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# ***DACMC Military Retirement Committee Report***

***July 20, 2005***

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# Compensation and Personnel System

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- **Goals**

- Attract an entry pool qualified to perform a wide variety of military jobs now and in future.
- Motivate personnel to work hard and identify those most qualified for advancement.
- Induce voluntary separation at the desired time.

- **Constraints include**

- hierarchical rank structure
- lack of lateral entry



# Current Military Retirement System

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- **Cliff-vests at 20 years of active duty**
- **Provides a lifetime, inflation-protected annuity**
- **Annuity =  $0.025 * YOS * \text{High-3 Basic Pay}$** 
  - **50% at 20 years**
  - **62.5% at 25 years**
  - **75% at 30 or more years**
- **System's second-career annuity serves the purpose of separation pay**
- **System is more generous for officers**
- **FY 2004 per-capita accrual cost was \$9,000**
  - **1/3 as big as basic pay outlays**



# Force Structure Outcomes under Current System

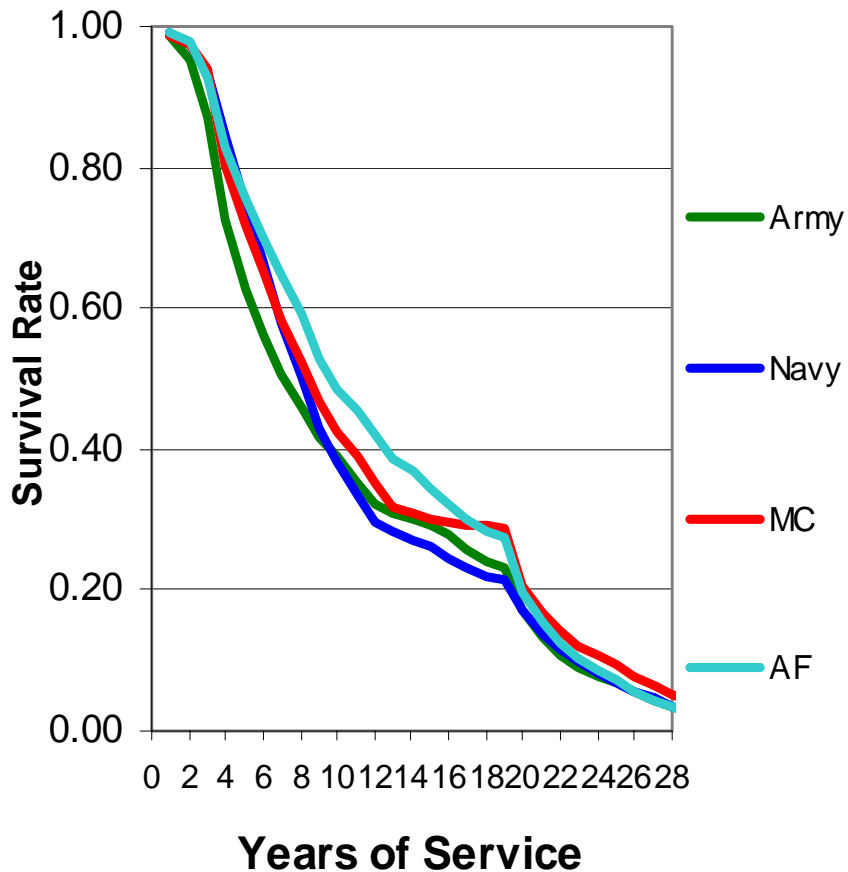
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- **Years per accession between 5 & 8 for enlisted personnel and around 12 for officers**
- **High turnover in first term but higher retention thereafter**
  - average annual retention from YOS 6-20: 90%+
  - average annual retention from YOS11-20: 95%+
- **Chance of a 20-year career:**
  - 47% for officers
  - 15% for enlisted personnel
- **High turnover after YOS 20**
  - 10% of officers who stay for 20 years stay for 30
  - less than 5% of enlisted personnel do so
  - Up-or-out system a strong influence on post-20 retention

