

July 2005

MILITARY PERSONNEL

DOD Needs to Improve the Transparency and Reassess the Reasonableness, Appropriateness, Affordability, and Sustainability of Its Military Compensation System



G A O

Accountability * Integrity * Reliability



Highlights of [GAO-05-798](#), a report to congressional committees

Why GAO Did This Study

Over the years, the Department of Defense's (DOD) military compensation system has become an increasingly complex and piecemeal accretion of pays, allowances, benefits, and special tax preferences. DOD leaders have expressed concern that rising compensation costs may not be sustainable in the future and could crowd out other important investments needed to recapitalize equipment and infrastructure. Given the looming fiscal challenges facing the nation in the 21st century, GAO believes it is time for a baseline review of all federal programs to ensure that they are efficiently meeting their objectives. Under the Comptroller General's authority, GAO (1) assessed whether DOD's approach to compensation provides adequate transparency over costs; (2) identified recent trends in active duty compensation, and how costs have been allocated to cash and benefits; and (3) reviewed how active duty servicemembers perceive their compensation and whether DOD has effectively explained the value of the military compensation package to its members.

What GAO Recommends

GAO is making a number of recommendations to improve the transparency, reasonableness, appropriateness, affordability, and sustainability of the military compensation system. DOD generally concurred with GAO's recommendations. www.gao.gov/cgi-bin/getrpt?GAO-05-798.

To view the full product, including the scope and methodology, click on the link above. For more information, contact Derek Stewart at (202) 512-5559 or stewartd@gao.gov.

MILITARY PERSONNEL

DOD Needs to Improve the Transparency and Reassess the Reasonableness, Appropriateness, Affordability, and Sustainability of Its Military Compensation System

What GAO Found

DOD's historical piecemeal approach to military compensation has resulted in a lack of transparency that creates an inability to (1) identify the total cost of military compensation to the U.S. government and (2) assess the allocation of total compensation investments to cash and benefits. No single source exists to show the total cost of military compensation, and tallying the full cost requires synthesizing about a dozen information sources from four federal departments and the Office of Management and Budget. Without adequate transparency, decision makers do not have a true picture of what it costs to compensate servicemembers. They also lack sufficient information to identify long-term trends, determine how best to allocate available resources to ensure the optimum return on compensation investments, and better assess the efficiency and effectiveness of DOD's current compensation system in meeting recruiting and retention goals. To address this and other major business transformation challenges in a more strategic and integrated fashion, GAO recently recommended the creation of a chief management official at DOD.

Transparency over military compensation is critical because costs to provide compensation are substantial and rising, with over half of the costs allocated to noncash and deferred benefits. In fiscal year 2004, it cost the federal government about \$112,000, on average, to provide annual compensation to active duty enlisted and officer personnel. Adjusted for inflation, the total cost of providing active duty compensation increased about 29 percent from fiscal year 2000 to fiscal year 2004, from about \$123 to \$158 billion. During this time, health care was one of the major cost drivers, increasing 69 percent to about \$23 billion in fiscal year 2004. In addition, military compensation is weighted more toward benefits compared with other government and private sector civilian compensation systems. Furthermore, less than one in five service members will serve 20 years of active duty service to become eligible for retirement benefits. Increasing compensation costs make the need to address the appropriateness and reasonableness of the compensation mix and the long-term affordability and sustainability of the system more urgent.

DOD survey results and analysis of GAO focus groups and survey data have shown that servicemembers are dissatisfied and harbor misperceptions about their pay and benefits in part because DOD does not effectively educate them about the competitiveness of their total compensation packages. About 80 percent of the 400 servicemembers that GAO surveyed believed they would earn more as civilians; in contrast, a 2002 study showed that servicemembers generally earn more cash compensation alone than 70 percent of like-educated civilians. Servicemembers also expressed confusion over aspects of their compensation, like retirement, and many complained that benefits were eroding despite recent efforts by Congress and DOD to enhance pay and benefits. By not systematically educating servicemembers about the value of their total compensation, DOD is essentially allowing a culture of dissatisfaction and misunderstanding to perpetuate.

Contents

Letter

Results in Brief	1
Background	4
DOD's Compensation System Lacks Transparency to Identify Total Costs and How Compensation Is Allocated	7
Heavy Reliance on Benefits May Not Be Appropriate for Meeting Key Human Capital Goals or Not Sustainable in the Long Term	8
DOD's Lack of an Effective Communication and Education Effort on Compensation Has Allowed Servicemembers' Misperceptions and Concerns about Their Compensation to Perpetuate	14
Conclusions	27
Recommendations for Executive Action	35
Matter for Congressional Consideration	37
Agency Comments and Our Evaluation	37

Appendixes

Appendix I: Scope and Methodology	42
Appendix II: Sample of a Personal Statement of Military Compensation	49
Appendix III: Comments from the Department of Defense	53
Appendix IV: GAO Contact and Staff Acknowledgments	56

Related GAO Products

Tables

Table 1: Total Costs to Provide Active Duty Servicemembers Compensation (Source and Types)	10
Table 2: Summary of Changes in Compensation Costs, Fiscal Years 2000 and 2004	19
Table 3: Composition of Focus Groups	46

Figures

Figure 1: Total Compensation Cost and Per Capita Cost for Fiscal Years 2000-2004	16
Figure 2: The Allocation of Cash, Noncash, and Deferred Compensation Costs per Active Duty Servicemember in Fiscal Year 2004	22
Figure 3: 2003 Mix Salary/Wages and Benefits in Civilian Compensation	24

Figure 4: Percent of Enlisted Personnel and Officers Who Serve a 20-Year Career	26
Figure 5: Reasons for Servicemembers' Dissatisfaction with Pay and Benefits	31

Abbreviations

DHP	Defense Health Program
DOD	Department of Defense
MEPS	Medical Expenditures Panel Survey
VA	Department of Veterans Affairs

This is a work of the U.S. government and is not subject to copyright protection in the United States. It may be reproduced and distributed in its entirety without further permission from GAO. However, because this work may contain copyrighted images or other material, permission from the copyright holder may be necessary if you wish to reproduce this material separately.



July 19, 2005

Congressional Committees

The military compensation system has had the same basic structure since the end of World War II, but over time, it has become a complex and piecemeal culmination and accretion of pay, benefits, and special tax preferences—each designed to meet a specific need in managing an evolving force. Today, the total military compensation package includes dozens of pays and allowances; several noncash benefits to take care of troops who, increasingly, are married with children; certain preferences; as well as lifetime retirement pay and health care for retirees and their families. Valuing military service is complicated. Serving in the military offers personal and professional rewards but also requires many sacrifices—frequent moves and jobs that are arduous and sometimes dangerous. Moreover, military culture is paternalistic, and servicemembers expect the United States to take care of them and their families as reward for their service. Since the late 1990s, the Department of Defense (DOD) and Congress have sought to improve military pay to make it more competitive. Congress has improved benefits by repealing the unpopular REDUX retirement system in 1999 and expanding health coverage to cover retirees and their families for life in 2002, among other enhancements.¹ Even with these efforts, however, reports of dissatisfaction with some pays and benefits among military members still abound, and public perceptions linger that enlisted military members and their families are living in poverty.

¹ The Military Retirement Reform Act of 1986, also known as REDUX, had changed the retirement system by (1) reducing the amount received at 20 years of service, (2) raising the growth in retired pay for each year served after 20 years of service, and (3) reducing the real value of retired pay in an inflationary environment.

In recent years, Congress has taken steps to fund enhanced compensation and benefit programs for active duty and reserve personnel at a time when many military personnel are spending months or years away from home, often in harm's way, as the nation is heavily engaged in the war on terrorism. Moreover, as of 2005 DOD's budget had grown to nearly half a trillion dollars, including supplemental funding to support activities related to fighting terrorism. In our recent report on the challenges facing the United States in the 21st century, we expressed concerns about whether the current trends are both affordable and sustainable.² Many federal programs—such as military compensation—were designed decades ago to address earlier challenges related to labor markets, security conditions, organizational structures, and compensation strategies of prior eras. Some DOD leaders have expressed similar concerns, specifically that the increasingly expensive compensation system could crowd out other important investments needed to recapitalize aging defense-related equipment and infrastructure. Moreover, DOD leaders are particularly concerned about the growth in compensation entitlements—such as health care and concurrent receipts for disability and retirement—that do not have a significant impact on recruiting and retention. In 2005, the compensation debate was reopened when mounting concerns within the department about the growth in compensation cost—and the limited management flexibility afforded by the current system—led the Secretary of Defense to form a committee to comprehensively assess the approach the department uses to compensate its personnel.

Given the nation's increasing fiscal imbalance, we believe it is time for a baseline review of all major federal programs and polices, including military compensation, to ensure that they are efficiently and effectively meeting their objectives and well adapted to 21st century realities. We recognize that this will not be a simple or easy process and careful consideration must be given to any compensation changes because the stakes are high. We are convinced, however, that this reexamination offers compelling opportunities to both redress our current and projected fiscal imbalance while better positioning government to meet the new challenges and changing expectations of the 21st century.

In light of the above and under the statutory authority of the Comptroller General, we (1) assessed whether DOD's current approach to military

² GAO, *21st Century Challenges: Reexamining the Base of the Federal Government*, GAO-05-325SP (Washington, D.C.: February 2005).

compensation provides adequate transparency over total costs to the federal government; (2) identified the recent trends in active duty military compensation costs, and how compensation has been allocated to cash and benefits; and (3) reviewed how active duty servicemembers perceive their compensation and whether DOD has effectively explained the value of the military compensation package to its members.

In conducting this review, we limited our scope to the compensation system for active duty military personnel. Numerous methods were used to gather and assess information for this work. We reviewed congressional justification budget books for DOD as well as the Department of Veterans Affairs (VA). We calculated the federal tax expenditure and accrual cost of some programs, such as those run by the VA. We conducted 40 focus groups with over 400 servicemembers across all four services and enlisted and officer pay grades at eight military installations in the continental United States. While the information from the focus groups is not generalizable to the entire DOD population of active duty servicemembers, it provides valuable context as to servicemembers' perceptions about their compensation and augments DOD survey findings. We reviewed DOD's Status of Forces survey data on satisfaction with compensation. The 2002 survey administered to over 30,000 servicemembers had a response rate of 32 percent. DOD has conducted and reported on research to assess the impact of nonresponse rate on overall estimates. It found that, among other characteristics, junior enlisted personnel (in pay grades E1 to E4), servicemembers who do not have a college degree, and members in services other than the Air Force were more likely to be nonrespondents. We have no reason to believe that potential nonresponse bias not otherwise accounted for by DOD's research is substantial for the variables we studied in this report. Therefore, we concluded the data to be sufficiently reliable for the purposes of this report. See appendix I for more detailed information on our scope and methodology. We conducted our review from August 2004 through May 2005 in accordance with generally accepted government auditing standards.

Results in Brief

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 to active duty servicemembers and (2) assess how compensation investments are allocated to cash, benefits, and deferred compensation. No single source exists to show the total cost of military compensation, and tallying the full cost required us to synthesize information from several different portions of the federal budget. In a typical civilian firm, managers know the costs of compensation among other costs, such as capital and technology, in order to make decisions on the most efficient and effective use of resources. Furthermore, federal accounting standards are aimed at providing relevant and reliable cost information to assist Congress and executives in making decisions about allocating federal resources. Therefore, we believe it is good business practice for decision makers to establish a foundation that provides them transparency over total compensation costs including the long-term cost and implications of current decisions. Without transparency, DOD and Congress do not have adequate visibility over a basic foundation of what it is truly costing the government to compensate servicemembers. Furthermore, they lack sufficient information to (1) identify long-term trends in costs, (2) determine how to best allocate resources to ensure the optimum return on compensation investments, and (3) assess the efficiency of the current compensation system on DOD's ability to meet recruiting and retention goals. This lack of transparency over the total military compensation costs is another indication that DOD needs a Chief Management Official (CMO)—a recommendation we recently proposed to address a range of business transformation challenges in a more strategic and integrated fashion.³

³ GAO, *Key Elements Needed to Successfully Transform DOD Business Operations*, GAO-05-629T (Washington, D.C.: Apr. 28, 2005).

The federal government's total costs to provide military compensation are substantial and rising, and 51 percent of the total compensation costs are allocated to noncash and deferred benefits. In fiscal year 2004, the federal government's total annual cost to provide military compensation was about, on average, \$112,000 per active duty servicemember (including enlisted and officer personnel) when compensation costs for cash, noncash, and deferred benefits are considered.⁴ Adjusted for inflation, total cost of compensation increased from about \$123 billion in fiscal year 2000 to \$158 billion in fiscal year 2004—about 29 percent. The main drivers in the growth of total compensation costs from fiscal years 2000 through 2004 included: (1) basic pay (from \$38.4 to \$47.4 billion, about 23 percent); (2) allowances for private housing (from \$7.3 to \$12 billion, more than 66 percent); and (3) health care benefits for current servicemembers, retirees, and dependents (from \$13.8 to \$23.3 billion, about 69 percent). Continued significant future increases in these costs, particularly health care, raise questions about the long-term affordability and sustainability of the system. For example, the Congressional Budget Office estimated that DOD could spend as much as \$52 billion annually on health care by 2020.⁵ Furthermore, the mix of compensation for servicemembers is weighted toward noncash and deferred compensation, with these types of compensation accounting for slightly over half of annual compensation costs in fiscal year 2004. This mix in compensation stands in contrast to private sector and federal civilian workforces, which typically receive one-third or less of their compensation in the form of benefits and deferred compensation. Furthermore, deferred compensation, like retirement pay, represents about a third of total military compensation costs, but less than one in five servicemembers will serve a full career and become eligible for active duty retirement pay and benefits. Given the rapid rise of compensation costs and the significant emphasis on noncash and deferred compensation, it is unlikely that DOD's current approach to compensation is reasonable, appropriate, affordable, and sustainable over the long term.

