

# Strategy Research Project

## Key Elements of Military Retirement System Modification

by

Lieutenant Colonel David Smith  
United States Air Force



United States Army War College  
Class of 2014

### DISTRIBUTION STATEMENT: A

Approved for Public Release  
Distribution is Unlimited

This manuscript is submitted in partial fulfillment of the requirements of the Master of Strategic Studies Degree. The views expressed in this student academic research paper are those of the author and do not reflect the official policy or position of the Department of the Army, Department of Defense, or the U.S. Government.

The U.S. Army War College is accredited by the Commission on Higher Education of the Middle States Association of Colleges and Schools, 3624 Market Street, Philadelphia, PA 19104, (215) 662-5606. The Commission on Higher Education is an institutional accrediting agency recognized by the U.S. Secretary of Education and the Council for Higher Education Accreditation.

**REPORT DOCUMENTATION PAGE**

Form Approved--OMB No. 0704-0188

The public reporting burden for this collection of information is estimated to average 1 hour per response, including the time for reviewing instructions, searching existing data sources, gathering and maintaining the data needed, and completing and reviewing the collection of information. Send comments regarding this burden estimate or any other aspect of this collection of information, including suggestions for reducing the burden, to Department of Defense, Washington Headquarters Services, Directorate for Information Operations and Reports (0704-0188), 1215 Jefferson Davis Highway, Suite 1204, Arlington, VA 22202-4302. Respondents should be aware that notwithstanding any other provision of law, no person shall be subject to any penalty for failing to comply with a collection of information if it does not display a currently valid OMB control number. **PLEASE DO NOT RETURN YOUR FORM TO THE ABOVE ADDRESS.**

|  |                          |  |                                   |   |   |
|--|--------------------------|--|-----------------------------------|---|---|
| <b>1. REPORT DATE (DD-MM-YYYY)</b><br>15-04-2014   |                          | <b>2. REPORT TYPE</b><br>STRATEGY RESEARCH PROJECT |                                   | <b>3. DATES COVERED (From - To)</b>             |   |
| <b>4. TITLE AND SUBTITLE</b><br>Key Elements of Military Retirement System Modification  |                          |  |                                   | <b>5a. CONTRACT NUMBER</b>                      |   |
|  |                          |  |                                   | <b>5b. GRANT NUMBER</b>                         |   |
|  |                          |  |                                   | <b>5c. PROGRAM ELEMENT NUMBER</b>               |   |
| <b>6. AUTHOR(S)</b><br>Lieutenant Colonel David Smith<br>United States Air Force   |                          |  |                                   | <b>5d. PROJECT NUMBER</b>                       |   |
|  |                          |  |                                   | <b>5e. TASK NUMBER</b>                          |   |
|  |                          |  |                                   | <b>5f. WORK UNIT NUMBER</b>                     |   |
| <b>7. PERFORMING ORGANIZATION NAME(S) AND ADDRESS(ES)</b><br>Colonel Timothy Frantz<br>Department of Military Strategy, Planning, and Operations   |                          |  |                                   | <b>8. PERFORMING ORGANIZATION REPORT NUMBER</b> |   |
| <b>9. SPONSORING/MONITORING AGENCY NAME(S) AND ADDRESS(ES)</b><br>U.S. Army War College, 122 Forbes Avenue, Carlisle, PA 17013   |                          |  |                                   | <b>10. SPONSOR/MONITOR'S ACRONYM(S)</b>         |   |
|  |                          |  |                                   | <b>11. SPONSOR/MONITOR'S REPORT NUMBER(S)</b>   |   |
| <b>12. DISTRIBUTION / AVAILABILITY STATEMENT</b><br>Distribution A: Approved for Public Release. Distribution is Unlimited.  |                          |  |                                   |   |   |
| <b>13. SUPPLEMENTARY NOTES</b><br>Word Count: 5,332  |                          |  |                                   |   |   |
| <b>14. ABSTRACT</b><br>The precedence of a military pension system was established in the colonies well before the birth of the United States and was modified throughout our country's history to accommodate economic realities, social norms and military requirements. Although the current system has enjoyed a period of relative constancy since 1980, massive federal debt and the threat that military compensation liability will consume the DoD budget compels exploration of cost reduction modifications. Within the DoD, the Defense Business Board and 10-15-55 initiatives propose to restructure the current system to reduce costs and realign it towards the private sector model. Although the 10-15-55 proposal is superior, it remains unaligned as it does not adequately consider existing educational benefits, strategic communications and professionalism aspects of the military profession. |                          |  |                                   |   |   |
| <b>15. SUBJECT TERMS</b><br>Military Compensation  |                          |  |                                   |   |   |
| <b>16. SECURITY CLASSIFICATION OF:</b>   |                          |  | <b>17. LIMITATION OF ABSTRACT</b> | <b>18. NUMBER OF PAGES</b><br>32                | <b>19a. NAME OF RESPONSIBLE PERSON</b>      |
| <b>a. REPORT</b><br>UU   | <b>b. ABSTRACT</b><br>UU | <b>c. THIS PAGE</b><br>UU                          |                                   |   | <b>19b. TELEPHONE NUMBER (w/ area code)</b> |



USAWC STRATEGY RESEARCH PROJECT

**Key Elements of Military Retirement System Modification**

by

Lieutenant Colonel David Smith  
United States Air Force

Colonel Timothy Frantz  
Department of Military Strategy, Planning, and Operations  
Project Adviser

This manuscript is submitted in partial fulfillment of the requirements of the Master of Strategic Studies Degree. The U.S. Army War College is accredited by the Commission on Higher Education of the Middle States Association of Colleges and Schools, 3624 Market Street, Philadelphia, PA 19104, (215) 662-5606. The Commission on Higher Education is an institutional accrediting agency recognized by the U.S. Secretary of Education and the Council for Higher Education Accreditation.

The views expressed in this student academic research paper are those of the author and do not reflect the official policy or position of the Department of the Army, Department of Defense, or the United States Government.

