



Defense Advisory Committee on Military Compensation

**PUBLIC MEETING
CRYSTAL CITY HILTON
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Transcript

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PARTICIPANTS

This list includes members of the Committee participating in the meeting. (Committee member Dr. Martin Anderson was not present.)

No.	Name	Role
1	ADM Don Pilling	Chairman of the Committee
2	Mr. Frederick Cook	Committee Member
3	Mr. Joseph Jannotta	Committee Member
4	General Les Lyles	Committee Member
5	Dr. Walter Oi	Committee Member
6	Dr. John White	Committee Member
7	Mr. Paul Hogan	Chief of Staff

SIGNED-IN VISITORS

This list includes all signed-in (non-staff) visitors to the public meeting.

No.	Name	Organization Symbol
1	Vince Crawley	Army Times
2	Tom Philpott	Military Update
3	Lisa Bryes	Stars & Stripes

TRANSCRIPT

Admiral Pilling: Good morning. We will start with our second public meeting of the Defense Advisory Committee on Military Compensation. And what I would like to do is to start off this session with sort of an overview of what we've learned in the administrative briefs that we have received, and to have a discussion among the committee members of things that we should be thinking about doing here in the near term, remembering that our schedule is for an interim report in September to the Secretary of Defense, with a final report in about the April timeframe in the year 2006.

Just to make sure we're all focused on the same structure, what we have been asked to do is basically come up with a strategic architecture for military compensation. In other words, provide a framework, or a theory, or a set of principles on which you can make changes to the compensation system.

We recognize, of course, in this environment you can't have a clean sheet of paper, there's a lot of history involved with the way the compensation structure, the way it's structured today. But at least we can think about where we might want it to be.

For example, the preliminary data that we have seen indicates that, in the private sector at least, there is an increasing emphasis on current compensation and less emphasis on deferred compensation, whereas, within the Department of Defense structure for military compensation, we see an increasing share of total compensation on the deferred compensation side, and, not to say that that's wrong, but it is a difference between the current military compensation system and the private sector compensation system.

So as we think about how a compensation system should be structured, we want to make sure that it's simple and flexible and easily understood, and we want to make sure it has two characteristics:

Ensure the ability to recruit, retain and motivate the right people; and we have to recognize that the all-volunteer force has been very, very successful. But we can't be – we cannot ignore the fact that the Army, and to some extent the Marine Corps, are having some trouble in recruiting. And so the balance between the monies that are spent on recruiting and retention, we might want to think about a short-term change in that, but, strategically, where do we want to have the emphasis in how we structure a bonus program to recruit and retain the right people.

And then the other important aspect is force management. And you want to make sure that a compensation system allows force managers the ability to train, distribute, transition between active and reserve, and to separate gracefully those people who choose to come on active duty.

So those are sort of the goals. And I would ask the committee if they have any comments that they would like to add. Joe?

Mr. Joseph Jannotta: Admiral Pilling, we've talked about the notion of some underpinning principles that would guide our actions. And I wonder if we ought not to come down on three or four that might help us, as a sort of a compass. And one of them, as a start, is this idea of keeping the military force human. Certainly ought to be one of our goals. That could be one of the underpinning principles. So, I'd like to at least get other members' ideas, thoughts about that, that we might, a subcommittee or just a group of us, talk about that and come up with some underpinning thoughts that will help us in our work.

General Lyles: Joe, could you define – when you say, human, what the context is of that, because it's obviously a broad term.

Mr. Joseph Jannotta: The idea, the principles? Well, they would be kind of values, I think. What are the values that are going to guide us in our deliberations? And, as I said, I think the first one might be this notion of human, the keeping the force human. We – thanks, Fred – we've seen data that suggests that there is some difficulty in this period of – we're in a voluntary – we're in a protracted war – that this puts tremendous stress and strain on the family. So I think we ought to be looking at how do we help. And that we – there's a lot of concern about this. We've been briefed on it. But I think we can even go further, in that whole area of, how do we make this more human, and this piece, uh, element. And I think it starts with the family and, in particular, the spouse.

Admiral Pilling: I think in our briefings yesterday, from OSD, we learned that one of the major issues they have is spouse employment. And there are things you can do to think about, that may not be directly related to compensation. But homesteading policies, and length of tours and, how you figure out a way to make sure spouses can have a career as well, or something of a career, recognizing [that] you have to maintain the flexibility of being able to move the active duty member, or the member, anywhere. So I think you're right, and in this brief we sort of focus on four areas that we might examine. But I think based on what we learned yesterday, I think we might need a fifth sub-group to look at these human aspects of management of force.

Mr. Jannotta: The notions of...

Mr. Cook: Uh, one more, Admiral? In the first bullet there, when we say "right people," I – just for emphasis I think we mean both caliber and numbers, don't we? It's a quality and quantity issue.

Admiral Pilling: Yes, it is.

General Lyles: Don, let me – can I go back to one thing, just, and this is perhaps for my edification, and certainly I don't have the experience in the private sector that Fred has – or perhaps many others in this panel. But we've mentioned a couple of times about the difference between the private sector putting emphasis on current compensation versus deferred. My current experience, serving on a couple of corporate boards, and being on a compensation committee of those corporate boards, I see just the opposite. All the emphasis and all the discussions we have on those boards when we talk about compensation, granted, for the middle level or senior level executives, is all about deferred. There is very little – I mean, there is [an] emphasis on current, but there is a balance.