⁴ Our average costs of compensation includes cash (e.g., basic pay, housing allowance, and special tax preference), benefits (e.g., health care, education assistance), and deferred benefits (e.g., contributions to retirement pay) divided by the end strength. According to DOD, over 100,000 mobilized reservists have been paid out of active duty cash compensation since fiscal year 2002. If these personnel were included, the average cost would be about \$5,000 lower in fiscal year 2004.

⁵ Congressional Budget Office, *Growth in Medical Spending by the Department of Defense* (Washington, D.C.: September 2003).

According to recent DOD survey results, which were supported by our focus group analysis, some servicemembers are dissatisfied, and in some cases, harbor misperceptions about their pay and benefits in part because DOD does not effectively inform them about the competitiveness of their total compensation packages. It is industry best practice for employers to educate employees about the value of their compensation in terms of the pay and benefits they receive. We believe it is also important to inform employees on how their total compensation compares with the employment market. DOD's efforts to communicate pay and benefit information to servicemembers—mainly through Internet Web sites and distribution of annual earnings statements—have not positively influenced servicemembers' perceptions. Repeated DOD-wide surveys have consistently found that a high proportion—almost half of servicemembers in some cases—are dissatisfied with aspects of their compensation from basic pay to allowances for subsistence and housing. Furthermore, DOD officials acknowledge that servicemembers harbor misperceptions about their compensation. Our focus group findings, though not generalizable, corroborated these perceptions and revealed that servicemembers often misunderstood their compensation and harbored concerns about it. When we compiled the data from the survey administered during our focus group sessions, we found that about 9 in 10 participants underestimated the cost of their compensation packages, and 80 percent believed they would make more in a civilian job. However, a recent DOD-sponsored study showed that, on average, military cash compensation alone—not including benefits—was at the 70th percentile of like-educated civilians.⁶ Servicemembers participating in our focus groups also expressed confusion over certain aspects of their compensation, such as how their retirement system worked. We heard frequent complaints from senior enlisted servicemembers and officers that benefits were eroding, despite recent efforts to enhance benefits. This perception, as mentioned before, is in direct contrast to the reality that costs to compensate servicemembers have risen dramatically in recent years and benefits costs are projected to rise even more dramatically in the future. By not systematically informing servicemembers about the value of their total compensation, DOD is essentially allowing a culture of dissatisfaction and misunderstanding to perpetuate even though the department and Congress have made significant efforts in recent years to increase military compensation.

⁶ Office of the Under Secretary of Defense for Personnel and Readiness, *The Report from the Ninth Quadrennial Review of Military Compensation* (Washington, D.C.: May 2002).

We are making recommendations that should improve the transparency, reasonableness, and appropriateness of the military compensation system. In commenting on a draft of this report, DOD generally concurred with our recommendations.

Background

DOD is one of the nation's largest employers—employing approximately 1.4 million active duty military personnel and 1.2 million reservists. In addition, 2 million retirees receive pay and benefits from the department. DOD is also the largest employer and trainer of young adults in the United States, recruiting about 200,000 individuals into active duty in 2004—the majority of them recent high school graduates. Although DOD competes with academia and other employers for these qualified people, the military's distinctive culture and job experience are unique from any other government or private sector employer. To maintain national security, DOD must meet its human capital needs by recruiting, retaining, and motivating sufficient numbers of qualified people.

The Office of the Secretary of Defense, Personnel and Readiness is principally responsible for establishing active duty compensation policy. However, reservists fall under the active duty compensation policy if they have been mobilized for active duty. The department also sponsors regular studies on military compensation called the Quadrennial Review of Military Compensation—most recently completed in 2002—that typically focus on specific issues like flexibility in compensation. In 2005, the Secretary of Defense formed a committee to study military pay in order to seek ways to maintain a cost-effective, ready force. Although the structure of the military compensation system has been largely unchanged since the end of World War II, with the advent of the all-volunteer force in 1973, the system has been enhanced by adding various pays, benefits, and tax preferences over time. Currently, the system is a complex mix of pays, benefits, and tax preferences—about a third of which are deferred until after the completion of active duty service.

In the 1970s, DOD and Congress adopted the concept of “regular military compensation”—which is defined as the sum of basic pay, allowances for housing and subsistence, and the federal tax advantage⁷—to describe the foundation of servicemembers’ cash compensation which can be used to compare military and civilian pay.⁸ Basic pay—which is predicated on rank and tenure of service—is the largest component of regular military compensation. In addition to regular military compensation, there are over 60 authorized special and incentive pays—generally offered as incentives to undertake or continue service in a particular specialty or type of duty assignment—as well as the combat zone tax exclusion, which generally makes income earned while serving in a combat zone nontaxable.⁹ Furthermore, DOD offers a wide range of benefits, many of which are directed at members with family obligations. DOD believes benefits are central to morale and readiness as well as important in providing members with a quality of life to help cope with the sacrifices they make.

DOD’s Compensation System Lacks Transparency to Identify Total Costs and How Compensation Is Allocated

Decision makers in Congress and at DOD do not have adequate transparency over total costs for providing military compensation to active duty servicemembers in terms of how compensation is allocated in the near term, if compensation investments are cost effective in meeting recruiting and retention goals, how much changes to compensation will cost in the long term, and whether compensation costs are affordable and sustainable in the future. Lack of transparency over costs is in part due to the sheer number of pays and benefits that make up the military compensation system and to the lack of a single source to show total cost of compensation. Moreover, the lack of principles to guide military compensation policy is a long-standing problem for DOD.

⁷ The federal tax advantage is the additional income servicemembers would have to earn if their allowances for housing and subsistence were subject to federal income tax.

⁸ Pub. L. No. 93-419 (Sept. 1974).

⁹ The combat zone tax exclusion allows servicemembers to exclude income earned—including basic pay, bonuses, special pays, and allowances—for each month served in a designated combat zone. Servicemembers who serve a minimum of 1 day in a combat zone are eligible to receive the combat zone exclusion for the respective month. Enlisted members’ exclusions are not limited; however, officers can exclude up to the maximum earned by the highest enlisted member.

Cost of Compensation Is Scattered Across Many Budgets

A total cost to compensate servicemembers does not exist in a single source for decision makers to view, and transparency is further hindered by the sheer number and types of pays, benefits, and tax preferences in the military compensation system. Good business practice requires adequate transparency over investments of resources, especially in times of fiscal balance constraint. In a typical civilian firm, managers would know the costs of compensation among other investments, such as capital and technology, in order to make decisions on the most efficient use of resources because decision makers have to consider both the obvious and implicit costs of their actions. Furthermore, federal accounting standards are aimed at providing relevant and reliable cost information to assist Congress and executives in making decisions about allocating federal resources.¹⁰ Therefore, we believe it is good business practice for decision makers to establish transparency over total compensation costs, including the long-term cost implications of current decisions.

Because of the lack of a single source of compensation costs and the number and types of pays and benefits that combine to make up the compensation system, we had to gather information from multiple sources to compile our estimate of the total costs to provide military compensation. Funding for the numerous components of compensation resides in different budgets (see table 1). For example, the funding for cash compensation that servicemembers receive today, such as basic pay and housing allowance, are in DOD's military personnel budget. Despite its name, this title does not include all of the funding provided for military compensation and benefits. Funding for noncash benefits, such as health care and education assistance, is displayed partially in the department's Operation and Maintenance budget as well as in the VA's budget. And, deferred benefits like retirees' health care, which represent a significant portion of the costs of compensation, have long-term cost associations and are not adequately visible. Funding for military retirement is budgeted for on an accrual basis in the military personnel budget, as is health care for retirees over 65 years of age and their dependents.¹¹ However, health care

¹⁰ GAO, *Business Modernization: NASA's Integrated Financial Management Program Does Not Fully Address Agency's External Reporting Issues*, [GAO-04-151](#) (Washington, D.C.: Nov. 21, 2003). The Statement of Federal Financial Accounting Standards Number 4, Managerial Cost Accounting Standards, requires agencies to report the full cost of their programs in their general-purpose financial reports aimed at assisting congressional and executive decision makers in allocating federal resources.

¹¹ Accrual funding sets aside monies for future obligations.

funding for retirees less than 65 years of age and their dependents is appropriated annually in the Operation and Maintenance budget as part of the Defense Health Program. In addition to DOD's deferred benefits, some servicemembers are eligible for veteran's benefits after they leave the military. These benefits, such as health care, pensions, and other compensations, are funded annually through the VA's budget. Furthermore, the lost federal tax revenue—the federal tax benefit servicemembers' receive because part of their cash compensation is nontaxable—is not displayed in a DOD budget exhibit for decision makers to consider when assessing new proposals or changes to the compensation system. This amount is significant: we estimate that it totaled about \$6.4 billion in fiscal year 2004. Furthermore, we should note that our calculations underestimate the impact of compensation costs to the federal government annually, because we did not include significant outlays for the unfunded liabilities for current retirees' pay and health care benefits that are in the Department of the Treasury's annual budget, which totaled \$34.4 billion in fiscal year 2004. These unfunded liabilities are being paid out of current appropriations, because the government has not always set aside monies for future liabilities. In fact, the government did not start setting aside monies for retirement pay until fiscal year 1985 or for health care benefits for retirees until 2003.

Table 1: Total Costs to Provide Active Duty Servicemembers Compensation (Source and Types)

Federal department's budget and type of budget	Component of compensation
<p>DOD Military Personnel</p> <ul style="list-style-type: none"> • Contains all cash compensation received by servicemembers in their "pay check" while serving on active duty and some costs for benefits. 	<p>Cash components:</p> <ul style="list-style-type: none"> • basic pay • allowances for housing and subsistence • special and incentive pays • other allowances <p>Benefits:</p> <ul style="list-style-type: none"> • retirement pay accrual • health care accrual for retirees over 65 years of age • survivor benefits • death gratuities • other^a
<p>DOD Operations and Maintenance</p> <ul style="list-style-type: none"> • Contains a number of benefits available to active duty servicemembers and their dependents in various subcomponents, such as the Defense Health Program, Defense Commissary Agency, Department of Defense Education Activity, and the Morale, Welfare, and Recreation exhibit (OP-34). 	<ul style="list-style-type: none"> • DOD dependent schools (on-base schools) • morale, welfare, and recreation programs (i.e., child care and exchanges) • commissaries • health care for active duty servicemembers and their dependents • education benefits

(Continued From Previous Page)

Federal department's budget and type of budget	Component of compensation
DOD Future Years Defense Program (FYDP) <ul style="list-style-type: none"> • A planning document published by DOD; • Contains costs for upkeep and utilities costs for on-base family housing. 	<ul style="list-style-type: none"> • family housing upkeep and utilities • we were unable to identify similar costs for barracks (on-base housing for single servicemembers)
Department of Veterans' Affairs Budget <ul style="list-style-type: none"> • Although the VA's primary customers are retired or honorably discharged servicemembers, current active duty members are eligible for these education and home loan benefits.^b 	<ul style="list-style-type: none"> • Montgomery GI Bill (education benefit) • Guaranteed Home Loan program
Department of Education <ul style="list-style-type: none"> • Funds provided to local school districts to offset the impact of lost tax revenue because of military installations. 	<ul style="list-style-type: none"> • funding for local school systems impacted by military dependents
Department of Labor <ul style="list-style-type: none"> • Program for servicemembers who are leaving the active duty force and seeking civilian employment. 	<ul style="list-style-type: none"> • employment assistance
Other costs <ul style="list-style-type: none"> • Certain costs are not available in any budget. We estimated those costs using various methods: <ul style="list-style-type: none"> • The Office of Management and Budget provided an unofficial estimate of accrual costs for current active duty members' future veterans' benefits. • DOD's Office of the Actuary provided accrual cost estimates for health care benefits for retirees and their dependents. • We calculated lost federal tax revenue estimates based on information from DOD and the federal tax code. 	<ul style="list-style-type: none"> • compensation and benefits for retirees and honorably discharged servicemembers • health care benefits for retirees under 65 and their dependents • federal tax expenditure resulting from special nontaxable allowances

Source: GAO analysis.

Note: For more detailed information, see app. I.

^a Other includes education benefits, savings deposit program, adoption expenses, subsistence in kind, separation pay, partial dislocation allowance, transportation subsidy, permanent change of station, social security tax, unemployment benefits, and servicemembers' group life insurance hazard payments.

^b Upon joining active duty, servicemembers are enrolled in the Montgomery G.I. Bill unless they opt out of the program. In fiscal year 2005, a participating servicemember paid \$1,200 into the program and, if enrolled as full-time students at an approved educational institution, a servicemember received as much as \$12,000 annually.

Since the costs of compensation are scattered across the federal budget, no one organization has visibility over the total costs of military compensation. The lack of transparency over total costs to compensate servicemembers impacts decision makers' ability to manage the system, including (1) assessing the long-term cost implications, (2) determining how best to allocate resources to ensure an optimum return on investment, and (3) assessing the efficiency of the current compensation system on DOD's ability to meet recruiting and retention goals. As a result, the current compensation system is made up of a number of benefits and over 60 different pays and allowances that have been added piecemeal over the years to address specific needs. The main problem with this piecemeal approach is that it does not consider the system as a whole—and, as a result, new initiatives are considered in isolation and often with little consideration to how these will contribute to the ability of the military compensation system to efficiently meet recruiting and retention goals and if resources are being allocated to ensure the optimum return on compensation investments within current and expected resource levels. For example, in 2000 Congress enhanced retirement benefits to include health care for retirees over 65 years old and their dependents.¹² This additional benefit came at significant costs, about \$6.5 billion accrual funding in fiscal year 2004 alone, and with little evidence of whether, and if so how it contributes to the efficiency and effectiveness of the compensation system in terms of recruiting and retention.