U.S. Army War College  
CARLISLE BARRACKS, PENNSYLVANIA 17013



## **Abstract**

Title: Key Elements of Military Retirement System Modification  
Report Date: 15 April 2014  
Page Count: 32  
Word Count: 5,332  
Key Terms: Military Compensation  
Classification: Unclassified

The precedence of a military pension system was established in the colonies well before the birth of the United States and was modified throughout our country's history to accommodate economic realities, social norms and military requirements. Although the current system has enjoyed a period of relative constancy since 1980, massive federal debt and the threat that military compensation liability will consume the DoD budget compels exploration of cost reduction modifications. Within the DoD, the Defense Business Board and 10-15-55 initiatives propose to restructure the current system to reduce costs and realign it towards the private sector model. Although the 10-15-55 proposal is superior, it remains unaligned as it does not adequately consider existing educational benefits, strategic communications and professionalism aspects of the military profession.



## **Key Elements of Military Retirement System Modification**

The realities of the recent recession, anemic recovery, high federal deficits, the acceleration accumulation of unprecedented government debt and dysfunctional fiscal policy have triggered a series of efforts to reduce costs within the Department of Defense (DoD).<sup>1</sup> These realities, and the combination of growing defense requirements and the increase in the percentage of the DoD budget claimed by pay and benefits, has resulted in two competing visions to realign the overall DoD fiscal strategy.<sup>2</sup> These competing strategies seek to reduce risk and restore feasibility by restructuring the military retirement system to reduce costs. An examination of the Defense Business Board (DBB) and 10-15-55 proposals reveals that the 10-15-55 proposal is superior as it would produce greater DoD savings while preserving more value for service members.<sup>3</sup> Despite its current advantages, the 10-15-55 proposal could be improved if modifications were made to better accommodate the elements of education benefits, strategic communications and professionalism.

### **Background on the U.S. Military Retirement System**

The payment of pensions to disabled and retired military personnel predates the U.S Constitution and has evolved to meet the needs of our country. In the early days of the American colonies, legislatures created provisions to pay pensions to men who were injured defending colonists and their property from native uprisings.<sup>4</sup> This system was continued by the Continental Congress, which established a pension for its army and naval forces on August 26, 1776.<sup>5</sup> One of the first major internal challenges to the American Republic was the Newburgh Conspiracy, which occurred after the victory at Yorktown but prior to the formal end of hostilities with Great Britain. During this episode, a number of General Washington's officers met to discuss military solutions to

congressional inaction regarding military salaries, bounties and pensions. This potential challenge to the subordination of the military to Congress was resolved by the intervention of General Washington through a personal address to his officers:

And let me conjure you, in the name of our common country, as you value your own sacred honor, as you respect the rights of humanity, and as you regard the military and national character of America, to express your utmost horror and detestation of the man who wishes, under any specious pretenses, to overturn the liberties of our country, and who wickedly attempts to open the floodgates of civil discord and deluge our rising empire in blood.<sup>6</sup>

The issue of these payments was later resolved through partial payments after the constant petitioning of Congress by General Washington.<sup>7</sup> Although pension provisions were frequently modified over the years, one of the most notable issues was the differences between the source of funding between the Army and Navy systems. From its inception during the American Revolution, Navy pensions were financed with monies acquired from the sale of captured prizes, making revenue availability erratic with the fortunes of war and peace.<sup>8</sup> To better manage these monies, Congress established a Navy Pension Fund in 1800 and allowed trustees to invest in a wide range of assets, to include private equities. This investment in private equities later proved to be disastrous, as all the companies that the fund invested in went bankrupt, these investment choices were likely influenced by political pressure.<sup>9</sup> In contrast, the Army Pension System was always financed directly from general revenues on a pay-as-you-go basis and was therefore much more stable regarding revenue availability.<sup>10</sup>

The concept of voluntary military retirement was formalized in 1885 for enlisted personnel and in 1861 for officers. In 1916, the concept of an up-or-out selective promotion plan, based on age, was introduced. This provision was later modified with a service-in-grade standard in 1926. During the post World War I period, numerous

changes were made to balance personnel requirements in the wake of massive personnel reductions following the war. The next major change to the system was the Army and Air Force Revitalization and Retirement Equalization Act of 1948, which established uniform authorities for voluntary retirement for officers of all services. This was the last change prior to the Department of Defense Authorization Act of 1981 which established the basis for the current military retirement system.<sup>11</sup> This short history illustrates that although our country has a long history of a military retirement system, it is in a constant state of modification to align with larger fiscal and national requirements.

### The Current Retirement System

Currently, there are three active duty military retirement systems. All three systems require a minimum of 20 years of service to be eligible. The first system is called “Final Pay” and applies to personnel that entered service prior to September 8, 1980. This system calculates retirement pay by a multiplier of 2.5% of base pay for each year of service, to a maximum of 75% (see figure 1). The individual’s last month of base pay is used for this calculation. Additionally, there is an annual cost of living adjustment (COLA) that is added to the retirement pay annually that is based on the consumer price index (CPI).<sup>12</sup>

Table 1. Final Pay<sup>13</sup>

|  | Final Pay |       |     |       |     |       |     |       |     |       |     |
|--|-----------|-------|-----|-------|-----|-------|-----|-------|-----|-------|-----|
| Years of Service                           | 20        | 21    | 22  | 23    | 24  | 25    | 26  | 27    | 28  | 29    | 30  |
| Base Pay                                   | 50%       | 52.5% | 55% | 57.5% | 60% | 62.5% | 65% | 67.5% | 70% | 72.5% | 75% |
| Base pay is based on the last month of pay |           |       |     |       |     |       |     |       |     |       |     |
| Annual COLA increase is base on CPI        |           |       |     |       |     |       |     |       |     |       |     |

The second two systems apply to military members entering service on or after September 8, 1980. The “High-36” system is identical to the “Final Pay” system, with the

exception that it uses an average of the last 36 months of base pay to calculate retirement pay (see figure 2). The “REDUX” system, which is a voluntary alternative of the “High-36” system, calculates retirement pay by a multiplier that is reduced by 1% for each year less than 30 that the individual has served at retirement (see figure 3). There are two additional differences to the “REDUX” plan. The first is that it provides a \$30,000 bonus at 15 years of service. Additionally, the COLA is calculated at 1% below the CPI.<sup>14</sup>

