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SERVICE MEMBER COMPENSATION AND BENEFITS COMMUNICATION—COULD THE GRASS NOT BE GREENER ON THE OTHER SIDE?

December 2018

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COMMUNICATION—COULD THE GRASS NOT BE GREENER ON THE
OTHER SIDE?**

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ABSTRACT

Compensation systems, including cash payments and benefits, play an essential role in recruiting and retaining talents in both the private and public sectors; we argue that due to the complexity of the benefits systems, as well as a lack of communication, many military service members are not aware of the overall worth of their pay, allowances, benefits, and tax breaks. In several instances, military benefits are often much greater than those of civilian counterparts, yet many service members remain dissatisfied and misinformed regarding compensation packages and benefits. A comprehensive communication and education overhaul must be implemented in order to quell a growing culture of dissatisfaction and misunderstanding among service members facing the decision to extend their military career or terminate service. In an increasingly competitive economic environment, improvements in communication efforts regarding compensation and benefits will allow service members to make better-informed decisions and may ultimately contribute to improvements in Department of Defense retention efforts.

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TABLE OF CONTENTS

I.	INTRODUCTION.....	1
A.	MOTIVATION OF THE PROJECT.....	1
B.	RESEARCH QUESTIONS.....	3
C.	PURPOSE STATEMENT.....	3
D.	CONTRIBUTIONS.....	4
II.	OVERVIEW OF THE CURRENT COMPENSATION SYSTEM	5
A.	CASH	6
1.	Basic Pay	6
2.	Allowances	7
3.	Basic Allowance for Housing	7
4.	Special Pay and Bonuses	8
5.	Special Pay	8
6.	Bonuses.....	9
B.	IN-KIND BENEFITS (NON-CASH)	9
1.	Health Care.....	9
2.	Education	10
3.	Housing	10
C.	DEFERRED BENEFITS.....	10
D.	COMPENSATION AND BENEFITS HOLISTICALLY	11
E.	REGULAR MILITARY COMPENSATION (RMC)	12
1.	What Is RMC?	12
2.	Why Is RMC Important?	12
III.	PROBLEM IDENTIFICATIONS.....	15
A.	THE MYTH OF INADEQUATE COMPENSATION FOR MILITARY SERVICE MEMBERS	15
B.	PROBLEMS IDENTIFIED BY THE GAO	19
C.	INEFFICIENT MIX OF VARIOUS COMPENSATION/ BENEFIT TOOLS	21
D.	INSUFFICIENT COMMUNICATION OF THE COMPENSATION/BENEFITS SYSTEM.....	23
1.	Personal Statement of Military Compensation (PSMC)	23
2.	Inadequate Comparisons	25
3.	Career Development Boards.....	26
4.	Communication Efforts Are Inadequate and Inefficient	27
E.	CONTINUED RISING COSTS.....	27

IV.	HUMAN BEHAVIOR AND THEORY	31
A.	MAINSTREAM RATIONAL ECONOMICS.....	31
B.	BEHAVIORAL ECONOMICS	31
C.	PROSPECT THEORY	35
D.	ENDOWMENT EFFECT	38
E.	NUDGE THEORY	40
V.	FIX THE PROBLEM.....	45
A.	PRIVATE INDUSTRY RECOMMENDATIONS.....	45
1.	Society for Human Resource Management (SHRM)— State Employee Benefits in the Workplace.....	46
2.	How Four Employers Are Getting Benefits Communication Right	46
3.	SHRM—Employees Perplexed by Benefits Choices.....	48
4.	Conference Board Report: Corporate Communication Practices—Key Findings (2018 Edition).....	51
B.	PROPOSED SOLUTIONS	51
1.	Change the Mix—Getting the Biggest Bang for the Buck	51
2.	Better Communication of the Value of the System (Nudging)	53
VI.	CONCLUSION	61
	APPENDIX. PERSONAL STATEMENT OF MILITARY COMPENSATION	63
	LIST OF REFERENCES	67
	INITIAL DISTRIBUTION LIST	69

LIST OF FIGURES

Figure 1.	Components of Military Compensation for Active Duty Personnel, Fiscal Year 2000. Source: DoD (2012, p. 17).....	6
Figure 2.	RMC Calculation: Single E-4, No Dependents, Residing in Norfolk, VA. Source: DoD (2018b).	13
Figure 3.	Changes in Military and Civilian Compensation. Source: DoD (2012, p. 30).....	17
Figure 4.	Enlisted Regular Military Compensation vs. Civilian Earnings. Source: DoD (2012, p. 27).....	18
Figure 5.	Military-Civilian Compensation Comparison Provided during TAP Course. Source: Pequeno (2012).....	25
Figure 6.	Personnel Cost per Active Duty Service Member. Source: BPC (2016).....	28
Figure 7.	Enlisted Earnings Comparison: E-1. Adapted from Bureau of Labor Statistics (2018); BPC (2016).	29
Figure 8.	Prospect Theory: Depiction of Losses vs. Gains Relative to Value. Adapted from Barberis (2013).	36
Figure 9.	Allocation Mix of Salary/Wages and Benefits in Civilian Compensation. Source: GAO (2005, p. 24).....	52
Figure 10.	Original vs. Proposed Mix of Military Compensation Allocation.....	53
Figure 11.	Non-taxable Benefits and RMC Computation (Handout/Poster/Social Media Post)	56
Figure 12.	Policy Poster Recommendation	57
Figure 13.	Military-Civilian Compensation Comparison with RMC (Handout/Poster/Social Media Post).....	58

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LIST OF TABLES

Table 1.	Comparison of Weekly RMC and Civilian Earnings (BLS)	14
Table 2.	Frequency of Benefits Communication and Likelihood to Leave. Adapted from SHRM (2012).	50

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LIST OF ACRONYMS AND ABBREVIATIONS

BAH	Basic Allowance for Housing
BAS	Basic Allowance for Subsistence
BLS	Bureau of Labor and Statistics
BPS	Bipartisan Policy Center
CCC	Command Career Counselor
CDB	Career Development Board
DFAS	Defense Finance and Accounting Services
DoD	Department of Defense
DoN	Department of the Navy
GAO	Government Accountability Office
LES	Leave and Earnings Statement
MWR	Morale, Welfare, and Recreation
NLL	Navy Logistics Library
PSMC	Personal Statement of Military Compensation
QRMC	Quadrennial Review of Military Compensation
RMC	Regular Military Compensation
SAPR	Sexual Assault Prevention and Response

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I. INTRODUCTION

The Navy is concerned that service members making the decision to “stay in or get out” have no true understanding of how military compensation and benefits compare to those they may receive in employment elsewhere. Historical initiatives, such as the Navy Enlisted Retention and Career Development Programs, were created to improve a sailor’s ability to map out and accomplish career-oriented goals, while improving overall retention and a desire to remain on active duty. However, despite current internal efforts to improve retention, a culture of dissatisfaction and misinformation exists among junior service members who face decisions regarding their continuation of service. If the military fails to properly communicate the value of its pay and benefits, talented service members will continue to opt for other employment opportunities—and will likely make this decision without being adequately educated and informed. Over time, failure to properly relay the value of benefits will compound and ultimately result in a degraded operating force.

A. MOTIVATION OF THE PROJECT

Every individual serving in the U.S. military is a volunteer. The elimination of the draft in 1973 restructured general manpower and staffing requirements and indirectly impacted the overall importance and value of compensation and benefits. It is, therefore, extremely important for the military to adequately compensate its workforce in order to attract and retain qualified and competent personnel. Strides have been made since 1973 to make military compensation and benefits comparable to those in the civilian/private sector, and one could confidently argue that the majority of service members are appropriately compensated when compared to their civilian counterparts; however, service members often opt for employment opportunities in the civilian/private sector because they believe their compensation is less than adequate. Retention is an issue at the forefront of the highest levels of military leadership, and efforts are continuously made to keep the service’s best and brightest. Objectively (ignoring quality of life considerations), this poses the question: Why do service members assume “the grass is greener on the other side” when their current system of compensation and benefits is typically on par or better than those elsewhere?

The myth of inadequate compensation plagues the junior ranks. Unfortunately, this misguided assumption generates momentum because the Department of Defense (DoD) has historically utilized outdated compensation systems and methods to handle twenty-first century problems. A Government Accountability Office (GAO) report published in 2005 and the Eleventh Quadrennial Review of Military Compensation (QRMC; DoD, 2012) offer a stark counter to the myth of inadequate compensation and prove that military service members are actually well-paid—they simply do not know it. The complete value of military pay is shrouded by the complexities of multiple tangible and intangible factors that are not effectively communicated by the military services. The myth of inadequate compensation is duplicitous and lacks supporting data to warrant any actual consideration; however, the current structure of the military compensation system is so complex and varied that most service members truly believe that they are poorly compensated. For service members facing the decision to stay or go, it is absolutely critical to recognize the inherent value of their compensation and benefits package before departing for “greener pastures.”

Holistically, service members are adequately and fairly compensated. The culture of dissatisfaction that overshadows service member commitment decisions can be mitigated. Properly educating and informing junior service members is a sensible place to start. Junior service members typically do not realize that their benefits and compensation incentives are considerably larger than those of their civilian counterparts.

It is important to understand that problems exist and recognize that these problems are not being addressed by military leadership. This research intends to recognize that the status-quo mix of compensation (cash and non-cash) and benefits (current versus deferred) is likely to be suboptimal for the average service member—especially junior service members. Improvements in retention are more likely to occur if a shift in the mix and allocation of compensation and benefits are paired with the effective communication of their value in a method that service members can easily understand and appreciate.

B. RESEARCH QUESTIONS

The primary research question is as follows: *How can the military better design and more effectively communicate the value of its compensation and benefits to service members faced with the decision to extend or terminate service?*

The following are secondary questions for this research: Is the current mix of cash, in-kind (non-cash), and deferred benefits optimal? Does a comparative metric exist to compare military and civilian earnings? Are service members rational in evaluating various forms of compensation and benefits? What forms of communication and what mediums will be most effective for expressing value to service members? How are communication efforts structured? How often should communication efforts occur?

C. PURPOSE STATEMENT

The goal of this research is two-fold. First, this project intends to identify potential improvements to the current compensation system without further burdening taxpayers. In particular, we argue that the status-quo mix of cash, in-kind (non-cash), and deferred benefits is suboptimal; hence, significant efficiency can be achieved by shifting the mix toward areas that are more valued by junior service members. Secondly, this research intends to find ways to effectively educate and inform service members about the value of military pay, compensation, and incentives when they make “stay or leave” decisions. Specifically, the aim of this research is anchored around improvements in attracting and retaining service members by designing more effective compensation schemes and more appropriately conveying the value of such schemes. Junior service member retention is the overall objective, through which improvements should be expected.

The term “junior service member,” in the context of this paper, is defined as any service member serving under their initial service obligation/contract. Typical enlisted junior service members hold ranks from E-1 to E-5; typical junior officers hold ranks from O-1 to O-3.

D. CONTRIBUTIONS

Linking theory to policy and generating tangible courses of action will be the underlying contribution of this research. Additional contributions in the realm of awareness and mindfulness among senior military leadership is an expected byproduct of this project as well. The recognition of human behavior theories and behavioral economics will likely generate improvements in how compensation and benefits are shaped and communicated.

II. OVERVIEW OF THE CURRENT COMPENSATION SYSTEM

For most service members, military pay is a dependable and reliable source of income; however, the intricacies of what is taxable and non-taxable often preclude many service members from recognizing the true value of their compensation. What is the difference between “pay” and an “allowance?” What contributes to a service member’s gross income? Is the overall bottom line of a service member’s compensation better, worse, or on par with a civilian counterpart? Does a metric exist to compare military and civilian earnings? A brief explanation of the compensation and benefits package should provide more insight into the general value of a service member’s pay and the true benefits they receive. Additionally, an understanding of this system will allow for a better understanding of proposals and recommendations in later chapters of this research.

Compensation for military service members includes cash payments, along with a number of in-kind and deferred benefits (see Figure 1). The Eleventh QRMCM notes that

cash payments comprise approximately 51 percent of average military compensation; in-kind benefits 21 percent; and deferred compensation for retirees, veterans, and survivors another 28 percent. The percentage of military compensation made up of in-kind and deferred benefits is considerably higher than the noncash portion of civilian compensation. (DoD, 2012, p. 16).

The following sections explain cash, in-kind (non-cash), and deferred benefits.

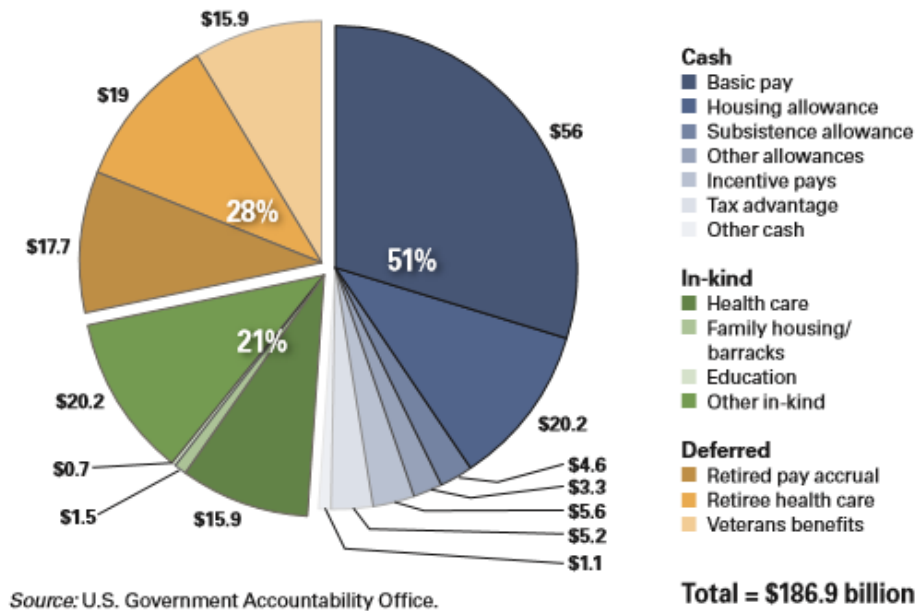


Figure 1. Components of Military Compensation for Active Duty Personnel, Fiscal Year 2000. Source: DoD (2012, p. 17).

A. CASH

Cash compensation makes up approximately 51% of total military compensation and comprises basic pay, allowances, and subsistence. Paired with tax advantages from allowances (which are not subject to federal income tax), the cash elements of compensation contribute to a comparison metric known as Regular Military Compensation (RMC), which is defined later in this chapter.

1. Basic Pay

Basic pay is the largest component of a service member's salary, corresponds directly to a service member's rank, and constitutes approximately half of overall cash compensation. Time in service is accounted for and directly contributes to increases in basic pay. Separate pay-tables exist for officers, warrant officers, and enlisted personnel; however, each member of a specific category is paid according to their respective pay-table. Basic pay contributes to overall gross income and is taxable.