¹² Floyd D. Spence National Defense Authorization Act for Fiscal Year 2001, Pub. L. No. 106-398, Sec. 712 (Oct. 2000)

Lack of Principles to Guide Military Compensation Policy Is a Long-standing Problem

Challenges associated with piecemeal changes and adjustments to the military compensation system have been a long-standing problem with the system. In 1979, we evaluated DOD's compensation system and concluded that piecemeal adjustments and a lack of overall guiding principles of compensation were a problem in establishing a basis for evaluating changes to the total compensation system.¹³ As a result, we recommended that Congress establish a permanent, independent military compensation board to identify and recommend pay principles, see that pay principles are appropriately implemented, and continuously monitor and make recommendations for changing the military compensation system consistent with the established principles. At the time, DOD officials believed that military pay increases should be linked to federal civilian pay increases—and that special and incentive pays could be used to alleviate critical skill shortages. Officials disagreed that a board should be established, indicating that it would be counterproductive to create a “headless fourth branch” of government. However, the underlying problems we pointed out in 1979—lack of explicit compensation principles and the difficulty in making major changes to compensation—still exist today. The Military Compensation Background Papers describe six principles that the compensation system is designed to achieve; those principles are: managing manpower, compatibility with the level of technology servicemembers employ, equity, effectiveness in war and peace, flexibility, and motivation.¹⁴ However, some 25 years later, these principles do not provide clear policy and doctrine to guide military compensation policy as described in this excerpt from DOD's Military Compensation Background Papers:

“the relationships between the individual components of compensation and their systemic interrelationships as a coherent structure remain largely implicit rather than explicit. Virtually every aspect of military activity has explicit doctrines, principles, and practices embodied in field manuals, technical manuals, and various joint publications. Military compensation is noteworthy in its lack of such an explicit intellectual foundation.”

Furthermore, the Secretary of Defense tacitly admitted the difficulty in changing military compensation from inside the department when he

¹³ GAO, *The Congress Should Act to Establish Military Compensation Principles*, GAO/FPCD-79-11 (Washington, D.C.: May 9, 1979).

¹⁴ Department of Defense, Office of the Secretary of Defense, *Military Compensation Background Papers: Compensation Elements and Related Manpower Cost Items, Their Purposes and Legislative Backgrounds*, sixth ed. (Washington, D.C.: April 2005).

formed an independent advisory committee to study compensation in 2005. Of particular concern to the department was the growth in entitlement spending for things like health care and the appropriateness of the mix of in-service and post-service compensation. However, Congress has taken certain measures to enhance post-service compensation or benefits that DOD has not requested or in some cases has discouraged, such as the expansion of concurrent receipts for retirees with disabilities. At the time of this report, the Secretary of Defense's committee was just beginning its work; however, the Secretary had requested the committee provide an interim report by September 2005 and conclude its work by spring 2006.

In order to achieve lasting and comprehensive change, organizations need sustained top leadership to help make significant and systematic changes become a reality and sustain them over time. We have recently recognized and suggested that to achieve such leadership a Chief Management Official with responsibility for DOD's overall business transformation efforts should be created.¹⁵ We believe the long-standing lack of explicit principles and the difficulty in changing military compensation from inside DOD is another example of how a Chief Management Official could be beneficial to DOD.

Heavy Reliance on Benefits May Not Be Appropriate for Meeting Key Human Capital Goals or Not Sustainable in the Long Term

The federal government's total costs to compensate its active duty servicemembers have increased significantly in the past 5 years, and given that costs are heavily weighted toward noncash and deferred benefits, the structure of the current compensation system raises questions about the reasonableness, appropriateness, and long-term affordability and sustainability of DOD's approach to compensating its military workforce. Between fiscal years 2000 and 2004, overall compensation costs increased from \$123 billion to \$158 billion—or about 29 percent, in 2004 dollars. Increases in costs were primarily driven by basic pay, allowances for housing, and health care benefits. Furthermore, over half of the mix of compensation costs is in the form of noncash and deferred benefits, which stands in contrast to private sector and federal civilian organizations that tend to rely more heavily on cash pay, and less on benefits. Military analysts have noted that benefits, especially deferred benefits like retirement, are a relatively inefficient way to influence recruiting and retention, compared to cash pay.

¹⁵ GAO, *Key Elements Needed to Successfully Transform DOD Business Operations*, GAO-05-629T (Washington, D.C.: Apr. 28, 2005).

Compensation Costs Have Significantly Increased

The total cost to the government to provide compensation for active duty members has grown about 29 percent, adjusted for inflation, between fiscal years 2000 and 2004, as shown in figure 1. Over this same time period, the number of active duty troops remained relatively constant at about 1.4 million people, but military compensation costs grew from \$123 billion to \$158 billion in fiscal year 2004 dollars annually.¹⁶ We estimate that the average cost of compensation per servicemember (i.e., both enlisted personnel and officers) in 2004 was about \$112,000. Three things are important to understand about our estimate. First, it is an average of what it cost the government to compensate servicemembers, not what the servicemembers “receive in their paycheck.” Individual cash compensation will vary significantly based on rank and other factors. Furthermore, the value of benefits also varies significantly depending on individual circumstances. Second, because agencies other than DOD provide compensation to servicemembers, our estimate includes costs appropriated to The Department of Veterans Affairs, the Department of Education, and the Department of Labor as well as the lost tax revenue as a result of special tax advantages received by military personnel among others.¹⁷ Third, it does not represent the marginal cost of adding servicemembers, because it does not include significant costs for acquiring and training military personnel. Such costs are substantial: DOD officials told us that the cost for training can be as much as \$36,000 per person if a broad range of training costs are included.

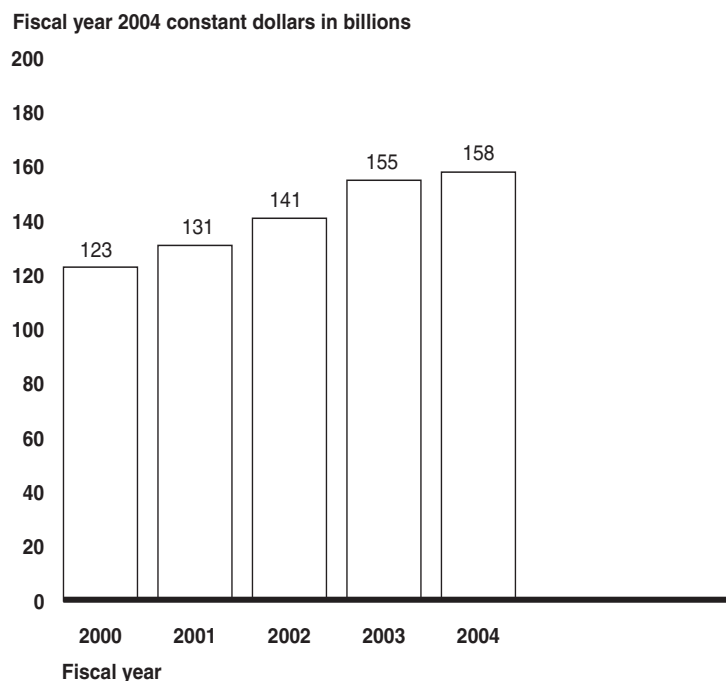
Recently, other defense analysts have made attempts to estimate the cost of compensation. While these estimates vary based on what costs are included in their analyses, the trends are the same. For example, the Congressional Budget Office (CBO) estimated that in 2002 compensation cost about \$99,000 per active duty servicemember. DOD’s Office of Program Analysis and Evaluations calculated all military compensation costs to be approximately \$117,000 per servicemember in fiscal year 2004.

¹⁶ Our calculations of compensation costs include supplemental funding for the war on terrorism. According to DOD officials, in fiscal year 2004 of the \$158 billion over \$17 billion was supplemental funding.

¹⁷ Our cost calculations capture cost to the federal government. As a result, we included costs assumed by other areas of government to compensate active duty servicemembers. These costs include the lost tax revenue because housing and subsistence allowances are not subject to federal income tax or Federal Insurance Contributions Act (FICA) tax as well as the estimated accrual cost of providing compensation—such as pension and health care—through the VA.

Other DOD officials have done similar work which included compensation costs; for example, officials in the Office of Secretary of Defense told us they recently estimated DOD's cost to add an additional servicemember at about \$109,000 per servicemember. Navy officials have done detailed work to estimate the cost of manpower to the Navy, and concluded that for example, the standard programming rate for officers in pay grade O4 was about \$126,000 and about \$79,000 for enlisted personnel in pay grade E-7; however, these costs do not include health care accrual costs for retirees.

Figure 1: Total Compensation Cost and Per Capita Cost for Fiscal Years 2000-2004



	2000	2001	2002	2003	2004	Percentage change 2000-2004
Total compensation (in billions)	123	131	141	155	158	29
End strength (in millions)	1.37	1.37	1.40	1.42	1.41	3
Per capita cost	89,636	95,096	100,894	109,245	111,783	25

Source: GAO analysis.

Note: Our per capita costs are based on active duty end strength. According to DOD officials, since fiscal year 2002 over 100,000 mobilized reservists were paid out of the active duty compensation

budget. If you considered these personnel, the average costs to provide compensation would be about \$5,000 lower.

Military Compensation Components Driving Total Cost

Growth in military compensation is attributed, primarily, to increases in (1) basic pay, (2) allowances for housing, and (3) health care cost.

- **Basic pay**, found in the military personnel budget, increased from \$38.4 billion to \$47.4 billion from fiscal years 2000 to 2004—an increase of about 23 percent—and is the largest component of the compensation system.¹⁸ DOD has asked for and Congress has supported sizable across-the-board raises in basic pay in order to address concerns that military members may be underpaid compared to comparable educated civilian counterparts. From fiscal years 2000 to 2004 the average pay increases to servicemembers exceeded average wage increases for all private sector employees.
- **Allowances for housing**, found in the military personnel budget, increased by about 66 percent from \$7.3 billion to \$12 billion between fiscal years 2000 to 2004. Prior to fiscal year 2001, DOD’s policy was for members to pay for 15 percent of their housing costs out of pocket; however, in fiscal year 2000, DOD introduced the “zero out of pocket” initiative that increased servicemembers’ housing allowances to eliminate their out-of-pocket expenses by fiscal year 2005.¹⁹ This effort was to encourage servicemembers to live off-base and is consistent with DOD’s policy that states it is the department’s preference for servicemembers to live in civilian housing.

¹⁸ We adjusted for inflation using DOD’s military personnel (MILPERS) deflator. Between fiscal years 2000 and 2004 military pay increases averaged over 21 percent. This compares to a 9.7 percent increase for fiscal years 2000 through 2004 for the all urban workers Consumer Price Index (CPI) and a 13.3 percent increase in the Employment Cost Index (ECI) for civilian wages and salaries over the same period.

¹⁹ GAO, *Military Personnel: Higher Allowances Should Increase Use of Civilian Housing, but Not Retention*, GAO-01-684 (Washington, D.C.: May 31, 2001).

-
- **Health care costs**, including the costs for active duty servicemembers and their dependents as well as accrual costs for retirees and their dependents, increased from about \$13.8 billion to \$23.3 billion between fiscal years 2000 and 2004, an increase of about 69 percent. This increase is attributable, in part, to the fiscal year 2002 expansion of health care benefits to retirees over 65 years of age to cover them and their dependents for life.²⁰ DOD raised concerns about expanding entitlements, such as health care, that do not provide them leverage over readiness. Also contributing is the higher-than-average increase in costs of medical care. A 2003 study by CBO projected that if DOD's medical spending increases at the same rate as per capita medical spending in the United States, as a whole, it could increase to possibly as much as \$52 billion, or \$38,000 per servicemember in 2002 dollars, by 2020.²¹ These costs include (1) current appropriations from the operations and maintenance, defense health program budget, for current servicemembers and their dependents; and (2) estimated accrual costs for retirees and their dependents from the DOD actuary.²² Given CBO's projections of substantial growth in future costs and the 69 percent increase over the past 4 years, serious questions about the affordability and sustainability of the current compensation system arise.

Officials within the department told us that they sought increases in basic pay and housing allowances because they think investments in these types of compensation are more efficient in meeting the department's recruiting and retention goals. Furthermore, continued, significant increases in these areas—especially health care costs, which could exceed \$50 billion annually by 2020—raise questions about the long-term affordability and sustainability of the current compensation approach. The summary of military compensation components displayed in table 2 shows the percentage changes in costs between fiscal years 2000 and 2004.

²⁰ GAO, *Defense Health Care: Observations on Proposed Benefit Expansion and Overcoming TRICARE Obstacles*, [GAO/T-HEHS/NSIAD-00-129](#) (Washington, D.C.: Mar. 15, 2000).

²¹ Congressional Budget Office, *Growth in Medical Spending by the Department of Defense* (Washington, D.C.: September 2003).

²² In fiscal year 2003, DOD began budgeting for the accrual cost of health care for retirees over age 65 and their dependents. This cost is in the military personnel budget. However, health care for retirees under 65 and their dependents is not currently budgeted for on an accrual basis.

Table 2: Summary of Changes in Compensation Costs, Fiscal Years 2000 and 2004

2004 constant dollars in billions			
Components of compensation	Fiscal year 2000	Fiscal year 2004	Percentage change
Cash			
Basic pay	\$38.4	\$47.4	23
Housing allowance	7.3	12.0	66
Subsistence allowance	3.1	3.4	8
Special and incentive pays	3.3	4.3	30
Allowances	1.9	3.5	84
Tax advantage	5.3	6.4	22
Total cash	59.3	77.0	30
Noncash benefits			
Subsistence in kind	1.2	3.5	185
Other ^a	10.3	10.0	(3)
Education ^b	.4	.7	68
Installation based benefits ^c	4.4	5.2	20
Health care	8.7	9.7	11
Family housing and barracks	3.2	3.1	(1)
Total noncash	28.2	32.2	14
Deferred benefits			
Retired pay accrual	12.2	12.8	5
VA compensation and pension	9.0	11.1	23
VA health care	8.4	10.3	23
VA other	.9	1.1	23
Health care accrual	5.1	13.6	166
Total deferred	35.6	48.9	38
Total compensation	\$123.1	\$158.1	29

Source: GAO analysis.