Table 2. High-36<sup>15</sup>

|  | High-36 |       |     |       |     |       |     |       |     |       |     |
|--|---------|-------|-----|-------|-----|-------|-----|-------|-----|-------|-----|
| Years of Service   | 20      | 21    | 22  | 23    | 24  | 25    | 26  | 27    | 28  | 29    | 30  |
| Base Pay   | 50%     | 52.5% | 55% | 57.5% | 60% | 62.5% | 65% | 67.5% | 70% | 72.5% | 75% |
| Base pay is based on the average highest 36 months of base pay |         |       |     |       |     |       |     |       |     |       |     |
| Annual COLA increase is base on CPI                            |         |       |     |       |     |       |     |       |     |       |     |

Table 3. Redux<sup>16</sup>

|  | Redux  |       |     |       |     |       |     |       |     |       |     |
|--|--|-------|-----|-------|-----|-------|-----|-------|-----|-------|-----|
| Years of Service   | 20   | 21    | 22  | 23    | 24  | 25    | 26  | 27    | 28  | 29    | 30  |
| Base Pay   | 40%  | 43.5% | 47% | 50.5% | 54% | 57.5% | 61% | 64.5% | 68% | 71.5% | 75% |
| Member receives \$15,000 bonus at 15 years of service          |  |       |     |       |     |       |     |       |     |       |     |
| Base pay is based on the average highest 36 months of base pay |  |       |     |       |     |       |     |       |     |       |     |
| Annual COLA increase is base on the CPI -1%                    |  |       |     |       |     |       |     |       |     |       |     |
| At age 62:   | 1. Base pay percentage permanently reverts to the "High-36" model  |       |     |       |     |       |     |       |     |       |     |
|  | 2. One-time CPI "catch-up" restores retirement pay to the "High-3" model but continues at CPI -1% thereafter |       |     |       |     |       |     |       |     |       |     |

In addition to these three defined benefit retirement systems, the National Defense Authorization Act for Fiscal Year 2001 authorized military members to voluntarily participate in the Thrift Savings Plan (TSP), which was originally intended for federal civilian employees. For military personnel, this provided the opportunity to save pre-tax income in a non-matching 401K-type plan to enhance their retirement savings.<sup>17</sup> The Thrift Savings Plan Enhancement Act of 2009 added provisions that allow “Roth” contributions (after tax contributions that grow and are withdrawn tax free).<sup>18</sup>

In December of 2013, Congress passed a budget proposal that included a provision that would reduce the COLA portion of the retirement calculation to 1% below the CPI from initial retirement until the age of 62 for all current and future military retirees. The provision also specifies that at age 62 retirees would receive a one-time catch up in their retirement pay that would restore it to what it would have been if they had received the full CPI during this period and all future COLA payments would be at the full CPI. This proposal is not scheduled to take effect until 2015. At the time of this writing, this proposal had not yet become law.<sup>19</sup>

### Recent Proposals to Military Retirement Modification

#### The Defense Business Board Proposal

In May of 2010 the Secretary of Defense tasked the DBB to review DoD policies and practices and to identify options to reduce costs. As part of this initiative, a Task Group was commissioned to assess the military retirement system and develop alternatives to reduce costs while still recruiting and retaining high quality personnel. In July of 2011 the Defense Business Board submitted their report to the Secretary of Defense which was entitled “Modernizing the Military Retirement System.”<sup>20</sup>

The DBB report was based on interviews with senior leaders from the military and other governmental departments as well as defense attaches from France and Canada. It also utilized analyses, studies and recommendations generated by government and private research on this subject over the last 30 years.<sup>21</sup>

This report contained three basic findings. This first finding is that the military retirement system is outdated. Specifically, it was designed when life spans were shorter, military pay was not competitive with civilian pay and when military skills were not easily transferred to the private sector.

The second finding is that the retirement system is more generous and expensive compared to the private sector. Specifically, retirement contributions are 10 times greater for military retirees than in the private sector. The expense issue is exacerbated by the fact that these defined benefits will likely be paid for 40 year for only 20 year of service. Conversely, military retirees will likely have a second career and their military skills are transferrable to the private sector.<sup>22</sup> The third finding is that the retirement system is inflexible. Specifically, the system is unable to be leveraged during downsizing and does not compensate those in high risk situations or circumstances (e.g., combat duty, family separation, etc...).<sup>23</sup>

The report also contained three assessments based on these findings. The first assessment is that the military retirement system is unfair. Specifically, the system is vested only with personnel that serve a minimum of 20 years (only 17% of those who serve receive a retirement benefit). Therefore, most of the personnel that have engaged in combat will not receive any retirement benefit. Additionally, there is no difference in retirement benefits between those who have served in high risk activities and those who have not.<sup>24</sup>

This second assessment is that the retirement system is unaffordable. The current liability for the system is \$1.3T however, if current rates of growth continue, this amount is projected to grow to \$2.7T by FY34.<sup>25</sup> Although these numbers are alarming, a more insightful illustration can be seen in the growth of retirement costs as a percentage of the DoD budget. Assuming a static DoD budget of \$600B, annual retirement obligations would increase from 9% to 20% of the DoD budget by 2035.<sup>26</sup> It is

this analysis that lead to the DBB to conclude that retirement costs, if not changed, will undermine future warfighting capabilities.<sup>27</sup>

