The United States military pension system: toward a rational reform with commentary on the report of the President's Commission on Military Compensation

L. Shelton Clarke
The United States Military Pension System
Toward a Rational Reform
With Commentary on the Report of the
President's Commission on Military Compensation

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By
L. Shelton Clarke, Jr.
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Approved by

[Signatures of Thesis Director and Committee Members]
# TABLE OF CONTENTS

<table>
<thead>
<tr>
<th>Section</th>
<th>Page</th>
</tr>
</thead>
<tbody>
<tr>
<td>Preface</td>
<td>i</td>
</tr>
<tr>
<td>I. Problem and Prognosis</td>
<td>1</td>
</tr>
<tr>
<td>II. Background and Description of Present Pension System</td>
<td>12</td>
</tr>
<tr>
<td>III. Design Problems and Consequences</td>
<td>24</td>
</tr>
<tr>
<td>IV. Current Reform Alternatives</td>
<td>41</td>
</tr>
<tr>
<td>V. Military Response to Reform Proposals</td>
<td>65</td>
</tr>
<tr>
<td>VI. Toward Rational Pension Reform</td>
<td>79</td>
</tr>
<tr>
<td>Appendix</td>
<td>92</td>
</tr>
<tr>
<td>Select Bibliography</td>
<td>96</td>
</tr>
<tr>
<td>Bibliography</td>
<td>98</td>
</tr>
<tr>
<td>Biography</td>
<td>101</td>
</tr>
</tbody>
</table>
Senator Symington: Mr. Rumsfeld, when you come before this committee you come before a very friendly committee. It has been my experience after thirty-one years in the government that you have four kinds of senators and congressmen. After World War I a group of people came here who voted for all of the guns before any butter. And the resistance that developed over the years, especially incident to the no-win procedures, resulted in another group coming up who voted for all the butter instead of any of the guns. Then you have another group who could be the most dangerous of all, based on my concept of true national security, who say well we will vote for all the butter and all the guns and we are sure to come back with a heavy majority, because nothing could every happen to the U. S. dollar. In that connection I was recently talking to the fiscal expert of the Senate, and I told him that the retired military pay between now and the year 2000 would add up to 300 billion dollars. He said the figure was too high. I asked the Chief of Staff, Mr. Braswell, to get me the figures. The memorandum from Mr. Braswell shows that if nothing is done the accumulated retirement pay that will go out is not 150 billion, it is not 300 billion, it is 470 billion.

In August of 1974, I wrote U. S. Senator Harry F. Byrd, Jr., the senior Virginia senator and T. Edward Braswell, Chief Counsel for the Senate Armed Services Committee for a good deal of material concerning the United States military pension system.

The system had intrigued me as a pension planner for many years for several reasons. First, the plan itself possessed grave design defects, which if allowed to exist in private plans would lead the employer corporation to
excessive cost and possibly fiscal insolvency. Second, with the quadrupling of the price of oil in 1974 and the creation of a cohesive oil cartel it seemed possible to predict that the delicate balance of costs-benefits-inflation upon which the 500,000 private plans rested for fiscal integrity was in real danger of becoming unseated from new economic forces over which there was no control and for which we had no experience. One could foresee a rash of private plan terminations and also a runaway military retirement system, both of which sadly took place and are continuing to take place as these words are written.

From the material sent me by Messrs. Byrd and Braswell, mainly documents from DoD and the Congressional Budget Office (CBO) plus hearings and transcripts and statistical data of all kinds dealing with the retirement system and efforts to contain it, I was able to determine that the subject was worthy of a major effort on my part to attempt to provide something of value.

The timing by pure chance was exquisite. Attempts at military pension reform had begun in 1971. It seemed that the appropriate congressional committees would turn to a final effort within a reasonable time after the blue ribbon President's Commission on Military Compensation, appointed in 1977, rendered its report to the President in April 1978.

I decided to try to write in simple language the first in-depth article on the subject designed for a specialized readership. The article, "The United States Military Pension System -- To Halt a Runaway", was published in October 1977 in the CLU Journal, a professional quarterly with a readership of 25,000 specialists from the various fields of financial planning. From the article came an invitation to testify before the President's Commission and an opportunity to be allowed to make a degree of input into the coming political process itself.
The reader will note that throughout the thesis there is the implied principle that in a participatory democracy the citizenry should and must take an active role in the spending of funds given by it to the government in the form of taxes. We must never again hold the politician in awe or, in the magnificent words of Dean Raoul Berger during the darkest hours of Watergate, he will again become awesome.

A sincere debt of thanks is owed to the following for their help and guidance: to John Outland, my friend and thesis advisor, whose courses I enjoyed so much and whose suggestions and criticisms were always to the mark; to John Whelan who gave me without complaint generous amounts of his time, his library and his gift of near-total recall; to Warren Nelson who fed me a constant supply of papers, testimony and reports from his position as Congressman Les Aspin's legislative assistant; and finally to Gary Nelson, Deputy Assistant Secretary of Defense and friend, who saw that my source material was always of high quality including much of his own work. I thank them all from my heart.
The United States Military Pension System

-- Toward a Rational Reform, with

Commentary on the Report of the

President's Commission on Military Compensation
CHAPTER I

Problem and Prognosis

In addressing the subject of military compensation, we feel that we must first address the financial condition of the United States government today. We are not speaking of the public debt figure as announced by the United States Treasury, of 712 billion dollars that is announced in the daily financial statement. As taxpayers we are much more concerned by a more awesome figure, the real debt of the U. S. government -- a figure that now approaches 8 trillion dollars. This figure is not dreamed up. It is based upon the State of Liabilities and other Financial Commitments of the United States Government (31 USC 757 f) and reflects the summary of real public debt as of July 1, 1977.

From statement of Sid Taylor, Research Director, National Taxpayers Union, before the President's Commission on Military Compensation, December 21, 1977.

The day is upon us when we can no longer postpone a reappraisal of our nation's military plan, for it represents a system in a degree of disarray approaching chaos. It is a system which provides benefits of a magnitude unheard of in the private sector -- benefits which have been judged to be up to ten times more generous than those provided by private plans and three times as great as those of the federal civil service system.¹

¹It is difficult to fairly affect a comparison of benefits between pension plans because of the various features which have different values. It is the author's belief that the figure of ten is low. The President's Commission reached a conclusion somewhat close to ten on page 31 of its report. The New York Times, April 11, 1978, page 22, estimated the difference at ten. The U. S. News and World Report, April 24, 1978, listed the difference in lifetime payout as tenfold.
It is a system which is escalating sharply in cost. By fiscal year 2000, if left alone, the annual outlay for military pensions will total $34 billion as against $9.5 billion for fiscal year 1978. However, should the plan be put on a funded basis, it is estimated that the cost for fiscal year 1979 along would total $16.7 billion.\(^2\)

In terms of cost-to-payroll, the military expenditure is approximately six times greater than the norm in private industry, requiring some 40% to 55% of military payroll as contrasted with approximately 8% in the private sector.\(^3\)

It is to these abnormalities and distortions in costs and benefits that the author's thesis is directed.

No attempt will be made therein to suggest the emasculation of the United States military retirement plan or the financial degradation of the men and women who serve therein. The author is fully aware of the patriotism, the personal dedication, the hardship, the separation from family that a military career often requires of those who chose it. Nor is the author unaware that periodically, three times within the last thirty years, the supreme price in life and limb was extracted from them. But there can be nothing but an utter waste of taxpayer funds when benefits of a level such as these are provided in times so fraught with uncertainty.

While plans of workers in private industry provide a benefit level of approximately 50% of earnings inclusive of Social Security, the military system


yields 75% of basic pay exclusive of Social Security, and indexed to the Consumer Price Index for cost-of-living adjustments.4

The following table shows two average retirements under the United States military retirement plan; one for an 0-6 Colonel or Captain (N), and one for an E-7 Sergeant or CPO (N). The table is designed to show retirements with a 5% Consumer Price Index improvement to age 65. The Social Security benefit assumes no reentry to the labor force from service retirement to age 65. The pension is extended to the life expectancy of a modern mortality table, and the lifetime military payout is indicated. The percent of pension to pay is also indicated. The dollars are in 1977 dollars:

Table 1-1
Effect of Social Security and CPI on Military Pension

<table>
<thead>
<tr>
<th>Rank</th>
<th>0-6 Colonel Captain (N)</th>
<th>E-7 Sergeant First Class CPO (N) 20-year career</th>
</tr>
</thead>
<tbody>
<tr>
<td>Retirement Age</td>
<td>52</td>
<td>41</td>
</tr>
<tr>
<td>Beginning Monthly Pension</td>
<td>$ 1,886</td>
<td>$ 455</td>
</tr>
<tr>
<td>Military Monthly Pension at Age 65</td>
<td>$ 3,383</td>
<td>$ 1,467</td>
</tr>
<tr>
<td>Social Security at Age 65</td>
<td>253</td>
<td>186</td>
</tr>
<tr>
<td>Total Monthly Pension at Age 65</td>
<td>$ 3,636</td>
<td>$ 1,653</td>
</tr>
<tr>
<td>Percent Pension to Pay at Age 65</td>
<td>193</td>
<td>151</td>
</tr>
<tr>
<td>Lifetime Military Payout</td>
<td>1,080,182</td>
<td>446,392</td>
</tr>
</tbody>
</table>

Source: The table is the author's own. The Social Security rates are those which reflect legislation to 1975. The military pay rates are those applicable currently.

The President's Commission in its report constructed a somewhat similar table but designed to illustrate the difference in lifetime payout between officers and enlisted personnel of the services to those of the military of other states, as well as civilian private sector employees:

Table 1-2

<table>
<thead>
<tr>
<th>Retirement Plan</th>
<th>20 Years of Service</th>
<th>30 Years of Service</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Life Pay-</td>
<td>Age Annuity</td>
</tr>
<tr>
<td></td>
<td>out Value Began</td>
<td>Begins</td>
</tr>
<tr>
<td>Officers:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>U. S. military</td>
<td>$420,000</td>
<td>43</td>
</tr>
<tr>
<td>Typical private sector (salary)</td>
<td>40,000</td>
<td>62</td>
</tr>
<tr>
<td>Typical non-federal public</td>
<td>70,000</td>
<td>60</td>
</tr>
<tr>
<td>(example: municipality)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Federal Civil Service</td>
<td>90,000</td>
<td>60</td>
</tr>
<tr>
<td>West German military (b)</td>
<td>260,000</td>
<td>50</td>
</tr>
<tr>
<td>British military</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Canadian military (c)</td>
<td>350,000</td>
<td>43</td>
</tr>
<tr>
<td></td>
<td>360,000</td>
<td>43</td>
</tr>
<tr>
<td>Enlisted persons:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>U. S. military</td>
<td>190,000</td>
<td>39</td>
</tr>
<tr>
<td>Typical private sector (wage)</td>
<td>15,000</td>
<td>62</td>
</tr>
<tr>
<td>Typical non-federal public</td>
<td>20,000</td>
<td>60</td>
</tr>
<tr>
<td>Federal Civil Service</td>
<td>25,000</td>
<td>60</td>
</tr>
<tr>
<td>Typical police and fireman plan (a)</td>
<td>90,000</td>
<td>50</td>
</tr>
<tr>
<td>West German military (b)</td>
<td>not entitled</td>
<td></td>
</tr>
<tr>
<td>British military</td>
<td>not entitled</td>
<td></td>
</tr>
<tr>
<td>Canadian military (c)</td>
<td>165,000</td>
<td>40</td>
</tr>
</tbody>
</table>

Source: The Report of the President's Commission on Military Compensation. Table 3-2, p. 32.

The estimated payout figures in the above table represent the lifetime value of retired pay in fiscal year 1978 dollars at the time the person completes 20 or 30 years of service. Social Security payments are not included in the estimates. For annuities protected from inflation, pensions remain in fiscal year 1978 dollars until death. When annuities have no CPI protection or partial CPI protection, future
pensions are deflated to convert to 1978 dollars. The estimates assume 4% annual inflation. Estimates assume enlisted members enter at age 19, and officers enter at age 23.

The lack of inflation protection accounts for a large part of the difference in lifetime values between the military programs and the civilian programs. References to private pension plans are assumed to have no protection from inflation.

(a) For 30 years of service it is assumed that an enlisted person enters at age 20 and retires at age 50, the earliest age the typical policeman or fireman can retire.

(b) The West German military does not allow retirement until age 52 and does not provide for deferred annuities. Therefore, estimates for enlisted persons with 30 years of service assume an entry age of 22 with annuity beginning at age 52. Note: the figure of $880,000 [sic] is an error in the Commission's calculations. The German benefit formula contains the same maximum as that of the U. S. Since the pay is comparable also and the annuity cannot begin until age 55, the error is obvious. The figure should be approximately the same as that for the U. S. for the officer classification.

(c) The Canadian military does not allow retirement before age 40. Estimate for 20-year enlisted person assumes entry age at 20 with annuity beginning at age 40.

With Table 1-2 the Commission was clearly of the opinion that a great difference existed between the United States military pension payout as between officer and employee; and as between enlisted person and worker. It is the thesis of this author that the military retirement plan should be reasonable in benefits and costs and at least in rough parity with the plans of the non-military taxpayer whose taxes fund it.

**Origin of Problem**

While the military retirement system may now well be in a dangerous state of imbalance as to benefits-and-costs, it is but a part of a larger problem, that of the entire pension concept. There are three basic types of pension systems in America. They are the private sector, non-government plans; the governmental-administered plans containing the railroad workers,
federal civilian employees, state and local employees and the military; the third system is the Social Security old age plan (OASDI).  

Table 1-3

<table>
<thead>
<tr>
<th>Plan</th>
<th>Number of Persons Covered</th>
</tr>
</thead>
<tbody>
<tr>
<td>Private plans (a)</td>
<td>42,000,000</td>
</tr>
<tr>
<td>Railroad Retirement</td>
<td>1,600,000</td>
</tr>
<tr>
<td>Federal civilian employees</td>
<td>4,000,000</td>
</tr>
<tr>
<td>State and local employees</td>
<td>11,000,000</td>
</tr>
<tr>
<td>Social Security System</td>
<td>109,000,000</td>
</tr>
<tr>
<td>Military</td>
<td>2,100,000</td>
</tr>
</tbody>
</table>


(a) Of the 42,000,000 persons indicated, some 10,000,000 are members of profit sharing plans, thus leaving the pension membership at over 30,000,000.

Two events occurred oddly within thirty-six months of each other in 1974 to bring into focus the peril which now confronts the American pension systems. The first was the Retirement Income Security Act of 1974 (ERISA) which was signed into law by President Gerald Ford on Labor Day of that year. It sought to mandate monetary protections to workers in the form of strict funding standards of their plans by their employers and in this respect was entirely laudable. However, the timing of the passage of this extremely complex legislation was unfortunate as it coincided roughly with the Arab oil embargo, the quadrupling of oil prices, a major recession and severe inflation. Under prior pension law, the Internal Revenue Service had historically taken a conciliatory attitude toward private employers who either from desire or necessity

had allowed their defined benefit pension plans to become underfunded. Defined benefit plans, numbering some 400,000, cover the major portion of the labor force. These plans provide definite, ascertainable benefits which are computed by formula. The military plan is of this type. However, the military plan is unfunded, i.e., the benefits are paid each year from the general revenues of the government. Also unfunded or severely underfunded are many plans in the public systems, i.e., the plans of the counties, cities and states.

Also in long range danger is the fiscal integrity of the Social Security old age system (OASDI). This condition was temporarily alleviated when on December 20, 1977, President Carter signed into law the largest peace time tax increase in history. This measure mandated a series of increases beginning in 1979 for Social Security payroll taxes which will raise 227 million dollars of additional revenue in the years 1979 through 1987. Its stated purpose was to end the deficits which had been building in the Social Security trust funds. Under present law, the disability trust fund would be depleted by 1979, the old age trust fund by 1982. In reality, this shoring up of the largest of all the public systems foretold of the problems and dangers which now exist across the entire spectrum of all the systems -- private as well as public -- problems which are only now beginning to be defined and problems for which there exist at present little or no consensus of thought for remedial action.