So I don't see this sort of a shift that we'd mentioned yesterday and mentioned today that the private sector is just the opposite of what DoD is. I see them putting a lot of emphasis, a lot of discussion, on deferred compensation for retaining and motivating people as opposed to what we described yesterday. So, maybe I'm wrong. I'd like to understand the context in which we are making that statement.

Admiral Pilling: Let me ask Mr. Cook to...

Mr. Cook: Well, I work in the private sector on compensation programs. And when we say that the private sector is deemphasizing deferred over current, we are basically talking about the broad-based pension plans and retiree medical. The private sector is moving away from defined benefit pension plans, you know, where you get an annuity, and toward 401 type K plans, which are voluntary, you know, and so if you don't participate in them, you don't have anything. The military has that in this TSP plan. But they're moving away from the pension plan because they found the people have a high discount rate – active employees don't, you know, it's costing more than they're getting credit for. And the employees like the idea of, you know, they put down a dollar and the company puts down 50¢ and they invest it the way they want it. They like that.

Retiree health care is, like, in terminal decline in the private sector, because the costs are just going out of sight. And the companies – the big, old smokestack industries – you've read the reports about how much it's costing General Motors to provide it for its retired people. And it's just, it's – it's a killer. The ones that are keeping it – well, first of all, there is two trends, all right? If you've got it in force, you've got kind of a promise, and you can't take it away from them. You can say, anybody new – anybody new coming in, sorry, you're not getting anything. So you get a bifurcated work force. And then – but for the people who have it, the private sector is in a cost-sharing mode that they've instituted. So they, you know, if they get a cost increase from the insurance company, they share it. The employees' enrollment fees, or their co-pays go up, or all the various things that you have here, and nobody likes that. People don't like it, but you know what? They would rather have it than not have anything. So that's what I meant by it.

General Lyles: Okay.

Mr. Cook: The executive level, yeah, there's all sorts of deferral schemes and equity schemes going on.

General Lyles: Gotcha. And in some respects, I guess, I was being a little myopic and just focusing on just a limited part of the compensation, as opposed to – which is really related to bonuses – and you've expanded the horizon so I thank you. I appreciate it that, Joe. Excuse me, Fred.

Dr. White: On the same subject, a couple of things. Fred, to some extent, aren't we seeing the private sector basically de facto push off the health care issue to the public sector? Over time, we are going to reduce, they are going to reduce their contribution and their commitment and rely on the government. Even if the government doesn't want to do it, that's what's going to happen.

Mr. Cook: Yes, Sir.

Dr. White: And, secondly, with respect to defined benefit plans, as you say, they are going away. And it isn't clear, is it, that the 401K type plan, in fact, will be adequate for the population, in terms of retirement later. So you may, there too, get a public response that says, hey, this process doesn't take care of me. Now I'm living longer, and so on and so forth. Is that...?

Mr. Cook: I'm actually a fan of pension plans as opposed to 401K investment plans. The 401K investment plan basically transfers the risk from the company to the employee.

Dr. White: Right.

Mr. Cook: The benefit also, if he invests in stocks, and there's a good run, he gets a benefit out of it. But then they can take a lump sum when they retire, and who knows if they will handle that wisely or not. The best model, which is actually what the military has, is a combination of pension, which provides, is designed to provide, a floor benefit, you know, you can't outlive it, and a 401K with a match, that is supplemental on top. So it's not one or the other. It's a combination of both, coordinated to provide a pretty good benefit. And I think our commission – our committee – ought to look at that possibility, going forward.

Because we now have a – they call it TSP, right? The Thrift Savings Plan. It's kind of just a generic name, isn't it? But there's no company – there is no match, no government match to it. So what we find in the private sector, if you don't have a match, you have very low enrollment. It's still advantageous, you know, because there's tax benefits to it. It's like an IRA. But if you throw a match to it, which would, like, vest maybe, after five years, so get you through your first tour. Your own money is always your own money right, but the match, you have to stay? That's what the private sector does. That would be something I think we should give some thought to.

Admiral Pilling: Dr. Oi?

Dr. Oi: The last data I've seen [inaudible] and we went down from 20-30% increases per year. Then the demand for 401Ks dropped. And it's now starting – and we've moved back to defined benefit plans. And I think it's coming back now toward defined contribution. But the question here is that, in addition to the retirement per se, and the dollar sum that we could use to buy travel, housing, and so forth, we ought to look at a concept of full income to consider not only what is provided to you in cash, in the pension, but also, in-kind, especially in terms of the medical benefits, which are a major part of the return to a retired military person, as opposed to a civilian retiree. And that we should count, and look at the full income of a retiree person.

Admiral Pilling: That's a fair point. I have a slide up now which says that there are certain principles, I think, that we have to follow, if we look at the current compensation system, and if we are going to make any suggestions as to changes in it.

First of all, I think it has to be fair. For people currently in uniform, it should never be perceived that we're taking away from them. It has to be fair and objective. So that is a principle I think we have to follow. And there are really three constituencies here. The force managers, who have to structure the force, and ensure they have tools that allow them to increase or decrease

certain characteristics of the force. So that's basically the perspective we come from in our guidance. But the other two constituencies are just as important, and that's the force members themselves, and of course, the Congress.

And then finally, we must make sure that we've got an incentive structure that meets the readiness goals under an all-volunteer force. And of course, we've already pointed out the fact that the Army, and to some extent the Marine Corps, are suffering some recruiting problems, so we want to make sure that we incorporate that into our thinking.