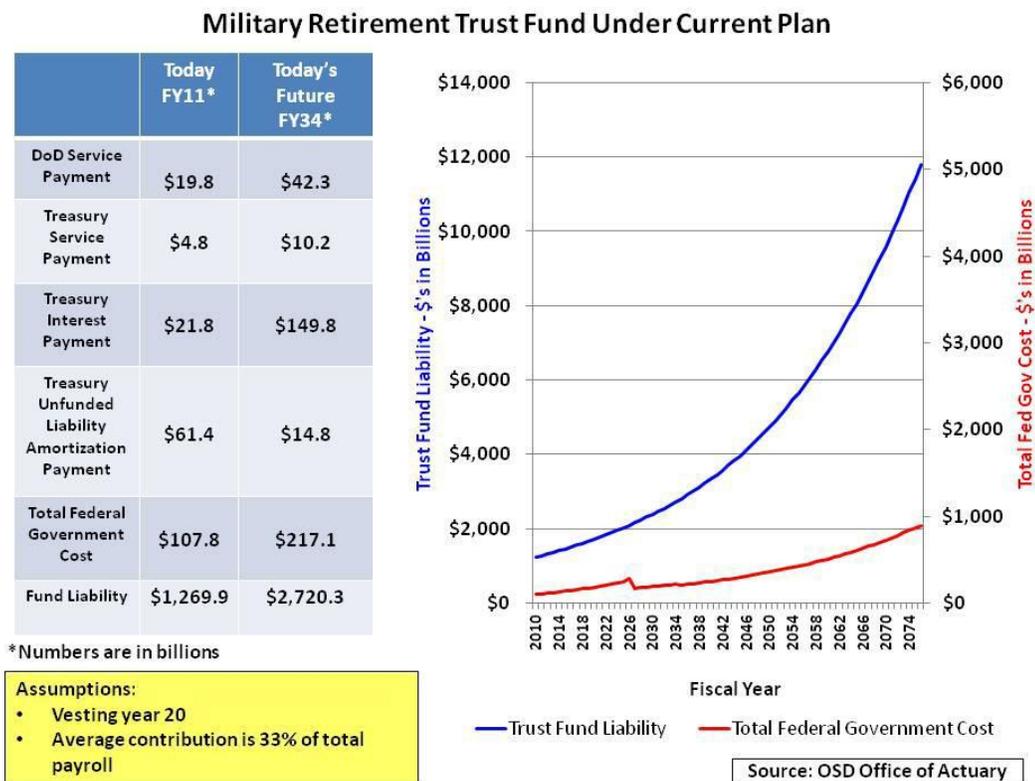


Figure 1. Military Retirement Trust Fund<sup>28</sup>

The third assessment is that the retirement plan is inflexible. The report documents that because retirement vestiture does not occur until the 20 year point, only 7% of personnel leave the military between the 15<sup>th</sup> and 20<sup>th</sup> year of service compared to 76% that leave between the 20<sup>th</sup> to 25<sup>th</sup> years. The report also reiterates that the member’s career risk profile has no bearing on their retirement benefit, years served is the only factor considered. The combination of these factors precludes the use of the retirement system as an effective force shaping tool.<sup>29</sup>

The DBB report also proposes a new military retirement plan intended to enhance fairness and flexibility and provide a more affordable cost structure. This plan

includes a menu of options to include the restructure the current defined benefit plan with a 2.0 multiplier (40% of base pay at 20 years to be increased by 2.0% for each additional year) with the initiation of benefit pay-out starting at age 67. Options also include a transportable defined contribution component utilizing the TSP. This account would include a government contribution comparable to the highest end of private sector pension plans. The TSP component would vest after 3 to 5 years and be payable at age 60-65 with provisions for partial withdraws (or loans) to cover education, healthcare or other specified emergencies. Additionally, government TSP contributions would be doubled for years in combat zones or high risk positions and would have a higher rate during hardship tours. Another option includes calculating retirement pay using an average of the last five years of base pay. The final option is a transition pay for departing service members that have at least four years of service. The value would be equal to the highest month's salary multiplies by years of service.<sup>30</sup>

Although the report does not make a recommendation regarding the timing of the transition to the new system, it provided two sets of data for projected savings. The first option included a grandfather provision for all current military personnel. The second option was for a rapid transition with no grandfather provision for current military personnel. The DBB claims a potential cost savings of \$920 billion under the grandfather plan and \$1.5 trillion under the rapid transition plan (2034 dollars) while reducing the value of the retirement benefit to service members by 39%.<sup>31</sup>

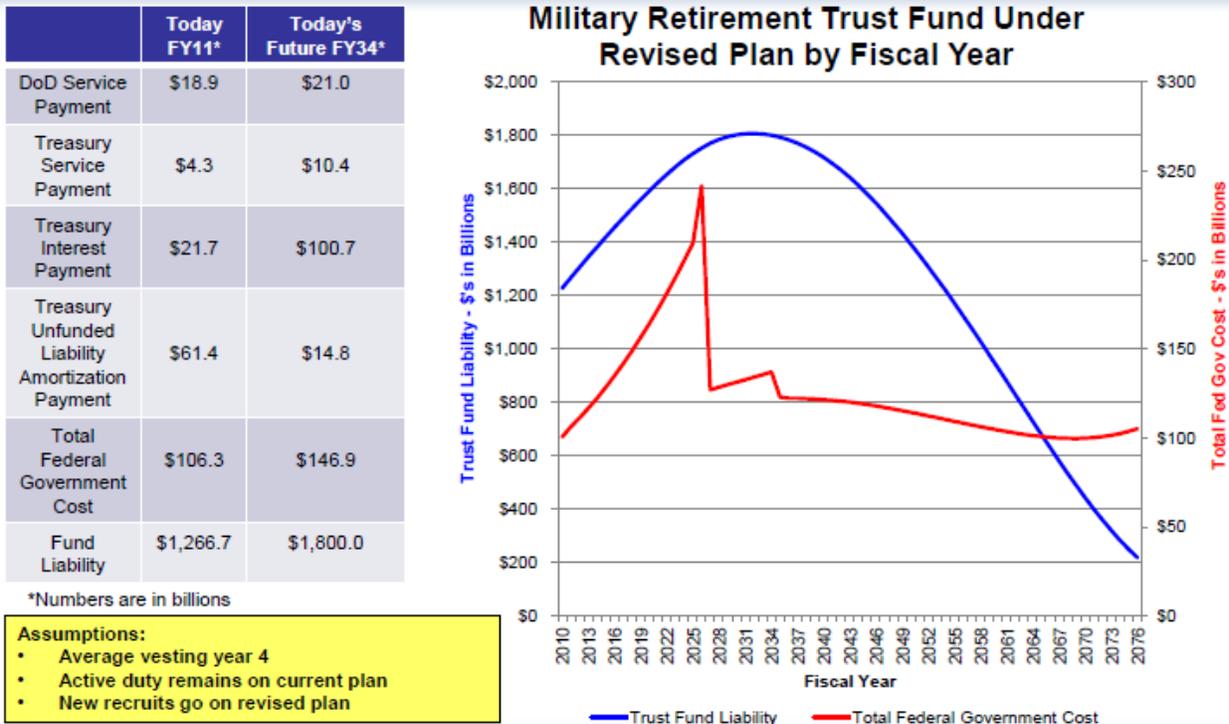


Figure 2. Military Retirement Trust Fund<sup>32</sup>

### The 10-15-55 Proposal

In 2013, the Strategic Studies Institute of the U.S. Army War College released a counterproposal to the DBB report entitled *A Framework for Restructuring the Military Retirement System*; entitled the 10-15-55 plan. This proposal was designed to address four key areas unique to military manpower requirements: personnel inventory, service member well-being, public perception and cost.<sup>33</sup>