The problems now facing the private sector funded plans (but underfunded) may be described so that the reader may also understand a major part

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6 The actual figure is, at present unknown. Prior to the passage of ERISA, there were approximately 470,000 defined benefit pension plans. Due to the constraints of the Act plus the recession of 1973, there is the distinct possibility that almost one-third of these plans have been or are now being terminated.
of the reason for the escalation of the costs of the unfunded public plans such as that of the military. For the major reason -- the inflationary wage and pension increase -- is a common thread which runs through the fabric of both the systems, threatening the employer with a plan curtailment or termination in the case of the former, and the taxpayer base of the nation with excessive costs in the case of the latter.\footnote{For a superb in depth discussion of the current state of the private pension system, the interested reader should read Robert D. Paul, "Can Private Pension Plans Deliver?", Harvard Business Review, October 1974, pp. 1-8. The author, at the point of the beginning of a new plateau in inflation, predicts with accuracy what is apparent four years later.}

The optimum form of pension -- or so it has been thought -- is the fixed benefit, final average-pay plan. Here a definite benefit is provided by formula upon a percentage of pay as it exists just prior to retirement. These plans worked with success during period of low inflation, i.e. when average yearly increases were 2\% to 2.5\% to 3\%, for the following reasons:

When an actuary calculates the cost of a defined benefit, final pay pension plan which involves determining the annual contribution rate needed to support the plan, he must make assumptions concerning many future events. Among these events are mortality, turnover of employment due to severance, age at retirement, rate of return on invested reserves, and career salary increases. In general he makes no assumption regarding the rate of inflation, but when inflation is in the 2\% to 2.5\% range, there is room in the other assumptions regarding the rate of investment yield to accommodate that degree of rise. In effect, the plans are open-ended; the costs are never predictable; at best it is only with difficulty that they can be made subject to long range planning. Rates of inflation higher than expected upset the delicate balance between what can and what cannot be planned.
For example, a typical assumption might be that salaries could be projected to rise an average of 2% to 3% per year. This is a projection which increases the employer contribution. With a 3% salary progression, a participant who starts employment at $5,000 per year is assumed to be earning $14,000 prior to retirement 35 years later; an employee who enters employment at $10,000 is progressed to $28,000 and so on. This increase is built into the cost calculation. So, however, is the yield on invested reserves which is currently figured at about 6%. Actually, the yield has normally been 2% or 3% higher than the assumption, and this difference historically could cover minimal inflation so long as it was in the 2% to 2.5% range.

But in 1973 the CPI rose 9.4%. We had entered a new world of economics. The age of cheap energy had come to an abrupt halt. Between 1968 - 1975, for example, the cost-of-living adjustments for the retirees of the military pension system averaged 8.5% per year while the average basic pay increase for the same period averaged 10.5%.8 If in the next decade the rate of inflation is 5% to 10%, pension plans now in effect will require investment returns of 10% to 13% a year to maintain costs at anywhere near a level percent of payroll.

The increase in pension cost from pay increases flowing from the new world of inflation is striking. For instance, in a typical defined benefit pension plan, military or private sector, assume that a 25-year old participant enters plan membership with a starting salary of $8,000. The plan provides a

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8 For the interested reader, see concise description of the military system, examples and pay ranges of personnel as well as retirement pay by rank and years of service in the Uniformed Services Almanac published each year. See page 44 of the 1977 Uniformed Services Almanac. Washington, D. C. 1977.
pension at retirement of 50% of final-average salary averaged over the last five years of employment. If the salary increases are in range of 2% to 3% per year, the amount necessary to fund the pension would be $84,900. But if additional increases of 5% or 7.5% are granted at different times to offset inflation, the amount needed for that participant would soar to between $325,000 to $600,000 plus.9 "In our inflationary future", notes author Paul "employees and employers -- in fact, the society as a whole -- will be faced with apparently irreconcilable alternatives: automatic cost-of-living increases in pensions (and pension costs) versus fixed benefits (with declining purchasing power). The economy may not be able to support the first; society may not be able to accept the second. A question is raised: can our pension promises be kept?"10

The reader may at this point suspect that he has been led into an unnecessary foray involving an over-exposure of basic pension planning mixed with fragments of rudimentary economics. But it has been for a purpose, since a degree of familiarity with retirement planning in general will be of help to the interested reader. What has been suggested is that a pension plan is a device which is uniquely ill-equipped to cope with high and mounting inflation. In the private sector thousands of plans have been and are being terminated because of it -- in large part. The plan of the military is subject to the same pressures. However, the United States military retirement system, of course, will not be terminated nor will the plans of the other public systems. This thesis suggests that the taxpayer base of the nation is the de facto

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9 Paul, op. cit., p. 3, Exhibit 1.
10 Ibid., p. 6.
employer of these systems. It is, therefore, in the public's interest to see that the plans are kept reasonable in benefits and costs. Indeed, it is no less than a duty. 

The author was gratified to see that the President's Commission on Military Compensation was of the same opinion. Its core recommendation was for a realignment of the military benefit structure downward. Its reasoning was that the present disparity in benefits resulted in an inequity. Report of the President's Commission on Military Compensation. Washington, D. C., Government Printing Office, 1978.
CHAPTER II

Background and Description of Present Pension System

The current system was originally intended to keep Federal pay (both military and civilian) competitive with wages in the civilian sector, but it has evolved to the point where far more than necessary is paid. Summing all the components of the compensation package reveals that military officers, for example, earn about 70 percent more and enlisted personnel about 30 percent more, than comparably aged and educated civilian workers. This did not happen by design but by accident.


The American military nondisability pension plan is technically extremely simple.¹ In retirement plan language it is a defined benefit pension plan with a unit benefit formula which provides a monthly benefit of 2.5% of final basic pay times years of service. The benefit is in the form of a life annuity, and it commences immediately upon retirement which can be at any time (for most grades and ranks) between the 20th and 30th years. It is not offset by the applicable Social Security benefit and is indexed for cost-of-living adjustments to the CPI. Benefits vest at the 20th year. The system is unfunded. Thus, applications of the benefit formula to a 20-year

¹Title 10; United States Code. Military retirement is, of course, a part of compensation and, as such, was expressly delegated to the legislative branch by the framers in Article One, Section eight of the Constitution. It is not unusual, however, for inquiries into potentially volatile and explosive issues such as military pension reform to be spearheaded by a blue ribbon President's Commission. President Kennedy appointed a similar commission to define the parameters of private pension reform in March of 1962.
career will produce a benefit of 50% of final basic pay while a benefit of 75% of basic pay is produced for a career of 30 years.

The compensation package of the military is extremely complex, comprising some 30 odd items. It is largely for this reason that the military man has never known exactly what he made and indeed today bases a portion of his resistance to any proposed changes in his retirement to this lack of understanding. His pension benefits, however, are based upon his main cash item called basic pay.

Most analysts, as well as the author, choose the middle sixties as the point to begin any examination of the present compensation-retirement system. It is about at that time that the ratio of military pay to comparable civilian pay stood at its lowest. Also it was then that American involvement in Southeast Asia was begun in earnest. A final reason for choosing the mid-sixties as a point of departure is that from the end of World War II through the 1950s there were relatively few changes in compensation rates and retirement policies, the main ones being the introduction of reenlistment bonuses in 1952, the Civilian Health and Medical Program for the Uniform Services (CHAMPUS) in 1956, and proficiency pay in 1958.

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Retirement and Pay Prior to Vietnam

In 1964 basic pay and retirement at representative grades and ranks were as indicated in Table 2-1, which shows total cash pay and basic pay for a 20 and 30-year career. The total pay and cash allowances column in Table 2-1 reflects the disgraceful level of military pay in effect in 1964.

Table 2-1

1964 Domestic Duty Pay and Pension (a)

<table>
<thead>
<tr>
<th>Grade</th>
<th>Total Pay and Cash Allowances</th>
<th>Monthly Basic Pay (b)</th>
<th>Mo. Pension 20 Years Service</th>
<th>Mo. Pension 30 Years Service</th>
</tr>
</thead>
<tbody>
<tr>
<td>O-6 Colonel or Captain (N)</td>
<td>$1,163</td>
<td>$945</td>
<td>$473</td>
<td>$814</td>
</tr>
<tr>
<td>0-4 Major or Lt. Commander (N)</td>
<td>933</td>
<td>740</td>
<td>370</td>
<td>555</td>
</tr>
<tr>
<td>0-3 Captain or Lieutenant (N)</td>
<td>818</td>
<td>640</td>
<td>320</td>
<td>480</td>
</tr>
<tr>
<td>E-6 Staff Sgt. or CPO (N)</td>
<td>478</td>
<td>330</td>
<td>165</td>
<td>248</td>
</tr>
<tr>
<td>E-5 Sgt. or Petty Officer 2nd Class (N)</td>
<td>423</td>
<td>280</td>
<td>140</td>
<td>210</td>
</tr>
<tr>
<td>E-4 Corporal or Petty Officer 3rd Class (N) (c)</td>
<td>358</td>
<td>215</td>
<td>108</td>
<td>161</td>
</tr>
<tr>
<td>E-3 Private 1st Class or Seaman Recruit (N)</td>
<td>308</td>
<td>165</td>
<td>83</td>
<td>124</td>
</tr>
</tbody>
</table>

Source: Uniformed Services Almanac, op. cit.

Military pay for enlisted personnel during their first two years of service had, by 1965, fallen to about half the comparable civilian rate. Indeed, when the Gates Commission rendered its recommendations to the President in 1969, military pay was still substandard, especially when considered as a mechanism for encouraging an all-volunteer army. The commission noted:

4 Ibid., p. 103.
Military compensation in the early years of service is now so low that it will not sustain an all-volunteer force of the quality desired. Until that condition is corrected an all-volunteer force cannot be realized.\(^5\)

It is interesting as well to note in historical perspective the comparison between compensation of the military to compensation of the civilian sector. Table 2-2 sets forth the comparison of enlisted earnings to civilian pay in manufacturing.

<table>
<thead>
<tr>
<th>Period</th>
<th>Annual Military Pay &amp; Allowances</th>
<th>Manufacturing Earnings</th>
<th>Percent of Forces Drafted</th>
</tr>
</thead>
<tbody>
<tr>
<td>Civil War (1865)</td>
<td>$427</td>
<td>$410</td>
<td>2</td>
</tr>
<tr>
<td>Spanish-American War (1898)</td>
<td>444</td>
<td>394</td>
<td>0</td>
</tr>
<tr>
<td>World War I (1918)</td>
<td>870</td>
<td>980</td>
<td>59</td>
</tr>
<tr>
<td>World War II (1945)</td>
<td>1,587</td>
<td>2,469</td>
<td>61</td>
</tr>
<tr>
<td>Korean War (1952)</td>
<td>2,584</td>
<td>3,721</td>
<td>27</td>
</tr>
<tr>
<td>1960</td>
<td>3,034</td>
<td>5,020</td>
<td>15</td>
</tr>
<tr>
<td>1965</td>
<td>3,567</td>
<td>6,130</td>
<td>16</td>
</tr>
</tbody>
</table>


The reader will note that in 1965, the year of the beginning of the Vietnam ground involvement, military pay to civilian manufacturing was low by a factor of almost one half.

\(^5\) Ibid., p. 107.
The second half of the sixties brought many changes in military compensation, including retirement. Whereas military pay had been increased at only infrequent intervals during the 1940's and 1950's, 1963 marked the beginning of annual pay increases for career military personnel. New recruits, whose pay had been frozen since 1952, began to receive annual pay increases staring in 1966.

The President's Commission in its report traces the origin of marked retirement cost increases during this period:

Much of the attention given to retirement has arisen simply because of the sheer magnitude of retired pay costs. In fiscal year 1964, retired pay amounted to $1.2 billion; in fiscal year 1978 retired pay outlays are estimated at $9.2 billion. The fiscal year 1978 figures represents 8% of the defense budget compared with 2% in fiscal year 1964. This significant growth has occurred primarily as a result of three factors: more retirees, higher military pay and inflation. The Congressional Budget Office has estimated that 36% of the nondisability retired pay growth between fiscal 1966 and fiscal 1976 was attributable to increases in the number of retirees, 22% to military pay raises, and 42% to CPI increases.6

What the report did not attempt to cover in this area of pay-raise-to-pension cost is more interesting. As was seen in Chapter I, the dynamics of the effects of substantial increases in the payroll in a defined benefit plan are destabilizing. Even three percent per year pay increases steadily and substantially raise costs. Funding to a $84,900 lump-sum benefit with such a salary scale assumption translates to a sum needed at retirement of between $325,000 to $600,000 should the salary increase become 5% to 7.5% per year. It should not be forgotten that the increase in the number of nondisability retirees (from 398,000 in fiscal

---

year 1966 to 917,000 in fiscal year 1976) which resulted principally from the World War II and Korean War build-up, has passed. Also the extremely large military basic pay raises which occurred from 1966-76 to correct the imbalance of military to civilian compensation are not likely to be repeated. What is left then to cause a near half-trillion dollar payout projected between now and fiscal year 2000 in the absence of pension reform is the effect of the inflationary wage increase feeding the CPI cost-of-living adjustment after retirement.7

Perhaps the most controversial and substantive compensation increase, and the one which most affected the retirement benefit, was the Rivers Amendment passed in 1967. It should be remembered that in 1961 the "comparability" pay principle for civilian employees of the federal government had been legislated under the Federal Salary Reform Act whereby the civil servant was paid at a level comparable to private sector wages and salaries. This is important in the context of the Rivers Amendment which tied military pay to that of the civilian federal employee to be expressed in percentages. The Rivers Amendment, however, dictated that the entire increase be applied as a percentage to basic pay. Basic pay, the main cash item, represents only about 75% of RMC (Regular Military Compensation) which is the total military pay and which is defined as the sum of basic pay, quarters and subsistence allowances and the tax advantage related to the tax exempt status of the allowances.8 However,

7 The estimate of 470 billion dollars to be disbursed between now and fiscal year 2000, referred to at the beginning to Chapter I was predicted in a 5% rate of inflation, an extremely optimistic rate under any political or economic scenario known to the author at this time.

8 For excellent description of military compensation in general and illustrative examples at all grades and ranks, see 1977 Uniformed Services Almanac. Moore and Moore, Inc., Washington, D.C.
to keep the percentage increase for RMC comparable to that for federal civilians, every 4% increase in federal civilian pay became a 5% increase in basic pay. Since the benefit formula of the retirement plan is applied to basic pay, the retirement plan adjustment was unnecessarily high, thus providing an unintended windfall.

In addition to the Rivers Amendment, so-called "catch up" pay raises for career military personnel were put into effect during the period of 1967 to 1969 to keep military pay in line with private sector wages and salaries. The chronology of events from the end of World War II to the present time is as follows:

Table 2-3

<table>
<thead>
<tr>
<th>Year</th>
<th>Event</th>
</tr>
</thead>
<tbody>
<tr>
<td>1946-48</td>
<td>20-year military retirements</td>
</tr>
<tr>
<td>1952</td>
<td>Reenlistment bonus</td>
</tr>
<tr>
<td>1956</td>
<td>Civilian Health and Medical Program for the Uniformed Service</td>
</tr>
<tr>
<td>1958</td>
<td>Proficiency pay program</td>
</tr>
<tr>
<td>1962</td>
<td>Federal Salary Reform Act: Beginning of GS &quot;comparability&quot;</td>
</tr>
<tr>
<td>1963</td>
<td>Beginning of annual pay increases for career military</td>
</tr>
<tr>
<td>1965</td>
<td>Cost-of-living adjustments for federal retired pay</td>
</tr>
<tr>
<td>1966</td>
<td>Beginning of annual pay increases for military recruits</td>
</tr>
<tr>
<td>1966</td>
<td>Variable reenlistment bonus</td>
</tr>
<tr>
<td>1966</td>
<td>Major revisions to CHAMPUS</td>
</tr>
<tr>
<td>1967</td>
<td>&quot;Rivers Amendment&quot;: Comparable pay increase for military</td>
</tr>
<tr>
<td>1967-69</td>
<td>&quot;Catch-up&quot; pay raises for career military</td>
</tr>
<tr>
<td>1969</td>
<td>&quot;1% kicker&quot; for adjusting federal retired pay</td>
</tr>
<tr>
<td>1970</td>
<td>Introduction of &quot;automatic&quot; annual federal pay increases</td>
</tr>
<tr>
<td>1971</td>
<td>AVF pay increase for first-termers</td>
</tr>
<tr>
<td>1971</td>
<td>Substantial pay increase (BAQ) for career military</td>
</tr>
<tr>
<td>1971</td>
<td>Authorization for enlistment bonus &amp; other AVF-related special pays</td>
</tr>
<tr>
<td>1972</td>
<td>Double pay increase for federal employees (January and October)</td>
</tr>
<tr>
<td>1975-76</td>
<td>Pay &quot;caps&quot; for federal employees</td>
</tr>
<tr>
<td>1976</td>
<td>Elimination of &quot;1% kicker&quot;</td>
</tr>
</tbody>
</table>

From the events listed in Table 2-3 the reader can see that increasing manpower costs, which have risen from $19 billion in fiscal year 1956 to $59.6 billion in fiscal year 1976, were the result of the individual and cumulative effects of many different policy decisions implemented since the end of World War II.