Notes: According to DOD officials, there were over 100,000 mobilized reservists paid out of the cash compensation in fiscal year 2004. For more detail on sources, see app. I.

^a Includes separation pay, partial dislocation allowance, transportation subsidy, permanent change of station, adoption expenses, savings deposit program, other personnel support, special support, social security tax, unemployment benefits, special compensation, VA home loan, death gratuities, survivor benefits, and other costs.

^b Includes education, off-duty voluntary education, and servicemember GI bill and certification.

^c Includes exchanges, commissaries, childcare, DOD dependent schools, and other morale, welfare, and recreation costs.

In addition, special and incentive pays grew about 30 percent—from \$3.3 billion to \$4.3 billion—from fiscal years 2000 through 2004. This increase is substantial on a percentage basis, but special and incentive pays are not driving the overall budget trends because the amount is a relatively small portion of the overall compensation cost. By our calculations, these special pays only represent about 6 percent of cash compensation, and about 3 percent of total compensation, on average. DOD has more than 60 different special pays that fall into this category including reenlistment bonuses and hazardous duty pay, as well as other pays for specific duties like aviation, medical, and incentives for servicemembers to take certain assignments among others. Because most compensation is determined by factors such as tenure, rank, location, and dependent status, these special pays and allowances are the primary monetary incentives DOD has for servicemembers other than promotions.

Heavy Emphasis on Benefits Reflects DOD Commitment to Servicemembers and Their Families, but Is Unlike Civilian Counterparts and Inefficient for Recruiting and Retention

Noncash and deferred benefits made up just over half of the total costs of providing military compensation since 2000. DOD has historically viewed noncash benefits as critical to morale, retention, and the quality of life for servicemembers and their families. In April 2002, DOD issued a strategic human capital plan addressing quality-of-life issues and benefits. According to DOD officials, the plan, entitled *A New Social Compact: A Reciprocal Partnership Between the Department of Defense, Service Members and Families*, is needed to ameliorate the demands of the military lifestyle, which includes frequent separations and relocations, and to provide better support to servicemembers and their families. It emphasizes the need to maintain programs and services viewed as benefits by servicemembers. Furthermore, we recently reported that DOD has instituted a number of benefits that reflect demographic changes in the active duty force—primarily the increase in servicemembers with family obligations.²³ Compared to civilians in government and in the private sector, the military’s compensation costs are much more heavily weighted toward benefits and deferred compensation like retirement and health care for retirees.

²³ GAO, *Military Personnel: Active Duty Benefits Reflect Changing Demographics, but Opportunities Exist to Improve*, [GAO-02-935](#) (Washington, D.C.: Sept. 18, 2002).

Efficiency, as defined by DOD, is the amount of military compensation—no higher or lower than necessary—that is required to fulfill the basic objective of attracting, retaining, and motivating the kinds and numbers of active duty servicemembers needed.²⁴ However, the efficiency of some benefits is difficult to assess because the value that servicemembers place on them is different and highly individualized. It is generally accepted and a recent study indicates that some deferred benefits, such as retirement, are not valued as highly by servicemembers as current cash compensation.²⁵

Military Compensation System Is Weighted Toward Noncash and Deferred Benefits

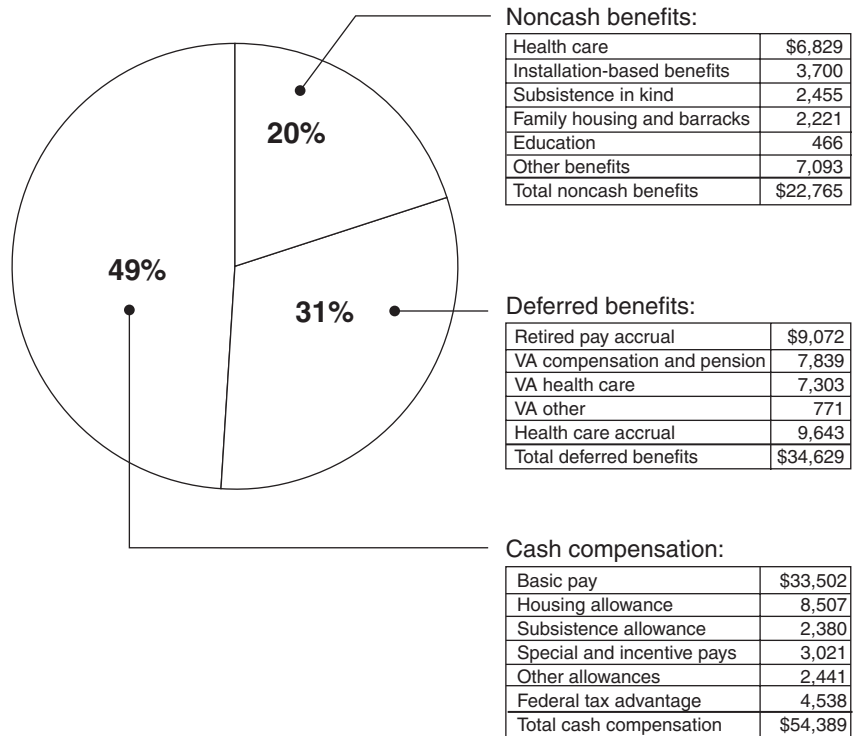
In fiscal year 2004, noncash and deferred benefits made up about 51 percent of total compensation costs, on average. This means that it costs the government more to provide benefits and deferred compensation than current cash compensation. Of this, deferred benefits represented a significant portion of noncash compensation, as figure 2 shows. Since 2000, deferred benefits have made up about one-third of total compensation costs. These benefits are the promise of future compensation—like retirement pay and health care as well as other benefits—for active duty servicemembers who retire with at least 20 years of service or who leave the force and become eligible for veterans benefits. Deferred benefits impact the current cost of compensation because monies must be set aside today to provide these benefits in the future, over the servicemember's lifetime.

²⁴ Department of Defense, Office of the Secretary of Defense, *Military Compensation Background Papers: Compensation Elements and Related Manpower Cost Items, Their Purpose and Legislative Backgrounds* (Washington, D.C.: Sixth edition, April 2005).

²⁵ John T. Warner and Saul Pleeter, "The Personal Discount Rate: Evidence from Military Downsizing Programs," *The American Economic Review* (March 2001).

Figure 2: The Allocation of Cash, Noncash, and Deferred Compensation Costs per Active Duty Servicemember in Fiscal Year 2004

Total cost to provide compensation was about \$112,000 per active duty member—benefits made up about 51 percent of this cost.



Source: GAO analysis.

Note: Over 100,000 mobilized reservists were paid out of total cash compensation. Accounting for those reservists, the average cash compensation was about \$49,000 per servicemember. These costs reflect the average costs to the government to provide these components of compensation. For example, all servicemembers do not receive a cash housing allowance, because some servicemembers live on base in family housing or barracks. The cost presented represents the total amount appropriated for housing allowances divided by the number of servicemembers, thus, an average cost to the government.

Civilian Compensation Emphasizes Salary and Wages

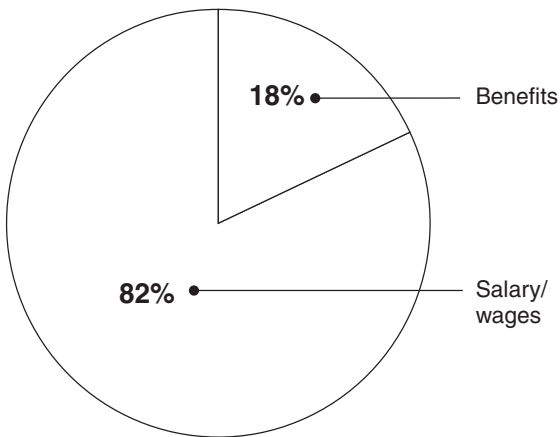
While it is difficult to make direct comparisons between military and civilian compensation because of the accessibility of some benefits (e.g., health care, retirement to private sector employees), it seems clear that, in general, DOD compensation is weighted much more heavily toward benefits. Some private sector organizations and the federal government provide benefits similar to those provided by the military, such as retirement, health care, paid time off, and life insurance; military benefits, in some instances, far exceed those offered by the private sector, such as free health care and housing as well as discount shopping.²⁶

In contrast to the mix of compensation for the military, figure 3 shows that civilian counterparts in the private sector and the federal government receive, in broad terms, most of their compensation in cash salary/wages. Civilians in private industry, on average, received about 82 percent in salary and wages while federal government civilians received about 67 percent in salary and wages. Thus, one third or less of these workers' compensation is typically in the form of benefits or deferred compensation.

²⁶ GAO, *Military Personnel: Active Duty Benefits Reflect Changing Demographics, but Opportunities Exist to Improve*, GAO-02-935 (Washington, D.C.: Sept. 18, 2002).

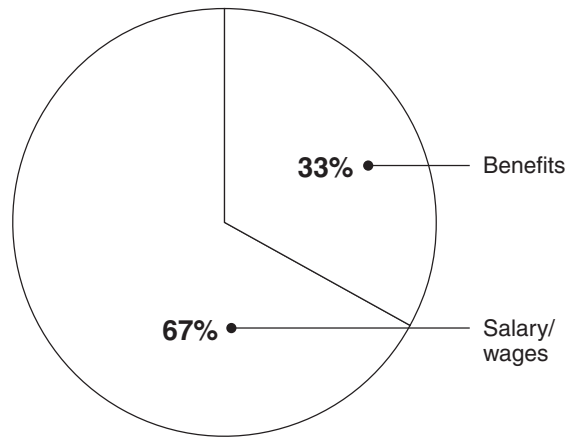
Figure 3: 2003 Mix Salary/Wages and Benefits in Civilian Compensation

Private industry - Total average costs of compensation \$50,509



Source: Department of Commerce, Bureau of Economic Analysis.

Civilian federal government - Total average costs of compensation \$92,330



Note: Average compensation costs are in 2004 dollars.

Current Mix Is Highly Inefficient for Recruiting and Retention

The mix of compensation is highly inefficient for meeting near-term recruiting and retention needs. Cash pay today is generally accepted as a far more efficient tool than future cash or benefits for recruiting and retention. 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. For example, a recent study offering servicemembers a choice of lump-sum payments or annuities found that a vast majority of servicemembers preferred a lump-sum cash payment versus deferred compensation in the form of an annuity.²⁷ According to the study, more than 50 percent of officers and 90 percent of enlisted servicemembers had discount rates of at least 18 percent; that is, they value \$1 received in 20 years to be worth only about 4

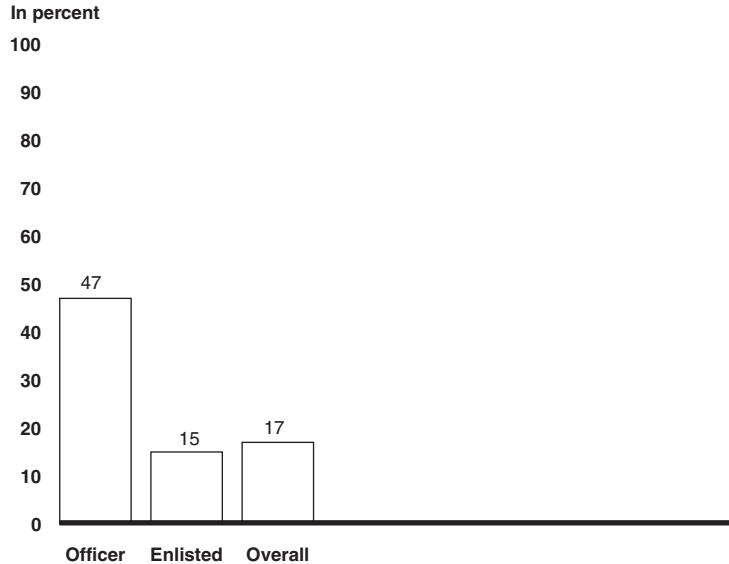
²⁷ John T. Warner and Saul Pleeter, "The Personal Discount Rate: Evidence from Military Downsizing Programs," *The American Economic Review* (March 2001).

cents today. The study also found that the preference for cash today was particularly strong among younger servicemembers.

This “personal discount rate” has important implications for military compensation policy, especially when it comes to considering deferred benefits or compensation. Not only do people heavily discount the value of future benefits, less than one in five in the military will receive the most lucrative and costly benefits offered by the military, specifically active duty retirement pay and health care benefits. This is because only 17 percent of those who join the military will ultimately serve a 20-year career and thus earn nondisability retirement pay and health care for life. Figure 4 illustrates that based on current actuarial assumptions, 47 percent of new officers and 15 percent of new enlistees attain 20 years of active duty service.²⁸ Thus, a significant portion of the compensation budget—about 17 percent—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.

²⁸ These percentages are based on a typical group of new entrants and do not include those military personnel who began their careers on active duty then moved to the reserves and retired from there.

Figure 4: Percent of Enlisted Personnel and Officers Who Serve a 20-Year Career



Source: DOD.