And finally, we want to make sure that whatever we suggest is competitive and equitable, and this is – we have to make it perfectly clear that what we're trying to do is improve our ability to attract and retain the right people. And this is not a budget drill – this is really all about force management: what's the best way to come up with a theory and a framework for compensation to manage the force?

Going the wrong way – here we are. Whoop! This is a hair trigger. Uh, okay.

The current compensation, that's near-term current compensation, is what I mean by that. What we have – what people see on their leave and earnings statements, plus the in-kind compensation. From what we understand from the administrative briefs, they seem to have worked in the recent past to, or seem to be adequate to recruit, retain and motivate the 85% of the enlisted force who never get to retirement eligibility, and it's about 50% of the officer force that never gets to retirement eligibility.

The recruiting problem may mean in the near term we might have to make some changes to current compensation, but in general it appears from our administrative briefs that what we're doing on current compensation appears to make sense.

There are other issues in the in-kind compensation which Mr. Jannotta mentioned, and that's his human dimension, and that's housing and homesteading and issues like that, we can look at.

But we did note that there seems to be a large number of special and incentive pays, many of which exist for historical reasons, and the actual amount of resources that is used for these special and incentive pays is somewhere on the order of 5% of military pay. And so the question becomes, should we be looking at streamlining special and incentive pays, and manage it more like, let's call it the selective reenlistment bonus with varying levels set by the services. And should we be thinking about, do you want more of, a greater percentage than 5% of military pay in that category, so you can really make it much more targeted and useful in shaping the force than we have now.

A second issue that came out of some of our administrative briefs were [that] the family housing benefit is primarily focused on people renting, not buying. And, if you do have a homesteading policy in the military service, if we could structure the family housing benefit to provide an incentive for people to buy their houses because they're going to be in a certain geographic area for a long period of time, that might be of great benefit to the enlisted force.

Dr. White: Mr. Chairman, I was struck yesterday in the briefing we had on the special incentive pay of the mix and variety, in the sense that so much of it – some of it seems to be targeted, like the reenlistment bonus. Some of it seems to be an artifact of something that's happened some time in the past. The fact that many of these are really quite modest and, in fact, haven't changed over time at least reflects to me that the institution and the force managers aren't seeing these as actually management tools, or at least, some of them. Does that comport with your view?

Admiral Pilling: I think that's right on. I mean, I noticed yesterday that what's called command-at-sea pay – and it has another name technically – but if you're an O5 in command of a ship at sea, you get \$100 benefit, which is what I realized – \$100 a month as a commanding officer of a ship twenty years ago – and it's still \$100. It hasn't changed. And it's recognition of responsibility, and perhaps, when you think about, would I have turned down an opportunity to command a ship at sea, if I wasn't offered that hundred dollars [Laughter] I don't think so. So there may be some benefit in looking at these bonuses, which really are recognition of certain characteristics, and it's not very much money, and whether we might want to propose a restructuring of these in some way and have – most of them are in law –

Dr. Oi: It's still a cup of Starbucks a day [laughter].

Admiral Pilling: They're in law, so, I mean, if we were going to suggest a change, it would have to be a real restructuring of a whole series of laws in which these 66 or 67 special and incentive pays exist today.

Dr. White: Why shouldn't we, perhaps, contemplate giving – constructing it in a way that gives the Department management more authority in this area and more of the ability to propose and adjust these particular pays, obviously with responsibility to report to the Congress and justify their decisions.

Admiral Pilling: And, I think that's right. The Department has flexibility on reenlistment bonuses. And so, maybe on these special and incentive pays that have a lot of history behind them, we would – you could argue that the Department would have more flexibility in managing them.

Mr. Cook: Another comment?

Admiral Pilling: Yes sir.

Mr. Cook: I have an interest in, when we examine special and incentive pays, in examining whether we should recommend – assuming we keep them in some form or other – that they remain a flat, you know, dollar amount per month, which go to you regardless of rank, or whether it is variable with your rank. Because, for example, if it's \$150 a month, that's one thing to an E1 through E3, as a percent of their pay – as a magnitude in relation to their base pay – and in the private sector, at least, we would have a concept that things like that would be stated as a percent of base pay, rather than as a flat dollar amount. So, I know it's a controversial thing, Joe, you're talking about, you know, what's its purpose? Is it hazardous duty, and is it more hazardous if you're an O6 than an E4? And it's very controversial, but I think it's worth examining.

Admiral Pilling: Okay. We now are engaged in the longest period of time that we've been in conflict overseas with the all-volunteer force, and so the ability to adapt to prolonged conflict, and the way we're using reserves today, it's only now being tested. But we want to make sure that a compensation system does give you the flexibility to compensate members in proportion to the risks we're asking them to take. Because clearly somebody on the ground in Iraq today is at much greater risk and hazard than those people who are back here at their normal peacetime base. And so we want to figure out a way to make sure that the way we compensate those people accurately reflect[s] what we're asking them to do.

And then this support of fully integrated operational reserve, most people – it's our understanding, my understanding at least, that when a lot of people joined the reserve and the guard, they didn't envision the way the reserves are being used now at their initial,

when they initially joined. That's not to say that they want out, but the point is, it is different, a different way of using the reserves today than it was thought about ten years ago. So we want to review how we support a fully integrated operational reserve within the total force.

Sir, Dr. White.

Dr. White: It would seem to me that, if we're going to look at that, and we must, there's a lot more here in terms of how you restructure the reserve; it isn't just a question of compensation. And you probably can't do it with just – you'll probably get it wrong, if you limit your analysis to compensation issues. So it's a very big subject, obviously. I don't know what the answer is, but do we want to take that on? I guess we'd have to, in terms of dealing with this issue.