By fiscal year 1977, the rate of pay and retirement had changed dramatically. No longer were the lower grades of enlisted personnel earning a substandard wage and no longer did a military retiree face a "second career" from necessity rather than choice. The President's Commission may have been influenced to some extent by this when it stated in Recommendation 7 that no

Table 2-4

<table>
<thead>
<tr>
<th>Grade</th>
<th>Total Pay and Cash Allowances</th>
<th>Monthly Basic Pay</th>
<th>Mo. Pension 20 Years Service</th>
<th>Mo. Pension 30 Years Service</th>
</tr>
</thead>
<tbody>
<tr>
<td>0-6 Colonel or Captain (N)</td>
<td>$2,574</td>
<td>$2,190</td>
<td>$1,095</td>
<td>$1,886</td>
</tr>
<tr>
<td>0-4 Major or Lt. Commander (N)</td>
<td>2,040</td>
<td>1,715</td>
<td>858</td>
<td>1,287</td>
</tr>
<tr>
<td>0-3 Captain or Lieutenant (N)</td>
<td>1,781</td>
<td>1,483</td>
<td>714</td>
<td>1,112</td>
</tr>
<tr>
<td>E-6 Staff Sgt. or CPO (N)</td>
<td>984</td>
<td>800</td>
<td>400</td>
<td>601</td>
</tr>
<tr>
<td>E-5 Sgt. or Petty Officer 2nd Class (N)</td>
<td>848</td>
<td>680</td>
<td>340</td>
<td>510</td>
</tr>
<tr>
<td>E-4 Corporal or Petty Officer 3rd Class (N)</td>
<td>712</td>
<td>564</td>
<td>282</td>
<td>423</td>
</tr>
<tr>
<td>E-3 Private 1st Class or Seaman Recruit (N)</td>
<td>622</td>
<td>494</td>
<td>247</td>
<td>371</td>
</tr>
</tbody>
</table>


military old age annuities should be paid to former military members while they are employed by the federal Civil Service. On balance DoD estimates show that
between the years 1964 and 1976 military manpower costs increased approximately 143% per person.

From examination and comparison of Tables 2-1 and 2-4 it is a simple matter to see what has caused the sharp growth in the cost of military retirement. The benefit formula of 2.5% produced a 50% of pay benefit in 1964 but the dollar value was small, ranging from $473 per month for a colonel with 20 years of service to $165 per month for a staff sergeant. However, by 1977 the same pensions had become $1,095 and $400 and payable at extremely early ages.

The percent value cost of an annuity becomes progressively higher as its starting age is advanced. For instance, approximately $1,100 is required to produce $10 a month starting at age 65 but $1,900 is required at age 40 which is close to the average retirement age for enlisted personnel.9

Scope and Cost of Present System

In Chapter I it was briefly noted that the present outlay for military retirement is $9.5 billion and if left alone will equal $34 billion by fiscal year 2000. These funds are currently disbursed to some 1.1 million military retirees. The average age of the fiscal year 1975 retiree was 46 for an officer who had served 25 years, and 41 years of age for enlisted personnel who had served an average of 22 years.

The projected cost of the current system can be expressed in either of two ways. The first method is in current dollars, i.e., dollars of the year in which the figure is cited and increased by the rate of inflation selected.

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9 Among the 1.1 million military retirees outstanding today, the average enlisted grade at retirement is the E-7; i.e., Air Force master sergeant, Army sergeant first class, Navy chief petty officer, and Marine Corps gunnery sergeant. The average officer retires at the rank of 0-5, i.e., Air Force Lt. Col.; Army Lt. Col., Marine Corps Lt. Col., and Navy Commander.
It is this method that the taxpayer should insist be used in all government studies and projections of future cost increases of any type, the reason being that it is in current dollars that taxes are levied. In other words, governmental agencies should be required to express their requests for funds for goods and services in the same dollars that the taxpayer base of the nation possesses with which to meet those requests; and to show projected cost increases in the same manner. And, of course, it is this method that shows most clearly the effects of inflation.

Constant dollar projections do the opposite. This is the method most often used by DoD, and it masks inflation by subtracting from the increase each year the rate of inflation used. Witness, for example, the following exchange during the fiscal year 1975 Military Procurement hearings of the Senate Armed Services Committee. 10

Senator Byrd. In your prepared remarks, Mr. Secretary, you state that the military fiscal year 1975 budget in constant dollars is smaller than the fiscal year 1964 budget of a decade ago?

Secretary Schlesinger. Yes, sir.

Senator Byrd. What inflation factor did you take to arrive at that conclusion?

Secretary Schlesinger. I don't have a chart that is handy on that Senator, but pay increases between 1964 and 1975 are on the order of 178 percent.

Senator Byrd. But you are speaking in constant dollars. What I am getting at is, I assume what you mean is if there had been no inflation, is that what you meant? When you say "constant dollars", doesn't that mean eliminating the inflation factor?

Secretary Schlesinger. Yes, sir.

Since it is inconceivable that Harry Byrd, the financial watchdog of the Senate, is ignorant of the use of constant versus current dollars in projecting increased costs, the reason for this questioning of Schlesinger must have represented an attempt to get on the record the explanation of what the author believes to be a prime example of sleazy DoD legerdemain.
Table 2-5 shows past and future military spending under both methods:

Table 2-5

| Past and Projected Military Retirement Outlays for Selected Fiscal Years: In Billions of Dollars |
|---------------------------------|----------------|----------------|----------------|----------------|----------------|
| Current-Year Dollars           | 1.2  | 9.1  | 9.9  | 13.8 | 15.6 | 37.5 |
| Constant 1978 Dollars          | 2.4  | 9.1  | 9.4  | 10.4 | 10.7 | 12.4 |


It should be remembered, however, that the U. S. military retirement system is an unfunded, pay-as-you-go system. The outlays which have been discussed herein reflect only the actual funds disbursed to retirees. However, they give no indication of the liability that the government is incurring for the future costs of today's active duty personnel. Sound pension planning in the private sector mandates the recognition of such a liability in the form of an accrual cost which must be ascertained and paid each year into a trust fund.

Estimates on such an accrual cost for the military vary. Congressional Budget Office estimates are $7.1 billion for fiscal year 1979.\(^{11}\) A strong case can be made for the implementation of the accrual charge since in so doing the defense budget will more accurately reflect its true cost. Under the present accounting system the defense function states the retirement costs of former military employees who do not contribute to today's defense, but it includes no charges for current military employees who are on active duty.

Above all, however, accounting changes of this type would increase incentives to economize on manpower. Retirement costs are a very important part of the total cost of compensation, representing 30% to 45% of military basic pay. But if these costs do not appear in the budget it is less likely that the true impact can be realized.
CHAPTER III

Design Problems and Consequences

The chief single obstacle to any hope of successful pension reform is the present provision which allows a high percentage of pay to be immediately distributed upon completion of twenty years of service. No private plan has met anything but waste and disaster with such a plan provision. Its need here is bottomed upon the youth and vigor concept — and promotion flow.

Let us rid ourselves of the illusion that a young and vigorous Army must be comprised of men in their late teens and early twenties. Most Americans would be shocked to know that the average age of the service arms is twenty four . . . On balance, except for a few MOS classifications in a very few parts of the world, I believe that the American service man or woman can function satisfactorily into their mid-fifties.

From testimony of Shelton Clarke, witness, President's Commission on Military Compensation, December 21, 1977, Washington, D. C.

Clearly the design feature of the immediate payout of an annuity equal to 50% of basic military pay for a twenty-year career has been subjected to as much or more criticism than any other by advocates of military pension reform. It has resulted, for instance, in an appalling exodus from the services at an age far in advance of the end of usefulness to country — indeed as has been noted, the average age of 1975 enlisted personnel was 41 1/2 and age 46 for officers. This in turn triggers an annuity payout for a period of time almost four times as long as is the case in the private sector where the normal retirement age universally is 65.1

1See supra, Table 1-1. Contrasted with the $1 million plus projected payout illustrated would be a payout less than 1/10 as great for a comparably salaried civilian plan participant in a 50% of pay defined benefit plan.
Besides the monetary or budgetary aspects is the effect on the force profile itself from the "twenty and out" feature. Largely because of this phenomenon, which reflects the occurrence of both voluntary and involuntary retirements at 20 years of service, DoD has found itself faced with excessive manpower replacement costs encouraged if not directly caused by the retirement plan itself. In terms of manpower management and the desired force profile, DoD would like:

(a) Increased retention at 4 to 12 years of service.
(b) Increased retention at service after 20 years.
(c) Reduced retention for 12 to 20 years of service.  

Table 3-1

<table>
<thead>
<tr>
<th>Years of Completed Service</th>
<th>Enlisted</th>
<th>Officers</th>
<th>and Enlisted</th>
</tr>
</thead>
<tbody>
<tr>
<td>0</td>
<td>1,000</td>
<td>1,000</td>
<td>1,000</td>
</tr>
<tr>
<td>5</td>
<td>194</td>
<td>411</td>
<td>211</td>
</tr>
<tr>
<td>10</td>
<td>121</td>
<td>329</td>
<td>137</td>
</tr>
<tr>
<td>15</td>
<td>97</td>
<td>327</td>
<td>115</td>
</tr>
<tr>
<td>20</td>
<td>89</td>
<td>318</td>
<td>107</td>
</tr>
<tr>
<td>25</td>
<td>11</td>
<td>134</td>
<td>21</td>
</tr>
<tr>
<td>30</td>
<td>3</td>
<td>46</td>
<td>6</td>
</tr>
</tbody>
</table>


2 One question which cries out for an answer is how even an unfunded pension plan, non-vested for service less than 20 years, can require a contribution of up to 45% of covered payroll, when at the end of 20 years only 107 employees out of 1,000 remain as employees. One answer is that "20 and out" is costly to an outrageous degree.
Within the implications of the inverted pyramid shaped force shown above, it may be easily seen that DoD has been unsuccessful in achieving its force management goals. One reason could be that without universal military training to assure it of an even inflow of personnel, it is forced to operate in a market environment, encountering recruitment problems in inverse relationship to the economic condition of the nation. Thus DoD must always plan upon several different assumptions of the economy. It must plan and forecast upon data always reflecting (a) high civilian employment; (b) present employment; and (c) lower employment.

The reader will note from Table 3-1 that almost 80% of enlisted recruits leave the service by the fifth year. Once an enlisted man has completed one term (usually 3 or 4 years) and reenlisted for another, the services

3 While the author freely admits that reasonable men may differ on many of the observations herein, there can be no difference of opinion in the sentence referred to by the footnote. Recently Senator Sam Nunn, in his Senate Subcommittee on Manpower and Personnel hearings of March 2, 1977 on the All-Volunteer Armed Force attempted to elicit a consensus from four experts on a possible return to the draft. On one point only were the witnesses in agreement, and it was that force management of the service arms was poor.

4 The question of the advisability of a return to a fairly administered and enforced system of universal military training as an obligation of citizenship is regrettably outside the scope of this thesis. It is noteworthy that in addition to all the communist bloc states, some 10 member states of NATO use the draft, including the Federal Republic of Germany and France. See especially the recent report to the Senate Armed Services Committee, Achieving America's Goals: National Service or the All-Volunteer Armed Force? 95th Cong. 1st Sess. 121 pages. The report was prepared by William R. King, Professor of Business Administration, Graduate School of Business, University of Pittsburgh. Needless to say, Professor King, as does the author, believes that the days of the volunteer army are numbered.
are unwilling to force that person to leave until he has completed 20 years
and becomes eligible for a pension. The President's Commission noted this
"lock-in" as well:

... Second, this "lock-in" constrains personnel
managers who may be reluctant to separate mandatorily any but
the very poorest performers and criminals. While specific
policies differ by service, it is likely that many marginal
personnel are carried to the 20-year point ... Both in
absolute numbers and as a percentage, very few members with
more than 9 years of service are mandatorily separated.  

Forcing a soldier out with less than 20 years, the services would
argue, is unfair. At the other end of the spectrum, i.e., the first reenlist-
ment period, there is waste as well. According to the Congressional Budget
Office, the Services hold down retirement costs consciously by limiting the
number of personnel permitted to reenlist. All of the services are turning
down some qualified persons who desire to reenlist after four years of service.  
This policy sacrifices the multiple benefits of higher first-term reenlistments,
including a larger number of experienced journeymen personnel, reduced need for
recruits and lower training and recruiting costs. This costly "tail wagging"
effect of plan-over-manpower is especially disturbing when studies have sug-
gested that second-term military personnel may be 50% more productive than first-
term personnel.  

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5Report of the President's Commission on Military Compensation. op. cit.,
p. 43.

6Congressional Budget Office. The Costs of Defense Manpower: Issues for
1977. op. cit., p. 80.

7Ibid., N. 10, p. 24.
Retirement benefits also have a strong effect upon retention later in a career. Few personnel leave after 10 to 12 years of service (see Table 3-1) when DoD desires an increase in service departure. This is partly unavoidable and a similar trend at this point is found in private employment -- but also because the "20 and out" point in time is anticipated. Nor, as it has been pointed out, do the services tend to force out personnel at this point because of lost pension rights. So here again the pension plan is whiplashing DoD into undesired and costly manpower management practices.

Once the 20 year point is reached, a large fraction of the force departs. This is the "20 and out" device and the heart of plan abuse. In sum, the 20-year benefit and distribution provision under the current system gives to the employer, who consists of the taxpayer base of the nation, the worst of both worlds. First, there is little retention incentive at the precise point at which DoD needs to improve retention (i.e., 4 to 12 years of service and more than 20); and secondly, substantial retention incentive for those whom DoD needs less (i.e., 12 to 20 years of service).

The President's Commission dealt harshly with the "20 and out" feature. It did so by a recommendation which would delay the distribution of a life annuity payout to a more realistic retirement age. Under the Commission system, old-age annuities would begin only at age 55 for 30 or more years of service; at age 60 for 20 to 29 years of service; and at age 62 for 10 to 19 years of service. However at age 65, the recommended annuities in combination with Social Security would still yield a very generous level of income. For example, the combination would replace more than 80% of after-tax active duty pay for a

\[8\] Ibid., p. 81.
30-year member and more than 65% of after-tax active duty pay for a 20-year member.

The new pension alignment of military pay plus Social Security would look as follows:

Table 3-2

Percentage of After-Tax Active Duty Income Replaced by After-Tax Military Retired Pay and Social Security at age 65

<table>
<thead>
<tr>
<th>Rank</th>
<th>Years of Service</th>
<th>Percent</th>
</tr>
</thead>
<tbody>
<tr>
<td>E-6</td>
<td>16</td>
<td>79.5</td>
</tr>
<tr>
<td>0-4</td>
<td>16</td>
<td>63.0</td>
</tr>
<tr>
<td>E-7</td>
<td>20</td>
<td>78.5</td>
</tr>
<tr>
<td>0-5</td>
<td>20</td>
<td>65.8</td>
</tr>
<tr>
<td>E-7</td>
<td>22</td>
<td>77.5</td>
</tr>
<tr>
<td>0-5</td>
<td>22</td>
<td>68.6</td>
</tr>
<tr>
<td>E-8</td>
<td>25</td>
<td>78.0</td>
</tr>
<tr>
<td>0-6</td>
<td>25</td>
<td>73.4</td>
</tr>
<tr>
<td>E-8</td>
<td>30</td>
<td>85.6</td>
</tr>
<tr>
<td>0-6</td>
<td>30</td>
<td>81.7</td>
</tr>
</tbody>
</table>

Source: Report of the President's Commission on Military Compensation. Table 4-9. p. 80.

Richness Level of Benefit Formula

Coupled with the key defect of the distribution of an immediate annuity at 20 years of service of 50% of basic pay is the question of what is an equitable benefit, both to the military retiree and to the non-military taxpayer whose taxes fund the system. In other words, what does the nation owe its military for a reasonable career of faithful and dutiful service?

9It is, of course, true that military personnel pay federal income taxes under the same Internal Revenue Code as is applicable to civilians. However, in 1976 some 89 million Americans paid taxes. Subtracting out the military who comprise some 2 million and adjusting for level of income etc., the author estimates that the civilian taxpayer bears over 98% of the cost of the military retirement system.
We must examine this eternally complex and classic question because in general the United States' military retirement benefit is unique in the world among governmental or private sector plans in the critical areas of level-of-benefit to pay, and timing of distribution of benefit. In the private sector the norm is a pension of 40% to 60% of final average pay when the applicable Social Security benefit is added. Less than 3% of private plans are inflation proofed for cost-of-living adjustments by a contractual tie to the Consumer Price Index (CPI). Congressman Les Aspin (D-Wis.) has suggested that when the tax structure is fed into the equation one finds that a pension equal to one-third of final pay will maintain the standard of living for a taxpayer who had been paid $10,000 a year, which is the pay of an E-6 Staff Sergeant or Chief Petty Officer (N). 10 A pension of 50% of pay will do the same for a married taxpayer paid $20,000, which is the pay of an O-4 Major or Lt. Commander (N).