The proposal contends that the issue of personnel inventory can be addressed by adding a portable retirement benefit to the system. The proposal further argues that because the current system does not provide vestiture until 20 years of service, retention of personnel with 10 to 20 years of service is viewed as obligatory because involuntary separation would leave the service member with no retirement benefit with only several years until retirement eligibility. Therefore, the addition of a portable benefit

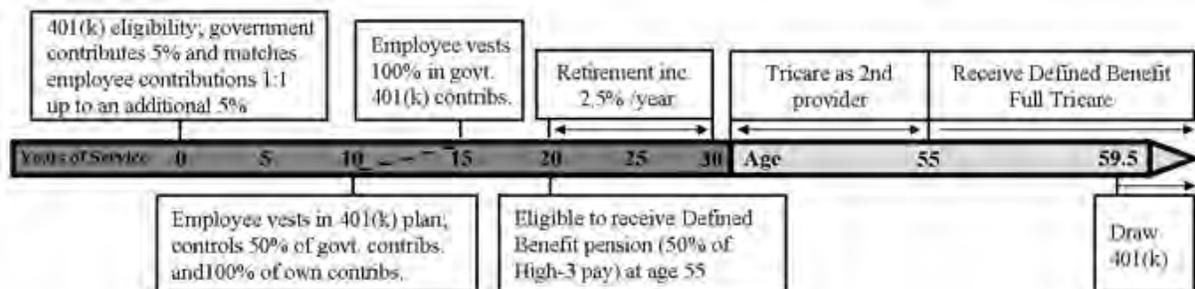
would make the retirement system more conducive for force shaping personnel between the 10 and 20 year point.<sup>34</sup> This was also one of the assessments in the DBB report.

Regarding service member well-being, the proposal asserts that the cost saving modifications to the system should be structured to minimize the risk to the service member. Specifically, the combination of a defined benefit and defined contribution system should be structured to mitigate the inherent risks of market volatility, remaining employed while aging, outliving retirement savings and guard against behavioral tendency to over consume.<sup>35</sup>

The issue of perceptions can be described as strategic communications to both internal (service member) and external (general public) audiences. The proposal contends that any attempt to modify the military retirement system must pass a minimum acceptable opinion threshold with these two audiences. One of the key aspects of this for this test is the inclusion of a grandfather clause. Any immediate modification of the retirement system that reduces benefits would be viewed as a breach of the social contract between the Nation and its service members; and unlikely to pass the minimum acceptable threshold. The second key aspect is simplicity. Although any reduction of benefits will result in disappointment by service members, replacing it with a system that is difficult to explain or understand will exacerbate the dissatisfaction and add an element of suspicion.<sup>36</sup>

The final key area is cost. Although the counterproposal does not go into as much detail regarding this aspect, it agrees with the DBB's conclusion that current military retirement system is unaffordable.

The 10-15-55 plan included the following provisions. First, it would keep the defined benefit component of the current retirement system (using a 2.5% multiplier and the average of the last 36 months of base pay) with only one change. This change is the delay of benefit payout until retirees reach the age of 55. Like the DBB proposal, it would also add a 401K-type of defined contribution component utilizing the TSP. This account would be established upon entry into military service. The government would automatically contribute the equivalent of 5% of base pay into the account and would contribute 1-for-1 matching on service member contributions, up to an additional 5%. Although the management of the TSP account would always be controlled by the service member and he would always control 100% of his contributions, vestiture of the government contributions would be phased in. After 10 years of service the service member would control 50% of the government contributions. This percentage would be increased by 10% each year so that the service member would control the entire value of the account at 15 year of service. Another provision of the plan is that the military health insurance coverage would only be available as a second provider from retirement until age 55. This plan included a grandfather clause for current service members or retirees.<sup>37</sup> The final provision of the 10-15-55 plan is transition pay. This benefit would be paid to service members who have severed 20 years or more. The value of this benefit would equal six months of pay.<sup>38</sup>



### Figure 3. The “10-15-55” Proposal<sup>39</sup>

Regarding implementation, the 10-15-55 counterproposal is more evolutionary than the DBB proposal. Specifically, it includes a grandfather clause for all current service members as well as an option for a phase-in period when incoming service members can choose between the old plan and the new 10-15-55 plan.<sup>40</sup> The counterproposal claims a potential cost savings of \$3.84 billion (2034 dollars) while reducing the value of the retirement program by 25%. This exceeds the cost savings of the DBB proposal by \$190 million while preserving 15% more value to service members.<sup>41</sup>

The primary difference between the cost savings between the two plans is due to the age difference at which retirees receive pension benefits (age 67 for the DBB plan compared to age 55 for the 10-15-55 plan), the timing for vestiture of the defined contribution benefits (TSP accounts) and the vestiture and amount of transition pay. Although both proposals realize savings from reductions in contributions to the pension fund, these savings will be offset by TSP contributions and transition pay. The DBB will pay higher amounts to more service members than the 10-15-55 plan, resulting in the higher costs.<sup>42</sup> These additional costs can be attributed to the DBB’s attempt to make the retirement system fairer by shifting the reduced benefits to those who serve less than 20 years.<sup>43</sup>

#### Analysis

##### Key Elements

Although there are distinct differences between the DBB and 10-15-55 proposals, they both adequately address the primary issue of cost but fail to appropriately address

several key elements. These include educational benefits, strategic communications and professionalism. Although not a retirement benefit, educational benefits provide a significant opportunity for service members to prepare for future employment regardless of when they leave the military. I believe that these benefits, if fully funded, preclude the need for retirement funds to be used for transitional pay. Proper strategic communications is needed to maintain a realistic focus on public and service member perceptions of new proposals, maintain a holistic approach to change and educate service members on their responsibilities within a defined contribution system. Lastly, these plans need to prevent an incipient shift from our current professional military model to an occupational model.