Admiral Pilling: I think it's the most complex issue we have in front of us, for a lot of historical reasons. And we have to have a compensation system that views the active-duty and the reserve components in a way that reflects the integration of the reserves into this operational force for an extended conflict, which is what we are doing today.

Any other comments on that?

Deferred – whoops, this has a hair trigger, there it is – deferred compensation, and by that I mean retired pay and retired medical care, yes, we all recognize that it's becoming more and more costly and the, in particular, retired pay structure is a holdover from the draft era. Yesterday we were exposed to some of the early studies on the retirement system, going as far back as 1948, where they were examining what sort of retirement system we needed to ensure that we had a young and vigorous force.

And so we have this cliff vesting perspective on our current retirement system, where if you leave before twenty years, you basically get no retirement, and you can see the impact is that it's very – it provides for a very stable force of people, in, let's say, the tenth through the twentieth year, and then about 90% of those people opt to leave at the 20-year point. And so there's some instability that happens because of that. It makes it very, very difficult for force managers if, for example, you have overages in certain years-of-service cells at the fourteen- to sixteen-year point, on how you manage that. Right now, you end up providing these people options to change their specialty. And in the 90's, when we were downsizing, we offered them things like reduced annuities, and lump-sum payments to change, but it's very, very painful because of this cliff vesting perspective. And I think we have to keep in mind that only about 15% of the enlisted force and 50% of the officer force actually get to a retired status. So there is an aspect of force management under the current system that I think we have to consider.

Now, on retired medical care, we can make recommendations on how to, perhaps, make that less costly by changing some of the co-pays, but nothing really structural there. Perhaps the way the Department funds it is a valid place to look.

Mr. Jannotta: Admiral Pilling, isn't it safe to say that we're very concerned, as we look at these projections, the projected numbers, and the curve, as you take that curve out, and, let's say, 2009, 2010, 2015, and 2020, that it's very concerning to see the impact, particularly on the medical care side. And I think we've got to look at that somehow or other, and it's a big issue. It's an issue for the Department of Defense, but it's also a societal issue, too. Health care costs going up and out of control.

Admiral Pilling: Right, I think Dr. Jones, when he talked to us yesterday, told us that in the year 2009, 11% of the defense budget is going to go for the medical care system, which is a pretty healthy share, whereas in the recent past it's been on the order of 3-4%. And so, if it's doubling, and possibly even tripling in the near term, then it's an issue that we ought to address.

Mr. Jannotta: A huge issue.

Mr. Cook: Just a related comment. The fact that only 15% of the enlisted force and 50% of the officer force benefits from it, I think it shouldn't really be thought of as diminishing the importance of it to a total comp program. I mean, I think a lot of active duty military, even if they're not planning on staying twenty, they appreciate – they should appreciate the fact that the government and the military takes care of the people who go beyond twenty, and that it is of value to them, even if they don't personally participate in it.

Mr. Jannotta: One of the things that we've heard is that there is a lot of misconceptions within the armed services, in terms of what they're getting, the value of what they're getting. So there's a, I think, something we need to look at, is how do we better communicate – how do we help these active duty people communicate these problems and, not problems, but the issues surrounding what they're getting.

Admiral Pilling: Right and I think we learned in one of the briefs we had yesterday afternoon on non-monetary incentives, that the first-tier managers in the force are really the ones that have to be familiar with what the total package is, because those are the ones that the average enlisted member goes to see to ask questions. And so...

Dr. Oi: It isn't quite [inaudible, who have formerly had the people receive the regular military retirement. Because there are other, better programs – medical care, disability pension, so forth. It proves regular military personnel who actually performed it 20 years ago.] So that we have to look at the balance of all of this in terms of what the right package is to ensure stability not only to the active-duty personnel, but to their families and dependents.

Admiral Pilling: Right, the numbers on the screen are just for the people who have, get to a regular retirement and not the people who might have a disability retirement because of a combat injury or peacetime injury. Dr. White?

Dr. White: One of the things that strikes me about the retirement system is that if I write down the attributes, which I think a retirement system ought to reflect, and back to our architecture, this one doesn't make it. It doesn't provide the flexibility; it seems to me it's uneven in terms of who it delivers benefits to. It doesn't allow extensive management adjustment in terms of whether or not we're going through downsizing, or whether we're going through a short-term increase in the force. Both of those events we have been experiencing, sometimes simultaneously, in different services. And it just seems to me that we ought to look at this in terms of whether or not it meets the criteria.

Admiral Pilling: I agree, and I think yesterday we were told that as long as the force structure is stable, it seems to work. But if you have significant downsizing, then the current retirement scheme presents a force management problem.

Dr. White: Well, it may also, even if you just want to experiment with changing the composition of the force – let's assume, for example, we wanted a force that over time reflected an increased experience base, because that provides you with a more skilled force. And since the budget constraints are going to drive us to reflect in our, in these decisions taking advantage of productivity,

in terms of the inter-mix of the weapons systems and the operations, that seems to me, there too, you want that flexibility and this doesn't give you that flexibility.

Admiral Pilling: All right. So what I have for the next couple of slides is a near-term action plan and I'm going to make an adjustment to reflect the human dimension. But I think in the near term, we would be well served if we looked at the special and incentive pay structure to see if streamlining makes sense, and perhaps look at some of those recognition pays that may appear outdated. And as I mentioned, if only 5% of military pay is in this category of funds, is that sufficient to help force managers target the individuals that they want to retain and reward?