2. Allowances

Allowances are pay allotments afforded to military service members for things such as food, housing, clothing, and travel. Service members receive allowances when the government is unable to provide for a specific need (i.e., military base housing cannot support all service members and their families). Most allowances are not taxed and greatly contribute to the quality of life for a service member. Allowances, because they are not taxable, are a unique way for service members to outpace/outperform civilian counterparts in the realm compensation. An analysis of some of these benefits should provide further insight into the value of this non-taxable income.

3. Basic Allowance for Housing

Service members who do not receive military-provided housing or rations are eligible for a Basic Allowance for Housing (BAH) and a Basic Allowance for Subsistence (BAS). Basic Allowance for Housing (BAH) is typically the largest non-taxable benefit that military service members receive. This allowance is given to service members based on their rank and the location of their duty station. BAH corresponds to the rental market in a particular area and is usually competitive with the market rate in that particular region. Service members with dependents receive a slightly larger monetary allotment than service members without dependents. Military members stationed overseas receive an Overseas Housing Allowance in place of BAH if housing is not provided for them by the military. The entire BAH rate is paid to the service member, regardless of the circumstances of their rent or mortgage cost. For instance, in Monterey, CA, the monthly BAH rate for a service member (O-4 rank) with dependents is \$3,975.00. This particular service member can use this housing allotment to pay monthly rent or contribute to monthly mortgage payments if they opt to buy a home. Regardless of whether or not the service member is renting or buying, the monthly allowance is received in full every month. If the service member is fortunate enough to find a property under the BAH rate—imagine they rent an apartment for \$2,000 per month—they can pocket the remaining money (\$1,975 for a service member with dependents) and use it as they wish. Essentially, this Monterey O-4 is receiving \$47,700 per year in non-taxable money through BAH alone. The additional \$1,975

(\$23,700 per year) is an advantage that most civilians do not receive. Circumstantially, the \$47,700 will likely keep the service member in a lower tax bracket than a civilian counterpart who takes home an equivalent salary. This tax advantage is estimated to make up 6% of RMC (DoD, 2012).

The same O-4 provides another example and gives some valuable insight into RMC (explained later in this chapter): Base pay for a single O-4 (no dependents; 10 years of service) is approximately \$84,632. Monterey annual BAH (\$40,068), BAS (\$3,052), and a \$12,162 tax advantage from BAH and BAS being non-taxable are added to this service member's base pay to yield an RMC value of \$139,915. Regardless of the additional boost from BAH, BAS, and the tax advantage, this service member will be taxed according to his base pay of \$84,632—putting the service member in the 22% tax bracket (2018–2019 Tax Brackets). This O-4's civilian counterpart taking home a similar yearly paycheck would be taxed at \$139,915 and fall into the higher 24% tax bracket. Over time, the tax-bracket difference will become significant. More importantly, however, junior service members will likely experience similar benefits, but at lower tax-brackets—most notably, the 12% and 22% brackets (a substantial difference of 10%).

4. Special Pay and Bonuses

Special pay and bonuses are noteworthy forms of payment because they are the only types of compensation that differ from pay due to rank and years of service. Typically, these incentives are utilized to influence recruitment and impact retention in specialized career fields that have comparable and competitive opportunities in the civilian sector. Despite the allure and appeal of these forms of compensation, they constitute a very small portion of total pay at around 4% historically (DoD, 2002, p. 77).

5. Special Pay

Special pay, a taxable allotment, is given to service members for operating in hazardous conditions, areas of high combat risk, or atypically rigorous duty cycles. Additionally, some special pay is afforded to service members to encourage entrance and retention in particular communities or fields of service. Aviators, for example, receive “Flight Pay” in addition to their Basic Pay allotment. Special pay is a flexible tool the

military uses to deal with unforeseen issues that may arise in response to changes in policy, inflation, or economic circumstances.

6. Bonuses

Bonuses are often offered to service members for reenlistments, department head tours, command tours, etc. These are typically evenly distributed over a number of years, rather than in the form of a lump sum. For instance, a previous Aviation Department Head Bonus was \$75,000, and paid in \$15,000 increments over a period of five years. Bonuses are considered pay, contribute to gross income, and are entirely taxable.

B. IN-KIND BENEFITS (NON-CASH)

In-kind benefits are a form of non-cash compensation provided to service members in addition to the aforementioned cash payments. These in-kind benefits exist in the form of health care, education assistance, and housing, and they make up 21% of the overall compensation budget (see Figure 1) (DoD, 2012, pp.19-20). Other non-cash benefits include annual leave and installation-based services such as commissaries, base exchanges, package stores, fitness facilities, golf-courses, and several other on-base amenities (DoD, 2012, pp. 19–20).

1. Health Care

All service members and their dependents are afforded all-inclusive health care services provided through military treatment facilities and a number of civilian providers. TRICARE is the health care system provided to active duty service members and their dependents at no charge; however, some out-of-pocket expenses can be expected for dependents who elect non-traditional TRICARE packages. Several health care options, with minimum expenses, are afforded to Selected Reserve members, retirees, and eligible dependents (DoD, 2012, p. 19). The Eleventh QPMC provides a concrete example about the value of the military health care system when compared to that of a civilian counterpart:

The average enlisted-equivalent civilian worker pays between \$3,000 and \$7,000 per year for out-of-pocket health expenses, depending on family size. ... Most military personnel, in contrast, do not incur out-of-pocket expenses for health care, so these avoided costs represent a measurable

difference between the military and civilian health benefit, and a “benefit” to service members. Put another way, the military health benefit boosts service members’ discretionary income compared to that of their civilian counterparts, who have less discretionary income after paying their out-of-pocket health care costs. Moreover, because civilian workers’ out-of-pocket health care costs have grown by 60–75 percent (in real terms) over the last decade, the value of the health benefit to military personnel—in terms of avoided costs—has increased substantially. To the extent that out-of-pocket health care costs continue to rise faster than wages, civilian workers will continue to see their discretionary income reduced because of growing health care expenses. (DoD, 2012, pp. 23–24)

The health care component is one aspect of a non-cash benefit that expands the value of the military’s compensation system. It drastically changes the difference in discretionary income when comparing service members to their civilian counterparts.

2. Education

Service members are afforded several educational options in the form of federal tuition assistance, individual service college funds, the Montgomery GI Bill, the post-9/11 GI Bill, and a number of loan repayment programs. Service members (and in some instances eligible dependents) have access to many of these educational benefits prior to, during, and after service obligations.

3. Housing

A large contingent (approximately one-third) of service members reside in military housing (DoD, 2012, p. 20). Military housing varies significantly based on a number of factors, but it is essentially government living quarters in which all expenses are covered. Barracks, ship berthings, apartments, and individual housing units are a few of the options afforded to service members. Rank and seniority typically factor into the housing circumstances for most service members.

C. DEFERRED BENEFITS

Deferred benefits are the final component of the military compensation system and comprise 28% of overall compensation (see Figure 1). Deferred benefits exist in the form of retirement pay accrual, health benefits, and veteran benefits.

Retirement Pay

Retirement pay is an incentive that drives retention for most service members; however, only about 19% of active duty service members will retire after a full 20 years of service. The other 81% terminate service at some point during their career (DoD, 2012, p. 20). Twenty years of service are required in order to receive 100% of the inflation-adjusted annuity. The annuity increases by 2.5 percentage points for every additional year of service beyond 20 years and stops at 30 years (DoD, 2002, p. 97). Retirement options and plans vary based on when an individual joined the military and recently shifted to the Blended Retirement System, which closely mirrors retirement plans offered in the civilian sector.

The Eleventh QRMC offers an interesting comparison of military and civilian retirement options:

Military retirement provides a generous annuity to personnel who remain in service for at least 20 years. Moreover, because the benefit is available to personnel immediately upon retirement, military retirees can begin receiving annuity payments when still in their late thirties or early forties. In the civilian sector, in contrast, employees typically have to work for longer periods and until an older age before they begin receiving full retirement benefits. (DoD, 2012, p. 24)

D. COMPENSATION AND BENEFITS HOLISTICALLY

The compensation and benefits package afforded to military service members is robust and circumstantially varies based on a number of factors. Ultimately, two important efforts should be made. First, a constant push to educate service members about the value of their paycheck must occur regularly in order to allow military service members to make informed and educated decisions regarding the termination or extension of service. Second, force managers must recognize that they have the flexibility to tweak packages and make adjustments that will ultimately affect recruitment and retention efforts in the future.

E. REGULAR MILITARY COMPENSATION (RMC)

1. What Is RMC?

Regular Military Compensation (RMC) is the primary metric the DoD uses to aid in recruiting and retention. A competitive labor market has forced the DoD to recognize that it must adequately compensate service members in order to recruit, retain, and shape its workforce. The Ninth QRMC states that “RMC includes basic pay, basic allowance for housing, and basic allowance for subsistence, plus an additional amount to account for the fact that allowances for housing and subsistence are not subject to federal income tax” (DoD, 2002, p. xxii). Essentially, *RMC is the approximate amount of an equivalent civilian salary*. It reflects the gross pay received by service members and provides a recognizable measure when making comparisons between civilian and military wages.

$$\text{RMC} = \text{Base Pay} + \text{BAH} + \text{BAS} + \text{Tax Advantage of BAH and BAS}$$

2. Why Is RMC Important?

Among the general population, deficiencies and a wide-ranging lack of awareness exist when attempting to compare civilian and military compensation. Historically, service member basic pay was compared to the wage of a comparable civilian counterpart; however, individuals making these comparisons were quick to recognize that basic pay only accounted for a small portion of a service member’s total cash compensation. Over time, the RMC metric was developed and has become universally recognized as the premier comparison assessment metric for military and civilian cash compensation. The Eleventh QRMC states, “RMC has been the standard measure for comparing military and civilian pay for more than four decades” (DoD, 2012, p. 23). RMC is important because it allows force shapers to improve awareness and recognition when making considerations about how to effectively adjust manpower considerations and restructure the allocation mix of military compensation. Individuals must also be aware that RMC is only one segment of overall military compensation; in-kind (non-cash) and deferred benefits provide additional value and increase the total worth of military compensation.

The RMC of a single E-4 (no dependents) with four years of service, residing in Norfolk, VA, is depicted in Figure 2. Base Pay (\$29,887) + BAH (\$15,408) + BAS (\$4,432), + Tax Advantage (\$2,705) = \$52,433. RMC for this particular service member equates to \$52,433 per year, \$4,369 per month, and \$1,092 per week.

Grade	E-4
Years of Service	4
Tax Filing Status	Single
Living OCONUS or Not Receiving BAH?	false
Living OCONUS?	N/A
ZIP Code of your Permanent Duty Station	23510
Annual Basic Pay	\$29,887.20
Annual Basic Allowance for Housing	\$15,408.00
Annual Basic Allowance for Subsistence	\$4,432.68
Non-Taxable Allowances (BAH + BAS)	\$19,840.68
Number of Exemptions for Previous Calendar Year	1
Personal Exemption Amount	\$0.00
Standard Deduction	\$12,000.00
Total Deductions	\$12,000.00
Taxable Income (Annual Basic Pay - Total Deductions)	\$17,887.20
Tax Rate	12%
Gross Up	\$22,546.23
Tax Advantage	\$2,705.55

Total Regular Military Compensation (RMC): \$52,433.43

Figure 2. RMC Calculation: Single E-4, No Dependents, Residing in Norfolk, VA. Source: DoD (2018b).

A comparison of RMC and the salary of a civilian equivalent provides some additional insight into the competitiveness of military pay. The Bureau of Labor and Statistics (BLS) estimates the median weekly earnings for individuals (civilians) with “some college, no degree” to be \$774 and the median weekly earnings for individuals with a bachelor’s degree to be \$1,173 (BLS, 2018). A single O-3 (no dependents) with four years of service, residing in Norfolk, VA, has an RMC of \$94,939 per year, \$7,911 per month, and \$1,978 per week. Table 1 provides a comparison of RMC and median weekly earnings of the aforementioned E-4, O-3, and their civilian counterparts.

Table 1. Comparison of Weekly RMC and Civilian Earnings (BLS)

<u>Rank / Education</u>	<u>Weekly Earnings</u>
Civilian with “Some College, No Degree”	\$774
Military E-4	\$1092
Civilian with Bachelor’s Degree	\$1173
Military O-3	\$1977

Despite its importance as a comparative economic measure, RMC is relatively unknown by the majority of military service members. A considerable effort must be undertaken to educate and inform all service-members about RMC and how it can provide them a wealth of information about how their compensation and benefits compare to their civilian counterparts. *They must be aware that a metric exists to approximate how much they are making (or will need to make) in the civilian sector.* This knowledge will be absolutely critical for those making the decision to extend or terminate service.

III. PROBLEM IDENTIFICATIONS

A. THE MYTH OF INADEQUATE COMPENSATION FOR MILITARY SERVICE MEMBERS

A myth exists within the DoD, especially among the junior ranks, that *military service members are not compensated as well as their civilian counterparts*. This assumption is misguided and is one of the major reasons that service members depart for civilian employment opportunities after the termination of their initial service obligation. Year after year, retention numbers are significantly impacted because service members do not recognize the value of their paycheck. Why does this problem continue to occur?

The misguided assumption of inadequate compensation is prevalent for two primary reasons. First, the compensation system utilized by the DoD dates back to the post-World War II era and has not changed significantly since that period. Nearly two-thirds of all compensation can be traced to a single set of pay/allowance tables that are responsible for all services and jobs within those particular services. This particular constraint places limits on how the military can adjust compensation for a wide array of jobs across a number of different branches and communities (DoD, 2002, p. xxi). Inflexible pay scales make it difficult for the military to compete with civilian sectors that can often pay more for highly-skilled laborers and professionals (Williams, 2004, p. 2). Second, and most importantly, the system is shrouded by the complexities of multiple variables and intangible factors that are not effectively communicated by the military and its leadership. Basic pay, housing allowances, subsistence allowances, health-care benefits, installation services, retirement options, tax advantages, and several other factors make it difficult for service members to truly appreciate the value of their paycheck. These two reasons explain why the myth of inadequate compensation continues to circulate throughout the ranks.

The Eleventh QRMC provides a stark contrast to the myth of inadequate compensation:

Military compensation has outpaced civilian wages and salary growth since 2002. Military pay began to increase in 2000, owing to a pay adjustment that responded to recruiting and retention difficulties, and was intended to

bring military compensation back in line with civilian pay. The pay adjustment was accompanied by a commitment to increase basic pay in step with the Employment Cost Index (a benchmark for civilian pay growth) plus one-half of one percentage point from 2002 through 2006—a policy that was ultimately extended through 2010. The increase in military compensation also reflects rapid growth in the housing allowance, which increased by 5.7 percent in 2007, 4.7 percent in 2008, and 5.0 percent in 2009.