Taking together the personal discount rate and the relatively few servicemembers who earn retirement benefits, defense compensation analysts have suggested that this is an inefficient allocation of the overall compensation investment. This insight is not new, and is likely a key reason why private sector companies have such a high proportion of cash in their compensation mix. Thus, DOD’s current approach to compensation raises serious questions about the reasonableness and appropriateness of continuing to weight compensation toward noncash and deferred benefits. However, DOD officials told us they feel that this efficiency argument about entitlements is often outweighed by the desire in DOD and in Congress to “take care” of servicemembers and their families. This makes adjusting compensation extremely difficult for decision makers, especially amid concerns of eroding benefits, as discussed later in this report. When concerns have arisen, benefits have often been added with little consideration of what they will cost, how they compare with overall market data, whether costs are affordable and sustainable over the long term, or their effectiveness and return in terms of recruiting or retention. The cumulative effect of this approach raises serious questions about the reasonableness, appropriateness, affordability, and sustainability of the

current military compensation system in light of 21st century trends and challenges.

DOD's Lack of an Effective Communication and Education Effort on Compensation Has Allowed Servicemembers' Misperceptions and Concerns about Their Compensation to Perpetuate

According to DOD surveys and analysis of our focus group findings and survey data, many servicemembers are dissatisfied, and in some cases, harbor significant misperceptions about their pay and benefits in part because DOD does not effectively educate them about the competitiveness of their total compensation packages. This has led to an atmosphere of perpetual dissatisfaction and misunderstanding about compensation among servicemembers. Servicemembers tend to be more satisfied with their total compensation packages than with specific aspects of their pay and benefits. They continue to express dissatisfaction with specific aspects of their compensation. In our focus groups, servicemembers had misperceptions about compensation; specifically (1) they underestimated the costs of their compensation and how it compares to civilian wages, (2) were unaware of or confused about certain aspects of their compensation, and (3) were concerned about erosion of benefits.

Servicemembers Have Found DOD's Efforts to Educate Them about Their Compensation Unreliable and Difficult to Access

It is industry best practice for employers to educate employees about the value of their pay and benefit components of their compensation. We also believe that by communicating the value of the compensation investment and ensuring it is understood, DOD will ensure an increased return on their investment because employees who know the value of their total compensation packages are more likely to be engaged and motivated in their work. In addition, past studies suggest that revealing more information about components of compensation has a greater impact on the component's satisfaction rate than the actual amount itself.²⁹ Servicemembers, especially enlisted personnel, said they frequently relied on unofficial sources of information, such as word of mouth or service newspapers. Many servicemembers discussed how the official sources of information available are often difficult to access or appear to them to be dishonest or misleading.

²⁹ *Improve Base Pay Return on Investment by Increasing Employee Knowledge*. WorldatWork, 2002. *Creating an Effective e Statement: A Primer*. Watson Wyatt World Wide 2004.

DOD makes various efforts to educate servicemembers by providing annual earnings statements (see app. II for a sample of Personal Statement of Military Compensation) providing online information on compensation, and providing servicemembers access to personnel specialists to answer questions. However, servicemembers stated that the online services frequently are down or that it is difficult to access services such as the “myPay” Web site.³⁰ DOD officials acknowledge that access to the “myPay” Web site has been a long-standing, recognized problem that is a result of efforts to ensure the security of the personal pay information available on the site. Over half of our focus groups commented on how unhelpful official sources are to them in understanding aspects of compensation. Many stated that the annual earnings statement, at times referred to despairingly in our focus groups as the “lie sheet,” was not believable because they do not understand how the amounts identified as their total compensation (noncash and deferred) were calculated.³¹ Enlisted members and officers told us that they felt recruiters and personnel specialists often gave misguided information or could not provide answers to servicemembers’ questions on compensation. Additionally, members often discussed how the lack of comprehensive communication and education on compensation is a problem because they often find themselves unaware of certain additions or changes to their pay and benefits. Servicemembers offered suggestions as to how to improve education on compensation by consolidating information into a single location to obtain information on all pay and benefit elements, while assuring it is clearly accessible and easy to understand. DOD officials acknowledge that generally servicemembers do not realize the full value of their compensation and have misperceptions about their compensation. The Defense Finance and Accounting Service is implementing tools to address these problems. To date, they have developed a newsletter—that provides information on changes to compensation or information about compensation that is widely misunderstood or unknown, such as how to get a “myPay” Web site access code, and bulletins that provide information on specific topics of interest

³⁰ “My Pay” is a Web site maintained by DOD’s Defense Financial Accounting Service. It provides servicemembers online access to their Leave and Earnings statements as well as other related compensation issues—such as tax deductions.

³¹ Annual earnings statements called the Personal Statement of Military Compensation are mailed to Army, Air Force, and Marine Corps servicemembers annually and provide them personalized information about the amount of cash pay they receive as well as general information about the value of their benefits. For example, servicemembers are provided an estimated value of their health care if they were to buy similar coverage in the civilian market.

that are sent to Army personnel and plan to expand these tools to the other services.

The efforts made to date by DOD to explain the value and competitiveness of compensation stands in contrast to the substantial investment the department makes to recruit new members. As of fiscal year 2003, the department was spending over \$13,000 per enlisted recruit for advertising, bonuses, incentives, and recruiter pay and support.³² We do not have comparable data on what the department spends to educate servicemembers on compensation, but 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 servicemembers.

Servicemembers Tend to Be More Satisfied with Their Total Compensation Package than with Specific Aspects of Their Compensation

During the 1990s, the military benefit package was significantly enhanced in response to servicemembers' concerns of eroding benefits; yet servicemembers have continued to express dissatisfaction with many aspects of their compensation. In the 2002 Status of Forces Surveys of Active Duty Servicemembers, participants were asked to rate their satisfaction with specific components within their military compensation. As figure 5 shows, a substantial percentage of servicemembers were dissatisfied with numerous aspects of their compensation, including basic and special pays and housing and subsistence allowances.

During more than half of our focus groups, servicemembers cited base pay, the subsistence and housing allowance, and special and incentive pays as reasons for dissatisfaction along with health care and others. In general, officers tended to be more satisfied with base pay than were enlisted personnel. Six of the eight focus groups with senior enlisted servicemembers expressed dissatisfaction with their pay especially compared to junior officers, who the senior enlisted servicemembers perceive as having less experience and relying on them for on-the-job training. While members recognized that there have been improvements in the housing allowance with DOD's recent effort to increase the allowance,³³

³² GAO, *Military Recruiting: DOD Needs to Establish Objectives and Measures to Better Evaluate Advertising's Effectiveness*, [GAO-03-1005](#) (Washington, D.C.: Sept. 19, 2003).

³³ In fiscal year 2000, the Secretary of Defense introduced an initiative to increase housing allowances so that servicemembers would be paying nothing out of pocket for rent and utilities by fiscal year 2005.

they complained that these increases have had little effect because they perceive that landlords increase rent by the same amount. Additionally, 8 of our 40 focus groups discussed how it is unfair that servicemembers with dependents receive more housing allowance than single members. Moreover, members had varying perceptions about special pays and incentives. Some were dissatisfied with the amount of special pays and thought they should be increased. Others were dissatisfied because it was unclear to them why everyone does not receive special pays. This is particularly true for senior enlisted pay grades that are ineligible for reenlistment bonuses. Furthermore, health care was most frequently discussed as a source of dissatisfaction as well as satisfaction. While servicemembers were satisfied with the minimal to no cost of health care for themselves and their family, 31 of our 40 focus groups commented on their dissatisfaction with the quality and access to health care. Additional reasons of why servicemembers most frequently reported these components and others as sources of dissatisfaction are listed in figure 5.

Figure 5: Reasons for Servicemembers' Dissatisfaction with Pay and Benefits

Components of compensation	2002 Active Duty Status of Forces survey		2005 results of GAO focus group discussions and survey of focus group participants			
	Percentage dissatisfied n=11,060		Percentage dissatisfied focus group survey n= 401		Themes of dissatisfaction reported during focus groups N=40	
	Enlisted	Officers	Enlisted	Officers		
Basic pay	52	26	59	19	While officers were relatively satisfied with base pay, both officers and enlisted personnel expressed concern about how their pay compares to civilians and the inadequacy of base pay for enlisted members.	
Basic allowance for housing	40	39	53	40	Servicemembers expressed much concern with the subsequent raises of their rent due to the recent increases of their housing allowance and the inequity of higher housing allowances for members with dependents compared to ones without dependents.	
Basic allowance for subsistence	48	42	54	56	While servicemembers have high dissatisfaction with the subsistence allowance, many inaccurately thought the allowance covered themselves and their family.	
Special and incentive pays	45	31	49	34	Overall, both enlisted personnel and officers were dissatisfied with special pays because they do not understand why some are eligible to receive pays and how the amounts of the pays are set.	
Servicemember medical/dental care	25	21	22 ^a	14 ^a	Although servicemembers' dissatisfaction rates are low, almost all 40 focus groups spoke extensively about their dissatisfaction with the poor quality of or difficulty in accessing their health care.	
Family medical/dental care	26	33	28 ^a	27 ^a	Enlisted personnel and officers often cited different reasons for dissatisfaction with family medical care, including not being able to maintain a rapport with one doctor and being unfamiliar with the billing processes for TRICARE.	
Commissaries and exchanges	19	17	25	17	While the rate of dissatisfaction is relatively low, servicemembers felt the commissaries and exchanges have outlived their usefulness because the savings are relatively minor and are not as convenient for those members living off base.	

Source: Defense Manpower Data Center and GAO analysis.

Note: For the Active Duty Status of Forces survey, DMDC utilized stratified random sampling, where all members of a population are categorized into homogeneous groups, procedures to ensure adequate sample sizes for their reporting categories, thereby creating generalizable findings with a sampling

error of +/- 2 percent. Our focus group survey results are not generalizable because we did not use random sampling to collect the data. For more information on our focus group methodology see app. I.

^a We asked servicemembers separate questions about their satisfaction with medical and dental care. The numbers reflected above are servicemembers' dissatisfaction with medical care. Nineteen percent of enlisted personnel and 12 percent of officers reported they were dissatisfied with their dental care, while 40 percent of enlisted personnel and 32 percent of officers reported they were dissatisfied with their families' dental care.

Although servicemembers expressed dissatisfaction with certain pays and benefits, many were more satisfied when considering compensation as a whole in the Status of Forces survey. DOD surveys in 2003 and 2004 showed that about 47 percent of servicemembers were satisfied with their overall cash compensation (i.e., base pay, allowances, and bonuses), which is significantly more than their satisfaction with specific aspects of their compensation. This was evident during our focus groups as well: servicemembers were often more satisfied with their compensation overall than they were with specific aspects of their compensation, like the housing allowance.

Despite their dissatisfaction with many aspects of their compensation, servicemembers expressed a clear preference for cash when asked if they would make any changes to the compensation system. In 35 of our 40 focus group sessions, servicemembers were willing to decrease their noncash benefits if those benefits were replaced with cash. For example, servicemembers in our focus groups said that they prefer frequenting off-base discount stores more than the commissaries and exchanges. Also, servicemembers in our focus groups said they would prefer the cash equivalent to their medical coverage in order to obtain their own health care because of their dissatisfaction with the present choice. Servicemembers, especially junior officers who said they do not intend to stay in the military for a full 20-year career, told us that they would prefer DOD to give them cash that they could invest toward their retirement.³⁴ Comments like these, which we heard frequently, seem to support past studies indicating servicemembers have a strong preference for cash compensation today.³⁵ However, such personal preferences were offset by other concerns. Specifically, during 16 of our 40 focus group sessions, servicemembers expressed concern that if they were to receive an increase

³⁴ The current retirement system requires servicemembers to generally serve 20 years before becoming eligible for nondisability retirement pay and benefits.

³⁵ John T. Warner and Saul Pleeter, "The Personal Discount Rate: Evidence from Military Downsizing Programs," *The American Economic Review* (March 2001).

in cash it would not equal the value of their current noncash or deferred benefit. Or, changing to more cash compensation might not be in the best interest of all members, especially the junior enlisted personnel, who might not manage their finances well.

Servicemembers in Our Focus Groups Expressed Certain Misperceptions and Concerns about Their Compensation

During our focus group discussions, servicemembers (1) underestimated the cost of their compensation and how their compensation compares to civilian wages, (2) were unaware of or confused about certain aspects of their compensation, and (3) were concerned about erosion of benefits. These findings suggest that a culture of dissatisfaction and misunderstanding about compensation exists among servicemembers.

Underestimation of Total Compensation

Servicemembers consistently underestimated how their pay compares to the private sector. Almost 80 percent of servicemembers participating in our focus groups reported in our survey of focus group participants that they believe they are paid less than their civilian counterparts.³⁶ In addition, during the focus groups servicemembers frequently discussed how they were dissatisfied with their military pay because they believe that they could make more “on the outside” as a civilian.³⁷ Moreover, when asked how much DOD spends on cash pays, retirement, and health care for them, 9 out of 10 servicemembers participating in our focus groups underestimated how much it cost to provide their compensation.

³⁶ We asked focus group participants to identify their civilian counterparts and how their pay compared with the counterpart they identified.

³⁷ Between fiscal years 2000 and 2004 military pay increases averaged over 21 percent. This compares favorably to the 9.7 percent increase in the urban workers Consumer Price Index (CPI) over the same period. Subtracting the 9.7 percent from the 21 percent yields the real wage growth of military personnel of over 11.3 percent. Compared to the Employment Cost Index (ECI) military wages grew over 7.7 percent more (21 percent minus 13.3 percent) than did civilian wages and salaries over the same period.

While some specific skill groups could likely make considerably more in civilian jobs, such perceptions of noncompetitive compensation seem to be inaccurate in broad terms. The most recent Quadrennial Review of Military Compensation—a DOD commission that reviews military compensation—found that cash compensation fares favorably overall to civilian wages. Specifically, they compared cash compensation (including tax advantage, but not including special pays or benefits) with comparably educated civilians. They found that, on average, military pay was at the 70th percentile or higher of civilian wages.³⁸ It should also be noted that this review of military compensation found that, based on historical data, when DOD pays servicemembers at around the 70th percentile of civilian wages it is competitive in the employment market—that is, DOD has generally not experienced recruiting or retention problems when compensating servicemembers at this level. In sum, this means that DOD seeks to pay servicemembers competitive cash wages when compared to civilians and, at the same time, provides increasingly expensive benefits that are in most cases much greater than those provided by the private sector.