A further significant basis of comparison is the 1975 Bankers Trust Company study. The corporate pension clients analyzed therein comprise some 150 companies. The 1975 work compares the various provisions of 271 plans of which 75% are conventional and 25% are union. 11 The following table is drawn

10 Aspin has made, and will continue to make in 1979, a very significant contribution to the actual modification of military retirement as recommended by the President's Commission. He introduced six bills in the 1976 Congress to that end. Aspin has a doctorate in economics, has worked as an economics analyst in the Defense Department and is a member of the House Armed Services Committee. He has championed the enlisted man's pay rights on several recent occasions.

from the statistical analysis showing median pension benefits as a percentage of pay for four different compensation ranges with a separate calculation for the Social Security benefit. The career assumption is 30 years:

Table 3-3

**Pension Benefits of Conventional Private Sector Plans**

<table>
<thead>
<tr>
<th>Final Year's Compensation</th>
<th>Final Pay Plans</th>
<th>Career Average Plans</th>
<th>Total Plans</th>
<th>Social Security Benefit</th>
</tr>
</thead>
<tbody>
<tr>
<td>$ 9,000</td>
<td>30%</td>
<td>28%</td>
<td>29%</td>
<td>39%</td>
</tr>
<tr>
<td>15,000</td>
<td>33</td>
<td>31</td>
<td>32</td>
<td>25</td>
</tr>
<tr>
<td>25,000</td>
<td>36</td>
<td>35</td>
<td>35</td>
<td>15</td>
</tr>
<tr>
<td>50,000</td>
<td>38</td>
<td>37</td>
<td>38</td>
<td>8</td>
</tr>
</tbody>
</table>

Note: 5% salary scale used in computations.


The reader should note that the companies which are reflected in the Bankers Trust data are among the nation's largest and most affluent, and possess richer plans in level-of-benefits to pay than is the norm. However, the data does cover some 8.4 million of the total labor force of approximately 80 million persons.

From Table 3-3 it may be seen that at the $15,000 civilian earnings level (representative also of the average-in-force enlisted grade at the time of retirement), the combined pension benefit plus Social Security is about 57% of pay. Note from Table 3-2 that the President's Commission recommended total pension-to-pay percentage at the E-8 (the average enlisted grade at retirement) is substantially higher; namely, 85.6%.
However, almost none of the plans in the private sector are cost-of-living indexed. The Bankers survey in general shows that more than 80% of the plans analyzed, exclusive of Social Security, yield a pension benefit of less than 40% of final pay for a 30-year career. Clearly the benefit level of the American military retirement system produces a level of benefits far more than the majority of non-military taxpayers can expect to receive.

It was in this general area of benefit comparability that the President's Commission broke most completely with the defenders of the present system within the military. Citing the conditions of inequity as perhaps its chief finding—albeit a philosophical one and expressed however implicitly in the report it stated in chapter three, "Military Retirement: Deficiencies of the Current System":

The military retirement plan received more of the Commission's attention than any other component of military compensation. While the cost of military retirement represents a substantial proportion of all defense expenditures, cost alone does not provide a case for change. Rather, the Commission concludes that change is needed because of three inherent deficiencies in the existing retirement plan.

1. The current system is inequitable. Compared to most public and private sector systems, it provides significantly more generous benefits. Military retirement provides generous benefits relative to private sector plans in a second respect: military retirees' pay is completely protected against inflation, an unusual and valuable feature.

The other two deficiencies referred to dealt with the lack of a vesting provision for service of less than 20 years, and the inhibiting effect of the plan upon force management. It is important that the reader understand the importance of the first deficiency especially, since it constitutes the very heart of the Commission's findings. The consequence of any pension plan of an excessive benefit level is excessive cost, and the only true method of reducing cost is to first reduce benefits.
Table 1-1 was prepared by the author for the CLU article mentioned in the Preface. It is repeated in this thesis to emphasize that it is inequitable for an Army Colonel or Navy Captain to receive $1,080,000 in retirement benefits in 1977 dollars for an average retirement under reasonable assumptions -- and that it is equally inequitable for a Sergeant First Class or Navy Chief Petty Officer to receive $446,000 in similar circumstances.

Because of the admitted need for a vesting schedule which will provide severance benefits for service less than 20 years, plus the need for an accrual fund for in-service personnel -- any savings to be realized from military pension reform will be disappointing. But above all the reader must realize that meaningful benefit reductions in the amount of total annuity payout will be required to produce any savings at all.

Social Security Integration

Another major inequity which exists in military retirement is the lack of the inclusion of the ultimate Social Security benefit in the computation of the 50% or 75% retirement benefit. Martin Binkin of Brookings formulated a table to show the "balloon" of benefits from this omission as did the author in Table 1-1. From the author's table it may be seen that the 0-6 Colonel or Navy Captain, at age 65, will have a combined military and Social Security benefit equal to 193% of pay; in the case of the Sergeant First Class or Navy Chief, 151%.

In the design and implementation of private pension planning, the integration of the applicable Social Security benefit under appropriate law and regulations is almost universally followed. In the Bankers Trust survey

12 Binkin, op. cit., p. 13.
some 87% of conventional plans used some type of Social Security integration. The Commission recommended the recognition of the benefit, as has every observer of the system familiar to the author.

The CPI Cost-of-Living Adjustment

The final, substantive defect in the system which has significant consequences in cost is the CPI cost-of-living adjustment used in military retirement as well as in the civil service plans in which the civilian employees of DoD participate. Under a complex allocation formula, the retirement benefits of these retirees are subject to cost-of-living adjustments (strangely the law does not provide for decreases) twice annually should the CPI increase sufficiently.\textsuperscript{13} This affords them a complete shelter from the loss of purchasing power during a post retirement period, in the case of the 20-year military career, which often lasts 35 years or more. The cost consequence of this device is substantial and is the singlemost important reason for the half trillion dollar payout mentioned in the motto of Chapter I. A reasonable estimate may be made of the dollar value of the inflation-created portion of the total payout projected from fiscal year 1975 to fiscal year 2000, the period of Senator Symington's estimate. The President's Commission estimated that without inflation military retirement pay would grow from $9.2 billion

\textsuperscript{13}The reader may secure a clear and concise explanation of the mechanics of the CPI adjustment, from the 1977 Uniformed Services Almanac, op. cit., pp. 43-44. It is here that public pressure upon the politician is in great need. Besides being inequitable to the participants of the civilian non-governmental labor force who have no comparable protection -- the immunity from inflation worry removes from the bureaucrat the personal involvement that he above all should have. It is imperative that the federal civil servant and the members of Congress whose pension plans are inflation proofed, have the same self interest in the fight against inflation as does the non-governmental taxpayer.
in fiscal year 1978 to $13.2 billion in fiscal year 2000. Using straight line
extrapolation from 1978 to 2000 beginning with $9.2 billion and ending with
$13.2 billion at year 2000, and adding in the cost for 1975 - 1977 of $27
billion, will yield a total non-inflated payout of approximately $292 billion.
Since the Symington estimate of payout with a 5% inflation factor was $470
billion, it may be seen that some $177.8 or $7.11 billion per year of the
twenty-five year average will be paid due to the cost-of-living CPI adjustment.
The reader should remain aware that similar projections and results may be
reached in a projection of the federal civil service plan. In some way we
must demand no less than this of our politicians and civil servants in the
fight against inflation, which the author believes to be far more dangerous
than all the divisions and tanks and missiles of the Soviet Union combined.
The public servant must be made equally vulnerable to inflation if he is to
fear it equally with the citizenry.

It is important for the reader to understand in at least a general
way how and for whom the Index is compiled and how it operates in changing the

14 The above calls to mind an anecdote told by Hedrick Smith in his book,
The Russians. Smith, in conversation with a Russian scientist one evening
asked:
"What was the best period in Russian history? 'The best times of our lives,'
he replied 'was the War.' 'Because at that time we all felt closer to our
government than at any other time in our lives. It was not their country then,
but our country. It was not their war, but our war. It was our country we
were defending, our war effort. The war was the one time when the poets were
writing poetry sincerely.'" (Hedrick Smith, The Russians, The New York Times
The anecdote is offered to suggest that while domestic inflation cannot be com­
pared to the Wehrmach of Adolph Hitler, it is no less the enemy -- and an enemy
which the U. S. politician and civil servant should share with the people as is
now not the case.
benefit level for several million Americans in an inequitable manner. First, as to how the CPI is compiled. The Consumer Price Index (CPI) measures average changes in prices of goods and services usually bought by urban wage earners and clerical workers. It is based on prices of about 400 items which are selected to represent the movement of prices and goods and services purchased by wage earners and clerical workers. Prices for these items are obtained in urban portions of 39 major statistical areas and 17 smaller cities which were chosen to represent all urban places in the United States. They are collected from about 18,000 establishments -- grocery and department stores, hospitals, filling stations, and other types of stores and service establishments. Prices of food, fuels, and a few other items are obtained every month in all 56 locations. Prices of most other commodities and services are collected every month in the five largest areas and every three months in other areas.

In calculating the Index, price changes for the various items in each location are averaged together with weights which represent their importance in the spending of all wage earners and clerical workers. Local data are then combined to obtain a U. S. city average. The Index measures price changes from a designated reference date -- 1967 -- which equals 100. An increase of 5% for 1968, for instance, would change the index to 105.

The reader will note that the Labor Department has not furnished to the Congress a separate index reflecting the buying habits of at least a partial sedentary life style which characterizes the retiree. Thus, the CPI used for the military as well as for the civil service pension plans will tend to over

---

15 The writer spent a good part of his testimony before the President's Commission attempting to show Commissioner John Filer that the principle of a percentage adjustment versus a flat dollar increase, resulted in excessive increases for the high ranking military at the expense of the lower enlisted grades. This line of reasoning will be fully developed herein.
compensate for that reason. Second, a good part of retirees live not in urban areas but in a rural environment, whereas the Index is compiled mainly from urban centers. This is a factor that will further tend to result in over compensation.

However, the main deficiency — a deficiency so blatant and obvious that it cannot have been overlooked by the architects of the Index who are themselves its beneficiaries — is the percentage principle upon which the adjustments are awarded. For example, the following table computes the effect of a 7% CPI improvement upon the retirements of three different members of the service.16

### Table 3-4

<table>
<thead>
<tr>
<th>Rank or Grade</th>
<th>Beginning Annual Pension</th>
<th>CPI Increase @ 7%</th>
<th>Total Benefit 2nd Yr.</th>
<th>CPI Increase @ 7%</th>
<th>Total Benefit 3rd Yr.</th>
</tr>
</thead>
<tbody>
<tr>
<td>0-9 General or Vice Admiral (N)</td>
<td>$29,700</td>
<td>$2,079</td>
<td>$31,779</td>
<td>$2,225</td>
<td>$34,004</td>
</tr>
<tr>
<td>0-6 Colonel or Captain (N)</td>
<td>22,632</td>
<td>1,584</td>
<td>24,216</td>
<td>1,695</td>
<td>27,606</td>
</tr>
<tr>
<td>E-7 Sergeant First Class or CPO (N)</td>
<td>9,828</td>
<td>687</td>
<td>10,515</td>
<td>736</td>
<td>11,251</td>
</tr>
</tbody>
</table>

Source: Table 3-4 was constructed by the author using current military pay rates.

It is basic to the principles of sound retirement planning that the benefit to be received should not require an unreasonable drop in living standard on the part of the retiree. In other words, the dollar value of the benefit should comprise a reasonable percentage of earnings. It is axiomatic

16 The use of a 7% improvement rate is entirely within reason. For the last 10 years the military have enjoyed an annual pension increase of more than 8%.
in the private sector, for example, for the corporate executive to receive a
higher benefit than a member of the rank and file. And, of course, this
philosophy is translated into the military wherein the general receives a
higher benefit than does the colonel and the colonel more than the sergeant.
The author finds no fault with that, since pension follows pay. However, and
most importantly, the principle of cost-of-living adjustments should be
expressed and allocated not on a percentage basis but on a flat dollar basis.
Note that the retired Lt. General and his wife presumably leading at least a
partial sedentary life with children grown and home paid for; with the drives
of economic acquisition presumably diminished -- receiving a first year allow-
ance for a diminishment of purchasing power of $2,079 which is the pension
itself of many thousands of non-military retirees who have no such inflationary
protection.17

Was this general's loss of purchasing power $2,079? Almost assuredly
not; possibly $500. What is wrong is that he was given a percentage increase
whereas he should have had a flat dollar allowance for the actual dollar value
of loss of purchasing power.

Contrast the adjustment of the general with that of the sergeant and
his wife. The author does not suggest that the sergeant should have the same
pension benefit -- certainly not. But the actual loss in purchasing power
experienced by the sergeant was not dissimilar to that of the general by a
factor of three. The taxpayer should not be compelled to bear the cost of

17 Less than 1/2 of the labor force have private pension coverage at all.
Nor does the present CPI reflect the discounts which the military retiree is
privy to such as Commissary rights, post recreation privileges and free medical
care.
such an absurd and wasteful level of over compensation to a favored few. Indices based upon flat dollar cost-of-living adjustments could be constructed and maintained by the Department of Labor.

The attempt, however, to convince the President's Commission of this inequity was in vain. The following exchange was between the writer and Commissioner John Filer, chief executive of the Aetna Life and Casualty Insurance Company. 18

Mr. Filer. My assumption is your colonel and your sergeant, each one's dollar was reduced by 7 percent of purchasing power, however,

Mr. Clarke. I am suggesting that maybe the percentage -- the percentage principle is wrong. The loaf of bread increased 10 cents for both the colonel and the sergeant.

Mr. Filer. You can argue that in terms of base subsistence and the ability to get along that one man's retirement is less than another. But nevertheless it is a factor that each one's purchasing power was reduced by the same percent.

Mr. Clarke. No. I was simply trying to say, Mr. Filer, that the loaf of bread increased 10 cents for the colonel and the sergeant alike, yet the colonel was compensated 4 times as much.

Mr. Filer. Each was reduced by 7%.

Mr. Clarke. But it was reduced by a percentage and not a flat dollar level which is more equitable. The loaf of bread increased the same for the colonel as the sergeant, so why should the compensation for the loss of purchasing power be dissimilar?

Mr. Filer. Because his $8,000 of purchasing power was reduced by 7% and the other man's $3,000 was reduced by 7%, and the function of a pension is not simply to continue to provide an absolute subsistence and no more. At least, I never thought it was.

18 The writer has seen nothing in the several thousand pages of source material studied for this thesis to suggest that the CPI should either be uncoupled or modified. Dr. Gary Nelson did suggest by letter that the Index is not geared to the expenses facing military retirees and indicated that large cumulative cost differences over a period of time could result therefrom. He stated that he believed the Department of Labor was working on other types of cost-of-living indices at the present time.
Mr. Clarke. You may be right as to the pension but not as to the cost-of-living adjustment. What brought this to my attention Mr. Filer, was a letter to the editor in the New York Times of September 18, 1976 in which a military retiree wrote a letter which was highlighted. He said, "enough is enough". He said, "although benefiting from it myself as a military retiree, I have become convinced that it is essentially a giveaway program which dispenses too much to those who don't need it and not enough to those who do."

"In my own case I have been glad to get these raises but enough is enough, and I don't think the generals really need that giant increase while the sergeants have to scramble for post-retirement jobs or go on relief."

And here is what he says that is important. He said that as a guess a flat increase of about $20 per month would be ample to offset the increased cost of living for that year. A flat dollar benefit instead of a percent. Perhaps the letter can be printed into the record.19

The reader has by now seen the scope and magnitude of a giant governmental retirement system and the chief design defects which have contributed to its excessive benefits and costs. The chapters which follow will describe the efforts which have been made to modify it, the military response to those efforts and finally a suggested plan which is equitable in benefits and reasonable in cost.

19 Needless to say the Commission did not recommend a change in the cost-of-living provision. The letter to the editor is appended so that the reader may read the words of one American who would reduce his consumption at the public trough.
Old age annuities should begin at age 55 for 30 or more years of service, at age 60 for 20 to 29 years of service, at age 62 for 10 to 19 years of service. These annuities should be similar to those provided civil servants, integrated with Social Security benefits and protected from the effects of inflation at age 65 the recommended annuities in combination with Social Security replace more than 80 percent of after-tax active duty pay for a 30-year member, and more than 65 percent of after-tax active duty pay for a 20-year member.