In contrast, there has been no real growth in civilian wages and salaries over much of the past decade—in part, reflecting a recessionary economy. At the same time, the cost of benefits in the civilian sector grew until about 2004, and then began to fall, only to increase again starting in 2010—fueled largely by growth in the cost of health care. (DoD, 2012, p. xvi)

These wage comparisons are encouraging and are the result of considerable efforts by Congress and senior military leadership to increase RMC and make military wages more competitive with civilian pay. Although negative wage gaps (unfavorable for military service members) existed between military and civilian pay in the 1980s and 1990s, Figure 3 provides evidence that RMC has outperformed the civilian sector in wages and salary growth since 2002.

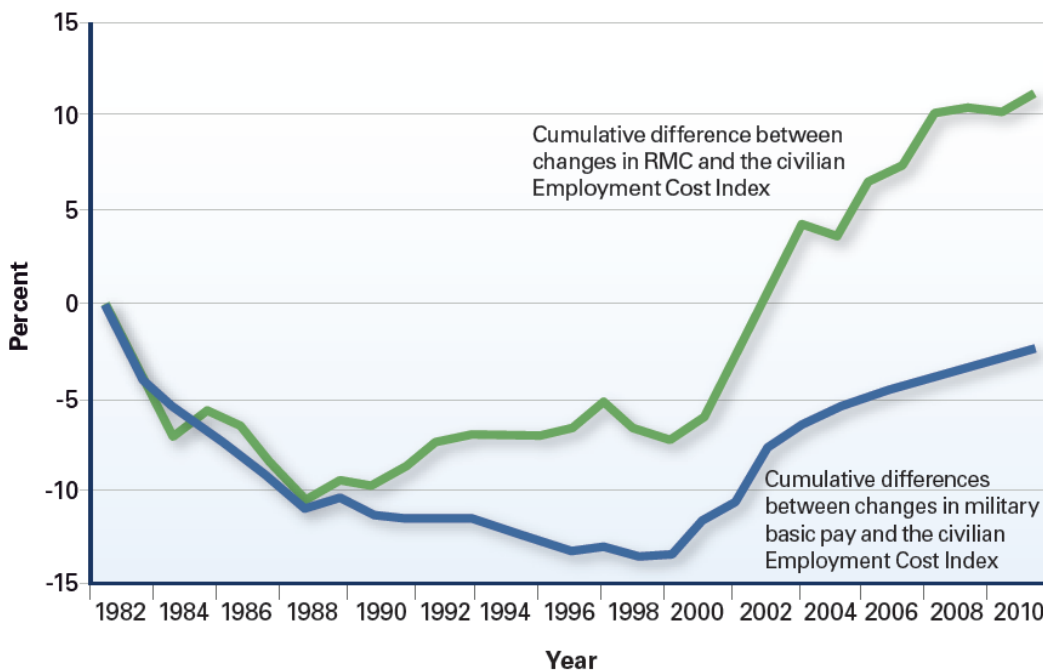


Figure 3. Changes in Military and Civilian Compensation. Source: DoD (2012, p. 30).

Adjusted for inflation, RMC for enlisted service members increased by more than 20% (approximately \$42,000 to \$51,000) from 2001 to 2009, while civilian counterparts experienced little to no wage growth during the same period (DoD, 2012, p. 30). This was ultimately the result of policy changes in Congress that generated increases in Basic Pay and Basic Allowance for Housing.

A 2005 GAO report substantiates the overall increase in military compensation during the early 2000s. The report states, “Adjusted for inflation, total cost of compensation increased from about \$123 billion in fiscal year 2000 to \$158 billion in fiscal year 2004” (p. 5). Compensation growth was the direct result of increases in RMC variables, such as base pay, which jumped “from \$38.4 to \$47 billion, about 23 percent; allowances for private housing (from \$7.3 to \$12 billion, more than 66 percent); and healthcare benefits for current service members, retirees, and dependents (from \$13.8 to \$23.3 billion, about 69 percent)” (GAO, 2005, p. 5). The report estimated that the DoD may spend \$52 billion on health care annually by 2020, a claim that was supported by a 2012 Congressional

Budget Office (CBO) report that stated the DoD requested approximately \$40 billion for health care benefits in 2013 (CBO, 2012). It is apparent that strides have been made; however, junior service members continue to assume that they trail the civilian sector and private industry.

Figure 4 provides a comparison of military and civilian earnings and provides additional evidence about the value and strength of military compensation. The Eleventh QRMC notes that during a 20-year career, RMC for enlisted service members is higher than comparable civilian salaries every year throughout the duration of the career (DoD, 2012, p. 27). This particular analysis considers civilians with AA degrees, some college, and those with high school diplomas and notes that military compensation is considerably higher—in some areas by greater than 50% (DoD, 2012, p. 27).

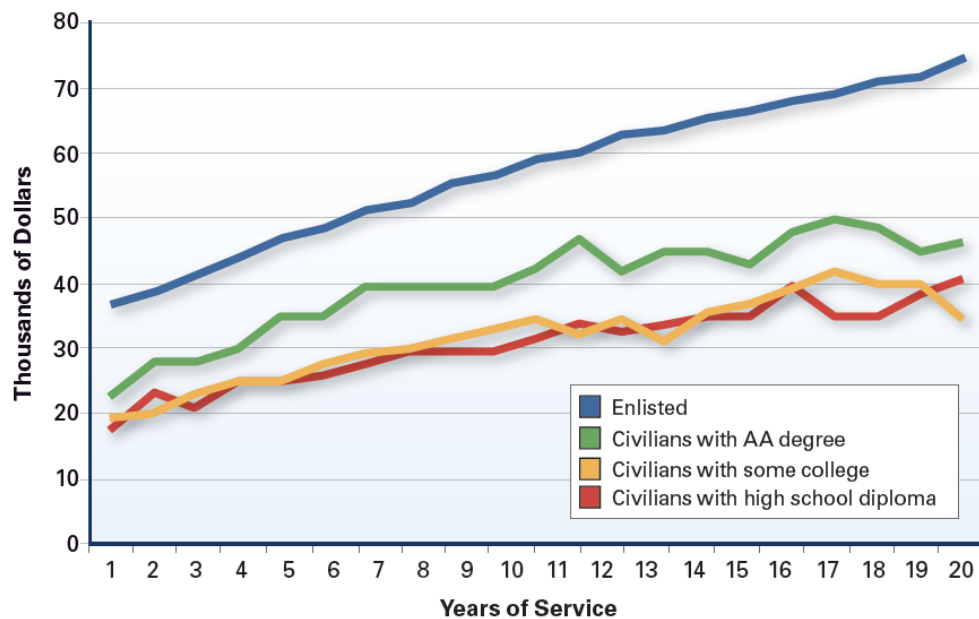


Figure 4. Enlisted Regular Military Compensation vs. Civilian Earnings.
Source: DoD (2012, p. 27).

Data exists to prove that the myth of inadequate compensation for military service members is misguided and unsubstantiated, while ignorance perpetuates a culture of negativity among the junior ranks. Military compensation corresponds “to the 90th

percentile of civilian wages for enlisted personnel and the 83rd percentile for officers” (DoD, 2012, p. 31). The average service member needs to be aware that their pay is competitive and extremely valuable. RMC is a critical metric that must be relayed to service members early in their career if they are truly expected to understand what they are surrendering if they opt to pursue employment elsewhere. More importantly, military leadership needs to recognize that status-quo communication efforts regarding compensation and benefits are unsatisfactory. Changes need to be made, specifically in the realm of how the military communicates the value of its extremely competitive compensation and benefits system.

B. PROBLEMS IDENTIFIED BY THE GAO

A 2005 GAO report entitled *Military Personnel: DOD Needs to Improve the Transparency and Reassess the Reasonableness, Appropriateness, Affordability, and Sustainability of Its Military Compensation System* assessed the military compensation system and reviewed how active duty service members perceived their compensation. The report makes note of problems in the percentage allocation of cash, in-kind (non-cash), and deferred benefits; problems in the DoD’s efforts to communicate the value of military compensation; and problems related to how service members perceive the value of their total compensation. Other than a 2010 GAO testimony on compensation, no follow-up reports have been published and no significant campaigns have been undertaken to suggest that the military has tried to remedy the for-action items determined by the report.

Of particular importance, this report determined several inefficiencies within the military related to communicating the value of compensation and benefits to its members. The report stated the “DoD’s lack of an effective communication effort on compensation has allowed service members’ misperceptions and concerns about their compensation to perpetuate” (GAO, 2005, p. 27). An immeasurable amount of money and time has been placed in training service members, and it is important to recognize that a majority of that will be lost to competitors in private industry if efforts are not undertaken to retain service members on the margin. According to the report, retention can be improved by

“systematically educating service members about the value of their total compensation” (GAO, 2005, Highlights).

The report recognizes the intricacies of the military compensation system and how they have contributed to the culture of dissatisfaction that exists among junior service members. Nearly 80% of service members participating in GAO-sponsored focus groups believed that they were paid less than their civilian equivalents (GAO, 2005, p. 33). Participants claimed that they were unhappy with military compensation because they assumed their civilian counterparts were taking home considerably more money. This is likely the result of a key takeaway from the report, which states,

The piecemeal approach to military compensation has resulted in a lack of transparency that creates two interrelated problems for decision makers. Specifically, this approach creates an inability to (1) identify the government’s total costs to provide compensation investments to active duty service members and (2) assess how compensation investments are allocated to cash, benefits, and deferred compensation. (GAO, 2005, p. 4)

GAO auditors determined that the military compensation system was so complex that decision-makers could not take action or make informed decisions relative to costs and the inherent structure of the system. Clearly, if leaders and decision-makers find the system complicated, what chance do junior service members have to truly understand the value of their earnings without any guidance?

The GAO notes that identifying long-term trends and determining the optimal mix of available resources is a challenge that the DoD will continue to face. Despite this challenge, the DOD has the ability to improve service member awareness about the value of their pay and potentially change their overall perception of it. Problem identification is important, and this GAO report recognized three key faults that require improvement. Specifically, service members (1) underestimated their compensation and how it compared to civilian earnings; (2) were confused or ignorant about the mix of their cash, in-kind, and deferred benefits; and (3) were concerned about how benefits would erode over time (GAO, 2005, p. 27). Improving these three areas and communicating the value of military pay will likely ensure a better return on the personnel investment that the DoD relies on for success.

Through a number of DoD surveys, focus groups, and survey data, the GAO determined that the DoD does very little to educate service members about how valuable their compensation package is. The GAO declared that no data exists to determine what the DoD spends annually in order to educate service members on compensation. Regarding educational efforts related to compensation, the GAO (2005) report notes, “DoD officials told us that **it has not been a priority department wide and DoD has never mounted a comprehensive campaign to explain the competitiveness of its compensation to service members**” (GAO, 2005, p. 29; emphasis added). Military leadership and decision-makers must recognize that recruitment and retention can be significantly impacted if the DoD opts to implement a strategy aimed at informing and educating service members about the value of their pay. Force shapers must capitalize on this extremely valuable, yet underutilized, asset.

C. INEFFICIENT MIX OF VARIOUS COMPENSATION/BENEFIT TOOLS

As previously mentioned, the Eleventh QRMC notes that the allocation of compensation for military service members (shown in Figure 1) includes a mix of cash (51%), in-kind (non-cash; 21%), and deferred benefits (28%). Military leadership argues that this allocation is flexible and affords force shapers the flexibility to adapt and make changes according to personnel needs; however, this research posits that the current allocation mix is not optimal for retention efforts aimed at junior service members.

Non-cash and deferred benefits make up 49% of total compensation. The promise of future compensation, in the form of deferred benefits (i.e., retirement pay, health care), is typically available for service members who retire with 20 years of service or those individuals eligible for veteran’s benefits. This provides very little benefit to current service members or those who have retired without having served 20 years. The majority of junior service members have trouble looking beyond their initial service contract—let alone 20 years ahead toward retirement; therefore, the allure of deferred benefits holds little merit. The GAO recognizes that cash pay can be considered a much more efficient tool for recruitment and retention because young adults tend to prefer being paid today, rather than in the future. The report provides an interesting example:

A recent study offering service members a choice of lump-sum payments or annuities found that a vast majority of service members preferred a lump-sum cash payment versus deferred compensation in the form of an annuity. According to the study, more than 50 percent of officers and 90 percent of enlisted service members had discount rates of at least 18 percent; that is, they value \$1 received in 20 years to be worth only about 4 cents today. (GAO, 2005, pp. 24–25)

Junior service members overvalue current benefits and undervalue future ones. The allure of payment today is significantly greater than future annuities, even if overall compensation in the long run turns out to be greater.

In her book *Filling the Ranks*, Dr. Cindy Williams argues that allocating Congressional funding for retirees (a deferred benefit) is a waste. Referencing a health care entitlement Congress approved in 2000 for military retirees over 65, Williams (2004) notes,

For the same money, Congress could have granted an extra pay raise of nearly 7 percent; that would have brought the pay raise for every individual in uniform into the double digits for the first time since the early 1980s. Instead, it will help only a small segment of today's force: just 9 percent of today's new Marine Corps recruits and 26 percent of new Air Force enlistees are likely to service the twenty years necessary to become eligible for it. Under current policies, even the recruits who stay that long will not see anything from the new benefit until some 46 years after they enlist. Moreover, while the new entitlement will eventually benefit the nation's 1.7 million military retirees, it will do nothing for the 23 million veterans who served in uniform for fewer than twenty years. Thus, to the extent that motivating individuals serving today and rewarding veterans for their service is the goal, the new entitlement is money wasted. (p. 304)

A GAO study from 2005 notes that the mix of cash and benefits offered to military members is misunderstood by greater than two-thirds of individuals surveyed—notably, junior service members. Moreover,

About 80 percent of the 400 service members that GAO surveyed believed they would earn more as civilians. ... By not systematically educating service members about the value of their total compensation, DoD is essentially allowing a culture of dissatisfaction and misunderstanding to perpetuate. (GAO, 2005, Highlights)

A realignment of cash, in-kind, and deferred benefits needs to be considered if the military hopes to retain junior personnel. While this research does not propose a mix that

aligns with the civilian sector, it does propose an adjustment of the current allocation of cash, in-kind, and deferred benefits that will entice the current active duty contingent and improve retention among those facing the decision to “stay or go.”

D. INSUFFICIENT COMMUNICATION OF THE COMPENSATION/BENEFITS SYSTEM

Communication efforts currently exist but are infrequent and less than optimal. Leave and Earnings Statements (LES) are difficult for junior service members to understand because the statement does not succinctly identify the overall value of compensation and benefits. The “myPay” website is available to all service members, but it is often difficult to access and does not offer much in the realm of education or value associated with compensation. Aside from information on the Blended Retirement System and a few calculators, the official Military Compensation website (militarypay.defense.gov) does not offer much in the form of educational tools. The site does contain some information about how military pay is comprised, but the interface is awkward and difficult to navigate. Newsletters from the Defense Finance and Accounting Service are allegedly in circulation; however, many service members claim to have never seen them. Navy Personnel Command sends community detailers out to engage the Fleet, but visits are infrequent and tailored to cover general information for large groups. As previously mentioned, no data exists to show what the DoD spends to inform service members about the value of compensation, and the DoD has never mounted a campaign to laud the value of military compensation to service members (GAO, 2005, p. 29). Military leadership and decision-makers can do a better job communicating compensation value to service members.