And following up on Dr. White's point, the current retirement pay system – is there some arrangement, which would allow more flexibility that might have earlier vesting? And you mentioned, Mr. Cook, maybe a five-year vesting or a 10-year vesting, some contribution to the member's TSP. And so, your money is always your money, but if the government starts contributing to a TSP, from the very first day, once you get vested, that money is yours as well. And is there some way to, perhaps, do a reduced annuity? Or a lump sum buyout for retirement prior to age 60? And then, when you get to age 60, or age 62, whatever year, whatever age makes sense, then you would have a full annuity, which would allow people, when they phase into retirement, have a lump sum payment, to invest it the way they see fit, and then, of course, knowing that they are going to see, essentially, a full annuity when they hit a certain age later on.

Mr. Jannotta: Why do we, Admiral Pilling, this is an off-the-top thought, but why is 60 such a magical point? Certainly in the private sector it's – they're taking those numbers out, aren't they, Fred? I think, looking at...

Mr. Fred Cook: Well, no, I think this is correctly stated here, Joe, because...

Mr. Jannotta: But why 60? Why is 60 a...

Mr. Cook: All it means is that it's a reduced annuity for retirement prior to 60. You know, it means that you get a hair cut. If you say, I want to start my pension before 60 – and it's generally thought that if you don't start your pension until 60, that's like a normal retirement, 60 or 65...

Mr. Jannotta: Well I'm thinking 65 or later is what I was wondering. Why wouldn't it be later?

Mr. Cook: Well, guys like you and me, we're vital, you know, we're ready to go [laughter]. Go to the end.

Mr. Jannotta: [laughing] we're not smoking anymore, we're...

Mr. Cook: But everybody isn't. You have an age. You have an age, you know? For a lot of reasons, you don't just – it's not individually determined.

Mr. Jannotta: It's just a question.

Admiral Pilling: Well, I mean, I had to pick a number. I could have picked age 62, which is essentially when officers have to retire – you can't stay on active duty. Or, the current generation that's in the force, their Social Security – full Social Security eligibility is...

Mr. Jannotta: at 62 years.

Admiral Pilling: at age 67.

Mr. Jannotta: Oh, 67 is it right now?

Admiral Pilling: So I mean, there are three numbers, but we've taken the age...

Mr. Jannotta: Three numbers we could work with.

Admiral Pilling: Yes.

Mr. Cook: Well this is an important slide, and let me just sort of play the bad guy and indicate how the private sector would deal with this here. The private sector would be right lined up, you know, where they're having both the TSP and a pension, they'd be right lined up with this. They would require that if you want to start taking your pension early, and you can if you're vested, and you start taking it early, you get what's called an actuarial reduction, because you're going to live longer. So you started early, there are going to be more payments made, so you get less each payment, same as the system that's built into Social Security. It's not built into the current military pay system. You start drawing your pension at, what, age 38, right? And it's good for life, and so that's different from the private sector.

The other thing is, the military pension is indexed to what? Cost of living. They virtually don't exist, indexed pensions, in the private sector. What the private sector does is instead of doing an automatic indexing, they – it's a flat pension based on your pay when you do retire, and periodically the company can take a voluntary, proactive action and do a catch-up to inflation, and get credit for it, rather than, you know, once you've indexed it, it's a right, it's an entitlement. So I'm not saying that's how we ought to proceed, but I wanted to point out the differences between the military pension and the civilian, how it works.

Admiral Pilling: And why don't we just point out that the current civil service retirement system is also indexed.

Mr. Cook: Is it?

Admiral Pilling: Yes.

Mr. Cook: Okay.

Admiral Pilling: General Lyles?

General Lyles: Yes, if I could go back just for a second to your first bullet there about examining the special and incentive pays. I would hope that, even though we got an excellent presentation yesterday from the OSD leadership in looking at this area, I would hope that we could find some time to talk to one of the service force managers who have to use these special and incentive pays. I don't think we'll get a different story, but I think we will find that, at least the case I know of in the Air Force, where it's worked very, very well, the current system – complex, but it's allowed them to make force management changes, to make rapid changes in some problems, addressing problems of needed skills in certain areas. And I just want to make sure we have an input from the actual people who execute it within the services.

And then finally, because we always want to make sure that what we do is fair to the members, it might be helpful to at least have somebody talk to an individual soldier, sailor, airman, whoever it might be, marine, who has received one of these special and incentive pays, and then had it taken away later, once their system or their particular career field got right-sized, if you will, to see what they think about it, just as an additional input to our deliberations.

Admiral Pilling: And [unclear] – I'm sorry, go ahead, Mr. . . .

Mr. Jannotta: I was just going to underline that idea. I think you could also get into this issue of the human piece, because it's the base manager, for instance, who is the one who really is overseeing that whole thing. So I think it would be good for us to hear – I was just thinking about this last night – hear from a series, two or three or four, I don't know how many we'd need to talk to, but it would be good for us – maybe someone from the Navy, someone from the Air Force, Marines, Army, that sort of thing – so that we get a sense of what they see as the issues out on the base, on the front line, and what are they doing about the spouses and the wife and that sort of thing.

Admiral Pilling: We are going to have an administrative brief by the assistant secretaries of the military departments responsible for manpower and reserve affairs at our July meeting, and then in the public meeting in July we are considering asking the senior enlisted advisors for each of the four services to come and talk to us about these sort of specific problems on, uh, the incentive pay program does change quite frequently, and some people get bonuses – everything is timing. And so what's the impact when they reduce the bonus level for certain skill sets?