The complexity and emotion surrounding change in the military retirement system point up the need to first establish criteria before attempting to choose between the current system and a revised one. The basic criterion is that total military compensation, including retirement, should be only great enough to attract and retain the personnel that the Department of Defense requires to carry out its mission. This criterion, because it is designed to at least match the sums other employers offer, takes account of the major aspects that must be considered in setting pay scales. The criterion requires that pay be high enough to allow DoD to compete successfully in a market environment for personnel, which is essential under conditions mandated by the all-volunteer force. On the other hand, the criterion should insure that costs to the taxpayer are kept to a minimum.
Other criteria may also be useful in choice and design of the system. For instance, military personnel must view the system as fair. If not, they may leave the military or, if they stay, they may perform less effectively. It is a balanced reform, rational pension reform meeting those criteria, that must be found if the system is to be modified in an acceptable and stable manner.

Alternate Reform Measures

Serious efforts at military pension reform began in 1971 when an Interagency Committee (IAC) was appointed by the President with participation from the Office of Management and Budget, Department of Defense, Department of HEW and Civil Service Commission) with a view toward reducing costs. This report was forwarded to the President in July 1971. The recommendations of the committee are shown in Table 4-2.

In 1972 the Secretary of Defense, following IAC action, established a DoD Retirement Study Group to evaluate the IAC recommendations and to recommend changes to the military nondisability retirement system. This inquiry resulted in the Retirement Modernization Act (RMA) which was before the 94th Congress as HR 7760. This legislation would have made two major changes. First, it provided for an early vesting of benefits. Secondly, pensions were to be reduced for 20-year careers.

1Indeed the armed services of Great Britain are now said to be in a crisis situation from low military pay and benefits. The British Army is one of the worst paid in Europe, five of twelve NATO members pay privates more than Britain pays lieutenants. Although having a first rate retirement plan, the armed forces are experiencing extremely high rates of voluntary discharges. It is, of course, well known in employee counselling that a competitive rate of cash pay is an absolute requisite to sound employee relations notwithstanding the adequacy of a retirement program. (See Associated Press Release, Richmond Times Dispatch. April 23, 1978.)
The third attempt came in the latter part of 1973 when the Defense Manpower Commission (DMC) was established by Congressional directive to conduct a broad and comprehensive study of overall DoD manpower requirements over the next ten years. These findings, along with the Aspin proposals, were reported to the President and the Congress in April of last year. Significantly it was here that the concept of a 30-point career was introduced with a weighting of pension benefits for combat service. The rationale here is that the "youth and vigor" concept is important to the combat MOS and yet early retirements in the non-combat specialities should be discouraged. Additionally, the writer believes that this concept would assist the DoD and the nation in solving the grave deficiency in our combat arms. The actual shortfall is classified and buried in the legerdemain and ambiguity of DoD statisticians. However, many civilian strategists believe it to be critical. The DMC proposals would grant a full annuity only after thirty years of service.

Every four years the President by law must initiate a review of military compensation. The Third Quadrennial Review of Military Compensation (QRMC) was formed in January 1975. Areas of inquiry were military salary, supplemental benefits and military retirement.

From a deep belief that the current military compensation system is chaotic and essentially a system that promotes early retirements and massive waste, Congressman Les Aspin introduced six bills in the 94th Congress to revise the military retirement system. His have become known as the Aspin Proposals. The heart of his reform goes to the elimination of the "quick pension". He would allow for voluntary retirements a full pension only at age 55 with 30 years of service; at age 60 with 20 to 29 years of service;
and at age 62 with 5 to 19 years of service. For those officers and enlisted men who are "forced out," he would provide an instant annuity under the benefit formula assuming there are 5 years of service. This annuity would be reduced $1.00 for every $2.00 of earned income. Instead of the present flat 2.5% of basic pay times years of service formula, Aspin would substitute a graduated benefit formula designed both to provide an equitable benefit for a career of service and to assist DoD in its management of manpower and force profile. This formula would give 1.25% times a different pay (RMC, which is the sum of basic pay, quarters and subsistence and the tax advantage) for each of the first 5 years, 1.75% for each of the next 5 years, and 2% for each year of service over 10.²

For a more equitable level of vesting, Aspin would make a participant eligible for a benefit after 5 years of service. Finally, Aspin would go to the Canadian model for a phase-in member contribution, and a fund to be paid by the services to assume actuarial solvency.

Table 4-1 notes the recommendations of the parties discussed above by plan provision, and offers to the reader a quick source of reference to a fiercely complicated subject.

## Table 4-1

A Comparison of Proposed Changes in Military Retirement/Compensation

<table>
<thead>
<tr>
<th>Plan Provision</th>
<th>Current System</th>
<th>Interagency Committee (IAC) Proposal</th>
<th>Retirement Modernization Act (RMA) Proposal</th>
<th>DMC Study</th>
<th>QRMC Services</th>
<th>Aspin Proposals</th>
</tr>
</thead>
<tbody>
<tr>
<td>Service Require-ments for a Pension Benefit</td>
<td>20 YOS</td>
<td>20 YOS</td>
<td>20 YOS</td>
<td>30, 20, or more YOS with 30 retirement pts.</td>
<td>Enlisted and officers RMC provisions supported</td>
<td>Enlisted and officers after 5 YOS at age 62; or at least 20 YOS, but less than 30 YOS at age 60; or at least 30 YOS at age 55. Recognize management need to force individuals out of service before a full career.</td>
</tr>
<tr>
<td>Voluntary Separation, enlisted</td>
<td>None</td>
<td>Enlisted and officers between 10-19 YOS, choice of: Deferred annuity at age 60 (2.5% x YOS x BP) or Lump sum: (5% x YOS x BP) at separation</td>
<td>Enlisted and officers between 10-20 YOS, pension at age 60 based on YOS x 2.5% of pay (CPI adjusted)</td>
<td>(10th YOS) Enlisted and officers—deferred annuity at age 65 (High-3 average pay x per pt. retirement multiplier x YOS completed). Note: Reduced deferred annuity at age 60.</td>
<td>RMA provisions supported</td>
<td>Enlisted and officers—between 5-20 YOS, pension at age 62.</td>
</tr>
<tr>
<td>Involuntary Separation, enlisted</td>
<td>None</td>
<td>Same</td>
<td>Enlisted and officers—between 5-20 YOS two options, a mo. benefit at age 60 plus immediate cash payment, or a cash payment double that in first option. Annuity at 60 computed on standard formula of 2.5% of pay x YOS (CPI adjusted). Cash payment in first option 5% of pay x YOS, and in second option 10% of pay x YOS.</td>
<td>Enlisted and officers—readjustment pay (mo. terminal pay x 24 x per pt. retirement multiplier) plus a deferred annuity at age 65 (reduced deferred annuity at 60) or an additional cash payment = to amt. of readjusted pay.</td>
<td>RMA</td>
<td>Enlisted and officers—immediate retired pay with 5 or more YOS. See employment restriction.</td>
</tr>
</tbody>
</table>

**Lost Time Pay:**
- Maximum $15,000 separation pay
- Average of High-3 years pay x no. of retirement pts.

**Benefit Formula Multipliers:**
- 2.5%/yr. 20 and over YOS
- 2.5%/yr. 20-24 YOS; 3%/yr. 25-30 YOS; 2%/yr. 31-35 YOS
- 2.66%/yr. 20-24 YOS 3%/yr 25-30 YOS
- RMA 1.5%/yr. to max. of 5 YOS 1.75%/yr. from 5-10 YOS 2%/yr. over 11 YOS
<table>
<thead>
<tr>
<th>Plan Division</th>
<th>Current System</th>
</tr>
</thead>
<tbody>
<tr>
<td>Pensions</td>
<td>Interagency Retirement Modernization (IAC) Plan (RMA) Study</td>
</tr>
<tr>
<td></td>
<td>Proposal</td>
</tr>
<tr>
<td></td>
<td>DMC QRMC Asplan</td>
</tr>
<tr>
<td></td>
<td>Services</td>
</tr>
<tr>
<td>Pension</td>
<td>Interentity</td>
</tr>
<tr>
<td></td>
<td>Conimilllon</td>
</tr>
<tr>
<td></td>
<td>Plan</td>
</tr>
<tr>
<td></td>
<td>Age 30 YOS</td>
</tr>
<tr>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
</tr>
<tr>
<td>Pensions</td>
<td>Full payment</td>
</tr>
<tr>
<td>and</td>
<td>from SS</td>
</tr>
<tr>
<td>Fiduciary</td>
<td>with 25 or more</td>
</tr>
<tr>
<td>Plan</td>
<td>30 YOS</td>
</tr>
<tr>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
</tr>
</tbody>
</table>
| plan       | Full payment | Dual Compensation | Same | Monthly retired pay of anyone in-
|             | from date of | Act (regular officers only). Forfeit ½ mil. retirement pay if em-
|             | retirement    | plan | Same | voluntarily retired pay if any-
|             |              |      | Same | one in-
|             |              |      | Same | volun-
| Fiduciary   |              |      | Same | tarily retired with at least 5 YOS and less than 62; at least 20 YOS but less than 30 YOS and less than 60 yrs. of age; at least 30 YOS but less than 55 yrs. of age. Will be offset mo. by any earned income rec’d = to 1/2 amnt. of such earned income. Earned income is defined in the IRS code of 1954. |
| Plan       |              |      | Same | Under consideration: a fund de-
|             |              |      | Same | veloped by contributions by the mem-
|             |              |      | Same | ber (7% of salary) matched by the federal government. |
|            |              |      | Same | Adjustments | Indexed | Semi-annually | Not addressed | Same as current system | Actual inc. in CPI | Under consideration: a fund developed by contributions by the member (7% of salary) matched by the federal government. |
|            |              |      |      | (March & Sept) | based on 5% of CPI in previous 6 mos. | Source: Excerpted and modified by the writer from a comparison prepared by Ad Hoc Committee of the United States Fleet Reserve Association. |
### Table 4-2

**Summary of Effects of Changes**

<table>
<thead>
<tr>
<th>Key Changes &amp; Effects:</th>
<th>Current System</th>
<th>RMA Proposal</th>
</tr>
</thead>
<tbody>
<tr>
<td>Annuity for 20-Year Retiree (a)</td>
<td>50% of basic pay</td>
<td>Reduced 30% below current level for 10 yrs. Then restored</td>
</tr>
<tr>
<td>Benefits for 0-19 Years' Service?</td>
<td>No</td>
<td>Yes</td>
</tr>
<tr>
<td>Member Contribution Required?</td>
<td>No</td>
<td>No</td>
</tr>
<tr>
<td>Phase-in for Reduced Annuity</td>
<td>-</td>
<td>20 Years</td>
</tr>
<tr>
<td>Lifetime Retirement Pay (b)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>30-Year Retiree</td>
<td>$310,000</td>
<td>$295,000</td>
</tr>
<tr>
<td>20-Year Retiree</td>
<td>190,000</td>
<td>155,000</td>
</tr>
<tr>
<td>10-Year Retiree</td>
<td>0</td>
<td>15,000</td>
</tr>
</tbody>
</table>

#### Summary of Effects:

| Overall Evaluation | Features large losses after 20 years of service, but few losses from 10-19 years. Costs increasing through end of this century. | Retains career pattern similar to today's, but costs less. Low risk. Proposed by DoD. |
| Effect on Career Patterns | See above | Continued high losses after 20 years likely. Retention may be higher from 5-9 years and lower from 10-19 years. |

| Required Changes in Personnel Management Policies | None | Few required |
| Costs (constant dollars) | |
| FY 2000 | $46.8 billion | Saves $1.2 billion |
| Total FY 1979-2000 | $936 billion | Saves $11 billion |
| Costs in DoD Budget if Accounting Procedure Change | $7.1 billion | Saves $1.6 billion |

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(a) Percentage reductions ignore high-1 or high-3 averaging, which depends on inflation assumptions.

(b) Total retirement pay for typical enlisted man expressed in today's dollars but undiscounted. Assumes retirement at median paygrade for given year of service, and average mortality rates.
<table>
<thead>
<tr>
<th><strong>IAC Proposal</strong></th>
<th><strong>Annuity at Age 55 to 62</strong></th>
<th><strong>President's Commission on Military Compensation</strong></th>
</tr>
</thead>
<tbody>
<tr>
<td>Reduced 34-42% below current level to age 60. Then restored (c)</td>
<td>Yes</td>
<td>Yes</td>
</tr>
<tr>
<td>No</td>
<td>No</td>
<td>No</td>
</tr>
<tr>
<td>10 Years</td>
<td>10 Years</td>
<td>4 Years</td>
</tr>
<tr>
<td>$265,000</td>
<td>$210,000</td>
<td>$281,109</td>
</tr>
<tr>
<td>110,000</td>
<td>65,000</td>
<td>191,971</td>
</tr>
<tr>
<td>15,000</td>
<td>10,000</td>
<td>8,600</td>
</tr>
</tbody>
</table>

Middle-ground option. More savings and longer careers than reduced-to-30 option. But no fundamental change.

Similar to reduced-to-30 except probably increase in those staying past 20.

Some to accommodate longer careers, but no fundamental changes.

Saves $2.2 billion

Saves $19 billion

Saves $2.4 billion

(c) Range depends on whether retiree is an officer (low end of range) or enlisted (high end).

Source: The basic table is reproduced from CBO, The Military Retirement System: Options for Change, Table 9, pp. 68-69. The author has added the analysis for the President's Commission heading and modified several column headings. Other modifications were made where indicated. The reader may by reference to Tables 4-1 & 4-2 quickly summarize the bulk of all pertinent potential reform measures.
Because substantial reform will almost certainly, in the absence of a national or international crisis, occupy the attention of Congress during the first half of 1979, the serious reader may appreciate an attempt to be provided with a narrative, descriptive summary of the philosophy and effect of the several major reform efforts marshalled in part by Table 4-1. The recommendations of the Carter Commission, which consisted of ideas both old and new, will be summarized in the concluding portion of this chapter.

In light of the substantial amount of time and effort which has been allocated and is being spent on military pension reform, it is possible that most of the components of the new system can be now identified. For instance, all of the studies, as well as DoD itself, have recommended changes in the military retirement system. They do not, however, agree on the amount of change. The studies illustrated in Table 4-1, as well as that of the Commission, illustrate a range of change from modest to severe. All of the studies have recognized a need for some degree of benefits for those who retire with less than 20 years of service. The packages differ in the benefit multiplier itself and the amount and length of reduction in annuity for service of between 20 and 30 years. The studies are roughly divided as to whether or not the military benefit should be reduced by all or a part of the Social Security benefit.

3 Shortly after the Report of the Commission was delivered to the Chief Executive he stated that he would make his recommendations known to the Congress in January of next year. The process, certain to result in an overall realignment of benefits downward to some degree, will be both emotional and explosive.

4 One item of reform, almost certainly is the elimination of the quick, 20-year pension of 50% of pay. Besides being exhorbitant in cost, it robs the force manager of a valuable tool in shaping the profile of the service arms, a principle fully explained in Chapter III. A second quess would be that the Social Security will be integrated into the military benefit in the same manner that it is used in the vast majority of private sector plans.
A. The Retirement Modernization Act (RMA) Proposal

This package was introduced in the Congress in 1974, 1975 and 1976. Legislative action was never completed. This option would reduce costs, but it should result in modest changes in career patterns. It is this option which would be most favored by those who believe that the military can best accomplish its mission with career patterns similar to those currently in force. Hence, for service of less than 30 years, this package would reduce annuities by creating a "two-step" annuity. The first step would last until the person would have completed 30 years of service, which is a full career. During the first step the annuity would be reduced by about 30 percent. During the second step, the annuity would be restored to close to its level under the current system. 5

This option would also provide deferred benefits for less than 20 years of service. A person leaving after 10 years of service would receive an annuity of 25% of basic pay, but payable at age 60. The system would remain noncontributory. In addition, this package would base annuities on average pay during the one year of highest pay, would increase the credit for retirement for service over 24 years, and would require an offset of the one-half of Social Security payments attributable to military service.

Under the current system for a typical enlisted man retiring at 39 after 20 years of service, an immediate lifetime annuity of $5,800 is granted. Under similar facts the RMA annuity during the first-step would be $4,010 for 10 years, then $5,370 -- then at 65 the military annuity would drop to $4,300 reflecting the Social Security benefit.

---

Finally, it is suggested that under the RMA proposal there would be an added incentive to complete a longer service career. On balance, however, this option would have relatively modest effects on career patterns.6

RMA Effect on Costs

Under the CBO classification of what is termed base-case behavior the RMA option would eventually reduce manpower costs.7 By the year 2000, outlays would go down by $1.2 billion a year in 1978 dollars and savings would continue to grow significantly in the years beyond 2000. The total savings between implementation in 1979 and the year 2000 would equal $11 billion. Most of the savings would occur because of reductions in annuities for those retiring with less than 30 years of service.