1. Personal Statement of Military Compensation (PSMC)

The DoD has made an effort to communicate the inherent value of total compensation through a document known as the Personal Statement of Military Compensation (PSMC). The PSMC was created in the late 1980s and had significant inertia and oversight during the 1990s. Implementation and incorporation of this document as an informative tool lost momentum in the early 2000s when military compensation tools

became readily available online. Since then, general awareness and oversight of this document has been sparse at best.

The PSMC offers service members extremely valuable information, as evident in the opening paragraph of the document:

This statement is intended to outline the total value of your military pay, allowances and benefits. By making your compensation more “visible,” this statement could be useful when applying for credit or loans (including home loans) from businesses or lending institutions. Another possible use of this summary is to help determine whether specific civilian employment offers would let you maintain the same standard of living you had while serving in the military. Start with the Total Direct Compensation on page 1, add the Federal Tax advantage from page 2, and then add any additional expense a civilian employer would expect you to pay for health and life insurance, retirement contributions, etc. This will tell you approximately what level of civilian salary you must earn in order to maintain a similar standard of living as that provided by your military take home pay. Each section of this statement contains an explanation. However, if you have any questions, please contact your local financial services office (FSO). (From Personal Statement of Military Compensation; see the appendix)

Despite the noble intent, *this document is extremely difficult to access, and the location through which it can be accessed differs between services*. According to the Defense Finance and Accounting Service (DFAS), PSMC is available in myPay for the Air Force and Army; for the Marine Corps, it is available through Marine Online; and for the Navy, it is available through BUPERS Online (Defense Finance and Accounting Service [DFAS], 2014). This research can confidently report that PSMC is not available for Navy service members via BUPERS Online, myPay, or any other DoD-related medium.

Efforts to communicate what the PSMC is, how to utilize it, and where it can be found are unsatisfactory. Information this valuable should be universally available and easily accessible; however, it is not. More importantly, efforts are not being made to educate junior service members about the document or its components. The depth and complexity of a PSMC can appear daunting for even the most financially savvy service member; therefore, educational efforts should be executed in a piecemeal fashion with repetition in order to appropriately inform the masses.

2. Inadequate Comparisons

Figure 5 is provided to service members during the Transition Assistance Program, a course designed to aid in a service member's transition to civilian life. It is also provided during community detailing briefs conducted by Navy Personnel Command. Although informative, the comparative figure does not provide much aid other than a simple recognition that military and civilian pay have similarities and differences. Without context, it is easy to overlook the advantages of the military compensation system. Why is RMC not mentioned? Were the tax advantages of BAH and BAS addressed? What about out-of-pocket health care expenses and their comparative differences? Educational perks, installation services, and deferred payment advantages are also overlooked because of their hidden nature.

What will you need to make?	
E5 with 6 years of service	Civilian
Base Pay - \$2,662 (31,944 year)	■ Base Pay -\$4833 (58,000 year)
BAH dep - \$948	■ Taxes - \$(474) (M,0)
BAS -\$ 348	■ SS tax -\$ (293)
Taxes -\$ (205) (M,0)	■ Medicare -\$ (69)
SS tax -\$ (112)	■ Medical - \$(550)
Medicare -\$ (39)	■ Life ins -\$ (40)
Medical -\$ (32)	■ 401K (5%) -\$ (242)
Life ins -\$ (27)	
TSP (5%) -\$ (133)	■ Total monthly Pay = \$ 3,165
Total Monthly Pay =\$3,410	

Figure 5. Military-Civilian Compensation Comparison Provided during TAP Course. Source: Pequeno (2012).

3. Career Development Boards

Career Development Boards (CDBs) are utilized by the Navy to inform personnel about issues that affect their growth, development, and future in the service. Commands are required to have a Command Career Counselor (CCC) responsible for the scheduling and execution of a service member's CDB, which should coincide with approaching career milestones. CDBs are critical opportunities for naval leadership to engage sailors on a litany of subjects such as personal backgrounds, goals, warfare qualifications, timelines, rotation dates, educational benefits, tuition assistance, collateral duties, physical readiness, and more.

CDBs present an excellent opportunity to actively communicate with sailors face-to-face, in one-to-one scenarios; however, some CDBs may not be approached with the seriousness and due diligence they deserve. When CDBs are taken lightly and not given the sincerity they deserve, sailors suffer and retention is most likely impacted. The chief of naval operations, in a NAVADMIN (095/18) released on April 14, 2018 stated, "We must ... retain more of our trained and experienced personnel to meet our manning requirements. We have to start that effort today" (Department of the Navy [DoN], 2018, p. 1). CDBs must be regarded as critical mediums through which value can be explained and accurately relayed. Individuals can be engaged intimately, and with sincerity, through this premier setting.

CDBs are conducted regularly, which affords opportunities for information to be introduced, explained, and eventually re-examined. CDBs occur when members report to their duty station and after 24, 48, and 60 months. They are also performed 15 months prior to a service member's projected rotation date (PRD). With only one required CCC aboard any command, CCCs can easily become overwhelmed and overburdened with their counseling responsibilities. Large commands, a laundry list of topics, and limited time presents challenges to the effectiveness and efficiency of communicative efforts. Opportunities exist, but opportunities are also missed.

4. Communication Efforts Are Inadequate and Inefficient

Multiple resources are available for service members to improve their aptitude regarding compensation systems. Websites, financial calculators, budget spreadsheets, and other tools exist to increase competence, but these valuable resources are not getting to the service member (GAO, 2005). Information is readily available in the modern era; however, ease of access does not necessarily translate into service members taking the initiative to educate themselves. Rational economics assumes that, as long as information is available, people will pursue it in order to optimize their overall utility. Unfortunately, this assumption is misguided, because the general population is irrational and unwilling to take the steps necessary to improve their situation to the maximum extent possible. Junior service members need to be pointed in the right direction if they are expected to make informed decisions in order to maximize their quality of life. This is why it is absolutely critical for the military to improve the way it communicates value related to compensation and benefits.

E. CONTINUED RISING COSTS

Over time, Congress has extended additional benefits to service members that have become costly, not well-received, and most importantly, not well-understood. Constituency allegiance has made it nearly impossible for members of Congress to vote against benefit packages for military service members or repeal any prior approvals (GAO, 2005). Essentially, any benefit added, regardless of its importance, applicability, or value, will be impossible to reverse. Ultimately, the result of this inability to redact policy has been a significant and permanent increase to DoD costs.

This research recognizes that the continued rising costs associated with military personnel compensation could pose potential problems in the future. Current fiduciary obligations are unsustainable and must eventually be addressed; however, in order for the DoD to attract talented individuals, service members must receive a salary at least commensurate with that of their civilian counterparts, especially in a modern service that does not rely on conscription. Military personnel costs are rising in a rapid fashion, which will continue to burden an already stressed DoD budget, but for now, leadership must stress

that military compensation has consistently outpaced the civilian sector since the turn of the century.

When military recruiting and retention struggled in the 1990s (Bipartisan Policy Center [BPC], 2016), Congress acted by increasing compensation. One byproduct of increased compensation was a reduction in overall personnel numbers (BPC, 2016). This reduction in manpower lead to an increased operational-tempo for all remaining service members, which resulted in increased stress levels throughout the military. Inevitably, this drawdown led to deficiencies in recruiting and retention (BPC, 2016). It is, therefore, more important than ever for military leadership to express the value of military compensation to junior service members facing the decision to extend or terminate service. Keeping service members is financially more palatable than recruiting, training, and investing in new members.

According to the BPC (2016), “Between FY2001 and FY2016, DOD’s average cost per active duty service member increased by 53 percent in inflation-adjusted dollars—from \$74,890 to \$114,614” (p. 12). Over the same period, civilian compensation experienced little to no growth (DoD, 2012, p. 31). The cost may have “negatively” affected DoD budget considerations, but it was a major benefit to service members, positively affecting their pay and benefits. This can be seen in Figure 6.

	FY2001	FY2016	Percent Change (2001 to 2016)	FY2017
Active-Duty End-Strength <i>(Not including Reservists or National Guard)</i>	1,386,000	1,311,000	-5%	1,301,000
Pay-Like Compensation	\$50,670	\$73,038	44%	\$74,001
Basic Pay	\$33,326	\$40,450	21%	\$41,299
Retirement Costs	\$12,560	\$16,635	32%	\$15,906
Normal Pension Costs	\$12,560	\$12,699	1%	\$12,102
TRICARE For Life	\$0	\$3,93 ^s		\$3,804
Defense Health Program	\$11,661	\$24,940	114%	\$25,979
Total Personnel Costs	\$74,890	\$114,614	53%	\$115,886

Figure 6. Personnel Cost per Active Duty Service Member. Source: BPC (2016).

Figure 7 provides a comparison of the compensation mix of cash and non-cash benefits. This particular comparison of an E-1 in the military compared to their civilian counterpart is insightful and shows that military pay consists of several variables. Many of these are often overlooked.

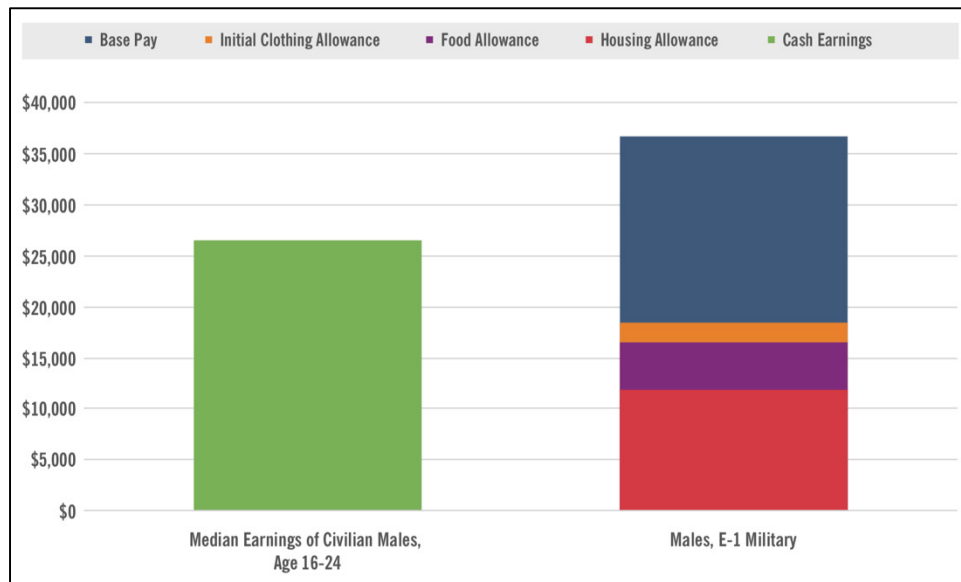


Figure 7. Enlisted Earnings Comparison: E-1. Adapted from Bureau of Labor Statistics (2018); BPC (2016).

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IV. HUMAN BEHAVIOR AND THEORY

Economic literature and theory may explain the difficulty in retaining qualified individuals in the military or the private sector. Behavioral economic theory may be the best theory when trying to understand why some individuals may not look at the economic facts before deciding to leave the armed forces for what they think is “greener grass,” even though it may not be. Additionally, behavioral economic theory also may provide very useful policy guidance.

A. MAINSTREAM RATIONAL ECONOMICS

Decision-making process are handled differently from person to person, but within the framework of rational economics, all individuals (civilians and military personnel alike) should be doing things relative to the same basic decision-making metrics. Rational economics assumes that individuals will choose to maximize utility subject to constraints and options available. Individuals, in theory, should make choices to optimize utility and achieve goals; therefore, rational economics posits that service members would favor the decision that would maximize overall compensation and quality of life considerations when making the decision to “stay or go.”

Behavioral economics, a contrary theory to rational economics, assumes that humans are not always, or rarely, rational. Humans are more likely to err and make decisions in haste, with less than optimal information. The ideas and theories in behavioral economics explain why individuals make misinformed decisions and choices. Theories associated with behavioral economics can help leaders understand how to anticipate the actions of junior service members throughout a number of certain situations.

B. BEHAVIORAL ECONOMICS

Behavioral economics is a theory that incorporates other disciplines like psychological and social influences into models of economic behavior (Baddeley, 2017). This, of course, deviates from mainstream economics, which bases its conclusions on the rational choice of an individual. The rational choice model is theoretically elegant, yet

practically flawed, because it assumes people are perfectly rational, which they are not. That is to say, the rational choice model assumes that people perfectly understand risk and uncertainty, they then consider all of the options in their choice set, and they are thorough and sophisticated enough to weigh all of their options. There is also an assumption that individuals only do things for their own self-interest. These assumptions from the rational model are challenged by the behavioral economic model. There are several aspects of this theory that are applicable to the problem of military compensation not being valued properly. They are as follows:

- Framing or presenting a problem in a certain way is an aspect of the behavioral model. Doing this will strongly affect the choice that results. Simply by framing a problem in a positive light instead of looking at the loss that may happen can have a tremendous impact on how the individual may look at the problem (Baddeley, 2017, p. 78). Because service members do not adequately value their compensation, they are framing their pay as a negative, which will make them look elsewhere (BPC, 2016).
- The economic model of rational choice assumes “rational self-interest,” while many people perform acts of generosity and exhibit altruism. People do get motivated by the concern for the welfare of others; people donating to charity is the most obvious example of this (Baddeley, 2017, p. 3). Despite those acts of generosity, people are much more likely to look out for themselves over anything else according to the rational choice model. This is more reason to disseminate accurate and compelling information to the military personnel. There are plenty of studies, and theory, that concludes people are not rational with valuation of the compensation on their own. If they were rational and had the diligence to see and understand all the information out there, they would be making decisions at a greater level (Baddeley, 2017).
- Overconfidence is another factor when looking at behavioral economics. Individuals believe their skill level and judgment are better than they

actually are, and they expect that better outcomes for them are more likely to happen than they truly are. Numerous studies show that humans tend to overestimate positive attributes about themselves. This overconfidence can be manifested by service members thinking they can get a much higher wage outside of the military than they most likely can.

In behavioral economics, there is an idea that people often use rules of thumb (heuristics) and biases when trying to come up with a decision. Humans all have busy lives, which are complicated, and do not sit down and spend a lot of time thinking about and analyzing everything. There are also instances when individuals really need to do this but do not. It is also a world where fast decision-making is valued. Therefore, people depend on simple *rules of thumb* to help us, because very often they are quick and handy. Behavioral economics uses what can be identified as “three main types of *heuristics* and the behavioral biases associated with them: availability, representativeness, and anchoring/adjustment” (Baddeley, 2017, p. 38).