#### Educational Benefits

Included within both solutions sets is a transition from defined benefit to defined contribution via the TSP. In addition to simply reducing costs, this shift provides more fiscal agility within the DoD budget by reducing the accrual costs of the current defined benefit system. In other words, by increasing the percentage of benefit provided through the TSP, less money needs to be appropriated and managed to ensure adequate funds are available for future inflation adjusted payments over the lifetime of each service member.

The shift from defined benefits to defined contributions also increases the commonality and transportability of the military retirement system to the private sector systems regardless of the time that the service member stays in the military. In addition to cost reduction, the DBB plan justifies this shift through its assessment that the current retirement system is unfair, outdated and inflexible. Specifically, those who serve less than 20 years do not receive any retirement benefit. Thus, both proposals attempt to

spread reduced benefits to more service members and make the military retirement system more similar to, and thus more compatible with, private sector plans. I believe that both proposals overestimate the degree of inequality of the current system and add a superfluous transition benefit by not considering nonretirement educational benefits such as tuition assistance and the 9/11 G.I. Bill.

Although there is some variation in the execution of the tuition assistance program among the services, the program pays for 100% of tuition and fees of service members (up to \$250 per semester hour) for all higher level degrees that the service member has not yet achieved. It should also be noted that the tuition assistance program also has immediate vestiture.<sup>44</sup> The tuition assistance program, which was created in the 1940s, was at risk of not being funded in the fall of FY13 due to sequestration cuts.<sup>45</sup> In FY14 the Army and Air Force have instituted some limitations on the amount and tempo of benefits to limit costs while the Navy has fully funded the program with no new limitations.<sup>46</sup> This benefit provides service members with the ability to increase their education level prior to departing the military, making them more marketable after their departure.

The 9/11 G.I. Bill, which was signed into law in July of 2008, provides a significant transportable nonretirement education benefit to military members with a phased in vestiture that starts after 90 days of active service with full benefits being earned after three years of active service.<sup>47</sup> This benefit also includes the ability to transfer the benefit to their spouse or child once they have served six years with the stipulation that they serve an additional four years.<sup>48</sup> Benefits at full vestiture include full payment of tuition and fees for in-state students for four academic years (with a cap of

\$19,198 per term for private or foreign schools), a monthly housing allowance (based on E-5 with dependent military housing rate for the location of the school) and a book/supply stipend of up to \$1000 per academic year. In addition to institutions for higher learning, the benefit may also be used for non-degree institutions, apprenticeships, national testing programs, licensing and certification exams, and vocational flight schools.<sup>49</sup>

In light of tuition assistance and 9/11 G.I. Bill nonretirement benefit programs, I believe that the DBB and 10-15-55 proposals overemphasize the need for separation pay for military members. Although an important issue, it is adequately covered by existing nonretirement programs. Additional expenditures on this requirement risks further diluting shrinking retirement benefit resources. I believe a more appropriate approach would be to exclude separation pay from the proposed mixture of the defined benefit and defined contribution plans.

#### Strategic Communications

The designers of both the DBB and 10-15-55 proposals correctly communicate the need for cost reduction of the military retirement system. The driver is the preservation of our national security through overall U.S. deficit and debt reduction, and more specifically, the reduction of retirement costs as a percentage of the overall DoD budget. Although it would be inappropriate for the military leadership to shift cost reduction discussions to federal expenses outside the DoD such as MEDICARE, MEDICAID and Social Security, senior leaders should maintain a political awareness of the limited affect that military retirement benefit reduction can have on the preservation of national security through cost reductions in the overall federal budget.<sup>50</sup>

The 10-15-55 plan correctly identifies the importance of strategic communications towards the various audiences regarding changes in military compensation. Public perception of the service members has remained very positive and the awareness of the sacrifice that service members and their families have endured over the last decade is widely empathized with. Any attempt to significantly reduce benefits could trigger opposition from a combination of the public and media as well as inherent political interests.<sup>51</sup> However, timing will be crucial as the perception of service members has, and will continue to, experienced dynamic changes. Changes to this perception could be affected by more than sacrifices from the current conflicts. A new recession, high inflation, resurgence of high unemployment or even the prolonged continuation of the current anemic economic recovery could significantly alter public perceptions of “fair” compensation of service members in light of economic conditions.

Another important audience is service members. Although service members are not decision makers regarding changes to the system, they will need to be influenced to make appropriate decisions in any plan that requires voluntary participation. This is required both for their personal well being in addition to being able to show proposal success. Under the current retirement system, participation in the TSP is voluntary. Although a significant benefit, service member participation in this plan is only 29%.<sup>52</sup> There are two basic options for increasing participation. These options are mandatory participation and voluntary participation. Although mandatory participation precludes the risk of service members not investing in the TSP, there is a risk of a negative perception of the proposal if service members do not understand and appreciate the reason why their pay is being involuntary diverted to a retirement account. Voluntary participation in

the TSP carries the risk of service member nonparticipation due to shortsightedness or a failure to understand the time value of money.

Regardless of the participation method selected, appropriate and synchronized strategic communication, as well as education, will be critical to service member success as well as a positive public perception of the proposal. Education will need to effectively communicate the time value of money, basic risk/reward investment theory, diversification and the propensity to over consume and underestimate retirement costs. For voluntary participation, this education should be universal upon service entry and be periodically reinitiated with service members that do not participate and be modified for their specific demographic circumstances.