General Lyles: Including impact on morale, which is one of those human things we really need to look at.

Admiral Pilling: And then the final bullet on this slide was something I alluded to earlier on: ensure that the guard and the reserve compensation is examined to make sure that it recognizes their full integration with the active in the current conflict, which is an extended conflict. The all-volunteer force hasn't lived through one of these before, so this is a very, very – and probably the most complex issue that I think we have in front of us. [low voices] Let me go back. There we are.

And then the retired medical plan – I don't think we're going to come up with any major structural ideas on this. Increasing Tricare fees may reduce the cost to the Defense Department, but really is not a structural change. We could examine Tricare as a second payer for retirees under 65, just like it is a second payer for people who are Medicare-eligible and are retired, because if we think about people who retire at, let's say, age 38, they're going to have a full second career where health insurance may be available to them, and for those people perhaps Tricare should be a second payer.

And then finally, when we were looking at what's now called Tricare for Life five years ago, the thinking in the Defense Department as I recall it was we were talking about accrual funding for all retired medical care, not just for those over age 65. That's not what the Congress gave the Department. But by targeting those over 65, the accrual cost for that percentage of the population is very high, because that's, obviously, as you get older you need more increased medical care. And just like retired pay is on full accrual regardless of your age at retirement, perhaps we want to look at all retired medical care being accrual funded. And that would be for everybody in the force today, and we'd have to work out some arrangement so how – until those people retire, what do we do for the retired medical care for under 65's that we're currently paying, until that force ages out? And I think that is the last slide with actual text.

Mr. Cook: Do you want me to try to give a comment on that?

Admiral Pilling: Yes, go ahead.

Mr. Cook: As one member of the committee, I think we've got to – while these enrollment fees and all may be a relative drop in the bucket, I think we've got to take a look at it. In my view, the idea that the enrollment fees, the co-pays, the deductibles, etc., were put in place in 1999 or whatever and have never been adjusted is just not right. And it's contrary to logic. I could see these things being indexed not to medical cost inflation but to the same cost of living index that the pension is indexed to. I see it perfectly fair and equitable that a retired member's costs, contributions to the retiree system bear a uniform relationship to his or her pension, and I don't think that's unfair at all, and for somehow that – and I know this might be a passionate subject among some people, but I think we have to take on sometimes controversial and passionate subjects and put a stake in the ground so, while we're not deciding these things now, I just want to, you know, say that this is something we've got to take a look at. Because the private sector does it, and they've found that when you participate in the economic decision to seek retiree health care, because there's a cost sharing, that as a consumer of health care services that you then make smarter health care purchase decisions, because you're participating in it.

Admiral Pilling: That's a fair point.

Dr. Oi: Can I ask a question here? This is ignorance on my part. Under the current retirement military system, you get a pension, Admiral. When the base pay goes up, does your pension go up?

Admiral Pilling: It does.

Dr. Oi: It does. So it's benchmarked to the basic pay?

Admiral Pilling: It's, uh, actually I think it's a half percent behind the increase in base pay.

Dr. Oi: But it's... [unclear/crosstalk]

Admiral Pilling: I can ask Saul. Saul, do you know off-hand?

Saul: It's increased by the CPI.

Dr. Oi: Is it the CPI and not the basic pay?

Admiral Pilling: Not ECI?

Saul: It's not the ECI.

Admiral Pilling: Right.

Dr. Oi: But it's based, it's not linked to the basic pay?

Saul: No.

UNIDENTIFIED: Not necessarily.

Admiral Pilling: No, not over time.

Dr. Oi: Okay.

Admiral Pilling: Your initial...

Dr. Oi: So we didn't make that dumb mistake.

Admiral Pilling: No, we didn't. [laughter, followed by unclear question] If you look back to the near-term action plan, the four groups on the side are sort of a way of focusing our work with subcommittees from the current members. Mr. Jannotta has added, would like to add a fifth one, and I think that's fair, which would pick up family and, uh, issues, and I think maybe the two of us, Joe, should be the members on that, and we have to think about which staff member could provide us some support, but that would be a fifth group, and I don't – I'll ask for the chief of staff Paul Hogan to give some thought about who that appropriate staff member may be. And we probably ought to flesh out a little bit of what that group is really going to look at to make sure that we don't go adrift on every issue. We really want to just focus on the very important things to maintain the family cultural values that we want for the families of our force members.

General Lyles: Mr. Chairman, if you're going to have that extra group looking at human things, I would like to volunteer to join you and Joe in looking at that, because of specific experiences I've had and some specific successful, if I can use that term, actions that I took in my most recent command of 82,000 people to always address family and family issues, and I'd like to offer those as benchmarks, if you will, of things that can be looked at.

Mr. Jannotta: Great, great!

Admiral Pilling: Well, but then I would propose just the two of you form that group. [laughter]

General Lyles: I had a feeling you were going to say that. [laughter and chatter] I had a feeling that was going to be the next statement.

Admiral Pilling: Thank you very much for volunteering, Les.

General Lyles: Isn't that the first lesson you learn in the military: never volunteer for anything? [laughter]

Admiral Pilling: Dr. White?

Dr. White: On that subject, which is really important and very complicated, I would hope that we could work, first of all initially with you two, but – and try to figure out some system to all of this, some architecture. What's in and what's out? What deserves emphasis and what doesn't? Because it seems to me, we all want to do what's right for the force, but we have trouble discriminating, I think, what's really important. Now your experience is invaluable in this case. Because we just can't say, well, "We want more. Quality of life is good, and more quality of life is better, we can afford it," and we'll misappropriate the funds.