- Availability, or readily available information, is an aspect of the theory. When individuals are making a decision, especially when they are in a hurry, they will use information that is easy to access, retrieve, and recall. Important to note is that it is *not* all the information. This heuristic links with concepts from psychology: primacy and recency effects. Primacy and recency effects are explained by Baddeley, “We remember more easily the first and last bits of information we come across, and information in the middle is much more easily forgotten” (Baddeley, 2017, p. 39). The primacy effect essentially means that information that is given to individuals first is remembered the most. The recency effect argues that someone will remember the last thing they heard the best. This makes it more important that the DoD disseminates all information on the true value of service member’s compensation so that information can become more “primary” than rumors or innuendos that exist about how they are not compensated adequately (GAO, 2005). The dissemination, for example, can be done during command indoctrination classes and during career development

boards. By doing this, service members have the correct information prior to making a decision on their future.

- Representativeness or “similar” heuristic is the theory that individuals sometimes decide things by analogy. People draw comparisons with other superficially similar events. People will also fit perceptions of others with pre-existing stereotypes. When studies continue to show that service members are dissatisfied with their compensation, something needs to be done to flip that the other way.
- Anchoring effects are the effects on choices of what may be irrelevant even though individuals use anchors in the decision-making process. Professor Richard Thaler noted, “Take the last three digits of your phone number and add two hundred. Write this number down. Now, when do you think Attila the Hun sacked Europe? Was it before or after that year? What is your best guess? (We will give you a hint, it was after the birth of Jesus.) Even if you do not know much about European history, you do know enough to know whenever Attila did whatever he did, the date has nothing to do with your phone number. Still, when we conduct this experiment with our students, we get answers that are more than three hundred years later from students who start with high anchors rather than low ones” (Thaler & Sunstein, 2008, p. 23). Because anchors help and influence the decisions individuals make in life, the DoD needs to fully disseminate the information so the correct “anchors” are out there for service members. Right now it is apparent that their anchor relative to total compensation is too low (GAO, 2005). Furthermore, if irrelevant information can affect a decision, it can be expected that relevant information used properly could make an even bigger impact.

Behavioral economics explains why individuals are not always rational when making decisions. Service members are principal agents of behavioral economics and exhibit irrational behavior when making insignificant or life-altering decisions.

C. PROSPECT THEORY

Prospect theory, a descriptive model created by Daniel Kahneman and Amos Tversky, poses an alternative to Expected Utility Theory and assumes that losses and gains are valued differently, ultimately influencing individuals to make decisions based on potential gains rather than potential losses. Amidst a background of risk and uncertainty, individuals will make decisions in terms of subjective utility relative to a reference point rather than an absolute outcome. The prospect theory model accounts for risk, centers itself about “loss aversion,” and notes that people dislike losses more than equivalent quantitative gains; people are, therefore, more likely to take risks and gambles in order to propel themselves out of the loss territory. Simply put, prospect theory is a description of risk attitudes in experimental settings in which “people derive utility from ‘gains’ and ‘losses’ measured relative to a reference point” (Barberis, 2013, pp. 178–179). Perception is a critical component of the theory and suggests that people’s behavior will be determined by whether they believe they are in loss territory or gain territory.

The value associated with losses and gains according to prospect theory is accurately depicted in Figure 8. The horizontal axis quantitatively measures gains and losses in monetary terms, while the vertical axis measures gains and losses in terms value. According to the figure, a \$100 gain has a value of 100. An equivalent monetary loss of \$100, however, has a value of 200. More value is associated with a loss (200) than with a gain (100) of equal magnitude, which suggests that people inherently take losses harder than they do gains. This behavior is known as loss-aversion.

The disparity between the curves provides some interesting insight into the nature of how people make decisions relative to a reference point. Individuals who perceive themselves to be in the “gain” territory can be considered “risk averse” and much more likely to take conservative approaches to future decisions. They are in the positive territory and will conduct themselves accordingly so as not to remove themselves from that favorable position. Conversely, those in the “loss” territory can be considered “loss averse” and will likely exhibit more risk-seeking behavior in order to get themselves out of the negative territory. Unfortunately, many military service members perceive themselves to be in the “loss” territory. This misguided assumption can be blamed on a number of

possibilities, but this research suggests that an inability to properly account for the future value of benefits paired with the lack of a strategic campaign touting the value of military compensation is the major contributing factor.

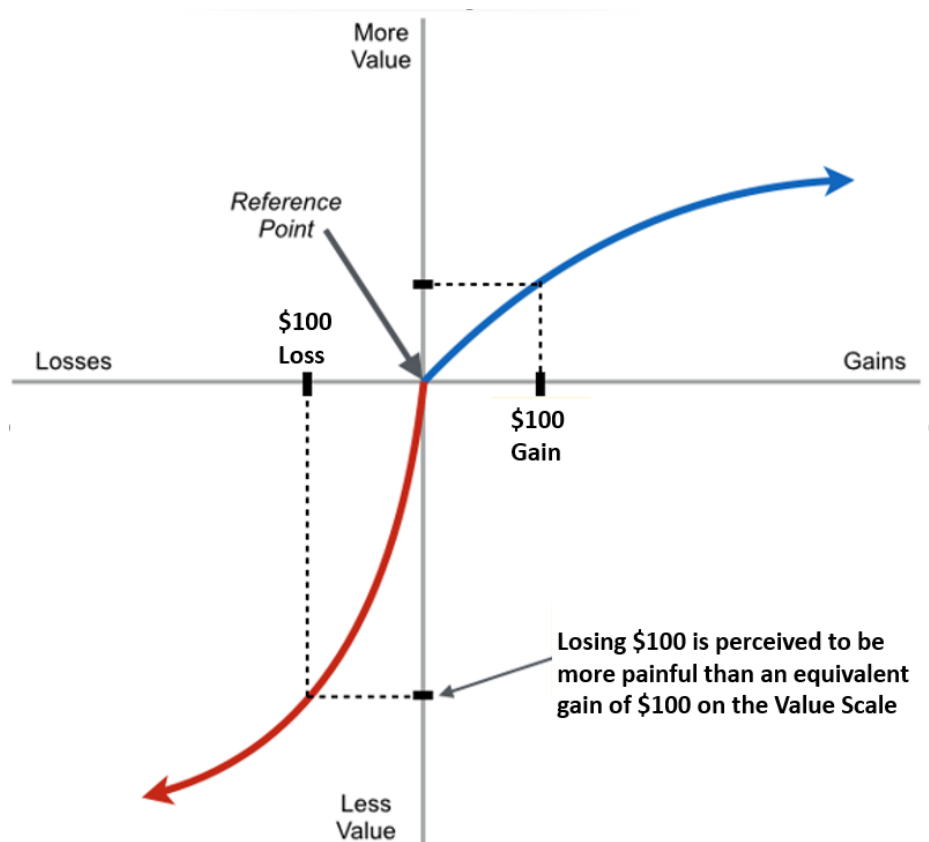


Figure 8. Prospect Theory: Depiction of Losses vs. Gains Relative to Value.
Adapted from Barberis (2013).

The concept of loss-aversion may explain the behavior of junior service members who opt to pursue employment opportunities outside of the military. A poor understanding of the compensation and benefits system contributes to the junior service member's assumption that they are in the loss territory of the prospect theory X-Y axis. These service members assume that the value of their compensation and benefits is less than what they could be receiving in the private sector; therefore, they are comfortable assuming the risks associated with departing the service. They assume they are in an inferior position and will openly accept the loss of a steady paycheck, reliable health care, and other monetary and

non-monetary incentives in order to pursue gains elsewhere. The nature of this assumption is a misperception that needs to be changed. Improved communication and a change in the allocation mix of cash, in-kind (non-cash), and deferred benefits will change the perception among junior service members, push them into gain territory, and allow them to make better long-term decisions.

It is important to acknowledge three main assertions when applying Prospect Theory to our research questions:

1. **Departing the military for employment opportunities in the civilian-sector is risk-taking behavior.** One could confidently argue that changing jobs in any industry, regardless of position, seniority, and expertise, is risky behavior; however, junior service members need to be cognizant of the fact that the likelihood of landing a job of equivalent compensation and benefits is going to be exceedingly difficult. Recall that military compensation corresponds to the 90th percentile of civilian wages for enlisted service members and 83rd percentile for officers (DoD, 2012, p. 31). Surrendering that type of paycheck certainly comes with significant costs and uncertainties.
2. **The risk attitudes of individuals are different depending on whether an individual assumes they are in “loss” or “gain” territory.** Individuals perceived to be in “loss” territory will take extreme measures to propel themselves toward gain territory on the Prospect Theory X-axis. These individuals are “loss averse” and consider departures from normal behavior in pursuit of the unknown. Conversely, those perceived to be in the “gain” territory will assume a more risk-averse posture. Normal behavior will be rooted in conservative action because these individuals perceive what they have to be of high-value. They will be less likely to forsake what they know and are familiar with.
3. **A large contingent of junior service members believe that they are in “loss” territory.** Most junior service members are not sufficiently

educated about the value of their paycheck and, therefore, assume that they can make a better life for themselves by pursuing employment opportunities outside of the military.

This research intends to change the perception that military service members are in “loss” territory. Senior leadership owes it to the military’s junior service members to employ a strategic campaign that properly relays the value of military compensation. Sustained communication paired with repetitive efforts to educate and inform junior service members about the value of their pay is the best way to impact perception, transition from loss to gain, and encourage “risk averse” behavior.

D. ENDOWMENT EFFECT

In behavior economics and psychology, a concept intrinsically related to loss aversion postulates that individuals associate higher values to things they possess simply because the items belong to them. This particular theory is known as the Endowment Effect and is another example of how human behavior deviates from standard economic theory and rational behavior. The Endowment Effect provides additional insight into the value associated with military compensation and pairs well with the aforementioned Prospect Theory of Behavior Economics.

Economist Richard Thaler “identified the ‘endowment effect’ as an example of how loss aversion in prospect theory might affect choice in settings without risk” (Ericson & Fuster, 2013, p. 2). The prospect theory curves (see Figure 8) go hand-in-hand with the endowment effect by noting that a loss in utility relative to surrendering an item is substantially greater than the gain in utility relative to acquiring an item” (Ericson & Fuster, 2013, p. 2). Simply put, individuals expect compensation higher than market value for items that (1) they possess and (2) assume to be valuable. The scenario below provides a quantitative example:

- Individual X, a wine connoisseur, purchases and sells vintage bottles of wine at auction with regularity under two stipulations: (1) He would never spend more than \$35 when purchasing a bottle, and (2) he would never sell a bottle for less than \$100. Essentially, for bottles of wine auctioned off at

prices above \$35, he would not bid. Any bids for bottles of wine he was selling below \$100, he would not sell.

- Economic theory suggests that a rational individual recognizes a single value for the bottle of wine—in this instance, \$50; therefore, if a particular bottle is worth \$50 to Individual X, he should be willing to bid or purchase it as long as the price is at or below \$50. Conversely, he should be willing to sell a bottle for any amount offered to him above \$50.
- Surprisingly, when propositioned by other wine connoisseurs to sell some of the bottles he had acquired over the years, Individual X expressed reluctance to part with the bottles—even if bids were significantly higher than market value for the bottles. He refused to sell unless he was offered \$100 or greater. If someone offers \$95 for a bottle that has a market value of \$25, a rational being would accept; however, Individual X would refuse such a proposal because it was less than his \$100 threshold.
- Individual X's minimum price to sell (\$100) was significantly higher than his maximum purchasing price (\$35). This is irrational.

This behavior pairs surprisingly well with Prospect Theory and the notion of associating action relative to a particular reference point. Individual X's reference point varied depending on if he owned a bottle (\$100) or if he intended to purchase one (\$35). Ownership of a bottle and the value he associated with it put Individual X in “gain” territory and suggested risk averse behavior. What is the ultimate implication of this example?

The principles of Prospect Theory and the Endowment Effect are directly applicable to the value that military members associate with their compensation. Many service members assume they are inadequately compensated; they assume the private sector to be more favorable; they perceive themselves to be in “loss” territory; they are risk-seeking.

Suppose this perception could be changed. If the value associated with military compensation becomes something that people revere, perceptions can be shifted and the implications would be staggering. If service members perceive themselves to be in “gain”

territory, they would be unlikely to pursue employment opportunities in the private sector (Prospect Theory). Moreover, if service members perceive they are endowed with a great compensation package which they value, the private sector would need to offer a substantially higher compensation and benefits package than what the DoD is offering to persuade a service member to leave (Endowment Effect).

E. NUDGE THEORY

The theory of rational economics purports that individuals are rational beings and, therefore, should make rational decisions; however, this typically does not happen as demonstrated by behavioral economists. Nudging is an economic theory that consciously attempts to influence the decisions people make by steering their behavior in a certain direction. Professor Richard Thaler defines a “nudge” as any aspect of a choice “that alters a person’s behavior in a predictable way without forbidding any options or significantly changing their economic incentives. To count as a mere nudge, the intervention must be easy and cheap to avoid. Nudges are not mandates” (Thaler & Sunstein, 2008, p. 6). Regarding junior service members and retention, military leadership should be aware that nudges are a cost-effective tool that can be utilized to influence decisions service members make.

When do people need a nudge? Thaler argues, “People need a nudge for decisions that are difficult and rare, for which they do not get prompt feedback, and when they have trouble translating aspects of the situation into terms that they can easily understand” (Thaler & Sunstein, 2008, p. 72). Essentially, nudges should be utilized to help people improve their lives without exerting any overt influence or inflicting any harm. From a choice architect’s perspective, nudges can be extremely useful when developing strategies aimed at improving retention.

Politically and morally, nudges are a form of “libertarian paternalism.” An in-depth understanding of the term “libertarian paternalism” should be addressed in order to soften two individual terms that typically have off-putting connotations if left unencumbered without context. *Libertarian* implies that people should be free to make their own decisions and opt out of undesirable arrangements if they choose to do so. Policies, options, and

default settings should be designed to allow the freedom of choice. Thaler provides insight on something that is *paternalistic*:

The paternalistic aspect lies in the claim that it is legitimate for choice architects to try to influence people's behavior in order to make their lives longer, healthier, and better. In other words, we argue for self-conscious efforts, by institutions in the private sector and also by government, to steer people's choices in directions that will improve their lives. In our understanding, a policy is "paternalistic" if it tries to influence choices in a way that will make choosers better off, *as judged by themselves*. Drawing on some well-established findings in social science, we show that in many cases, individuals make pretty bad decisions—decisions they would not have made if they had paid full attention and possessed complete information, unlimited cognitive abilities, and complete self-control. (Thaler & Sunstein, 2008, p. 5)

Libertarian, in the sense that it is modifying the term paternalism, literally means "liberty-preserving." Libertarian paternalists, therefore, want to simplify the decision of choice and do not want to burden or inhibit individuals from exercising their freedom (Thaler & Sunstein, 2008, p. 5). The libertarian aspect suggests that people retain power over their own choices, while the paternalistic component suggests that nudges should come from a higher entity (Thaler & Sunstein, 2008, pp. 4–6). The nudge, therefore, is a form of libertarian paternalism because it relies on choice architecture to influence behavior in predictable ways without denying the ability to have freedom of choice regarding available options. This project hopes to influence the behavior of junior service members by encouraging them to make decisions in their best interest while still maintaining the freedom to determine their own outcomes.