Summary of RMA Option

This option will save money. The RMA option would probably lead to modest changes in the pattern and length of military careers. Among the options under consideration in this chapter, this option would be the least consistent with the idea that military careers should be lengthened. It was originally drafted by DoD and championed in the Congress by the hawks of Vietnam. It has been overtaken by time and the economic forces of inflation.

6 Ibid., p. 43.

7 Base-case turnover assumes that there is no change from voluntary career retention that cannot be offset by involuntary severence from the service. Under base-case, the only deviation from current behavior is an increase in the number of involuntary separations between 10 and 19 years of service in the enlisted grades.
B. The Interagency Committee (IAC) Proposal

This option was designed by an interagency committee in 1971. The Department of Defense was well represented on the committee.\(^8\) The package is a middle ground option in fiscal savings and on career patterns. It would call for changes in the force profile.

Like the RMA option preceding, this one would create a two-step annuity except that here the reduction in the first step would be larger and last longer. The reductions here would range from 34 to 42 percent below current levels versus about 30% under RMA.\(^9\) The reductions under this option are designed to reduce military retirement pay during years when the retiree is presumed to hold a civilian job.\(^10\) Changes would be phased in over 10 years, and would provide benefits to separations from service with under 20 years.

Contrasted with the current system which in the case of a typical enlisted man retiring at 39 with 20 years of service would receive an immediate lifetime annuity of $5,800; this option would yield him $3,110 to age 60, then $5,360 til 65 at which point the military annuity would fall to $4,000 being partially offset by the applicable Social Security benefit.

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\(^8\)Edward T. Braswell, permanent counsel to the Senate Armed Service Committee sent the author a copy of the original report in 1974. The heavy hand of the career military bias was in every chapter and on every page. It was later modified.


\(^10\)The percentage of military retirees who seek and hold second career employment is very high, approaching 85%.
IAC Effect on Costs

Given again base-case career behavior, the initial savings here would be similar to RMA, but eventual savings would be larger. By the year 2000, costs under this option would diminish by $2.2 billion a year in 1978 dollars. Total savings between 1979 and 2000 would equal approximately 19 billion dollars. Outlays would, as they will in all the proposals, increase in the first few years.

Summary of IAC Proposal

This option is estimated to save about $19 billion between now and year 2000. However, the IAC package seems unlikely to result in a drastic change in current career patterns, which feature large numbers of retirements after 20 years of service. The option would reduce annuities for 20-year enlisted retirees. There would also be substantial reductions for officers although the IAC plan would permit annuities to continue to grow for those who stay past 30 years reaching a maximum of 88% of pay for 35 years of service.

On balance, IAC's larger and longer annuity reduction for 20-year careerists combined with higher annuities for those who stay past 30 years should reduce the number of 20-year terms and increase the numbers of those serving beyond 20 years. It is this option which may approach the largest cost savings possible without significant changes in career patterns and force profile management.

C. The Annuity at Age 55 to 62 Package

This package, which comes most closely to satisfying the desires of those who believe that immediate and meaningful pension reform is needed,
is a hybrid mix containing elements of the DMC Study and Aspin Proposals found in Table 4-1, and strong overtones of certain portions of the recommendations of the 1977 President's Commission. Its characteristics and effects are noted in Table 4-2 and comprise the third option for that table. This option is far-reaching and would result in significantly longer military careers. The eligibility rules for age follow those currently in effect for the federal civil service. The completion of 5 to 19 years of service begets an annuity beginning at 62; while those completing 20 to 29 years of service receive an annuity at 60. Those completing 30 years or more will receive an annuity at age 55.

While similar to the federal civil service for eligibility (see above) the plan differs from it in two ways. It would be non-contributory, and it would provide a cash bonus equal to one year's pay for involuntary severance at 20 to 30 years of service. This bonus, as well as the combat credit in the DMC option, would be designed to provide the Department of Defense with the flexibility to attract and retain those personnel, particularly enlisted combat personnel, who must be separated with less than 30 years of service for purposes of youth and vigor.

The annuity-at-55 proposal would radically change the pattern of annuity payout. Rough calculations indicate that for a typical enlisted man retiring after 20 years of service, lifetime retirement earnings would equal $65,000 as compared with $190,00 under the current system, a cut of 66%. For a typical enlisted retiree with 30 years of service, lifetime retirement earnings would go down some 32%.

11This is a most important point. The average American would be shocked to know that the average age of the entire U. S. Armed Forces is about 24. This option, as did the recommendations of the President's Commission, employed provisions which if implemented, will mandate substantially longer military careers.
Force Management Under the Annuity at Age 55 to 62 Option

The pattern of incentives offered by retirement would be substantially different from those in the previous option packages. An entirely different career pattern might evolve, reflecting the provision of some benefits after only five years. The pull to stay for twenty years might be significantly reduced. Whereas the previous retirement options feature a drop in value of retirement after 20 years of service, this option would not. The value of retirement benefits would continue to grow, in fact would grow most quickly as the 30-year service mark was approached.\^12 Losses after 20 years of service should be much lower, with the typical career lasting for 30 to 35 years. Losses from 10 to 20 years of service should occur more evenly (see Chapter III for discussion of desired force profile of the service arms). Losses from 5 to 9 years of service would be uncertain though they could be substantially higher.

Effect on Costs Under the Annuity at 55 to 62 Option

This option, of course, would result in substantial savings. By the year 2000 costs would be reduced by $4.5 billion a year and savings would continue to grow afterwards as well. Cumulative savings between 1979 and 2000 would total more than $36 billion in 1978 dollars. Costs would increase for several years as they would under all the optional packages. It is likely that the more senior force resulting from the implementation of this option would be

\^12 The serious reader should study the philosophy behind such formulation. Pension practitioners in the private sector have always counted this type of design as desirable and basic and have been puzzled at the inability of DoD and Congress to realize that a badly designed pension plan can corrupt desirable employee pattern objectives.
more productive, resulting, in the author's judgment, in substantial additional savings. However, of all the options hitherto discussed, this one would present the greatest potential risk to the force manager and to the nation. It cannot be ruled out that this option might not allow DoD to attract and retain adequate numbers of personnel.

It would appear that the Carter Commission weighed heavily the pros and cons of this option. The reader will note that when the Commission did render its report a new, radical device had been added, namely a deferred compensation trust fund to "assist former service members in their transition to civilian life and to provide additional incentives to remain on active duty through arduous and difficult duties."

On balance, however, it is highly likely that the reformed system will have heavy overtones of the Annuity at 55 to 62 Option. Further, this option, as well as the proposed plan of the President's Commission, is perfectly compatible with the Aspin Proposals which are not included in Table 4-2 but are described in Table 4-1.

D. The President's Commission Option

Of all the options discussed, this, the latest, will perhaps most influence the draftsmen of the ultimate, revised system. On June 27, 1977, President Carter established the Commission and charged it directly to:

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The Commission may have seriously erred in creating an additional fund of such magnitude. It would yield an additional $122,850 at 1% interest, for a 25-year career to a typical officer entering the service after 1978. It would yield in similar circumstances some $57,610 to the typical enlisted person. This fund, however, may not be dismissed out of hand. Some provision may have to be made for personnel between the time of retirement and the commencement of the annuity payments -- for reasons of equity.
review at least the analyses, findings and recommendations related to military compensation which have been completed by the Quadrennial Reviews of Military Compensation, the Controller General, the Interagency Committee Study of Uniformed Service Retirement and Survivor Benefits, the Department of Defense Retirement Study Group, and the Defense Manpower Commission.

Carter directed that the Commission identify, study and make recommendations on critical military compensation issues, specifically addressing the following issues:

... What are the purposes of the military retirement system?  
Is the present system effective in achieving these purposes?  
What changes are appropriate?

The Commission was composed of eight Commissioners and a chairman, Charles J. Zwick, who was a former Rand analyst, a former Director of the Budget, and now President of the Southeast Banking Corporation of Miami, Florida.¹⁴ The Commission was staffed heavily with in-service personnel and former members of the military who have been employed by the government in various civilian capacities thus giving rise to the possibility that the Commission members, all busy men and women, would be staff directed and staff run.¹⁵

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¹⁴ The Commissioners were Benjamin O. Davis, Jr., Lieutenant General, U. S. Air Force (Ret); William E. DePuy, General, U. S. Army (Ret); Thomas Enrlich, President, Legal Services Corporation; John F. Filer, Chairman of the Board, Aetna Life and Casualty; Phillip A. Odeen, Vice President, Wilson Sporting Goods; Walter H. Page, Chairman of the Board, J. P. Morgan & Co.; Jane C. Pfeiffer, Management Consultant; and Herbert F. York, Director, Program in Science, Technology, and Public Affairs, University of California, San Diego.

¹⁵ Indeed, this extremely heavy military influence caused observers to predict that little meaningful would come from its efforts in the way of military pension reform. The author believes that these fears were essentially incorrect.
President's Commission Retirement Recommendations and Their Significance

As the epigraph of this chapter would suggest, the "20 and out", quick pension would be eliminated and the present benefit formula multiplier of a straight 2.5% of salary would fall to those of the federal civil service, namely:

<table>
<thead>
<tr>
<th>Years of Service</th>
<th>Per Year Multiplier</th>
</tr>
</thead>
<tbody>
<tr>
<td>1 to 5</td>
<td>2.00</td>
</tr>
<tr>
<td>6 to 10</td>
<td>2.25</td>
</tr>
<tr>
<td>11 to 35</td>
<td>2.75</td>
</tr>
</tbody>
</table>

These multipliers are designed as they should be, to encourage service over a longer career. If the Commission had stopped at that point the military would have a plan roughly comparable to that of their civilian counterparts -- one of the finest in the nation, but without the burden of the 7% of pay annual personal contribution now borne by the civil servant.

In addition, the Commission option called for a continuation of inflation protection and a partial Social Security offset.¹⁶ No longer would military old-age annuities be paid to former military members while they were in the federal Civil Service; and a grandfather cloak would be thrown over the shoulders of the present force -- exempting from the retirement rules of the Commission those with 4 or more years of service, serving their second enlistment, or serving beyond their initial period of obligated service at the date of enactment.

¹⁶ The military pension reduction at age 65 would vary from 17% with 20 years of service to 11% with 30 years of service at rank of 0-5 and 0-6 to prevent a full superimposition of the Social Security benefit.
The President's Commission Deferred Compensation Trust Fund

The Commission would create a deferred compensation trust fund for each member who completes five years of service. The government's contribution to the fund for each member would be a decreasing percentage of basic pay each year, starting with 20% for years 6 to 10, and dropping to 5% for years 26 to 30. Members with 10 or more years of service could withdraw a portion of this account while on active duty.

This trust fund philosophically would serve at least two functions. First, it would assist former service members in their transition to civilian life and secondly, it would provide funds through periodic withdrawal to fund the "blackout period" from the day of discharge to the commencement of the old age annuity.17

The amounts to be provided as envisaged by the Commission are substantial and may be seen below:

Table 4-3
Amount of Deferred Compensation Accrued for an Individual Who Enters Active Duty in 1978*

<table>
<thead>
<tr>
<th>Years of Service</th>
<th>Officers</th>
<th>Enlisted Persons</th>
</tr>
</thead>
<tbody>
<tr>
<td>10</td>
<td>$18,320</td>
<td>$8,610</td>
</tr>
<tr>
<td>15</td>
<td>48,550</td>
<td>23,230</td>
</tr>
<tr>
<td>20</td>
<td>88,960</td>
<td>42,400</td>
</tr>
<tr>
<td>25</td>
<td>122,850</td>
<td>57,610</td>
</tr>
<tr>
<td>30</td>
<td>140,890</td>
<td>66,210</td>
</tr>
</tbody>
</table>

*Figures shown are fiscal year 1978 dollars for an individual who enters 1 January 1978 and leaves in the future with the stated years of service. Calculations are based on assumed 1.5% real wage growth and a 1.0% real interest rate on the fund.

Source: Report of the President's Commission. Table 4-7, p. 69.

17 However, the Commission did offer data which indicate that between 73% and 89% of all retirees seek and take a second career and that the average officer is successful within 3 to 6 months, while the enlisted person requires 2 to 12 months. There is a comparative earnings loss in the subsequent career of between 1% to 24% for enlisted retirees, and 6% to 38% for officer retirees as against comparably aged and educated civilians.
In addition to the deferred compensation fund, the current severance pay provision, presently limited to officers terminating at 5 - 15 years, would be broadened and enlarged to include enlisted personnel:

Table 4-4

Comparison of Severance Pay: Commission Plan Vs. Current System

<table>
<thead>
<tr>
<th>Years of Service at Separation</th>
<th>Officers</th>
<th>Enlisted Persons</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Current System</td>
<td>Commission System</td>
</tr>
<tr>
<td>5</td>
<td>$12,804</td>
<td>$ 1,431</td>
</tr>
<tr>
<td>10</td>
<td>15,000</td>
<td>3,475</td>
</tr>
<tr>
<td>15</td>
<td>15,000</td>
<td>8,493</td>
</tr>
<tr>
<td>20</td>
<td>NA</td>
<td>15,325</td>
</tr>
<tr>
<td>25</td>
<td>NA</td>
<td>24,621</td>
</tr>
<tr>
<td>30</td>
<td>NA</td>
<td>32,050(b)</td>
</tr>
</tbody>
</table>

(a) Enlisted reservists with 5 or more years of active duty are entitled to severance pay.

(b) Maximum of 1 year's basic pay.

Source: Report of the President's Commission. Table 4-8. p. 71.

The net effect of the recommendations of the Commission on military retirement is extremely difficult to assess. Without doubt, however, the total pension payout for the 20 and 25-year service career has been reduced vis a vis that of the current system.  

A sharply worded and lengthy dissenting view inserted in the record by Lt. Gen. Davis bespeaks of the Report as a proposal that "would cut military careerists' lifetime compensation in half", a view that the author holds to be gross exaggeration. The Commission Report contains copious tables and

18 The 20-year career is approximately the average career for enlisted personnel while the 25-year career is slightly greater than the average for the officer corps.
Illustrations which compare total payout for various grades and ranks for different length service careers which make Gen. Davis's charge untenable. But there is a diminishment of comparative payout for any length career less than 30 to 35 years.

Perhaps the key chart, which more than any other contained in the report would aid the reader in a comparison of total payout, is a present-value analysis which compares benefits at various years of service. In this table the reader will note that the current internal inequity borne by short service (less than 20 years) enlisted careers has been replaced by incentives to stay on until a full length career has been attained.

It was this writer's testimony at the hearings that it is rank foolishness to attempt to design a retirement plan which would be meaningful to a 18-year old enlisted person. This was done after prior witnesses had suggested that even at that age the current retirement plan constituted a powerful recruitment tool. Fortunately, the Commission accepted a similar view and the proposed plan should have little effect on recruiting or retention during the initial enlistment period.
Table 4-5

Present Value at Termination: Current System and Combined Old-Age Retirement and Deferred Compensation

<table>
<thead>
<tr>
<th>Years of Service at Termination</th>
<th>Value ($000)</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Officer</td>
</tr>
<tr>
<td></td>
<td>Enlisted</td>
</tr>
<tr>
<td>5</td>
<td>10</td>
</tr>
<tr>
<td>15</td>
<td>20</td>
</tr>
<tr>
<td>25</td>
<td>30</td>
</tr>
<tr>
<td>35</td>
<td>40</td>
</tr>
</tbody>
</table>

Assumes discount rate equals inflation rate; this is, real discount rate equals 0%

Source: Report of the President's Commission on Military Compensation. Figure 4-9, p. 82.
Overall, the pattern of force management and retention rates of the Commission proposals should follow that of the previously discussed Annuity at 55 to 62 Option as well as that of the Aspin Proposals. The distinguishing feature of the Commission plan is the extremely substantial-in-amount deferred compensation fund provided to compensate for the military "X" factor.

Cost Effect of the President's Commission Option

It is in the extremely disappointing monetary area that the Commission option might be most vulnerable, for although it purports to cut total pension payout substantially it offers little savings over the current plan until the turn of the century. The reasons are both obvious and hidden.