Another important issue that would need to be addressed in any new retirement system is whether or not to include a grandfather clause for service members currently serving or already retired. The DBB proposal includes both options while the 10-15-55 plan specifies the inclusion of a grandfather clause. Although it may appear that this decision should be primarily driven from a cost perspective, strategic communications would also be an important driver for this decision. In a recent survey, 45% of military families polled said they would be “extremely” or “very” affected by planned cuts in the military retirement system. Additionally, reduced retirement benefits were the top concern for 32% of respondents, which is double the percentage from the previous year.<sup>53</sup>

Changes, or even proposals to change the military retirement system, could trigger significant unintended consequences to force structure, particularly now that not grandfathering current service members is being considered. This issue is exacerbated

by the piecemeal process by which retirement modification is being pursued. Although the 2013 DoD Budget requests that Congress establish a commission to review military retirement system in the context of overall military compensation, Congress recently approved a budget provision to reduce military retirement COLA payments independent of the commission.<sup>54</sup> Although increased separations due to retirement system modification may not be perceived as a minor risk due to proposed force reductions, required force levels can be quickly and dramatically changed due to geopolitical events which we have little to no control.

### Professionalism

One of the most important considerations that can easily be overlooked by the magnitude of the fiscal issues and the mechanics of the individual proposals is the perception of the military institution. The military is perceived as a profession by both those within it as well as those that it serves. In a 2013 Gallup poll that quantified confidence that the American people have in institutions, the military ranked at the top of the list with 76% of those polled responding that they have either “a great deal” or “quite a lot” of confidence in the military.<sup>55</sup> Although this perception is positive, it is by no means permanent. The professionalism of the military is perishable and must be continuously cultivated to endure. Both the changes made to the military retirement system as well as the role that the military plays in the process could incipiently erode this essential aspect of the military institution.<sup>56</sup>

General Martin Dempsey, Chairman of the Joint Chiefs of Staff, defines key military professional attributes as knowledge, skills, attributes and behaviors. He also describes trust as a key strength of our collective character, both internal and external. One crucial aspect of the trust between the American people and the military is the

expectation that the military remain apolitical. The issue of reducing military benefits is obviously an important and personal issue for every service member. There are also a number of political interest groups that will seek to engage on behalf of service members. It is appropriate for the military, as an institution, to be involved in the process. However, maintaining objectivity, refraining from self-interest, a judicious choice of messaging and the medium of engagement will be crucial to maintaining the trust of the American people and preserving the professionalism of the military institution. Maintaining this balance will be much more difficult if the changes to the retirement system are retroactive.<sup>57</sup>

In addition to the role that the military plays in this process, the actual changes could also erode the perception of the military as a profession. Both the DBB and 10-15-55 plan advocate moving towards a retirement system that is similar to the private sector model, specifically the TSP defined contribution plan. Although a transition to this model supports the goals of reducing costs, spreading benefits to service members that serve less than 20 years and making military compensation more compatible with private sector employment, it also incipiently shifts the military from a professional to an occupational model. This is done by shifting away from a traditional defined benefit to a contractual exchange of labor for monetary compensation.<sup>58</sup>

The importance of maintaining the professional perception and expectations for the military is best conveyed in an examination of the basic purpose of the military, which is the sectioned use of lethal force on the behalf of the American people.<sup>59</sup> This basic purpose combined with the fact that service members are entrusted with the lives of the nation' sons and daughters as well as the sovereignty and reputation of the

country demands the full spectrum of professional qualities.<sup>60</sup> These include the pursuit of a higher purpose that transcends individual self-interests, specialized expertise, autonomy, self-sacrifice, stewardship and self-regulation.<sup>61</sup> These qualities are obviously more desirable than that of an occupation, which is basically a contractual exchange of labor for benefit based on self-interest.<sup>62</sup> This larger issue of the professional expectations of the military institution should not be overlooked during the design of a new retirement system due to the immediacy of fiscal issues.

### Conclusion

The U.S. military retirement system has been evolving since its inception. These changes have accommodated economic realities, social norms and military requirements. The countries' current fiscal challenges require significant reduction in expenditures and the DoD will play an important role. The aggregate cost of military compensation, and its percentage within the overall DoD budget, must be reduced to preserve the fiscal initiative required to ensure our national security. The DoD must be proactive in its attempts to influence proposals to preclude the negative unintended consequences of proposals that are myopically focused on cost reduction.

Although the 10-15-55 proposal is superior to the DBB proposal because it offers greater cost reduction while providing more value to service members, it fails to adequately address the key elements of educational benefits, strategic communications and professionalism. The 10-15-55 proposal misaligns resources by failing to account for the benefit that tuition assistance and the 9/11 G.I. Bill provides service members to prepare them for future employment. Although there is a logical division between educational and retirement compensation, the introduction of a separation pay to prepare retiring service members for future employment to the retirement compensation

system requires the inclusion of current educational benefits into the analysis. This misaligned emphasis on separation pay dilutes already constrained retirement compensation resources. Within the 10-15-55 proposal, separation pay resources should be applied to the pension benefit. Specifically, reducing the age at which service members start to receive their pension. In addition to better aligning financial resources, this change would help preserve the professional aspects of the military by emphasizing the distinct and uncommon pension benefit that represents the qualities of specialized expertise, autonomy, self-sacrifice, stewardship and self-regulation. The strategic communications aspect of the proposal needs to maintain a realistic focus on public and service member perceptions of a new system, maintain a holistic approach to modifications in today's dynamic environment and most importantly to educate service members on their responsibilities within the new system.

## Endnotes

<sup>1</sup> Peter G. Peterson Foundation, "Analysis of the President's Fiscal Year 2014 Budget," April 18, 2013.

<sup>2</sup> David Barno et al., "The Seven Deadly Sins of Defense Spending" *Responsible Defense Series*, June 2013, 6-7.

<sup>3</sup> Roy Wallace, David Lyle, and John Smith, *A Framework for Restructuring the Military Retirement System* (Carlisle Barracks, PA: U.S. Army War College, 2013), 20.

<sup>4</sup> Robert Clark, Lee Craig, and Jack Wilson, *A History of Public Sector Pensions in the United States* (Philadelphia: University of Pennsylvania, 2003), 1-3.

<sup>5</sup> "Pensions Enacted by Congress for American Revolutionary War Veterans," [http://cagensearch.com/American\\_Revolution/Pensions.html](http://cagensearch.com/American_Revolution/Pensions.html) (accessed 29 December, 2013).

<sup>6</sup> "Newburgh Address," <http://www.mountvernon.org/educational-resources/encyclopedia/newburgh-address> (accessed 29 December, 2013).