The following scenario provides a simple example of how decision-makers can subtly impact the choices others make. In a cafeteria, the arrangement of items, how they are displayed, and the order in which they are displayed ultimately determines the selections people make. For instance, sandwiches can be placed first or last in a queue; fruit can be placed at eye level; candy bars and beverage coolers can be positioned next to registers; unhealthy snacks can be placed in areas that are less easily accessible. Ultimately, the arrangement of items can influence the overall consumption of food items by as much as 25% (Thaler & Sunstein, 2008, p. 1). Small changes in context influence decisions for

better or for worse and yield copious amounts of data upon which informed decisions are made. In this particular cafeteria example, the person who arranges the cafeteria layout and food displays is referred to as a “choice architect.” This particular individual wields a tremendous amount of power and heavily influences the purchases individuals make.

Military leadership can utilize these same principles throughout the course of a junior service member’s career. By conscientiously communicating the high value of military compensation, leadership can expect to improve retention, especially if service members begin to perceive that they are in a better position than their civilian counterparts. Thoughtful, well-timed nudges are a form of choice architecture that leadership needs to strategically implement. Ultimately, the individuals who make decisions that influence choice have an immense responsibility regarding how to shape, influence, and dictate the choices our junior service members make when facing the decision to extend or terminate service. Individuals conducting career counseling, making manpower decisions, affording retirement options, and executing behind-the-scenes decisions are making long-term, force-shaping decisions that will undoubtedly impact retention.

Components of nudge theory can be paired with prospect theory and the endowment effect to lead service members toward loss averse behavior. Loss aversion is typically considered a cognitive nudge—encouraging individuals to not make changes and stick with the status quo. Recall that if service members perceive themselves to be in gain territory, they will be less willing to abandon military service for employment opportunities elsewhere. Loss aversion “helps produce inertia” and creates a reluctance to give up items out of a fear of lost value (Thaler & Sunstein, 2008, p. 34). Nudge theory can be paired with loss aversion to influence the decisions that service members make.

Nudging is a tool that can be utilized by military leadership to influence junior service member behavior regarding retention. Junior service members are the premier candidates for individuals who need a nudge, especially when facing the life-altering decision to extend or terminate service. Libertarian paternalism shows that service members can maintain their freedom to choose while simultaneously being influenced by leadership to make decisions in their best interest. Default settings regarding compensation, deferred benefits, and incentives will likely remain unchanged if service members are not

adequately educated about their options. If properly educated and informed through a comprehensive campaign that utilizes nudging techniques, leadership should be able to steer service members in the right direction when they are faced with their decision to “stay or go.”

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V. FIX THE PROBLEM

Although multiple issues exist, this research focuses on three primary problems and how to solve them. First, a large contingent of service members assume that they are inadequately compensated relative to their civilian counterparts. Second, the current mix of cash, in-kind (non-cash), and deferred benefits is suboptimal for junior service members. Third, DoD communicative efforts regarding compensation are unsatisfactory and, in some instances, nonexistent. A comprehensive campaign that focuses on effectively communicating the value of military compensation must be undertaken in order to change service members' perception and educate them about the true value of their pay. This effort must be strategically implemented, operationally supported, and tactically executed. Doing so will yield an immeasurable number of benefits for the services, most notably in the realm of recruitment and retention.

The notion that “talking about money” is taboo is an assumption that typically prevents most people from discussing the quantitative values of salaries and earnings. Military pay tables, bonuses, allowances, special pay, and incentives are public knowledge. Military leadership should not shy away from the discussion of compensation, but rather, embrace it. Junior service members must know that they are making more than the majority of their respective peers. They deserve to be properly informed and educated when making the decision to stay in or get out. Military service members are paid well; force shapers need to capitalize on this luxury in order to positively impact recruitment and retention efforts.

A. PRIVATE INDUSTRY RECOMMENDATIONS

The following section reviews civilian studies, surveys, and reports regarding the effective communication of employee benefits in the workplace and can be considered a soft-template for military use. An analysis of these communication-focused research documents provides insight about human behavior and the best practices of corporations and industry when making decisions about how to effectively and efficiently communicate information. Cognizance of these practices, principles, and findings should provide force

shapers with recommendations about how to improve communication efforts with service members.

1. Society for Human Resource Management (SHRM)—State Employee Benefits in the Workplace

In 2012, the Society for Human Resource Management (SHRM) conducted a survey examining the state of employee benefits in the workplace. Thorough and all-encompassing, this particular segment of the survey (Part 6 of 6) specifically dealt with the communication of benefits, employee knowledge of said benefits, and effective mediums through which information could be relayed. The survey interviewed 447 organizations from a randomly selected sample of SHRM members across multiple sectors and industries.

Key findings determined that the majority of organizations (86%) reported that employees are “very knowledgeable” or “somewhat knowledgeable” about employer-sponsored benefits available (Society for Human Resource Management [SHRM], 2013). Of the organizations surveyed, 77% believe that they are “very effective” in informing employees about benefits; however, only 22% of organizations had an employee benefits communication budget in Fiscal Year (FY) 2011 (SHRM, 2013). Military leadership may *assume* service members are properly informed about compensation and benefits; however, deficiencies clearly exist and improvements must be made.

The top three communication methods utilized by these organizations were online or paper enrollment materials (84%), group employee benefits communications with a designated representative (65%), and one-to-one employee benefits counseling with a designated representative (51%; SHRM, 2013). The report noted that very few organizations use social media in their communications efforts. One must recognize that social media communication efforts have significantly increased in the private-sector since the time this survey was conducted.

2. How Four Employers Are Getting Benefits Communication Right

Aon, BlackRock, Formstack, and Fujifilm are pursuing innovative approaches to effectively enhance their ability to communicate with employees about benefit plans.

Segmentation, personal choices, demographic targeting, and gaming are the key approaches that have been making significant impacts for these organizations' communicative efforts.

a. *Segmentation*

Segmentation targets employees based on specific demographics and personally tailors communications to individual staff members. Employees often dismiss HR communications, especially if information is disseminated via mass email. If messages do not directly relate to them, employees will often overlook or ignore the information. *Segmentation aims to determine ideal communication methods for the communication of benefits.* Some segmentation options include: paper mailers to people's homes, in-person seminars, webinars, and text messaging. Employees have the option to opt-in to these message through preference pages in their individual online employee profiles (Eisenberg, 2017). Kate Sanderson, a global HR representative for Aon, states,

Our multi-channel approach has improved communication because we are meeting our colleagues and their families where they are and taking into account that individuals want to receive information in different ways.... Our approach appears to be working, as post-enrollment surveys indicate a high level of satisfaction with the tools, resources and information provided. (Eisenberg, 2017)

b. *Personal Choices*

Employees are likely to participate in benefits communication when they are afforded communication methods that they can choose themselves. Internal Wiki pages have proven to be a useful communication tool. Wiki pages allow employees to log in to a system and tailor communicative efforts on their own terms. This medium also allows the organization to communicate with and engage employees about a number of initiatives (Eisenberg, 2017). Ultimately, leveraging technology allows organizations to reach employees across the globe.

c. *Targeting Demographics*

Understanding the background and perspectives of employees is useful in order to effectively communicate benefits. For instance, many millennials are not typically familiar

with the workforce, how programs work, what they do, and how benefits apply to them. Members of this demographic may require additional training and tailored communications in order to properly educate them about issues. The majority of junior service members in the military fall into this “millennial” category. Although generational gaps may exist, the format by which information is communicated remains universal. Videos and slideshows are still popular communication mediums and are often easy to disseminate worldwide. Physical copies of annual benefits (in the form of pamphlets, booklets, and newsletters) are still effective (Eisenberg, 2017). As previously mentioned, social media should be a primary focus.

d. Gaming

Technology can aid employees in benefit enrollment efforts. Embedding plan information within communication mediums helps individuals understand complicated acronyms, terms, and definitions. An organization known as Nicholson “worked with Formstack’s insurance management team to create a one-page explainer of benefit terms and their definitions and broke down plan costs, which was distributed to employees prior to an information session. Nicholson uploaded the explainer to Confluence for employees to access when it came time to waiving or enrolling in their benefits as well. Additionally, when Aon employees are selecting their benefits, they can hover their mouse over certain terms, such as PPO or deductible, for an explainer of what those terms mean,” (Eisenberg, 2017). Options like these allow individuals to make informed decisions and choices in a short window of time without having to perform any extensive research. MyPay is the military’s primary online platform to push compensation tools such as Leave and Earnings Statements (LES), tax forms, and retirement allocations. Service members have noted, however, that the site is difficult to access, not user-friendly, and uninformative regarding educational explainers.

3. SHRM—Employees Perplexed by Benefits Choices

An SHRM report in August 2012 determined that most employees were not confident that they were making the right choices regarding benefits choices. Common mistakes were found in the selection of benefits options, policy changes, and contribution

amounts. Additionally, a perception gap exists between organizations and employees regarding the communication of company benefits. Nearly half of employers surveyed believed they communicated company benefits effectively to employees; however, employees typically disagreed (SHRM, 2012). Similar trends were evident in a 2005 GAO report regarding the communication of military benefits.

The SHRM report determined that companies can improve organizational effectiveness by developing more effective communication strategies. Best practices included surveying employees, communicating year-round, offering voluntary benefits, and marketing benefits offerings to employees.

Utilizing concise and easily understandable communication strategies should help employees recognize their available options and determine how certain benefits apply to them. This particular survey determined that some effective communication strategies include: online communication platforms, savings and retirement plan enrollment tutorials, employee-focused newsletters, informal luncheons between mentors and protégés, customized benefits pamphlets, and mediums through which frequently asked questions can be addressed (SHRM, 2012). Firms, today more than ever, are recognizing the necessity and importance of education related to communication strategies.

This SHRM report references an Aflac Workforces Report compiled in 2012 that shows a correlation between an employee's likelihood to quit/leave and the frequency with which benefits are communicated. Forty-five percent of employees interviewed expressed infrequent communication with their organizations regarding benefits communication. Furthermore, employees in organizations with little to no benefits communication were substantially more likely (63% vs. 34%) to depart their jobs the following year (SHRM, 2012). The way in which information is relayed is important, but the frequency of communication efforts appears to be more important. Employers need to conscientiously make efforts to communicate the importance of compensation and benefits regularly if they wish to retain talented employees.

Table 2. Frequency of Benefits Communication and Likelihood to Leave. Adapted from SHRM (2012).

Frequency of Benefits Communication and Likelihood to Leave	
	Extremely or very likely to leave their job in next 12 months
Communicates about benefits only at open enrollment or new hire enrollment	65%
Communicates 2 times throughout the year	18%
Communicates 3–5 times throughout the year	12%
Communicates 6–9 times throughout the year	3%
Communicates 10+ times throughout the year	1%

The same SHRM report noted additional findings on the effectiveness of benefits communication determined by yet another survey of employment organizations in May 2012. The survey, conducted by Benz Communications, determined three key takeaways:

78 percent of employers cited getting employees engaged year-round among their biggest challenges, yet less than a third (28.9 percent) communicated with employees year-round.

Employers' top goals included executing a successful annual enrollment (60 percent), increasing workers' use of preventive care (48 percent) and increasing employees' 401(k) savings. However, fewer than a quarter (24 percent) reported meeting these goals in 2011.

More than two-thirds (68.3 percent) had budgets of less than \$25,000 for benefits communication, while just over 10 percent reported budgets between \$25,000 and \$75,000. However, the majority of these budgets weren't being spent strategically. For example, two-thirds (66 percent) reported print and postage costs (one-time non-renewable expenses) as consuming most of their budget. (SHRM, 2012)

Failing to communicate with regularity, failing to meet goals, and the mismanagement of funds plagued these organizations. This parallels well with lapses and deficiencies in the military regarding the communication of compensation.

4. Conference Board Report: Corporate Communication Practices—Key Findings (2018 Edition)

A 2018 Conference Board report analyzed the corporate communication practices of a sample of public companies registered with the U.S. Securities and Exchange Commission (SEC) and other international securities commissions. A key finding from this report noted that budgetary restraints inhibit communication departments—most companies reported unchanged or decreased budgets from the previous fiscal year (Conference Board, 2018). The report notes that budgetary constraints are occurring in the face of growing teams (i.e., larger, more robust communication divisions) which suggests that increases in manpower and overall responsibilities are occurring without in-kind budgetary increases. This particular lack of budget growth in communications departments is evidence that many organizations consider money spent regarding communication as an expense, rather than an investment.

Another key finding from the 2018 Conference Board report noted that social media has become a core component of large companies. *The majority of companies (85.7%) with revenue of more than \$25 billion reported the utilization of Facebook, Twitter, YouTube, and Instagram as mediums through which information can be effectively relayed* (Conference Board, 2018). Social media has become the primary component for fast, effective communication in the modern era and must be utilized in marketing, customer service, and employee feedback. The military currently utilizes all of these social media platforms; however, it does not have a dedicated campaign to communicate the value of compensation through any of them.

B. PROPOSED SOLUTIONS

1. Change the Mix—Getting the Biggest Bang for the Buck

Flexibility of the allocation mix is one of the pros that the military compensation system prides itself on. As described in the 2018 Military Compensation Background Papers (Eighth Edition),

FLEXIBILITY. The fifth principle underlying the overall compensation system is that it ought to be designed in a way to adjust quickly to changing conditions of combat tactics, technology, and manpower supply and

demand. Here again, there are several sub-principles involved. An effective system cannot be designed without a reasonable specification of the force size and manpower profile that the system is to support; i.e., a definitive statement of manpower requirements is needed which has as its foundation reasonable standards. (DoD, 2018a, p. 4)

DoD-approved documentation exists to support adjustments to the allocation mix and percentages associated with them; therefore, this research recommends adjusting the mix of allocation percentages in an effort to improve the retention of junior service members.

The DoD weighs the importance of deferred benefits heavily, which is contrary to practices embraced by private industry and the civilian sector. We recommend a slight decrease in deferred benefits from 28% to 20%, which will allow an additional 8% to be allocated toward cash compensation—51% to 59%. Benefits such as health care, housing, and other in-kind benefits will be unaffected by this change. This adjustment will more accurately align with compensation in the civilian private sector and civilian federal government as seen in Figure 9.