Admiral Pilling: This is my last slide, so I think I'd like to open it up for discussion on what I may have missed, or things you might disagree with or agree with and we're not doing enough. So...

General Lyles: Mr. Chairman, I don't think you missed anything, and I haven't, I admit, haven't looked at our charter again this morning just to make sure about my next statement, but you mentioned the civil servants earlier, and I notice, even though our title of our organization is Advisory Committee on Military Compensation, I'm wondering if we need to at least address civil servant compensation. And I'm not thinking in terms of deferred or medical or retirement or anything like that, but bonuses and the things of that nature, or things we need to do to both recruit and retain – adequate civil servants are an extremely important part of the mission of the Department of Defense, and one that I think sometimes doesn't get the light that it should.

And I'm speaking again from personal experience – in my command I just mentioned of 82,000 people, only 32,000 of them were military. Fifty thousand were civil servants, so I paid a lot of attention to that subject. And I've always heard comments from those civil servants, "What about us? You put all the attention in the Department of Defense on the military people. Nobody even talks about us." And so I'm wondering if our charter specifically excludes us from at least quickly examining to see if that issue is okay, it doesn't meet the intention, or are we prohibited from addressing it? [END OF SIDE A]

Mr. Cook: [joined in progress] ...very controversial, and there's a lot of work being done in pay-banding, merit pay, removing the ten-step automatic increases by time, and getting rid of the 15-grade structure. My own personal view is that it's a very important subject, but it's not within our charter and we'd best stay away from it.

General Lyles: Okay, I can accept that.

Mr. Cook: That's my own personal view.

General Lyles: By the way, I've always been a supporter of NSPS, in part because there's some examples and that precedence we started in my command that led to some of things in NSPS. I don't think NSPS went as far as it could go, so I just want to make sure we're in agreement [that] we don't need to address that subject.

Mr. Cook: I'm not – I'm just one man talking.

Dr. White: Well, let me make a different comment, Fred, and that is, uh, as we look at the compensation system, and as you said before, we want to think about this in terms of learning from the private sector, shouldn't we also want to think about it in terms of learning from the civil service? Not an evaluation or maybe a recommendation, maybe that's too far, but certainly the employees in the Department of Defense, they're going to compare the two, what we do relative to the others. And there are some good ideas there, and in terms of the new system it seems to me that it's perfectly [unclear/crosstalk].

General Lyles: I think that might be a better way of stating it. Thank you, sir.

Admiral Pilling: And I think we can check with our principle sponsor, Dr. Chu, and say [that] the charter doesn't specifically address this, but we want to make sure that we give sufficient – have sufficient visibility into it to take the good ideas that are there. Any other comments from the committee?

Mr. Cook: On the broad subject, or...?

Admiral Pilling: On the whole broad subject.

Mr. Cook: One of the ones that I just want to have us take a look at, when we do our work, and I'm not sure where it fits up there, but it's in the base pay structure, you know, of the E1 to E9 and O1 to O10. As I understand it, the steps that you progress through, if you're a certain rank, before you're promoted, are a function of your time in service – time in the total service, right? As opposed to time in grade.

Admiral: There's – there are – for officer promotions there are certain gates you have to have gone through, time in service, before you are eligible for a promotion.

Mr. Cook: No, that's a different subject. I'm saying, if you were an O5 and you each had the same number of years in military service, say 10 years, you would be paid the same base pay. Correct? What if one of the O5's had been early promoted because of strong performance and potential and had actually been an O5 for three years, and the other one was just promoted that year. If I'm understanding how the system works correctly, they each get the same pay. The fact that one of them had been an O5 for three years longer than the other would make no difference. That's assuming I'm correct on that. [unclear]

Admiral Pilling: You are correct and – you're right, the base pay is based on time in service, not time in grade.

Mr. Cook: Not time in grade.

Admiral Pilling: Time in grade, I think, was a recommendation that came out of one of the QRMCs(?), where they said, "Restructure the pay table so it's not time in service," so that if you are deselected, the following year, when your peers normally would make it, I still have one additional year in grade, so you would have some higher salary.

Mr. Cook: That seems to me to make sense. I'm wondering why it was not accepted, or I wonder what the arguments against it are, for example, because the arguments for it seem compelling.

Admiral Pilling: Why don't we ask Paul Hogan, since I think he supported the last QRMC.

Mr. Hogan: Actually the recommendation was from the President's Commission on Military Compensation in 1978, and the – I think Mr. Cook's exposition is exactly right, and it was a relatively small recommendation, but it focused right on the rewarding performance part of the system. And again, it was – the reason why it wasn't implemented, I believe, was because – not because there were focused arguments at that particular recommendation. I think that the overall package from the PCMC did not get, you know, it was dominated by the retirement system and it did not get a particular strong hearing by the services. If one had to construct reasons why not do it, perhaps, is to look on the other side, that if you are passed over, should you – is your incentive for keeping on trying reduced by a time-in-grade system relative to a time-in-service system? In other words, if you are passed over now, you can get back in the swing of things with a promotion, and you'll be right there where your peers are. That, I mean, that's one argument on the other side.

Admiral Pilling: But the percentage of the force that that would be applicable [to] is fairly small.

Mr. Hogan: Small on the officer side, but perhaps there are a little bit – there are some late bloomers more on the enlisted side.