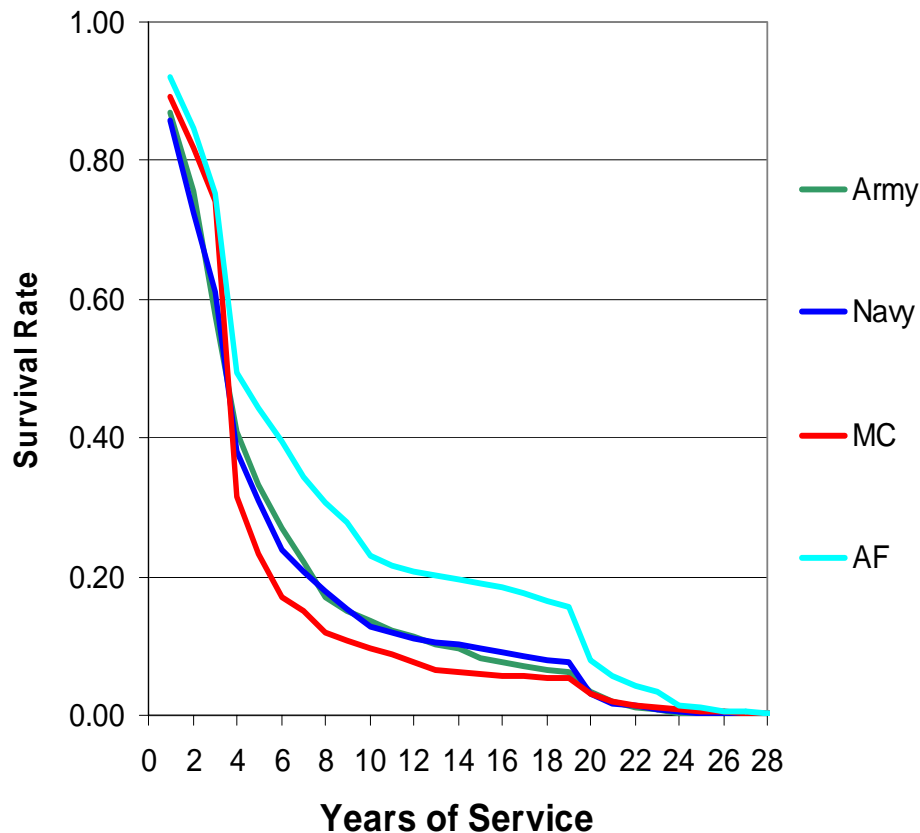


# Survival of Entrants to Given YOS

## Officers



## Enlisted Personnel





# System has been criticized for

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- **failing to contribute to the old-age needs of the bulk of personnel who leave without becoming vested.**
- **deferring too much compensation to the second-career period.**
  - personnel would prefer more up-front compensation
  - system causes individuals to make career decisions too early
- **inhibiting force management.**
  - similar retention patterns and career lengths across the spectrum of occupations despite big differences in training costs and productivity growth with respect to experience
  - limited capacity to use active duty pays to shape the force
  - DSB (1999) and OMSG (2000): officer assignments and careers generally too short
  - reductions-in-force are particularly to manage



# Previous groups have recommended overhaul

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- **Defense Manpower Commission (1976):**
  - vest personnel in an old-age annuity after YOS 10
  - pay immediate annuity to Combat Arms personnel after YOS 20 & all others after YOS 30
- **President's Commission on Military Compensation (1978):**
  - vest personnel in an old-age annuity after YOS 10
  - provide a cash transition fund financed by annual DOD contributions into a TSP-like account
- **President's Private Sector Commission on Government Cost Control (1985):**
  - vest personnel in an old-age annuity after YOS 5
  - eliminate the second-career annuity
- **Three recent DOD study groups recommended systems similar to Federal Employee Retirement System (FERS)**
  - FERS vests early
  - provides combination of old-age annuity & TSP contributions



# Costs and Effects of Alternative Systems

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- **Alternatives we evaluated include**
  - **Current System**
  - **Old-age annuity system (OAS)**
  - **PCMC proposal**
  - **Federal Employee Retirement System (FERS) coupled with Separation Pay available**
    - » for all personnel after 10 years of service
    - » at HYT points but not before
  - **Old-age annuity supplemented with government TSP contributions and *career gate payments* paid at 5-year intervals beginning at YOS 10**
    - » Gate payments like a basic pay increase, but have advantages discussed in committee report
- **Asch-Warner model calibrated to FY 2004 Army enlisted force of 413,000 personnel used to estimate costs and effects on retention and force structure**





# Summary of Findings

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- **Elimination of second-career annuity in OAS results in a less experienced force requiring much higher accessions**
  - need more active duty pay or system of deferred separation payments to maintain the force
- **PCMC and FERS systems (with old-age benefits and separation payments vested much earlier) maintain or improve the force at same cost**
  - Plans keep constant or increase man-years per accession and may reduce percent in first term
  - Percent in YOS 6-10 and 21-30 range rises while percent in 11-20 range falls
- **OAS coupled with system of active duty gate payments also improves the force at same cost**

**Implication: Different mixes of active duty pay and separation benefits can have similar effects on retention and force structure at same cost.**



# What do these plans gain over the current system?

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- **Earlier vesting in a combination of benefits helps many more personnel accumulate for old-age.**
- **Alternatives offer opportunity for better, more flexible force management.**
  - **Smooth benefit growth from YOS 10 onward eliminates 20-year focal point with its golden handcuffs.**
  - **This would permit skill-by-skill management of HYT points and eligibility for separation payments.**
    - » push back HYT points and delay start of separation pay when that is desirable (officers, high training cost skills)
    - » make separation payments available earlier in the youth and vigor skills
    - » longer careers for some, shorter careers for others
  - **Under alternatives, adjustments to force size less difficult**
- **Reducing reliance on deferred compensation permits more proactive use of active duty pays to manage the force**