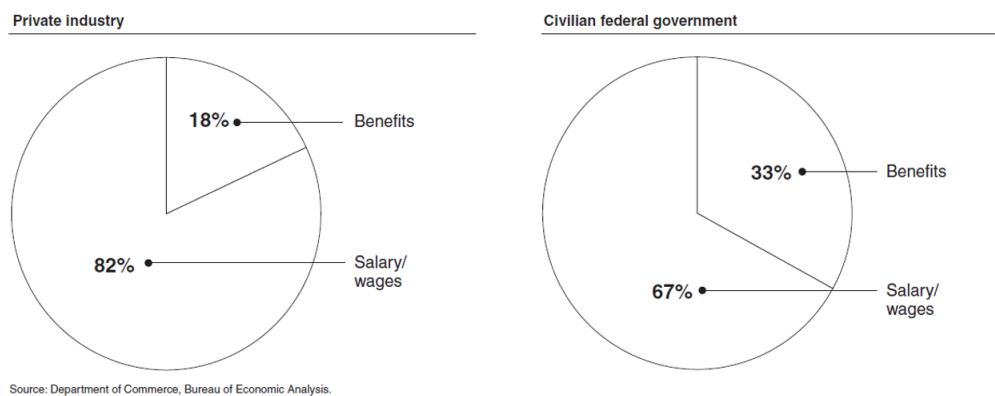


Figure 9. Allocation Mix of Salary/Wages and Benefits in Civilian Compensation. Source: GAO (2005, p. 24).

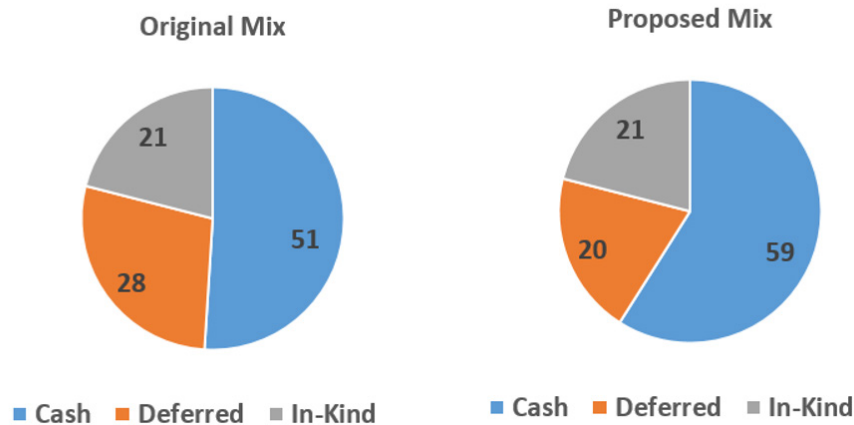


Figure 10. Original vs. Proposed Mix of Military Compensation Allocation

Manipulating the allocation mix in this manner will appeal to the preference that junior service members have for cash. A GAO report notes, “Because the preference for cash is particularly strong in young adults, this adage is especially true for the military because the active duty workforce is mainly comprised of people in their twenties” (GAO, 2005, p. 24). Additionally, retirement pay, in the form of deferred benefits, impacts only 19% of service members—the other 81% terminate service at some point prior to 20 years. The GAO (2005) states that

a significant portion of the compensation budget is being allocated to provide for future retirement pay and health care for current active duty members who will become eligible to receive these benefits *even though a relatively small percent of the force will ultimately receive these benefits.* (p. 25; emphasis added)

Individuals heavily discount the value of future benefits; therefore, decision-makers should adjust the mix in an effort to entice junior service members to “stay in.” Shifting away from deferred benefits and making adjustments to increase cash will improve satisfaction and nudge service members in the direction of extending service, rather than terminating it.

2. Better Communication of the Value of the System (Nudging)

A comprehensive, all-encompassing campaign must be undertaken in order to educate and inform junior service members about the value of military compensation. Improved communication is critical for two reasons:

1. It will educate and inform junior service members about the critical aspects of their pay and benefits, which will help them make informed choices when faced with the decision to extend or terminate service.
2. If junior service members recognize the competitiveness of military compensation, retention will likely improve.

Communicative strategy needs to be considered on a national level (Big Navy), imposed operationally (Fleet level), and executed tactically (individual commands). Communication must occur frequently and with regularity in order to serve as constant reminders that military pay is competitive and, in many cases, stronger than civilian pay. We recommend simple, succinct monthly handouts or posters that communicate one value of military compensation at one time (see Figure 11), paired with an extensive social media campaign. For instance, a handout that explains the tax advantages of BAH and BAS could be disseminated during the month of April. We do not want to overwhelm service members with information, but gradually and repetitively educate them about the value of their compensation.

Posters, handouts, pamphlets, brochures, and social media posts can be considered nudging mediums that will effectively relay information to junior service members; however, efforts will be fruitless if a campaign is not strategically organized and executed at the operational and tactical levels. Manpower and Public Affairs need to push primary initiatives, while individual commands need to take ownership of the initiative to educate service members about the value of their compensation. Thoughtful nudges will influence service member behavior and allow leadership to improve retention efforts, while still providing members with the freedom to make decisions on their own.

a. Create a Dedicated Campaign

Informative and educational campaigns exist in several areas that the military considers important—especially with regard to the education and enlightenment of personnel. Sexual Assault Prevention Response, Alcohol and Drug Abuse Prevention, Domestic Violence Awareness, and Keep What You’ve Earned are a few examples of

Navy campaigns that help commands promote, market, and educate sailors about prevention and abuse. The majority of these campaigns keep materials available online through the Navy Logistics Library (NLL) at no cost to Navy commands. The principles utilized to push information about abuse and prevention can easily translate to an informative campaign aimed at educating and informing junior service members about the value of military compensation and benefits. This research recommends a robust social media campaign as well. These low-cost initiatives will be invaluable if they are able to improve overall retention numbers. Additionally, a smart, easy-to-follow social media campaign will likely generate interest in the service and aid in recruitment efforts if the high-value of military compensation is effectively relayed. Other mediums through which information could be relayed include command indoctrination classes, petty officer indoctrination classes, and Career Development Boards.

An example of a handout/poster/social media post mentioning RMC and non-taxable benefits is depicted in Figure 11.

How Do Non-Taxable Benefits Affect You?

Allowances such as Basic Allowance for Housing (BAH) and Basic Allowance for Subsistence (BAS) are non-taxable and are a unique way for members of the military to outpace/outperform civilian counterparts in the realm of taxable income.

How does this impact you? Refer to the following example:

- **MILITARY**
 - A single E-4 (with 4 years of service) earns an annual base pay of \$29,887
 - This service member falls into the 12% tax bracket (according to the 2017–2018 Tax Bracket).
 - With the Norfolk BAH, BAS, and the Tax Advantage factored in, the service member receives **\$52,433** annually
 - Remember, BAH and BAS are not taxable and there is a Tax Advantage associated with those allowances not being taxable
 - According to the Federal Government, this E-4 will only be taxed according to their base pay of \$29,887.
 - Taxes would equate to \$3,586.44.
- **CIVILIAN**
 - A civilian taking home a salary of **\$52,433** would be taxed at full value
 - This civilian would fall into the 22% tax bracket
 - Taxes would equate to \$11,535.26.

The tax difference between Civilian (\$11,535) and Military (\$3,586) equates to **\$7,949!**



	<u>E-4</u>	<u>Civilian</u>
Base Pay	\$29,887	\$52,433
BAH	\$15,408	N/A
BAS	\$4,432	N/A
<u>Tax Advantage</u>	<u>\$2,705</u>	<u>N/A</u>
Total (RMC* or Civilian Salary)	\$52,433	\$52,433
Federal Tax Bracket	12%	22%
Taxes Owed to IRS**	\$3,586	\$11,535
Total Money Kept	\$48,847	\$40,898

*RMC = Base Pay + BAH + BAS + Tax Advantage. RMC is the approximate amount of an equivalent civilian salary.

**Tax deductions are not factored into this example as they vary depending on a multitude of factors (filing status, dependents, etc.)

Grade	E-4
Years of Service	4
Tax Filing Status	Single
Living OCONUS or Not Receiving BAH?	false
Living OCONUS?	N/A
ZIP Code of your Permanent Duty Station	23510
Annual Basic Pay	\$29,887.20
Annual Basic Allowance for Housing	\$15,408.00
Annual Basic Allowance for Subsistence	\$4,432.68
Non-Taxable Allowances (BAH + BAS)	\$19,840.68
Number of Exemptions for Previous Calendar Year	1
Personal Exemption Amount	\$0.00
Standard Deduction	\$12,000.00
Total Deductions	\$12,000.00
Taxable Income (Annual Basic Pay - Total Deductions)	\$17,887.20
Tax Rate	12%
Gross Up	\$22,546.23
Tax Advantage	\$2,705.65

Total Regular Military Compensation (RMC): \$52,433.45

Figure 11. Non-taxable Benefits and RMC Computation (Handout/Poster/Social Media Post)

An example of a poster mentioning the value of military health care is provided in Figure 12.



Figure 12. Policy Poster Recommendation

b. Communicate RMC

We strongly recommend expressing the value of RMC. Circumstances vary between individuals, but recognizing the value of individual worth is ever-present for every service member. Am I getting paid enough? Can I do better on the other side? Should I stay in? Should I get out? A simple explanation of RMC and an example of RMC paired with a comparable civilian salary (to include educational pedigree) would alleviate the cloud of confusion that hovers over many service members. Figure 13 is an example of a job-specific handout/poster/social media post mentioning RMC that would be a low-cost, effective, and efficient way to communicate value.

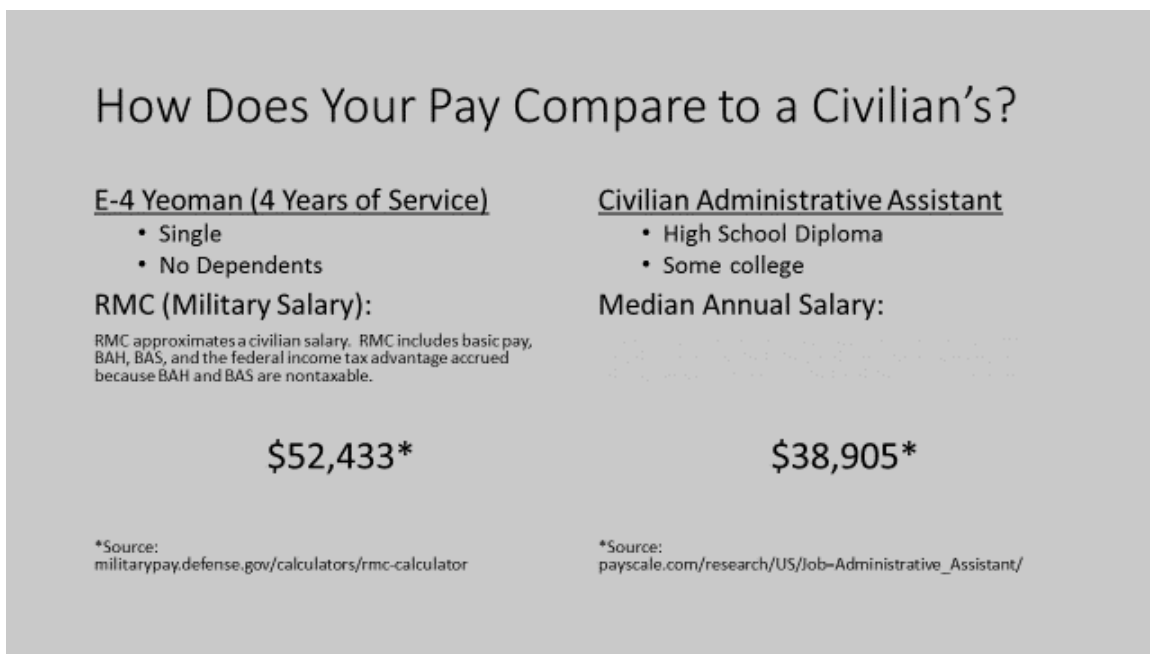


Figure 13. Military-Civilian Compensation Comparison with RMC (Handout/Poster/Social Media Post)

c. Communicate PSMC

The principles that make RMC important apply to PSMC. PSMC is an underutilized tool that comprehensively expresses the value of military compensation and benefits. It is the most all-encompassing tool available to service members; however, most service members do not know that it exists and do not know how to access it. Multiple improvements must be made to maximize the utility of this asset.

- 1. Service members need to know that PSMC exists.**
- 2. PSMC should be universally available through myPay, regardless of service.**
- 3. Abbreviated versions of the PSMC document should be available, in the form of a one-page document/summary.** The Marine Corps automatically computes a PSMC statement through Marine Online that calculates the value of cash, in-kind (non-cash), and deferred benefits. Other services should take a similar approach and employ an algorithm that creates a PSMC based on the circumstantial variables of that particular service member. This could be similar to an annual Comparative Benefits Statement that many corporations provide employees in private industry.
- 4. PSMC should be made available on the official DOD Military Compensation website.**

PSMCs are more important now than ever. In a tight labor market with employers fighting to recruit and retain talent, the military must employ every available tactic to keep members in the ranks. RMC proves that military compensation is competitive; PSMC shows that, when paired with RMC, the value of military compensation is almost unbeatable.

d. Education First, Perception Next

A comprehensive educational campaign should swing the theoretical pendulum from a culture of dissatisfaction and misunderstanding to one of pride and acceptance. *Perception* will change after educational efforts are conducted. Human behavior, prospect

theory, and the endowment effect suggest that if service members perceive themselves to be in gain territory, they will exhibit risk-averse behavior and be hesitant to abandon military service for employment opportunities elsewhere. The intent of this research is not to force service members to stay in, but rather, ensure that they are adequately informed in order to make decisions in their own best interest. They have the freedom to make their own choices, but they should be doing so in ways that maximize utility while capitalizing on optimal alternatives.

A strategic campaign must be created, supported, and executed accordingly. Service members need to be aware of RMC and PSMC in order to understand how their compensation package compares to a civilian's annual salary. A change in perception will only occur if junior service members are properly educated.

VI. CONCLUSION

Holistically, the current military compensation system is sensible and compensates service members adequately, given the circumstances and nature of their profession. Enlisted and officer RMC is economically substantial and, in many instances, higher than the compensation of comparably educated civilians. Despite its great value, many service members perceive the military compensation system to be inadequate and less valuable when compared to civilian compensation. This research posits that the culture of dissatisfaction is the result of poor efforts by leadership to educate and inform service members about the value of their pay. Service members assume “the grass is greener on the other side” because they are misinformed about the value of their compensation. Retention among junior service members nearing the end of their initial service obligation would likely improve if they become fully aware of RMC (and its components), non-taxable benefits, and how their compensation compares to the compensation of their civilian counterparts.

The current military compensation system contains the necessary firepower to remain competitive with wages and earnings in the civilian sector; however, changes can be made to the allocation mix in order to improve junior service member retention. Modifications to certain policies and procedures set forth by Congress are likely required if a significant impact is to be expected in the current versus deferred compensation system; however, policy is often difficult to implement and enact in a timely manner.