Lack of Awareness or
Understanding of Aspects of
Compensation

Although most servicemembers were aware that their compensation was a complex mix of cash and benefits, some servicemembers were unaware of certain aspects of their compensation; for example, servicemembers were not aware of which retirement system they fell under or specifics about their retirement benefits. Some servicemembers expressed confusion on the repeal of the REDUX retirement system or did not realize that retired members and their dependents now receive health insurance for life under the military's healthcare system, TRICARE. Also, servicemembers did not understand and had misperceptions about many components of their cash compensation. For instance, some enlisted members were unsure as to how special pays were allocated, while others were not as familiar with the federal tax advantage they receive. Additionally, servicemembers showed frequent misperceptions about the subsistence allowance being designed for the member and not the family. Moreover, servicemembers often complained of how they did not know how to access information about health care benefits for their family.

³⁸ Officers were compared with civilians who have 4-year college degrees, while enlisted members were compared with civilians who have high school diplomas and some college.

In contrast to pay and benefits, focus group participants seldom raised deferred compensation as a reason for dissatisfaction or satisfaction, and few junior enlisted personnel included deferred benefits when describing their compensation. Some servicemembers expressed concern about losing deferred benefits that were implicitly promised to them as part of joining the military. In addition, a majority of the focus groups did not recognize veterans' benefits as a component of their military compensation. Of the servicemembers who discussed veterans' benefits, they focused on the home loan program.³⁹

Concern about Eroding Benefits

During the 1990s, some servicemembers expressed concerns that their benefits were eroding, particularly their health care and retirement benefits. In response to such concerns, the military benefit package has been significantly enhanced. In recent years, for example, Congress restored retirement benefits that had previously been reduced for some servicemembers, significantly expanded their retirement health benefits, and allowed concurrent receipt of disability and retirement pay. However, leaders in both the enlisted and officer ranks in our focus groups were concerned that their benefits have still been eroding despite these recent efforts. They often talked about retirement benefits worsening as well as about decreases in base services provided through the Morale, Welfare, and Recreation organization—such as outdoor recreational equipment discounted rentals.

Conclusions

DOD is maintaining an increasingly expensive and complex military compensation system comprising a myriad of pays and benefits. With the costs scattered across the federal budget, decision makers within the administration and Congress have insufficient transparency over the total costs to compensate servicemembers, particularly with respect to deferred costs, such as TRICARE—which is projected to experience explosive growth in the future. Moreover, changes to the compensation system are made in a piecemeal fashion with an imprecise understanding of how the changes will affect the total cost of compensation or what return on investment decision makers should expect in terms of recruiting and retention. This lack of transparency is becoming a more urgent matter today as DOD and all federal agencies face tough choices ahead managing

³⁹ The Department of Veterans Affairs offers different programs to active duty members such as the Montgomery GI Bill, which provides education assistance, and a guaranteed home loan program, which provides government-backed mortgages to buy homes.

the serious and growing long-term fiscal challenges facing the nation. For DOD, these trade-offs could become as fundamental as investing in people versus investing in hardware—tough choices for a military with aging infrastructure and equipment that could have readiness implications in the future. Compiling comprehensive information about the total cost of compensation—as well as how it is allocated to cash and benefits—would be a crucial first step for the department and Congress to lay a foundation for future decisions. Without such information, decision makers at DOD and Congress do not know what it is costing the government to compensate servicemembers. Furthermore, DOD has not performed the analysis necessary to determine whether its current allocation to cash and benefits is reasonable or appropriate. With dramatic increases in compensation costs and an expanding budget—mostly resulting from supplemental appropriations from Congress to fund activities and operations related to the Global War on Terrorism—it is highly questionable whether the rising costs and current allocations are affordable and sustainable over the long term, especially when supplemental funding recedes. Again, because DOD’s compensation system lacks transparency over these issues, the decision makers in the administration and Congress cannot adequately assess whether DOD’s current approach to compensation is most efficiently meeting its needs for both today and tomorrow.

DOD also faces a sobering marketing challenge—convincing skeptical servicemembers that their compensation is competitive, overall. The department’s efforts thus far have been ineffective, and military members are still dissatisfied with key aspects of their compensation, and harbor several misperceptions and concerns that their compensation is eroding, or will in the future. Pay comparison studies conducted by DOD, however, show that military compensation is quite competitive even without considering benefits. Recent efforts to improve benefits for retirees have done little to address dissatisfaction among current members. This dilemma exists for two reasons: (1) while servicemembers do not want to lose benefits, they value future benefits much less than current cash; and (2) fewer than one in five of those servicemembers who begin military service will ultimately receive those benefits. Without more emphasis on marketing the value of the cash pay as well as the total compensation received overall, DOD will be unable to improve servicemember perceptions, which could have implications for future recruiting and retention efforts.

Recommendations for Executive Action

To improve transparency over total compensation; to ensure the compensation system is reasonable, appropriate, affordable, and sustainable; and to better educate servicemembers about the competitiveness of their compensation, we recommend that the Secretary of Defense take the following three actions:

- Compile the total costs to provide military compensation and communicate these costs to decision makers within the administration and Congress—perhaps as an annual exhibit as part of the President’s budget submission to Congress. In preparing the annual exhibit, DOD may want to work with the Office of Management and Budget.
- Assess the affordability and sustainability of the compensation system and its implications on readiness as well as the reasonableness and appropriateness of the allocation to cash and benefits and whether changes in the allocation are needed to more efficiently achieve recruiting and retention goals in the 21st century.
- Develop a comprehensive communication and education plan to inform servicemembers of the value of their pay and benefits and the competitiveness of their total compensation package when compared to their civilian counterparts that could be used as a recruiting and retention tool.

Matter for Congressional Consideration

The Congress should consider the long-term affordability and sustainability of any additional changes to pay and benefits for military personnel and veterans, including the long-term implications for the deficit and military readiness. Furthermore, Congress should consider how best to proceed with any significant potential restructuring of existing military compensation policies and practices, including whether a formal commission may be necessary.

Agency Comments and Our Evaluation

DOD’s comments are included in this report as appendix III. DOD generally concurred with our recommendations, but raised some technical concerns about the way we compiled compensation costs data.

DOD partially concurred with our first recommendation to compile the total costs to provide military compensation and communicate these costs to decision makers. In DOD’s response, it noted that it agrees with the goal

of making total compensation costs transparent to decision makers; however, the department noted that this may be a more appropriate issue for the Office of Management and Budget since the costs extend to four departments. As we noted in our report, lack of transparency over costs is in part due to the sheer number of pays and benefits that make up the military compensation system and the lack of a single source to show total cost of compensation. By establishing transparency of total military compensation costs, DOD would have a more complete picture of how its military members are being compensated and be in the best position to compile these costs for decision makers.

DOD concurred with our second recommendation and stated that it is already engaged in multiple simultaneous efforts to assess the overarching military personnel compensation strategy. In addition, DOD said that it will continue to actively point out the impact of the legislative process to Congress as it did with concurrent receipt, the survivor benefit program, and expanding retiree health care.

DOD partially concurred with our third recommendation to develop a comprehensive communication and education plan to inform servicemembers of the value of their pay and benefits and the competitiveness of their total compensation package when compared to their civilian counterparts. The department acknowledged that there is a perception that military compensation is underreported and undervalued, but pointed out that all of the services as well as the Office of the Under Secretary of Defense for Personnel and Readiness currently have multiple resources available for servicemembers, including Web sites, such as the Navy's electronic pay and compensation calculator, and brochures, such as the Air Force's compensation fact sheet. We believe, as discussed in our report, that these official sources are not effective, because of the continuing dissatisfaction with compensation. DOD said that it will explore an information/marketing campaign that will improve understanding of the system.

DOD also raised technical concerns; specifically, it believed that we did not adequately describe the impact of the increase in funding related to the Global War on Terrorism as well as how we converted the costs to constant year dollars. In its comments, DOD stated that the fiscal year 2004 compensation costs included over \$17 billion in supplemental funding for the war on terrorism, and much of this funding was used to pay for mobilized reservists. While it is true that our estimates include supplemental funding, we do not believe that the inclusion of this funding

changes our findings or conclusions. Supplemental funding represents real costs to the federal government that we believe are appropriate to include when calculating how much the federal government spends on compensating military members. However, we took DOD's concerns into account and added footnotes in our report to explain our approach. DOD also raised concerns about our use of end strength instead of average strength in our per capita calculations. We believe that end strength, which represents only active population, is an appropriate denominator to calculate per capita active duty costs because it provides a consistent population to spread costs of cash, noncash benefits, and deferred benefits. To use average strength, which includes mobilized reservists, would not have been an accurate representation of active duty per capita costs for noncash and deferred benefits. However, in response to this comment, we added footnotes that indicate that the cash compensation for fiscal year 2004 includes costs for mobilized reservists and including those reservists in our per capita calculations would have decreased cash compensation by about \$5,000 per servicemember. Finally, DOD raised concerns about our adjustments for inflation in our data. We used the *National Defense Budget Estimates* published by the Office of the Under Secretary of Defense (Comptroller). According to the document, the deflators we used provide inflation indexes in base years for each DOD appropriation title to be used in converting total obligation authority from current to constant dollars. To address DOD's concerns that the total cost data are not accounting for the fact that the military pay raises have been larger than other civilian pay raises, we added footnotes that compared military pay increases, which averaged over 21 percent between fiscal years 2000 and 2004, to the all urban workers Consumer Price Index and the Employment Cost Index for civilian wages and salaries, which over the same period increased 9.7 percent and 13.3 percent, respectively.

We are sending copies of this report to the Secretary of Defense. In addition, the report will be available at no charge on GAO's Web site at <http://www.gao.gov>.

If you or your staff have any questions regarding this report, please contact me at (202)512-5559 (Stewartd@gao.gov). Other staff members who made key contributions to this report are listed in appendix IV.

A handwritten signature in black ink that reads "Derek B. Stewart". The signature is written in a cursive style with a large initial 'D' and a long horizontal stroke at the end.

Derek B. Stewart
Director, Defense Capabilities and Management

List of Congressional Committees

The Honorable John Warner, Chairman
The Honorable Carl Levin
Ranking Minority Member
Committee on Armed Services
United States Senate

The Honorable Duncan L. Hunter, Chairman
The Honorable Ike Skelton
Ranking Minority Member
Committee on Armed Services
House of Representatives

The Honorable Lindsey Graham, Chairman
The Honorable Ben Nelson
Ranking Minority Member
Subcommittee on Personnel
Committee on Armed Services
United States Senate

The Honorable John M. McHugh, Chairman
The Honorable Vic Snyder
Ranking Minority Member
Subcommittee on Personnel
Committee on Armed Services
House of Representatives

The Honorable Ted Stevens, Chairman
The Honorable Daniel K. Inouye
Ranking Minority Member
Subcommittee on Defense
Committee on Appropriations
United States Senate

The Honorable C. W. Bill Young, Chairman
The Honorable John P. Murtha
Ranking Minority Member
Subcommittee on Defense
Committee on Appropriations
House of Representatives

Scope and Methodology

Calculation of the Costs of Providing Active Duty Compensation

To calculate the cost of compensating active duty servicemembers to the federal government, we interviewed officials from the Department of Defense (DOD) including the Office of the Secretary of Defense, Undersecretary for Personnel and Readiness' office of compensation, the office of the Comptroller within the Office of Secretary of Defense and the services, the Office of the Actuary, and Health Affairs. In addition, we interviewed officials from Department of Veterans' Affairs (VA), Department of Labor, Department of Education, Office of Management and Budget, and the Congressional Budget Office. See table 4 for an overview of our sources of information. In comparing the mix of cash and noncash compensation of active duty servicemembers to that of private industry employees and federal civilians, we used the Department of Commerce's Bureau of Economic Analysis data to determine the typical percentage of compensation that is allocated to salary/wages and benefits in private industry and federal civilian compensation systems.

We examined and compiled data for fiscal years 2000-2004 from the Army, Air Force, Marine Corps, and Navy's military personnel and operations and maintenance budget justification books. Within the operations and maintenance justification books, we reviewed the budgets of the defense health program; the defense commissary agency; the morale, welfare and recreation activities (OP-34 exhibit); and DOD dependent education activity. In addition, we reviewed and compiled data from the future years defense planning document. We also reviewed and compiled data from the VA benefits and health care budget justification books. We used deflators to adjust the budget appropriations into current fiscal year 2004 dollars.

To estimate the total federal tax expenditure that results from the tax-exempt housing and subsistence allowances military personnel receive, we grouped servicemembers by earnings, allowances, and tax status for the years 2000 to 2004 and used the National Bureau of Economic Research's TAXSIM Model to simulate tax liabilities under different scenarios.¹ Only military income was considered. Nonmilitary income, such as spousal earnings or investment income, would likely increase marginal tax rates and, thus, increase our tax expenditure estimates.² A servicemember's earnings and tax status were determined by rank, years of service, and number of dependents.³ Allowances are determined by rank and number of dependents, and we assumed servicemembers living on-base received the average housing allowance of similar servicemembers living off-base. The number of servicemembers in each group for each year was provided by the DOD's Selected Military Compensation Tables. The tax expenditure for each group is estimated as the number of servicemembers in the group multiplied by the difference in the tax liabilities of a representative member of the group assuming that the allowances are and are not taxable.