<sup>7</sup> Ibid.

<sup>8</sup> Clark, Craig, and Wilson, *A History of Public Sector Pensions in the United States*, 3.

<sup>9</sup> Ibid., 9.

<sup>10</sup> Ibid., 3.

<sup>11</sup> Bruce Breth, *An Historical Analysis and comparison of the Military Retirement System and the Federal Employee Retirement System*, Naval Post Graduate Thesis (Monterey, CA: Naval Postgraduate School), 38-44.

<sup>12</sup> *The Office of the Secretary of Defense Military Compensation Homepage*, <http://militarypay.defense.gov/pay/bp/index.html> (accessed 21 December, 2013).

<sup>13</sup> Ibid.

<sup>14</sup> Ibid.

<sup>15</sup> Ibid.

<sup>16</sup> Ibid.

<sup>17</sup> Ibid.

<sup>18</sup> *The Thrift Savings Plan Homepage*, <https://www.tsp.gov/representative/announcements/announcements.shtml> (accessed December 21, 2013).

<sup>19</sup> Jonathan Weisman, "Senate Ends Budget Debate, Clearing Way for Passage", *New York Times*, December 17, 2013.

<sup>20</sup> "Modernizing the Military Retirement System," briefing slides with scripted commentary, Washington, DC, July 21, 2011.

<sup>21</sup> Ibid.

<sup>22</sup> Ibid.

<sup>23</sup> Ibid.

<sup>24</sup> Ibid.

<sup>25</sup> Ibid.

<sup>26</sup> Thomas C. Fisher, *Judging Retirement Reform Using the Strategic Thinking Framework*, Strategy Research Project (Carlisle Barracks, PA: U.S. Army War College, June 21, 2012), 17-18.

<sup>27</sup> "Modernizing the Military Retirement System,"

<sup>28</sup> Ibid.

<sup>29</sup> Ibid.

<sup>30</sup> Ibid.

<sup>31</sup> Modernizing the Military Retirement System”; Wallace, Lyle, and Smith, *A Framework for Restructuring the Military Retirement System*, 9.

<sup>32</sup> “Modernizing the Military Retirement System.”

<sup>33</sup> Wallace, Lyle, and Smith, *A Framework for Restructuring the Military Retirement System*, 12.

<sup>34</sup> Ibid., 16.

<sup>35</sup> Ibid., 18.

<sup>36</sup> Ibid., 19-20.

<sup>37</sup> Ibid., 23-24.

<sup>38</sup> Ibid., 15.

<sup>39</sup> Ibid., 12.

<sup>40</sup> Ibid., 19-20.

<sup>41</sup> Ibid., 20.

<sup>42</sup> Ibid., 20-21.

<sup>43</sup> Ibid., 15.

<sup>44</sup> *Military.com Education Home Page*, <http://www.military.com/education/money-for-school/air-force-tuition-assistance.html> (accessed January 16, 2014).

<sup>45</sup> *Online Military Education Home Page*, <http://www.onlinemilitaryeducation.org/faq/what-does-the-future-look-like-for-military-tuition-assistance/> (accessed January 16, 2014).

<sup>46</sup> Jeff Schogol, “New Tuition Assistance Rules Beginning Oct 1,” *Air Force Times*, August 29, 2013; “Tuition Assistance Policy Changes New Years Day,” [http://www.army.mil/article/117569/FY14\\_tuition\\_assistance\\_policy\\_changes\\_New\\_Year\\_s\\_Day/](http://www.army.mil/article/117569/FY14_tuition_assistance_policy_changes_New_Year_s_Day/) (accessed January 20, 2014); Mark Faram, “Tuition Assistance to Stay the Course in Fiscal '14,” *Navy Times*, September 28, 2013.

<sup>47</sup> *Military.com Education Home Page*, <http://www.military.com/education/gi-bill/new-post-911-gi-bill-overview.html> (accessed January 16, 2014).

<sup>48</sup> *U.S. Department of Veterans Affairs*, [http://www.benefits.va.gov/gibill/post911\\_transfer.asp](http://www.benefits.va.gov/gibill/post911_transfer.asp) (accessed January 16, 2014).

<sup>49</sup> Ibid.

<sup>50</sup> Donald Marron, “America in the Red,” *National Affairs*, Spring 2010, 14.

<sup>51</sup> Wallace, Lyle, and Smith, *A Framework for Restructuring the Military Retirement System*, 8.

<sup>52</sup> Military.com, "Why do Members of the Military not Invest in the Thrift Savings Plan," <http://paycheck-chronicles.military.com/2010/08/12/why-do-members-of-the-military-not-invest-in-the-thrift-savings-plan/> (accessed January 17, 2014).

<sup>53</sup> "Budget Cuts Worry Military Families," *Financial Advisor*, January 15, 2014.

<sup>54</sup> Jonathan Weisman, "Senate Ends Budget Debate, Clearing Way for Passage", *New York Times*, December 17, 2013; U.S. Department of Defense, *Fiscal Year 2013 Budget Request*, (Washington, DC: U.S. Department of Defense, February 2013).

<sup>55</sup> "Robert Rubin's Graph(s) of the Year," *The Washington Post*, December 31, 2013.

<sup>56</sup> U.S. Joint Chiefs of Staff, *America's Military – A Profession of Arms*, White Paper (Washington, DC: U.S. Joint Chiefs of Staff), 1.

<sup>57</sup> *Ibid.*, 4.

<sup>58</sup> Charles Moskos, "The All-Volunteer Military: Calling, Profession, or Occupation?" *Parameters* 40, no. 4 (Winter 2010-11): 26.

<sup>59</sup> U.S. Department of the Army, *The Army Profession*, Army Doctrine Reference Publication No. 1 (Washington, DC: U.S. Department of the Army, April 10, 2013), 1-3.

<sup>60</sup> *Ibid.*, 2-4.

<sup>61</sup> Charles Moskos, "The All-Volunteer Military: Calling, Profession, or Occupation?" *Parameters* 40, no. 4 (Winter 2010-11): 24; U.S. Department of the Army, *The Army Profession*, 1-1-1-5.

<sup>62</sup> Moskos, "The All-Volunteer Military: Calling, Profession, or Occupation?", 25.