An aggressive campaign to educate and inform sailors would be most beneficial and can be achieved at a relatively low cost. Social media must be utilized and heavily relied upon in this modern era. Efforts must be planned at the strategic level and eventually filtered down to individual commands in order to ensure proper execution and widespread dissemination. Over time, human behavior research suggests that perception will change as a result of increased awareness through education and well-placed nudging techniques. Retention will likely improve if junior service members recognize the value of their paycheck. It is the responsibility of leadership to ensure that these efforts are pursued

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APPENDIX. PERSONAL STATEMENT OF MILITARY COMPENSATION

This statement is intended to outline the total value of your military pay, allowances and benefits. By making your compensation more "visible," this statement could be useful when applying for credit or loans (including home loans) from businesses or lending institutions. Another possible use of this summary is to help determine whether specific civilian employment offers would let you maintain the same standard of living you had while serving in the military. Start with the Total Direct Compensation on page 1, add the Federal Tax advantage from page 2, and then add any additional expense a civilian employer would expect you to pay for health and life insurance, retirement contributions, etc. This will tell you approximately what level of civilian salary you must earn in order to maintain a similar standard of living as that provided by your military take home pay. Each section of this statement contains an explanation. However, if you have any questions, please contact your local financial services office (FSO).

SUMMARY:	A. Basic Military Compensation as of January	\$
	B. Special Pay and Bonuses	\$
	C. Expense allowances	\$
	TOTAL DIRECT COMPENSATION	\$
	Added value of indirect compensation	\$
	Added considerations/programs (Your estimate)	\$
	TOTAL COMPENSATION	\$

The following information provides more details on the value of your personal compensation. Adding the indirect compensation and additional considerations to your direct compensation should provide a clearer picture of your total military compensation package.

DIRECT COMPENSATION AS OF MARCH (NOTE 1)

A. BASIC COMPENSATION. Describes the basic elements of compensation paid to all military members. It includes Basic Pay, the value of living quarters or Basic Allowance for Housing (BAH), and the value of meals furnished or Basic Allowance for Subsistence (BAS). Your basic compensation is:

	<u>Monthly</u>	<u>Annual</u>
Basic Pay	\$	\$
BAH or quarters valued at national average BAH rate .. (See Note 2 on page 2)	\$	\$
BAS or meals valued at BAS rate .. (See Note 2 on page 2)	\$	\$
TOTAL BASIC COMPENSATION	\$	\$

B. SPECIAL PAY AND BONUSES. Is in addition to Basic Compensation for people in certain skills and assignments. Your bonuses, special and incentive pays are:

Special and Incentive Pays	\$	\$
Bonuses	\$	\$
TOTAL SPECIAL PAY AND BONUSES	\$	\$

C. EXPENSE ALLOWANCE. You may receive allowances to help compensate you for extra expenses you incur based on the location of your duty assignment. These include the overseas housing allowance (OHA), cost of living allowance (COLA) only payable in certain areas, family separation allowance (FSA), and clothing replacement allowance (CRA) (Note 1). Your total expense allowances are:

TOTAL EXPENSE ALLOWANCES	\$	\$
---------------------------------------	----	----

INDIRECT COMPENSATION

Other programs supplement your direct compensation. These have a cash value to you in terms of spendable income. They are an important part of your compensation and should be considered in adding up your real pay value.

A. MEDICAL CARE. As an active duty member, the military provides you and your family with comprehensive medical care. TRICARE is the name of the Defense Department's regional managed health care program. Under TRICARE, there are three health plan options: TRICARE Prime (all active duty are automatically in Prime, but family members may choose to enroll in this HMO-type plan); TRICARE Standard (an indemnity plan, formerly called CHAMPUS); TRICARE Extra (a Preferred Provider Organization plan). Under TRICARE Prime, you will have an assigned military or civilian primary care manager who will manage all aspects of your care, including referrals to specialists. Prime has no deductibles, cost-shares, or co-payments except a nominal co-payment for prescriptions filled at a retail pharmacy or through the National Mail Order Pharmacy program. TRICARE Standard offers more choice of providers, but requires an annual \$150 deductible/person or \$300/family (E-1 to E-4: \$50/person, \$100/family) plus a 20% cost-share for outpatient care and an \$11/day charge for inpatient care. TRICARE Extra offers the same as Standard, but if you elect to use a Prime network provider, the outpatient visit cost-share is only 15%. The average total premium of a civilian plan that would provide similar benefits is conservatively estimated at \$205/month/individual, \$2,461/year/individual, \$470/month/family and \$5,646/year/family – these premiums do not take into consideration cost-shares and deductibles often required in civilian plans like the TRICARE Standard and Extra options. Please contact the Beneficiary Counseling and Assistance Coordinator at the nearest military treatment facility for additional information. The personal costs experienced by you or your family will vary depending on the TRICARE option you select.

Monthly Rate \$ _____ Annual Rate \$ _____

B. DEATH AND SURVIVOR PROGRAMS. If you die on active duty, your survivors are eligible for life insurance and other payments. You may buy life insurance in \$10,000 increments up to \$250,000 at a very low cost. Also, your dependents would receive a death gratuity payment of \$6,000 and monthly Dependency and Indemnity Compensation (DIC) payments (non-taxable) of \$911 for the surviving spouse and an additional \$229 for each surviving child. DIC is adjusted annually for inflation. Also see Survivor Benefit Plan on page 3 of this statement. You are currently paying premiums for \$ _____ in life insurance coverage.

C. **FEDERAL TAX ADVANTAGE.** This represents the amount of additional Federal tax you would have to pay if your quarters (BAH), and meals (BAS) were taxed. Your tax advantage is based on

INDIRECT COMPENSATION (A + C)

Monthly Rate \$ _____ Annual Rate \$ _____
 Monthly Rate \$ _____ Annual Rate \$ _____

- Note 1: Pay items on your June 1999 LES, marital status and dependents taken from your personnel records. Annual rates for OHA, COLA, and enlisted BAS are for 365 days, not 12 times the June rate.
- Note 2: If BAH or BAS was not in effect in June 1999, we assumed you received quarters or meals worth about as much as BAH or BAS. If you received partial BAH, we assumed that the partial BAH and value of quarters together roughly equal full BAH.

RETIREMENT SYSTEM

One of the most attractive incentives of a military career is the retirement system that provides a monthly retirement income for those who serve a minimum of twenty years. Currently, there are three retirement plans in effect -- Final Basic Pay, High-3, and Choice of High-3 or Redux with \$30K Career Status Bonus. A description of each follows. Additional information on all three plans is available at: <http://www.afpc.randolph.af.mil/>. Additional information on the new High-3 and Redux/\$30K Career Status Bonus choice is available at: <http://pay2000.dnc.mil>.

Plan	Eligible (as determined by DIEMS) (Note 1)	Retired Pay Formula (Notes 2, 3 & 4)	Cost-of-Living Adjustment (COLA) (Note 5)
Final Basic Pay	Entered service prior to 8 Sep 80	2.5% times the years of service times final basic pay	Full inflation protection; COLA based on Consumer Price Index (CPI)
High-3 (Note 6)	Entered service on or after 8 Sep 80 and before 1 Aug 86	2.5% times the years of service times the <i>average</i> of the highest 36 months of basic pay	Full inflation protection; COLA based on Consumer Price Index (CPI)
High-3 Choice -----OR----- Redux/Career Status Bonus Choice: Instead of retiring under High-3, members may choose to receive a \$30,000 "Career Status Bonus" at 15 years of service in exchange for agreeing to serve to at least 20 years of service and then retiring under the less generous Redux plan.	Entered service on or after 1 Aug 86	High-3: 2.5% times the years of service times the <i>average</i> of the highest 36 months of basic pay -----OR----- *Redux/Career Status Bonus option: 2.5% times the years of service, minus one percentage point from the product for each year less than 30 years, times the <i>average</i> of the highest 36 months of basic pay. At age 62, retired pay is recalculated without deducting the one percentage point for each year less than 30, which allows it to catch up to what it would have been without the Redux penalty.	High-3: Full inflation protection; COLA based on Consumer Price Index (CPI) -----OR----- *Redux/Career Status Bonus option: Partial inflation protection; COLA based on Consumer Price Index (CPI) minus 1 percent. At age 62, retired pay is adjusted to reflect full COLA since retirement. Partial COLA then resumes after age 62.

- Note 1: Date initially entered military service (DIEMS) refers to the fixed date the member was first enlisted, appointed, or inducted. This includes cadets at the Service Academies, students enrolled in a reserve component as part of the Services' senior ROTC programs or ROTC financial assistance programs, students in the Uniformed Services University of the Health Sciences, participants in the Armed Forces Health Professions Scholarship program, officer candidates attending Officer Training School, and members in the Delayed Entry Program.
- Note 2: The maximum multiplier is 75 percent times basic pay.
- Note 3: Members should be aware that the Uniformed Services Former Spouses Protection Act allows state courts to consider military retired pay as divisible property in divorce settlements. The law does not direct state courts to divide retired; it simply permits them to do so.
- Note 4: Retired pay stops upon the death of the retiree unless he or she was enrolled in the Survivor Benefit Plan. See "Survivor Benefit Plan (SBP)" on page 3 for additional information on this program.
- Note 5: COLA is applied annually to retired pay.
- Note 6: High-3 is a reference to the average of the high three years or, more specifically, the high 36 months of basic pay as used in the formula.

(For Retirement-Eligible Personnel) If you were to retire in your present grade, your initial gross monthly retired pay would be _____ increased annually for inflation. For each year you continue to stay on active duty, you will receive an additional 2.5% of your basic pay up to a maximum of 75%. Your retirement represents a considerable value over your life expectancy. While retired pay stops upon death, you can ensure your survivors receive a portion of it by enrolling in the Survivor Benefit Plan when you retire (see next page). Retired pay calculation is for illustration only. It does not consider any active duty service commitment or time-in-grade requirement which may preclude your retiring immediately in your present grade. Further, the date used to determine years of service in your actual retired pay computation (the "1405" date) will be determined by the MPF from paper records and could be different than the total active Federal military service used in this example.

ADDITIONAL CONSIDERATIONS

When adding up the total worth of your compensation package, you should also consider the many other programs and privileges you have. Their worth will be different for each person depending on use. This page is presented for you to determine the yearly value/savings you estimate each of these programs has been worth to you.

Your Estimate of Annual
Value/Savings

PAY GROWTH. Pay raises each year, longevity increases, and competitive promotion opportunities.

\$ _____

STATE/LOCAL TAX ADVANTAGE. Besides being exempt from Federal taxes, your BAH, BAS, overseas allowances, and in-kind food and housing may be exempt from State and Local taxes, depending upon your residency. Relative to the tax laws of legal residence, this can save you hundreds of dollars each year. \$ _____

COMMISSARY. The 1999 comparison study found that commissary shoppers on average save 27%. If you spend the following, your savings will be approximate:

<u>Monthly Purchases</u>	<u>Monthly Savings</u>
\$200	\$54
\$300	\$81
\$400	\$108

ARMY AND AIR FORCE EXCHANGE SERVICE (AAFES). "We Go Where You Go" is the motto of AAFES. For more than 105 years, the exchange service has remained true in its commitment to Value, Service, and Support for the military customer and their families worldwide. AAFES helps you in two principal ways. First is its guarantee to "meet or beat" any other retailer's price on the same item (under \$5, no questions asked; over \$5, within 30 days of the retailers advertisement). Second, profits are used to support the Services' morale, welfare, and recreation programs. And now, AAFES offers 24/7 convenience through its new website www.aafes.com

SURVIVOR BENEFIT PLAN (SBP). All pay stops when a member dies. However, if you die on active duty with 20 or more years of service, your surviving spouse and children are automatically protected by the SBP--at no cost to you. The surviving spouse will get an annuity equal to the difference between the dependency and indemnity compensation DIC payment and the SBP payment that would be paid if you had been retired on the date of your death. To determine the amount of the SBP, the maximum applicable rate of retired pay that would be due you will be used. The only way retirees can guarantee their survivors receive a share of their retired pay is to enroll in SBP before they retire. The maximum annuity is equal to 55% of retired pay until the spouse attains age 62. At age 62, the annuity is reduced to 35% of retired pay unless the retiree purchases the Supplemental Survivor Benefit Plan (SSBP) which restores the annuity to between 40 and 55 %, depending on the amount selected. SSBP is not authorized for surviving spouses of retirement-eligible members who die on active duty--that's why it's better for your survivors if you are retired before you die. The SBP annuity for your survivor is adjusted each year by the same percentage increase given to military retired pay.

\$ _____

EDUCATION PROGRAMS. Members in authorized off-duty education programs may have up to 75 percent of their tuition, up to a maximum of \$187.50 per credit hour, \$3,500 per fiscal year, paid by the Government. Members who had established an account in the Veterans Educational Assistance Program (VEAP) by contributing \$25-\$100 each month or by lump sum payment (up to \$2700), have a Government \$2 for \$1 matching contribution for a total of up to \$8,100. Members who elected to participate in the Montgomery GI Bill upon entering active duty (after 30 June 1985), and agreed to payroll reduction of \$100 per month for a total of 12 months, can receive a benefit of \$ 23,400 with yearly increases as determined by the consumer price index.

\$ _____

SERVICES (SV) ACTIVITIES. Provide conveniently located, low-cost, professionally managed activities and entertainment. You and your family members receive significant savings when you participate in SV programs such as fitness, libraries, child development and youth programs, skills development, golf, bowling, clubs, outdoor recreation activities, equipment checkout, aero clubs, etc.

\$ _____

COUNSELING AND ASSISTANCE PROGRAMS. Military members can get free legal counseling and assistance, education services counseling, and may be provided personal financial management training, where available. Zero interest emergency loans and grants may be provided by the Air Force Aid Society.

\$ _____

SPACE AVAILABLE TRAVEL. Space available travel for Uniformed Services members can provide substantial savings over commercial airline fares. Space available travel is defined by DoD policy as a privilege (not an entitlement) which accrues to Uniformed Services members as an avenue of respite from the rigors of Uniformed Services duty. Under one of the categories of space available travel, members on leave can travel with one dependent on permissive TDY house hunting trips. For additional information on this special privilege, consult the GENERAL SPACE AVAILABLE INFORMATION PAMPHLET, (AMC Pamphlet 24-203) on AMC's web page at

<http://public.scott.af.mil/hqamc/pubs/hqamc.htm>

\$ _____

TRICARE DENTAL PROGRAM (TDP). TDP eligibility includes spouses and eligible children of active duty members of the Uniformed Services, Selected Reserve and Individual Ready Reserve. Additionally, the Selected Reserve and Individual Ready Reserve members themselves are eligible for the TDP. Enrollees may be treated in both CONUS and OCONUS locations. TDP monthly premiums for Selected Reserve members and family members of active duty are cost-shared by the Department of Defense (DoD) (i.e., the government pays 60% of the premium, sponsor pays 40%). The sponsor's monthly premium payment is \$7.63 for a single enrolled family member and \$19.08 for families with two or more members enrolled. This equates to an annual savings conservatively estimated at \$137 for single and \$344 for family enrollments. Basic preventive services are covered at 100%; the plan pays 50%-80% of the cost for certain specialized services such as restorations, orthodontics, and prosthodontics. Moreover, DoD cost-shares other specialty care (periodontic, endodontic, and oral surgery) at a higher percentage for E-1s to E-4s.

\$ _____

(add this amount to Summary Total on page 1)

TOTAL

\$ _____

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