages to military basic pay
 - Easy to compute
 - Narrow measure of earnings
 - May not reflect retention over the longer term
 - Levels of military and civilian pay, adjusted for education and experience
 - Who is in the comparison group
 - May not reflect retention problems
- Retention problems
 - Related to many factors
 - Economy, deployments, work and living conditions
 - Actions of Congress may lag substantially



Estimates of Military Compensation

- Average compensation per service member between \$100,000 and \$150,000
 - Estimates based on data from 2000 through 2006 and may be higher at present time
- Cash earnings total 40% to 50% of compensation
 - Basic pay, allowances, special pays and tax advantage
 - Basic pay averages about 55% to 60% of RMC
 - Special pays are about 5% of the military personnel account
- Noncash and deferred cash compensation comprise remainder
 - Base-provided services, retirement pay, health care benefits, educational benefits
 - Majority of which are deferred benefits



Effectiveness of Cash Pay

- Across-the-board increases in pay
 - May be appropriate when widespread difficulties in manning
 - 1% increase in pay: retention increases 0.5% to 2.0%

- Targeted pay (reenlistment bonus)
 - When manning shortages are experienced only within selected occupational fields
 - SRBs are more cost-effective if targeted to occupations
 - With higher responsiveness (higher elasticities)
 - Where retention is relatively low
 - One level SRB: reenlistment increases 1 to 3 ppt



Manning Shortfalls

- Many enlisted occupations are chronically under- or over-staffed
 - 30% regularly had manning shortfalls from 2000 to 2007
 - 40% were overstaffed during that time

- Variation in pay is relatively small compared to the civilian sector
 - Bonuses are a small part of compensation



CBO Budget Option

- Proposal
 - Increase basic pay by ECI minus 0.5% for 2010 through 2014
 - Target additional compensation to occupations with manning shortfalls in those years

- Impact for the Army
 - Reenlistments drop about 300 to 350 soldiers, compared to total reenlistments of about 65,000
 - One level SRB to $\frac{1}{4}$ of the first-term soldiers in targeted occupations buys that back and saves money immediately

- Impact service-wide
 - Retention held constant
 - Multi-year savings could be several billion



Considerations for a Shift to Bonuses

- **Flexibility**
 - Bonuses can be more easily adjusted year to year to match retention goals
 - Bonuses can be focused on the years of service when service members make career decisions

- **Equity**
 - Should all service members receive similar pay because they're all warfighters first?
 - Or, should military pay be more closely aligned with civilian alternatives?

- **Lower overall compensation than otherwise in out-years**
 - Bonuses do not compound the same way as do increases in basic pay
 - Shift to bonuses reduces retirement pay and other benefits



Not All Compensation Is Equal

- **Noncash compensation**
 - May be offered because it can be provided more cheaply than buying it in the individual market
 - Promotes military readiness and ensures quality of life
 - May be less effective than cash as a retention tool
 - Restricts choices of service members
 - Service members may not value a military-provided service as much as it costs to provide

- **Deferred benefits**
 - Many service members will never be eligible for some of the deferred benefits
 - Only 15% of enlisted personnel stay to retirement
 - Younger service members attach little value to the benefit
 - High discount rate



Some Compensation May Suppress Retention

- Educational benefits for veterans
 - Have to separate from active duty to use it intensively
 - Research suggests that a \$10,000 boost in benefits increases separations up to 3 percentage points

- Cliff-vesting of retirement pay
 - Roughly one-quarter of service members who serve 19 years stay through 24 years
 - Early retention effects are positive but small, although it provides incentives for higher seniority service members to stay
 - DoD contributes, on average, more than \$8,000 per year to the Military Retirement Fund; service members at first-reenlistment value the entire benefit at about \$8,000