The Commission plan, as do all the option packages, calls for the earning of meaningful benefits during the first 20 years. This in itself is a quite consequential and substantive expense and is probably the singlemost prominent reason that monetary savings are modest and distant.\(^{19}\) However, it is entirely possible that the administration will request that the military retirement plan be put on a funded basis as are the plans of the private sector.\(^{20}\)

\(^{19}\) Data indicate that projecting costs as they are now carried, i.e., on a pay-as-you-go basis unfunded, the proposed President's Commission plan would add $60 million in cost in 1983, increasing to $700 billion extra by 1989 which is the high-water year -- then producing a net savings in 1998 of $300 million going to an annual net savings of $4.4 billion in the year 2019.

\(^{20}\) See Congressional Budget Office. Retirement Accounting Changes. op. cit. Since the first year accrual change would add $7 billion to the budget, the political feasibility of such a move is not unimportant.
Here there is a charge for retiree's annuities but in addition there is an interest bearing fund to which payments must be made annually which, on an actuarial basis of soundness, must be capable of reasonably amortizing the costs of the in-service force. At the present time this unfunded liability stands at $268 billion.

Should the nation transition to a funded plan, however, the President's Commission proposals would become more fiscally attractive, relative to the accrual amount which would have to be added under the current plan. In such circumstances the President's Commission Plan would require a contribution of approximately 28.5% of basic pay for each member of the system while the current system would require 36.7%.

The reader will note that the path leading to a revised military pension system has been long and varied. Serious efforts were begun almost seven years ago. There is, however, a direct precedent for such a time span in the legislative history of private pension reform. Efforts to effect reform among those plans were begun in 1962 with the creation of a blue ribbon commission by President Kennedy and final action was not taken until Labor Day of 1974 when Gerald Ford signed into the law the Employee Retirement Income Security Act. In the next chapter many of the factors which have contributed to the delay in military pension reform will be discussed and developed.
CHAPTER V

Military Response to Reform Proposals

The Air Force and other military services are unique callings. The demands we place on our military men and women are unlike those of any other country. Our worldwide interests and commitments place heavy burdens and responsibilities on their shoulders. They must be prepared to live anywhere, fight anywhere and maintain high morale and combat efficiency under frequently adverse and uncomfortable conditions. They are asked to undergo frequent exposure to risk, long hours, periodic relocation and family separation. They accept abridgement of freedom of speech, political and organizational activity, and control over living and working conditions. These are all part of the very personal price our military people pay.


It is doubtful that a more eloquent description of the military "X" factor has ever been delivered than the one which is reproduced above, and it is mainly this "X" factor upon which the members of our armed forces rely as the principle rationale for a continuation of the status quo in the issue of pension reform. The "X" factor, as applied to the military and as it is perceived by service personnel and members of their families, is that particular inconvenience and added degree of personal sacrifice and physical risk which is experienced and which sets them apart from the general population. It varies greatly both among the services as well as the MOS classifications among the personnel.

For the vast majority of the men and women of today's service arms this factor does not contain meaningful added physical risk or danger since
the overwhelming percentage of today's forces are non-combatant.¹ Combat-to-support ratios for the active Army stood at approximately 25% of total strength in 1971.

In 1975 the Army, in an effort to reverse this trend, reclassified manpower from support-and-headquarters to combat classification. Units from the National Guard and Reserves have been factored into the active force to where at the present time if the nation became engaged in a major conflict, 58% of its field artillery will come from these reserve components. Likewise 65% of the Army's combat engineer battalions, 52% of its infantry and armor battalions and 45% of its aviation forces as well as 65% of all Army tactical support would be from the irregular forces. It is estimated that of the 220,000 Army ground personnel now assigned to NATO and stationed in Europe, less than 64,000 are combat troops.²

These statistics are not intended to demean those men and women in our armed forces to whom patriotism has some degree of meaning. The VA hospitals and the military graves of the nation bear heartbreaking testimony to the fact that honor, duty and country does exist in the service arms. But the American military press and the servicemen's lobby groups which strive so mightily for

¹Perhaps in no other war in our history was the "X" factor among the soldier and sailor more unevenly distributed than in Vietnam. The author will never forget an attempt to console two friends, parents of a slain Navy medic in 1970. "It was so unfair," said the mother bitterly. "Our son joined the Navy. He wasn't supposed to be in danger but when he got to Vietnam, he was attached to the Marines". Of the 525,000 troops in-country at the height of the war -- less than 25,000 were in the field in a combat capacity. For the vast number of the American forces, their tour in Vietnam was less dangerous than the crossing of a busy New York City street.

the destruction of any attempt at pension reform should not be permitted to have it both ways. They may not, for example, plead the case for the continuation of a lavish pension plan on the grounds that to be in the military is to be in jeopardy of life and limb when there is ample data to show that in our wars, the one-tour citizen soldier has always borne the brunt of battle mortality. However, because the "X" factor syndrome is the rationale most ardently advanced and defended, it is necessary to thoroughly analyze and develop its composition and applicability.

The following examples should be of value to the reader. At the close of World War II and the subsequent demobilization of the armed forces of the Unites States there grew, in the context of the cold war which followed, a fear that we had dissolved at too rapid a rate our forces in being relative to those of the Soviet Union. Out of this fear there was fashioned an incredibly disciplined deterrence system -- indeed for 15 years our only credible deterrent was the Strategic Air Command. From the level of discipline and selfless dedication imposed upon and accepted by both the air crews, who suffered appalling divorce rates, and the ground crews, who displayed no less a degree of fanaticism, a fearsome "X" factor evolved and was sustained without the justification of war as a causation factor.  

Consider, on the other hand, the example of an Air Force major engaged in computer technology. Having entered the service in 1950 and serving a 25-year career during which he rose from the rank of lieutenant -- this officer served

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3In the annals of American peace time military history the dedication of the men of SAC remains unique. It was not until the December bombing of Hanoi during Linebacker II in 1972 that the matchless record of excellence was ended when several B-52 crew members declined to fly.
through two wars, Korea and Vietnam totally untouched by either. During his career he, his wife and their children tasted and participated in the cultures of two foreign host states. Never was this officer or any of his family in physical danger. Where was his "X" factor? First, his wife was never happy with or could she become reconciled to the periodic uprooting of her home and loss of friends. Her children were forced to change school frequently. She lived in a subculture totally comprised of the military. Consequently, she was never supportive of the career of her husband. Was there an "X" factor present here deserving of special pension treatment or is the situation described presently being experienced by a good part of the labor force?

Or, lastly, consider the example of four young citizen-soldier Marine officer candidates enrolled in the Basic Course at Quantico, Virginia in 1967. They had volunteered for the Marine Corps, three to fly and one to be an infantry platoon leader. For 6 months they suffered the rigorous, physical demands, social deprivations and isolation which at that time characterized the free world's most demanding combat training course. On the day before graduation one of the four went before a special board of officers and declined his commission. The other three were graduated as commissioned officers; two went on to Pensacola, Florida for flight training while the other stayed on at Quantico for advanced infantry training.

The first, who had declined his commission went to Vietnam with a rifleman's MOS. During the aftermath of Tet 1968 he was killed while leading a night patrol in Quang Nam province.

The two pilots, former college roommates, remained together flying most of a tour in 1969. One returned safely. The other, while incoming from his last mission, a medivac rescue flight, was shot down in flames and killed as he neared DaNang.

The fourth was attached to the 3rd Marine Division on the DMZ. In 1971 he suffered a severe head wound in hand-to-hand combat with North Vietnamese regulars and was returned home.4

4 These young men were once dear to the author and his wife, who was the mother of one and the "foster mother" for a year of the other three. Their loss is but one example among countless others of the senseless waste of war and the culpability of old men who throughout history have sent young men to die in them. Suffice to say, the First and Second Indochina wars, at a cost of 3 million human beings and more than $1 trillion in treasure, decided nothing. The decolonization of Indochina was merely delayed for a few seconds of history.
Thus, for two of the four the "X" factor was of the highest magnitude and for the other two it was total. What is suggested here is simply that within the rank and file of the military there is a great dissimilarity of burden and risk. The reader must confront the question for himself for it is only within the principle of excessive risk and deprivation that a case can be made for the justification of surplus benefits in the military retirement system. Congressman Les Aspin covers this critical issue more succiently:

It is popular to attribute the level of military pension to the "X" factor, otherwise described as the rigors of military life such as long hours, risk of life and limb, assignments away from one's family. Military life is certainly not the same as civilian life. Therefore, there is no reason why military pay, pensions and perquisites should be identical with the civilian world... Some argue that the extra benefit is warranted by the risk of life and limb inherent in a military career. Of course, most of the men who see combat are one-tour soldiers who never put in enough time to qualify for a military pension. As for the careerists, most Marines have certainly seen combat, but how many Navy men, apart from aviators have? Lobbing shells at Korea or Vietnam from a floating steel platform several miles offshore doesn't fall into the same category as the G-I chin deep in mud with bullets whizzing overhead.5

Aspin further notes that if the added risk is deserving of extra compensation perhaps that degree of extra risk can be identified and tied directly to extra retirement credits. The Defense Manpower Commission Plan (Table 4-1) briefly analyzed in Chapter III suggested, for example, that for pension purposes a career should be comprised of 30 points for 30 years of service and that for each year in a combat status the participant would be awarded 1.5 points. Thus, a combat soldier could be eligible for a unreduced benefit after 20 years of service. The author strongly endorses a principle of this type and will argue on its behalf in the concluding chapter.

5 Aspin, Guns or Pension. op. cit., p. 11.
Other elements of the military factor upon which Aspin comments are those of frequent station changes, and separation from family. As to the former, many civilian jobs require frequent transfers and, of course, many families find the opportunity to live in a variety of countries one of the attractions of the military. Unless the writer is mistaken, the verse "Join the Navy and see the World" antedates World War II.

The sacrifice of separation from family, however, is another matter and represents an area where there is relatively little comparison with private sector employment. But again Aspin states that even here, within the military itself, there is a great deal of variation.

The Air Force reports that it has 22,000 plus assignments scattered about the world that are labeled unaccompanied. This means that about 3.5% of the men and women in the Air Force are in assignments away from their families. The Navy is different -- any shipboard assignment involves family separation.

The Navy concludes that the average male enlisted man will spend 32.4 percent of his career away from his family due to sea duty... Monetary payments could be made for family separations, but with such variation it makes no sense to increase pensions for everyone because some suffer extended separations.

Aspin concludes, on balance, "the military is a community of more than 2 million persons. As in any society there are more onerous and less onerous jobs, more desirable and less desirable assignments. To consider that there is a specific "X" factor is to lump military lawyers in with a ship's boiler room men. We can no more stereotype the military than we can the population of Oregon, which is virtually the same size as our military population."^6

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^6 For an eloquent and enthusiastic advancement of these views, see rebuttal to this writer's CLU article by Col. Minter L. Wilson, Jr., representing the Retired Officers Association. CLU Journal, Bryn Mawr, Penn., January 1978, pp. 72-74.
Subsidiary Responses

Subservient to the issue of the military "X" factor are a series of subsidiary responses advanced by the military. Five will be briefly addressed and developed.

Costs as Percent of National Indices

One such issue is the allegation that the pension system is escalating in cost at a rate little or no different from that in the private sector and that its costs are projected to level off when taken as a percentage of the defense budget or the GNP. It is further suggested that the inclusion of the cost-of-living adjustment projections, which point to the half trillion dollar payout by the year 2000, that when that year has been reached the cost of all products, goods and services will have inflated in a like manner and at the same rate.

The Deferred Compensation Theory

Because of the historically low cash pay of the military, more perceived than actual except at the lowest enlisted grades, there is also firmly embedded in the military mind the notion that the retirement plan consists of a method of deferred compensation and not a pension plan per se. As deferred compensation, whatever degree of over generosity may be present is justifiable to make up for the lack of comparability in military pay to civilian pay.

This conviction is most keenly felt among retirees of the fifties to middle sixties whose pensions in spite of CPI adjustments as applied during those years are relatively small in amount. This theory was forcefully brought home to the author when an angry letter was received in response to
the CLU article mentioned previously, and written by a pilot who had served in three wars. This position is not without merit. As was stated in Chapters I and II the compensation plan of our military has been a historical disaster inasmuch as its personnel have never known what they actually earned. Their compensation package consists even at present of some thirty odd items. It has been badly communicated and explained to them and it is little wonder that surveys have reflected both confusion and low perception levels. The blame for this lack of comprehension should be laid squarely on the doorstep of the DoD force managers at all levels.

The Recomputation Grievance

A third rationale from the military has to do with recomputation which is a sensitive issue and is closely tied to the grievance discussed above. It is also identified in the loose classification of the perceived "erosion of benefits" which is now prevalent in the military philosophy. The roots of recomputation lie in the manner in which retired pay has been adjusted during the post retirement period. This grievance is held by retirees of the pre-1958 period.

Prior to 1958 the retirement benefits to military retirees were increased by a direct tie-on with the pay increases given to active duty personnel. This practice was halted in 1958. Not until 1963 was legislation passed which did permit one final recomputation and then substituted the CPI as the pension adjustment indicator for years subsequent to 1958. The perceived inequity lies in the fact that had the old system continued the pension

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7 See Exhibit I in the Appendix. (i.e. Letter of Major Jack B. Stowers.) The forcefulness of Stower's remarks leaves little doubt that he perceived his retirement plan as a contractual, albeit implied, obligation of deferred compensation, the manipulation of which would constitute a breach of faith.

8 See Cooper. op. cit., p. 366.
would be substantially higher than in the case under the new system because since 1958 retired pay has grown by 230% whereas active duty pay has grown by 430%.  

Erosion of Benefits

An important but surely unjustified military response is that of an "erosion of benefits". This is a general and vague allegation. It consists of the erroneous view that there is currently in being an ongoing erosion of military benefits and that present attempts to modify the retirement system are simply a continuation of that process.

The origin of this total misconception is both insidious and mysterious. It may have arisen as a deliberate propaganda campaign by the organized military lobby groups to mitigate certain pension reform. There are some 22 different military lobby groups, associations, committees, print organs, etc. who actively strive to maintain the status quo. They are powerful and vocal. The role of the three service newspapers, is instructive. Congressman Aspin assigns a high level of effectiveness to them, saying:

The Navy, and Army, and Air Force Times, are private publications which have won a large readership precisely because they look after the interests of servicemen and defend every financial redoubt. The principal officers of the various organizations are elected and must respond to the main demands of their activists, which is the preservation and enhancement of benefits.  

Professor John B. Keeley, former career Army officer, West Point educator, and now professor at the Miller Center of Public Affairs at the

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9 See Exhibit II in the Appendix in which a retired major expresses the grievance of recomputation.

10 *Guns or Pension*, op. cit., p. 18.
University of Virginia adds, "the nation's soldiers are angry and defensive over attempts to reduce benefits and increase efficiency. Military employees are retirees are organizing because their traditional defenders appear to have deserted them." Professor Keeley noted that when medical benefits for retirees were curtailed at Fort Lee near Petersburg, Virginia in March 1977, "Army retirees organized a political campaign that took them all the way to Washington to protest the cuts. They organized and they won." Keeley later testified before the President's Commission. Included in his testimony was a reference to the Association of Air Force Sergeants, an organization which when founded in 1970 contained 7,000 members. The Association now has 100,000 members and has its own full-time lobbyist and offices in Washington. Keeley asserted that the military today has a siege mentality:

The trauma of withdrawal from the eventual fall of Vietnam, coupled with the pardon of draft evaders, the upgrading of undesirable discharges and the vocal and strident attacks on military pay and benefits have left a bitterness that is deeper and more serious than is generally appreciated. We need reform, but we also need flexibility. We can't lose sight of what the military is for.


12Ibid. It should not be surprising to the reader to learn that the miscalculation of Vietnam occupies such a position of prominence as a principal cause of the deterioration of the Army. It is entirely possible that our Army, as these words are written, has so declined in quality as a fighting force that it can no longer be counted upon to help implement the foreign policy of the chief executive.

It is the author's conviction, based upon the study of voluminous written material, discourses with combat returnees, and with two of the principal civilian policymakers of our nation during the era, that for a period of time spanning the entire war including events leading to the fall of Saigon itself, the high military consistently and consciously misled three successive heads of government as to both the nature of the war and the capabilities of the enemy. These men now occupy the highest positions in the three services. Throughout the entire war only three highly placed men, two military and one civilian, placed their personal honor and their country over their professional careers to the extent that they resigned and attempted to effect a withdrawal from a hopeless cause. In 1968 Lt. Col. William Corson, Marine combat soldier-scholar, resigned from the Corps to write the first great book of the war, The Betrayal. In 1973 the Army's most highly decorated combat soldier, Col. David Hackworth, resigned brokenhearted over the fruitless loss of young American citizen soldiers he had led. Daniel Ellsberg, who saw much combat as an advisor in the pacification program during the formative years of the war, is the third.
Retirement Costs Stable as Percent of Budget

It is especially distasteful to see the repeated use of irrelevant and false data and legerdemain by military spokesmen in their efforts to defend present pension costs and project military costs in general. A favorite device is the comparison of the subject item, as a percentage of one of the several natural indices, with the use of constant dollars tied to a year far in the past. The exchange mentioned earlier in Chapter II between Senator Harry Byrd, Jr. and the then Secretary of Defense James Schlesinger is, again, highly illustrative. In contrasting in constant collars the cost of his military budget to a ten-year prior current dollar cost, Schlesinger was guilty at the very least of a breach of professional honesty. We must learn to insist that the politician include the monetary effects of inflation upon the cost of his project when he comes to the market place for money. In the Byrd-Schlesinger exchange it was utterly irrelevant that the 1975 DoD budget was relatively low in constant dollars. What was relevant was the fact that his source of funds was and still is the federal income tax which is itself computed on the current income of 80,000,000 odd taxpayers -- and in which inflation itself pushes the taxpayer into an ever increasing tax rate.