¹ NBER's TAXSIM Model simulates the U.S. federal income tax rules. See Daniel Feenberg and Elisabeth Coutts, "An Introduction to the TAXSIM Model," *Journal of Policy Analysis and Management*, Volume 12, No. 1, 1993 pp. 189-194.

² In the case where servicemembers are eligible for the Earned Income Tax Credits (EITC), any extra income would likely result in a lower marginal tax rate, because of the structure of the EITC phase-out.

³ The first dependent is assumed to be a spouse. Other dependents are assumed to be children.

To estimate health care accrual costs, we used official estimates of accrual health care costs for all retirees and their dependents provided by DOD's Office of the Actuary. Since 2003, health care costs for retirees over 65 years of age and their dependents are accrual-budgeted in the DOD Military Personnel budget. However, health care costs for retirees under 65 years of age and their dependents are budgeted through an annual appropriation to the Defense Health Program (DHP). Because the DHP annual budget includes health care costs for active duty servicemembers and their dependents as well as retirees under 65 and their families, we had to estimate the share of DHP costs associated with active duty servicemembers and their dependents for the fiscal years 2000-2004. Using similar methodology employed by the Congressional Budget Office, we transformed DHP enrollee data (broken out by gender, age category,⁴ and whether they were active duty personnel, family of active duty personnel, retirees under 65, or family of retirees under 65) into equivalent demand units, because enrollees do not all have the same underlying demand for health care services—average health care expenditures and reliance upon DHP differ across the groups.⁵ The estimated share of DHP dollars due to active duty service is the ratio of equivalent demand units for active duty personnel and their families to the total number of equivalent demand units in DHP. We first used the Medical Expenditures Panel Survey (MEPS) to estimate the average total health care expenditures each year (2000-2004) by gender and age category.⁶ Estimates of relative use were derived by dividing all estimates by the average total health care expenditures for males ages 18 to 44 (the comparison group). Second, reliance rates for DHP were provided by the DOD from the annual Military Health Care Survey for active duty personnel, their families, and retirees under 65 and their families.

To calculate the costs of future veterans' benefits for current active duty servicemembers, including the costs for health care, compensation, pension, and other types of benefits, we used notional costs as a percentage of basic pay of accruing and actuarially funding VA benefits in

⁴ The age categories used are: 0 to 17 years old, 18 to 44 years old, 45 to 64 years old, and over age 65.

⁵ See Congressional Budget Office, "Growth in Medical Spending by the Department of Defense," appendix B (2003) for a more extensive discussion of this methodology.

⁶ The 2002 estimates are used for 2003 and 2004, because MEPS data for those years have not been released. There is no apparent trend in the relative use data and using an average over previous years did not affect the results.

the DOD budget. The notional cost percentages we used were unofficial Office of Management and Budget estimates. These estimates were based on the most recent official percentages shown in table 12-2 of the 1999 President's Budget.

Determination of Active Duty Servicemembers' Perceptions of Their Compensation

To determine servicemembers' satisfaction and dissatisfaction with components of their compensation, we reviewed past DOD surveys, including the 2002, 2003, and 2004 Status of Forces Surveys. The 2002 survey administered to over 30,000 servicemembers had a response rate of 32 percent. DOD has conducted and reported on research to assess the impact of nonresponse rate on overall estimates. It found that, among other characteristics, junior enlisted personnel (in pay grades E1 to E4), servicemembers who do not have a college degree, and members in services other than the Air Force were more likely to be nonrespondents. We have no reason to believe that potential nonresponse bias not otherwise accounted for by DOD's research is substantial for the variables we studied in this report. Therefore, we concluded the data to be sufficiently reliable for the purposes of this report. To determine active duty servicemembers' perceptions of their compensation, we conducted 40 focus groups at eight military installations across all four services. We gathered supplemental information from focus group participants through a survey that asked questions to assess knowledge, individual opinions, and attitudes toward compensation.

Focus Groups

We conducted 10 focus groups with active duty servicemembers in each of the four services, for a total of 40 focus groups. Focus groups involve structured small group discussions designed to gain in-depth information about specific issues that cannot easily be obtained from single or serial interviews. As with typical focus group data collection, our design involved multiple groups with certain homogeneous factors—such as rank, service, and installation. Each group was designed to involve 8 to 12 participants. Discussions were held in a structured manner, guided by a moderator who used a standardized list of questions. Our overall objective in using a focus group approach was to obtain servicemembers' views, insights, and feelings about military compensation.

Scope of Our Focus Groups

To ensure we achieved saturation, the point where we were no longer hearing new information, we conducted 40 focus groups with multiple active duty servicemembers at eight military installations (see table 4). This design allowed us to identify differences in perceptions of servicemembers

Appendix I
Scope and Methodology

in different branches of the military and in different pay grades. In all focus groups, in order to hear from different perspectives, efforts were made to select participants with differences in sex, marital status, if the member lived on base or off base, and if the member had been recently deployed. Focus groups were conducted from November 2004 to March 2005.

Table 3: Composition of Focus Groups

Service	Location	Servicemember pay grade					Total
		Enlisted			Officer		
		E1-E4	E5-E6	E7-E9	O1-O3	O4-O6	
Air Force	Pope Air Force Base, North Carolina	1	1	1	1	1	5
	Scott Air Force Base, Illinois	1	1	1	1	1	5
Army	Ft. Benning, Georgia	1	1	1	1	1	5
	Ft. Bliss, Texas	1	1	1	1	1	5
Navy	Naval Station Norfolk, Virginia	1	1	1	1	1	5
	Navy Region Southwest, California	1	1	1	1	1	5
Marine Corps	Camp Pendleton, California	1	1	1	1	1	5
	Camp Lejeune, North Carolina	1	1	1	1	1	5
Total		8	8	8	8	8	40

Source: GAO analysis.

Methodology of Our Focus Groups

A guide was developed to assist the moderator in leading the discussions. The guide helped the moderator address several topics related to servicemembers' perceptions of their compensation including their definition of compensation, sources of information on compensation, satisfaction and dissatisfaction with compensation, and any needed changes to compensation. Each focus group started with the moderator describing the purpose of the study and explaining how focus groups work. Participants were assured that all their comments would be anonymous in that their names would not be used in write-ups of the sessions or in the report. The participants were then asked open-ended questions about their perceptions of military compensation. All focus groups were moderated by a GAO analyst, while at least one GAO analyst observed and took notes. After each focus group the moderator and note taker reviewed the transcript together to verify that all comments were captured.

Content Analysis

We performed a systematic content analysis of discussions to categorize and summarize participants' perceptions of their compensation. Using the primary topics covered in the focus group guide, GAO analysts reviewed responses from several of the focus groups and created a list of subcategories within each of the primary focus group topics. A GAO analyst then reviewed the responses from each focus group and assigned each comment to a corresponding category. To ensure inter-rater reliability, another analyst also reviewed each comment and independently assigned it to a corresponding category. Any comments that were not assigned to the same category were then reconciled and adjudicated by the two analysts, which led to the comments being placed into one or more of the resulting categories. Agreement regarding each placement was reached between at least two analysts. The responses in each category were then used in our evaluation of how servicemembers perceive their compensation.

Limitations

Methodologically, focus groups are not designed to (1) demonstrate the extent of a problem or to generalize results to a larger population, (2) develop a consensus to arrive at an agreed-upon plan or make decisions about what actions to take, or (3) provide statistically representative samples or reliable quantitative estimates. Instead, focus groups are intended to provide in-depth information about participants' reasons for the attitudes held toward specific topics and to offer insights into the range of concerns and support for an issue.

The projectability of the information produced by our focus groups is limited for several reasons. First, they represent the responses of only the active duty servicemembers in our 40 focus groups. The experiences of other active duty servicemembers who did not participate in our focus groups may have varied. Second, while the composition of the groups was designed to assure a distribution of active duty servicemembers by several characteristics, including sex and marital status, the groups were not randomly sampled.

Despite these limitations, we gathered data from a broad range of servicemembers at several strata of the military hierarchy and obtained a better understanding of how servicemembers perceive their compensation and where they obtain information about their pay and benefits. We were also able to obtain information complementary to the Status of Forces Survey, which seeks information on satisfaction and dissatisfaction among military servicemembers but does not address reasons for these perceptions.

Use of a Survey to Supplement
Focus Group Findings

We conducted a survey of focus group participants to provide further information on servicemembers' perceptions of their compensation. The survey was administered and received from the universe of focus group participants, which numbered 401. The survey collected additional specific information on servicemembers' satisfaction and dissatisfaction with their pay and benefits, sources of information on their compensation, recommendations for changing compensation, and demographic information.

Since the survey was used to collect supplemental information and administered to focus group participants only, the results cannot be generalized across the population of active duty servicemembers. The results from this data collection effort represent only those who participated in our focus groups.

The objectives of our survey were to collect (1) data that could not easily be obtained through focus groups and (2) collect some of the same data found in past DOD surveys.

The practical difficulties of conducting any survey may introduce certain types of errors, commonly referred to as nonsampling errors. For example, differences in how a particular question is interpreted, the sources of information available to respondents, or the types of people who do not respond can introduce unwanted variability into survey results. To reduce nonsampling errors, we conducted five pretests with active duty servicemembers, both enlisted and officers, and revised it based on the pretest results. We also performed statistical analyses to identify inconsistencies and had a second independent reviewer for the data analysis to further minimize such error. The surveys were administered in person directly after each focus group session.

To analyze survey results, we ran frequencies for all questions and highlighted those where a significant response occurred in a particular category. We also compared responses by pay grade and service.

We conducted our review from August 2004 through May 2005 in accordance with generally accepted government auditing standards.

Sample of a Personal Statement of Military Compensation

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 pay office.

SUMMARY:

A. Basic Military Compensation as of March 2005.....	\$
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 2005 (NOTE 1)

A. BASIC COMPENSATION. Describes the basic elements of compensation paid to all military members. It includes Basic Pay, the value of living in government 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 actual BAH for your location, rank and dependency status (see Note 2).....	\$	\$
BAS	\$	\$
TOTAL BASIC COMPENSATION	\$	\$

B. SPECIAL PAY AND BONUSSES. 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 BONUSSES	\$	\$

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) (Note 1) only payable in certain areas, family separation allowance (FSA), and clothing replacement allowance (CRA). Your total expense allowances are:

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

Note 1: Pay items on your March 2005 LES, marital status and dependents taken from your personnel records. Annual rates for COLA are for 365 days, not 12 times the **March** rate.

Note 2: If BAH was not in effect in March 2005, we assumed you received quarters or meals worth about as much as BAH. If you received partial BAH, we assumed that the partial BAH and value of quarters together roughly equal full BAH.

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 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 \$13.90/day charge for inpatient care. TRICARE Extra offers the same benefit as Standard, but when 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 to TRICARE Prime is conservatively estimated at \$374.27/month/individual, \$ 4,491.24/year/individual, \$1,022.03/month/family and \$ 12,264.36/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.

**Appendix II
Sample of a Personal Statement of Military
Compensation**

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 **\$12,000** and monthly Dependency and Indemnity Compensation (DIC) payments (non-taxable) of **\$967** for the surviving spouse and an additional **\$241** for each surviving child. DIC is adjusted annually for inflation. More information can be found at <http://www.vba.va.gov/>. Also see Survivor Benefit Plan on page 3 of this statement. You are currently paying premiums for SGLI coverage of \$ _____ on yourself and \$ _____ on your spouse.

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

INDIRECT COMPENSATION (A + C)

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

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 (CSB). A description of each follows. Information on all three plans is available at: <http://www.afpc.randolph.af.mil/>. Additional information on the new High-3 and Redux/\$30K CSB choice is available at: <http://dod.mil/militarypay/>.

Plan	Eligible (as determined by DIEUS) (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	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	High-3; Full inflation protection; COLA based on Consumer Price Index (CPI)
-----OR----- Redux/CSB Choice: Instead of retiring under High-3, members may choose to receive a \$30,000 (Note 7) "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.		-----OR----- *Redux/CSB 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.	-----OR----- *Redux/CSB 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 uniformed service (DIEUS) 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 pay; 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.

Note 7: Effective 28 Dec 01, members may elect one of 5 options to receive the \$30K CSB: one lump sum payment of \$30k; two annual payments of \$15K; three annual payments of \$10K; four annual payments of \$7.5K; or five annual payments of \$6K.

(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.

**Appendix II
Sample of a Personal Statement of Military
Compensation**

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, and overseas allowances and in-kind housing may be exempt from State and Local taxes, depending upon **the state you claim as a legal residence.** Relative to the tax laws of your legal residence, this can save you hundreds of dollars each year.

\$ _____

COMMISSARY. Studies have found that commissary shoppers save an average of 30% or more on their grocery purchases, amounting to about \$2,700 annually for a family of four. If you spend the following, your savings will be approximately: \$ _____

Monthly Grocery Purchases

Supermarket	Commissary	Savings	% Savings
\$200.00	\$140.00	\$60.00	30%
\$300.00	\$210.00	\$90.00	30%
\$400.00	\$280.00	\$120.00	30%

Find your nearest commissary through the locations link at www.commissaries.com. Take advantage of the Savings You've Earned!

ARMY AND AIR FORCE EXCHANGE SERVICE (AAFES). Now in our second century of service, the Army and Air Force Exchange Service (AAFES) remains committed to serving you, the "best customer in the world". Your exchanges provide products and services to authorized customers worldwide and generate reasonable earnings to supplement appropriated funds for Army and Air Force morale, welfare, and recreation (MWR) programs. Earnings fund new and improved stores with most of the profits going to MWR programs - over \$2.30 billion last year. AAFES' shelf prices provide you 21.9 percent overall savings compared to off post/base retail operations. While you can enjoy your exchange benefit in many ways the greatest value is AAFES' pledge to "Go Where You Go." And remember, AAFES offers 24/7 convenience through its website 'www.aafes.com'.