Admiral Pilling: Thank you. Anything from...?

[mostly inaudible question regarding speed of promotions varying from service to service]

Mr. Hogan: It was pointed out by Dr. Warner also that because different services promote at different rates, that there would be incentives to support or not support the particular proposal based on their own particular policies on the speed of promotion.

General Lyles: That's certainly true. As an example, the Air Force did away with early promotion to major because we did it so frequently compared to the other services, and there was perceived to be an inequity in lots of different areas, so we stopped doing that completely, which I disagree with, but we stopped doing that, to be like the other services.

Admiral Pilling: Well I think it's a fair issue for us to consider. I mean, if we want to have a compensation that recognizes performance, if you are good enough to be deselected, this is one way of recognizing that.

Mr. Cook: It's the context, it's the whole – it goes back to also the special and incentive pays, maybe being indexed to grade. I think the military pay structure, both the enlisted and the officers, is a relatively flat structure. Sure you make more for being promoted, and you should, but the incremental amount is far less than it is in the private sector, which has a much steeper, maybe too steep, structure. But if you – to me the – keeping the best and the brightest in the career enlisted ranks and the career officer ranks is a very valuable thing to the service, and the best and the brightest have lots of opportunities in the outside market, and much more pay. So closing that gap somewhat through a variety of forces is something I'm going to be a fan of on the committee. So it's – I know it's more for the upper ranks, but somebody's got to say that if that's a needed thing to be done.

Admiral Pilling: Okay, are there any other comments from the committee members. Dr. White?

Dr. White: I want to make a different, um, but it relates to what Lester said about the Air Force practice on majors. We've heard in a number of these presentations about a number of concerns. One is that, certainly the Secretary and I think the system wants people to stay longer – have the opportunity to stay in longer – and there's been some action in the last few years to do just that. Clearly, it seems to me, a related issue is tour length, that, you know – often I think when we do the Defense Science Board program and so on, there was a very strong feeling, particularly among the senior officers who were retired, that we need to have a system that allows people to be in place longer, in terms of their experience base and also, it seems to me, in terms of making sure that we do a good job of managing them not just in the ticket sense but in the skill sense, so that they can take on the very most senior jobs. And there, I think, we've got a system that's so frenetic in terms of how we move people, and not only is costly to families and others but, I would argue, is probably costly to the quality of the force in terms of senior officers.

General Lyles: I certainly agree, Dr. White, and I guess the question is, is the system we have today one that's dictated by each individual service, or is there something from the top, if you will, from OSD, or even the joint staff for that matter, that causes that situation? I don't know. I know what the Air Force did, and we tried to stop some of that, but I don't know whether that was just our prerogative and we're like the other services or, Don, I don't know if you had the same problem within the Navy.

Admiral Pilling: Well, we had short tours for some of the officer skills, like aviators, because they had so many things they had to do in order to qualify for command, and then they also have at some point in their career, if they're going to be successful, they have to have a joint tour. And so you end up, you just have so many years you can – you have available to you. Some of the other

communities didn't have nearly that problem that we had with aviators. And it's really aviators of the fa[st], uh, that fly fast-moving airplanes that...

General Lyles: Yes, well, in the case of the Air Force, and again I'm talking about in my command, we had all the acquisition people, and what forced us to change and get away from that homesteading and, uh, sort of environment was – or putting a stigma on homesteading – was DAWIA, Defense Acquisition Workforce Improvement Act, which mandates that you have to be in an acquisition job a certain period of time. And at one point, when you got people in front of promotion boards, those who weren't involved in that saw a guy or a girl staying at a base for four years or so, and that was a stigma against them, and some people got passed over for promotion. We had to remind everybody that the law for acquisition people mandates that you stay a certain period of time. And through that we sort of got rid of this stigma about homesteading and realized that if a person is gaining experience in their career field, if they're doing all the right things to be a better person in that particular career field, it was okay, whether they stayed at a base two years or six years.

Admiral Pilling: Right, and now the BRAC may actually provide some incentive to have more homesteading as we reduce the base structure and have some bases taking on considerably more, greater numbers of people, so that perhaps you can have three tours in a row in the same geographic location, which is homesteading, but still it provides some stability to the family and ensures that the spouse employment problem that we heard about yesterday has some chance of being resolved.

Any other comments?

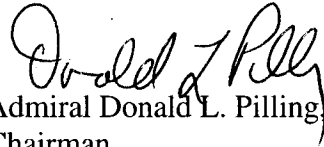
General Lyles: Do we have a sense of – maybe we ought to ask David Schubert – do we have a sense of the significance of the impact on these issues because of the realignments that are now going on within the Department and will go on for several years before their done? That is, bringing a larger number of people back to CONUS and so on? Because some of this may evolve in a way that redounds to the benefit of what we're talking about, and is already underway. But I don't know how, I don't know how big these changes are and of what significance they are.

Admiral Pilling: I think that's a fair question for Dr. Chu. We can raise that with him today if you'd like. Any other comments from any committee members?

All right, I'm going to bring this meeting to a close, but I thank you very much for your full participation, and we have a lot of work in front of us to be able, to be in a position in September to have an interim report on these very complex issues. Thank you.

END

I hereby certify that, to the best of my knowledge, the foregoing transcripts are accurate and complete.

A handwritten signature in black ink, appearing to read "Donald L. Pilling". The signature is written in a cursive style with a large initial "D".

Admiral Donald L. Pilling, USN(Ret.)
Chairman

Defense Advisory Committee on Military Compensation

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