SURVIVOR BENEFIT PLAN (SBP). All pay stops when a member dies. However, if you die on active duty, 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. The FY05 NDAA eliminated the reduction of SBP at age 62, with phase-in rates of 40% in 2005, 45% in 2006, 50% in 2007, and 55% in 2008. The SBP annuity for your survivor is adjusted each year by the same percentage increase given to military retired pay. Additional information can be found at <http://www.afpc.randolph.af.mil/>

\$ _____

UNIFORMED SERVICE THRIFT SAVINGS PLAN (TSP): You can gain additional tax deferred advantages through participation in the TSP. You are limited in the amount of Base Pay you may contribute (below), however you may contribute up to 100% of your special, incentive, or bonus pay. There are also annual contribution limits that apply (below). If you perform duty in a designated combat zone, your contributions to TSP will be tax-exempt (versus tax deferred) and will not count against your tax deferred limits. The combination of your tax-exempt and tax deferred contributions are limited to \$40,000 for any year. More information can be found at <http://www.tsp.gov/>

Year	% of Base Pay	Total Annual Tax Deferred Limits
2005	10	\$14,000
2006 +	(unlimited)	\$15,000

\$ _____

FEDERAL LONG-TERM CARE INSURANCE PROGRAM (FLTCIP): The FLTCIP is the only long term care insurance program sponsored by the Federal Government. It is managed by the Office of Personnel Management and offered by two insurance leaders--John Hancock and MetLife. It provides comprehensive benefits to included home care, informal care, and inflation options at competitive group premiums. The

Appendix II
Sample of a Personal Statement of Military
Compensation

FLTCIP helps preserve your retirement savings should a long-term care need arise. Those eligible for the FLTCIP include all Federal Employees (Uniformed Service members), their spouses, adult children (including natural, adopted & step), parents, parents-in-law, and stepparents. Call 1-800-LTC-FEDS (1-800-582-3337) or visit the web site at: <http://www.LTCFEDS.com> \$ _____

EDUCATION PROGRAMS. Members in authorized off-duty education programs receive up to 100 percent of tuition costs, up to a maximum of \$250.00 per credit hour, \$4,500 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 \$ \$36,144 with yearly increases as determined by the consumer price index. \$ _____

SERVICES ACTIVITIES. Provide conveniently located, low-cost, professionally managed activities and entertainment. You and your family members receive significant savings when you participate in Services 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 personal financial management counseling, relocation services assistance, transition counseling, spousal employment assistance, and assistance from a wide range of other programs available from Air Force Family Support Centers. Air Force Aid Society provides zero interest emergency loans and grants to members who qualify (total loans and grants given in 2004 was \$11,300,000 and 10,000,000 in community outreach and education programs). \$ _____

LEGAL COUNSELING. Military members can get free legal counseling and assistance. \$ _____

Consultations with an attorney:	\$150.00
Wills:	\$200.00
Notaries:	\$5.00
Advance Medical Directives:	\$75.00
Client Correspondence:	\$50.00
Powers of Attorney:	\$50.00

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 AMC Space Available web page at <http://public.amc.af.mil/Library/SPACEA/spacea.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 \$9.32 for a single enrolled family member and \$23.31 for families with two or more members enrolled. This equates to an annual savings conservatively estimated at \$175 for single and \$439 for family enrollments. Basic preventive, diagnostic and emergency 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 \$ _____

Comments from the Department of Defense



OFFICE OF THE UNDER SECRETARY OF DEFENSE
4000 DEFENSE PENTAGON
WASHINGTON, D.C. 20301-4000



JUN 24 2005

PERSONNEL AND
READINESS

Mr. Derek B. Stewart
Director, Defense Capabilities and Management
United States Government Accountability Office
Washington, D.C. 20548

Dear Mr. Stewart: *Derek*

This is the Department of Defense response to the Government Accountability Office (GAO) draft report, "Military Personnel: DoD Needs to Improve the Transparency and Reassess the Reasonableness, Appropriateness, Affordability, and Sustainability of Its Military Compensation System," dated July, 2005 (GAO-05-798). The Department has technical concerns with some of the calculations in the draft report, but generally concurs with the recommendations. The Department's comments are enclosed.

If you require additional information, please contact Dr. Saul Pleeter at (703) 695-9371. The Department appreciates the opportunity to comment on the draft report. Thank you for your interest in this matter.

Sincerely,

William J. Carr
Acting Deputy Under Secretary
(Military Personnel Policy)



**DEPARTMENT OF DEFENSE COMMENTS GAO DRAFT REPORT
GAO CODE 350563/GAO-05-798**

Subject: GAO Draft Report, "MILITARY PERSONNEL: DoD Needs to Improve the Transparency and Reassess the Reasonableness, Appropriateness, Affordability, and Sustainability of Its Military Compensation System," dated June 10, 2005 (GAO Code 350563/GAO-05-798)

Technical Issues: There are 3 main technical issues with the presentation of the data in the draft report (see attached):

1. No acknowledgement of the Global War on Terrorism (GWOT) costs and funding
2. Use of end strength vice average strength (workyears) in per capita calculations
3. Constant dollar adjustments

Recommendations:

RECOMMENDATION 1: The GAO recommended that the Secretary of Defense compile the total costs to provide military compensation and communicate these costs to decision makers within the administration and the Congress, perhaps as an annual exhibit as part of the President's Budget submission to Congress. (p. 39/GAO Draft Report)

DOD RESPONSE: Partially concur. GAO's recommendation is to improve transparency over total compensation. We agree with this goal. However, since the costs for a military member extend to four departments, including Treasury, Veterans Affairs, Labor and Housing and Urban Development, this may be a more appropriate issue for the Office of Management and Budget.

RECOMMENDATION 2: The GAO recommended that the Secretary of Defense assess the affordability and sustainability of the compensation system and its implications on readiness as well as the reasonableness and appropriateness of the allocation to cash and benefits and whether changes in the allocation are needed to more efficiently achieve recruiting and retention goals in the 21st Century. (p. 39/GAO Draft Report)

DOD RESPONSE: Concur. We agree with GAO in the need analyze the affordability and sustainability of the military compensation system. DoD is already engaged in multiple simultaneous efforts to assess the overarching military personnel compensation strategy including the Defense Advisory Committee on Military Compensation, the Quadrennial Defense Review and the 10th Quadrennial Review of Military Compensation. DoD will continue to actively point out the impact of the legislative process to Congress as we did with concurrent receipt, the survivor benefit program and expanding retiree health care.

RECOMMENDATION 3: The GAO recommended that the Secretary of Defense develop a comprehensive communication and education plan to inform service members of the value of

their pay and benefits and the competitiveness of their total compensation package when compared to their civilian counterparts that could be used as a recruiting and retention tool. (p. 40/GAO Draft Report)

DOD RESPONSE: Partially concur. All of the services currently have multiple resources available for service members, including websites, brochures and instruction. For example by linking through the Navy Personnel Command Website members can access an electronic Pay and Compensation Calculator at <http://www.npc.navy.mil/CareerInfo/StayNavyTools/CareerTools>. This tool calculates the sum of members' pay and benefits and breaks them out by direct, indirect, and deferred (retired) compensation. It also isolates taxable and tax-free compensation and calculates the comparable civilian wage that would have to be earned to match military pay and allowances. Additionally, the annual "Career Handbook" supplement to the Navy's monthly "All Hands" magazine was released in June 2005. The supplement provides details on Navy compensation, including pay and allowances, educational opportunities, career transition and retirement benefits, as well as training, advancement, and commissioning opportunities. DoD has also contracted with Ruehlin Associates to provide "Career Planning and Management Seminars," during which the total military compensation package is discussed as part of career decision-making when considering transition to the private sector.

The Air Force mails an Annual Statement of Military Compensation every spring to members. They also prepare a Compensation Fact Sheet distributed to First Sergeants (posted to Air Force Personnel Center Web site under enlisted/officer retention). Base Career Advisors provide briefings to members 13 - 15 months prior to the DOS/EOS for retention purposes. The Army also sends out an annual report on compensation and maintains a website offering additional information.

The Office of the Under Secretary of Defense for Personnel and Readiness has a website that offers comprehensive information concerning military compensation. There are nearly a million 'hits' to this website each month. In spite of these and other efforts, there is a perception that military compensation is underreported and undervalued. DoD will explore an information/marketing campaign that will improve understanding of the system.

GAO Contact and Staff Acknowledgments

GAO Contact

Derek Stewart, (202) 512-5559 (stewartd@gao.gov)

Acknowledgments

Lori Atkinson, Alissa Czyz, Natasha Ewing, Alison Martin, David Mayfield, Lindsey Mosson, James Pearce, John Pendleton, Charles Perdue, Terry Richardson, Samuel Scrutchins, and Sonja Ware made key contributions to this report.

Related GAO Products

Defense Management: Key Elements Needed to Successfully Transform DOD Business Operations. [GAO-05-629T](#). Washington, D.C.: April 28, 2005.

Military Personnel: Preliminary Observations on Recruiting and Retention Issues within the U.S. Armed Forces. [GAO-05-419T](#). Washington, D.C.: March 16, 2005.

21st Century Challenges: Reexamining the Base of the Federal Government. [GAO-05-325SP](#). Washington, D.C.: February 2005.

Military Personnel: DOD Needs More Data Before It Can Determine if Costly Changes to the Reserve Retirement System Are Warranted. [GAO-04-1005](#). Washington, D.C.: September 15, 2004.

Military Personnel: Survivor Benefits for Servicemembers and Federal, State, and City Government Employees. [GAO-04-814](#). Washington, D.C.: July 15, 2004.

Military Personnel: DOD Has Not Implemented the High Deployment Allowance That Could Compensate Servicemembers Deployed Frequently for Short Periods. [GAO-04-805](#). Washington, D.C.: June 25, 2004.

Military Personnel: Active Duty Compensation and Its Tax Treatment. [GAO-04-721R](#). Washington, D.C.: May 7, 2004.

Military Personnel: Observations Related to Reserve Compensation, Selective Reenlistment Bonuses, and Mail Delivery to Deployed Troops. [GAO-04-582T](#). Washington, D.C.: March 24, 2004.

Military Personnel: Bankruptcy Filings among Active Duty Service Members. [GAO-04-465R](#). Washington, D.C.: February 27, 2004.

Military Personnel: DOD Needs More Effective Controls to Better Assess the Progress of the Selective Reenlistment Bonus Program. [GAO-04-86](#). Washington, D.C.: November 13, 2003.

Military Personnel: DOD Needs to Assess Certain Factors in Determining Whether Hazardous Duty Pay Is Warranted for Duty in the Polar Regions. [GAO-03-554](#). Washington, D.C.: April 29, 2003.

Military and Veterans' Benefits: Observations on the Concurrent Receipt of Military Retirement and VA Disability Compensation. [GAO-03-575T](#). Washington, D.C.: March 27, 2003.

Military Personnel: Management and Oversight of Selective Reenlistment Bonus Program Needs Improvement. [GAO-03-149](#). Washington, D.C.: November 25, 2002.

Military Personnel: Active Duty Benefits Reflect Changing Demographics, but Opportunities Exist to Improve. [GAO-02-935](#). Washington, D.C.: September 18, 2002.

Military Personnel: Higher Allowances Should Increase Use of Civilian Housing, but Not Retention. [GAO-01-684](#). Washington, D.C.: May 31, 2001.

Defense Health Care: Observations on Proposed Benefit Expansion and Overcoming TRICARE Obstacles. [GAO/T-HEHS/NSIAD-00-129](#). Washington, D.C.: March 15, 2000.

Military Personnel: Preliminary Results of DOD's 1999 Survey of Active Duty Members. [GAO/T-NSIAD-00-110](#). Washington, D.C.: March 8, 2000.

The Congress Should Act to Establish Military Compensation Principles. [GAO/FPCD-79-11](#). Washington, D.C.: May 9, 1979.

GAO's Mission

The Government Accountability Office, the audit, evaluation and investigative arm of Congress, exists to support Congress in meeting its constitutional responsibilities and to help improve the performance and accountability of the federal government for the American people. GAO examines the use of public funds; evaluates federal programs and policies; and provides analyses, recommendations, and other assistance to help Congress make informed oversight, policy, and funding decisions. GAO's commitment to good government is reflected in its core values of accountability, integrity, and reliability.

Obtaining Copies of GAO Reports and Testimony

The fastest and easiest way to obtain copies of GAO documents at no cost is through GAO's Web site (www.gao.gov). Each weekday, GAO posts newly released reports, testimony, and correspondence on its Web site. To have GAO e-mail you a list of newly posted products every afternoon, go to www.gao.gov and select "Subscribe to Updates."

Order by Mail or Phone

The first copy of each printed report is free. Additional copies are \$2 each. A check or money order should be made out to the Superintendent of Documents. GAO also accepts VISA and Mastercard. Orders for 100 or more copies mailed to a single address are discounted 25 percent. Orders should be sent to:

U.S. Government Accountability Office
441 G Street NW, Room LM
Washington, D.C. 20548

To order by Phone: Voice: (202) 512-6000
TDD: (202) 512-2537
Fax: (202) 512-6061

To Report Fraud, Waste, and Abuse in Federal Programs

Contact:

Web site: www.gao.gov/fraudnet/fraudnet.htm

E-mail: fraudnet@gao.gov

Automated answering system: (800) 424-5454 or (202) 512-7470

Congressional Relations

Gloria Jarmon, Managing Director, JarmonG@gao.gov (202) 512-4400
U.S. Government Accountability Office, 441 G Street NW, Room 7125
Washington, D.C. 20548

Public Affairs

Paul Anderson, Managing Director, AndersonP1@gao.gov (202) 512-4800
U.S. Government Accountability Office, 441 G Street NW, Room 7149
Washington, D.C. 20548