Similarly the military and almost invariably the DoD analyst, in attempting to mask the runaway cost of the military retirement system, often alleges that "in constant dollars the system will not increase as a percent of the budget to fiscal year 2000," or whatever. Factually, nothing is further from the truth. The future costs of the United States military retirement system, if nothing is done, will escalate over the foreseeable future as will manpower costs itself. Total manpower costs of DoD, including inflation and increased retirement costs are projected to sharply increase.
Table 5-1  
Defense Manpower Costs

<table>
<thead>
<tr>
<th>Fiscal Year</th>
<th>Billions</th>
</tr>
</thead>
<tbody>
<tr>
<td>1977</td>
<td>55.8</td>
</tr>
<tr>
<td>1978</td>
<td>60.9</td>
</tr>
<tr>
<td>1979</td>
<td>66.0</td>
</tr>
<tr>
<td>1980</td>
<td>70.9</td>
</tr>
<tr>
<td>1981</td>
<td>75.9</td>
</tr>
</tbody>
</table>


Thus it may be seen that without the projected addition of the accrual fund itself which adds $7 billion to the 1979 defense budget, there will potentially be a 36% increase in defense manpower costs over the next four years.

Within the line and staff items which comprise manpower costs, the retirement plan costs will worsen both in terms of constant and current dollar projections. Cooper indicates that the source of the past 20-year increase, 1956-1977, of $477 million to more than $8 billion, is twofold. First, the number of retirees has grown by more than 500% during these 20 years, while the average cost per retiree has almost doubled; and secondly, the cost of military retirement has increased from about 1% of the DoD budget to about 7% and from approximately 4% of manpower costs to 17%. Moreover, Cooper adds, the problem will worsen. Assuming that the defense budget remains level in 1978 dollars, retirement costs are projected under current policy to grow to more than 12% of the DoD budget by the mid 1990's.

12 Cooper, op. cit., p. 372.
Table 5-2

Military Retirement Costs

<table>
<thead>
<tr>
<th>Fiscal Year</th>
<th>Retirees (000s)</th>
<th>Cost ($ billion)</th>
<th>Percent of DoD Budget</th>
</tr>
</thead>
<tbody>
<tr>
<td>Actual:</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Current dollars</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>1956</td>
<td>183</td>
<td>$ 0.48</td>
<td>1.3</td>
</tr>
<tr>
<td>1960</td>
<td>243</td>
<td>0.69</td>
<td>1.7</td>
</tr>
<tr>
<td>1964</td>
<td>411</td>
<td>1.21</td>
<td>2.4</td>
</tr>
<tr>
<td>1968</td>
<td>624</td>
<td>2.10</td>
<td>2.7</td>
</tr>
<tr>
<td>1972</td>
<td>867</td>
<td>3.39</td>
<td>5.2</td>
</tr>
<tr>
<td>1976</td>
<td>1,108</td>
<td>7.30</td>
<td>8.3</td>
</tr>
<tr>
<td>1978</td>
<td>1,180</td>
<td>9.04</td>
<td>8.3</td>
</tr>
<tr>
<td>Projections:</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>1978 constant dollars</td>
<td>1,196</td>
<td>9.83</td>
<td>9.0</td>
</tr>
<tr>
<td>1980</td>
<td>1,196</td>
<td>9.83</td>
<td>9.0</td>
</tr>
<tr>
<td>1985</td>
<td>1,256</td>
<td>11.21</td>
<td>10.2</td>
</tr>
<tr>
<td>1990</td>
<td>1,280</td>
<td>12.71</td>
<td>11.6</td>
</tr>
<tr>
<td>1995</td>
<td>1,250</td>
<td>13.58</td>
<td>12.4</td>
</tr>
</tbody>
</table>

Source: Richard V. L. Cooper, op. cit. Table 15-4, p. 375.

Thus, the reader may clearly see that the allegation by the military of a "leveling-off" in the cost of retirement is without foundation. This is in spite of the fact that as the year 2000 approaches, the abnormally large number of retirees from World War II and Korea will leave the rolls. Military retirement is inordinately expensive -- not because its costs are high per se, but because its benefits are excessive and both out of line with those of the private sector as well with long adhered to principles of sound employee benefit planning.\footnote{The author is in basic agreement with Professor William King's argument in \textit{Achieving America's Goals: National Service or the All-Volunteer Armed Force}. Dr. King is pessimistic over the chances for the survival of the AVF itself. King believes that all estimates of increased manpower costs are low and that only through significantly higher costs will the AVF be sustained into the 1980's.}

We owe the military an adequate and reasonable level of retirement and, as the reader will note in the concluding chapter, a better-than-average plan for certain segments of the military. But we do not owe all members of
our military establishment of 2 million persons, 85% non-combatant, a lavish plan with costs as a percent of pay more than 7 times that of the private sector. It is in this spirit and context that the subject matter for the concluding chapter will be approached; namely, how should a just and equitable retirement for the American military be structured?
CHAPTER VI

Toward Rational Pension Reform

Now I would like to consider that most important aspect of the AVF, its effectiveness. Although I have made no attempt at assessing the military effectiveness of the Armed Forces in either an absolute or relative sense, I do consider a number of aspects of the current All-Volunteer Force to be indicative of potential effectiveness deficiencies.

Among these are: the high adverse attrition rates, which cannot but negatively affect morale, and hence effectiveness; high rates for nonjudicial punishments, which have increased 35 percent since Vietnam era levels; survey results show that 25 to 30 percent of active enlisted personnel would try to avoid or probably refuse to serve in combat situations, depending on the nature of the emergency; the decreased quantity and quality of the reserves, which serve to amplify the peace time only view of our military forces.

Statement of Professor William King before Senate Subcommittee on Manpower and Personnel, Hearings on the All-Volunteer Armed Force, March 2, 1977.

In general, it is of great value for the pension planner to know what is the norm and what is the exception with regard to plan design. This does not lead to mediocre or sterile plan design, but does offer to the draftsman the suggestion that to part from the proven way is to tread carefully.

Further, from experience one may know that once a serious design defect is in operation in a plan, it is a delicate and frequently difficult task to rid the plan of that defect. This is true because the plan participants tend to look with suspicion upon any amendment that is drafted which will affect them as
plan participants and beneficiaries. It is largely for these reasons that "grandfather" or transition provisions almost always accompany a plan modification. In Table 4-2 it may be seen, for example, that the "phase-in" period ranges from four years for the President's Commission to twenty years for the RMA proposals.

In pension planning it is generally known that the richness level of the benefit formula should provide, at the conclusion of a realistic career of employment, a retirement benefit which when added to the applicable Social Security old age pension, is around 40 - 60% of pay as it stood just prior to retirement, or upon some averaged period of the highest income years. In the private sector there is a duality of obligation, delicately balanced. First, an equitable benefit should be paid to the long service, faithful and loyal employee. Second; there is an obligation to the stockholders who have contributed the capital for the formation of the company - employer that the contribution (cost) level required to keep the plan actuarially sound should be reasonable and in line with comparable levels of pension costs existing elsewhere. This level in the private sector would comprise as a percentage of covered payroll something in the range of 8% to 15%.

Just as we have been concerned throughout this paper with the effect of a retirement plan on force profile and force management -- terms used by DoD force planners -- in the private sector there is equal concern over the effect the plan will have upon the reduction of costly turnover. Most of the time in the private sector the employer desires his plan to assist him in the stabilization of the employment pattern.¹ In Japan, turnover of employment is practically

¹This is the objective in the majority of private plans. However, the author is presently designing a profit sharing plan for a large beverage distributorship with provisions and benefits which will result hopefully in large voluntary severances of employment at around age 50. Past that point the physical demands upon the route salesman tend to be excessive.
unknown among employees in the industrial corporations, contributing to both a very low per unit cost of production and a powerful competitive position in the international marketplace.

In private sector planning, two basic principles are well-known and adhered to. First, it is known that if the benefit formula provides benefits which are high enough to support the participant at ages prior to age 65, there will be pressure to retire early. Secondly, if the vesting schedule contains an immediate distribution provision when the vested percentage reaches 100% there will be an exodus from employment at that point with little regard to age. The pension planner should, therefore, tread his way carefully through the maze of desired benefits balanced against the limits of the budgeted cost.

The reformation of the United States military pension system would be child's play to any experienced pension technician if the political factor were removed. The simple adherence to the several basic principles enunciated above would lead to a reasonable and rational plan providing equitable benefits. Since, however, politics is in the last analysis the art of the possible, military pension reform will not be rational but will consist of what is left after an irrational period of infighting has elapsed between the executive branch, the legislative branch and the military special interest groups. To

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2 The New York City municipal plan is a recent case in point. Due to the lavish benefit formula under which the total pension is close to 90% of current pay at age 60, the plan is now facing a high actuarial deficit from a rash of early retirements and outmoded assumptions. Many municipal plans throughout the nation have benefit formula richness levels in excess of the probable ability of the taxpayers to fund them. Many if not most of them are either unfunded or severely underfunded.
paraphrase Congressman Aspin, "the growers of rutabagas will fight much harder to preserve their subsidy than the 99.9% of the American people who do not grow rutabagas will fight to abolish the subsidy." In spite of the near certainty that what might ultimately evolve in 1979 as the amended military pension system will bear little resemblance to this author's recommendations, what follows is a sincere attempt to put order into a disordered program of retirement income while at the same time attempting to solve a larger problem of which the retirement plan is but a small part.

The Benefit Formula

The President's Commission on Military Compensation chose the benefit formula of the federal civil service, as did Congressman Aspin in April of 1977, to provide the retirement annuities to the military. Under this formula pension credits are awarded as a percentage of pay times years of service which increases from 2% to 2.75% as years of service increase from 1 to 35. Application of this formula to a realistic career will result in a benefit level very much better than the norm that exists in the plans of private enterprise. Moreover, there is logic in a merger of this type. First, the vast majority of all government employees would be under the same basic benefit formula, a step toward uniformity. Second, such a merger might preempt any opportunity for the lobby groups to allege the charge of inadequate benefits. Third, there probably

3 Supra, Chapter III.

4 Supra, Chapter I. Table 1-2.

5 Members of Congress, federal judges, the chief executive, and certain other small groups have various other basic plans. Sid Taylor of the National Taxpayers Union estimates the total number to be 62.
is an "X" factor in all types of military employment, especially among those who are married, which is deserving of some degree of special recognition.

Under this ideal plan, however, certain segments of the uniformed forces would be entitled to extra pension credits. These segments would consist of the holders of the combat MOS classifications and would number 10% to 15% of the total force of 2.1 million. The categories would include those of infantry, armor and amphibious duties; artillery, gunnery, rocket and missile areas; combat engineering, combat air crews, and certain seamanship specialties. The exact method in which this extra allocation should be factored into the benefit formula is unimportant. There are an infinite number of ways this could be done. The simplest would be an addition to the formula in which it would be stated that for each year of qualified combat MOS service, the percentage of pay multiplier would be increased by 50% or some such percentage which would be acceptable and just. It should be remembered that the Defense Manpower Commission package recommended a bonus allocation for combat service but based on a point system. Either method is perfectly acceptable.

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6 Preliminary results of a GAO study not yet published and supplied to CBO show that only 8% of the career of the average enlisted retiree was spent in the most physically demanding jobs. Of all enlisted retirees, 80% spent no time at all in these jobs. For officers, the survey showed the average retiree spent 34% of his career in a job directly involving tactical operations while 30% of all officer retirees spent no time at all in such jobs. See CBO, The Military Retirement System: Options for Change, op. cit., pp. 11-12.

7 It has been suggested that such an idea would be difficult to implement because of the difficulty in the identification of the combat MOS -- an idea which the author rejects as nonsense. In fiscal year 1976, for example, some $60 million was paid to more than 25,000 enlistees as combat bonus. Presumably some criteria were used to identify them.

8 Supra, Chapter IV. Table 4-1.
There are practical and compelling reasons for the adoption of such a weighting mechanism. First, there is grave deficiency of men in the combat arms, a deficiency projected to worsen both in numbers and in quality. Whereas, the cost of recruiting the least hardest to get volunteer to the average is approximately $1,250 for DoD as a whole, the incremental cost of the most difficult-to-get recruit in the Army can go to $12,000. Also the high bonus costs which have proven to be necessary to attract recruits into the combat areas -- more than $60 million was paid to 25,000 recruits in fiscal year 1976, is a further indication that even current high rates of military pay are inadequate to attract recruits into combat MOS classifications. It is highly probable that there is now a critical deficiency in the qualitative makeup of the AVF which is submerged beneath the same can-do mentality that was expressed by the high ranking military during Vietnam, in the form of misleading and false declarations of "light at the end of the tunnel." We must be prepared to expect little in time of national crisis or danger from the thousands of present day combat personnel who joined the force for a monetary night's lodging. The disbursement of a combat bonus does not beget the quality of patriotism.

This writer believes, as does a growing body of critics, that the All-Volunteer Army is essentially a peace time force which would be of little value should it be called upon to project the foreign policy of the nation by force of arms. The military retirement plan, no matter how it is designed or what it provides, will not remake the armed services -- only a fool would

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9 Senate Subcommittee on Manpower and Personnel of the Committee on Armed Services, The All-Volunteer Armed Force, op. cit., p. 8.

10 See the recent 377 page study by Rep. Robin Beard, R-Tenn, on the lack of combat readiness of the AVF. See especially Senate Subcommittee on Manpower and Personnel, The All-Volunteer Armed Force, op. cit., pp. 1-55.
think as much, although many of the highest military have indicated that substantive modification would destroy it. But perhaps the combat weighting device would encourage substantial numbers of careerists to volunteer for high risk service. This latter idea is not new among other modern day armed forces. The French for instance, weight their plan for campaigns. It is in the armed forces of the Soviet Union, however, that maximum use of the retirement plan is made for hazardous duty credit. The Soviet military has a retirement system which has strong overtones of the Defense Manpower Commission package in the manner in which combat service is fed into the benefit formula.\(^{11}\) There the plan is designed to exert a maximum influence where, in the Russian mind apparently, it is most needed and deserved -- namely the special risk categories. In the best tradition of sound pension design, its provisions are simple and direct:

Officer Kotov served from September 1936 to October 1938 and from June 1941 through August 1971. From July 1942 to April 1958 he was on flying status, including the period May 1943 to February 1945 at the front, and from June 1945 to December 1952 on isolated Kanchatka Peninsula. Thus, he actually served for thirty two years and three months.

His one year and nine months at the front counts triple. His time on Kanchatka counts double, but only after September 1945. His flying time counts time and a half. Adding it all up he has forty-six earned years for his pension. He will get fifty percent of his last pay for serving twenty-five years, plus three percent for each extra year up to seventy-five percent of his last pay.\(^{12}\)

Sad to say, the President's Commission did not see fit to include in its recommendations this badly needed device. Overall, there is no contradiction in the awarding of dissimilar credits to different groups within the

\(^{11}\)Op. cit., DMC Study, Table 4-1.

military -- and the integrated, excess type plans of private industry. There, one level of pension credit is given on compensation not exceeding the Social Security wage base; and another, higher level is given on compensation above the wage base. The granting of extra credits to combat personnel reflects a somewhat similar philosophy.

**Secondary Plan Provisions**

In pension design, once the benefit formula and eligibility provisions have been defined and tested, and after computerized projections have yielded the necessary cost projections, the secondary provisions can be added. Here, the ideal military plan could contain the provisions of several of the reform packages enunciated in Chapter IV and summarized in Tables 4-1 and 4-2. Most would agree that the ideal plan should be integrated with Social Security, indeed it is wasteful and inequitable if it should not. Most would agree that short service personnel should have access to benefits at service separation -- perhaps along the lines suggested by the Commission and described in Table 4-4. To fail to do so would result in an inequity. A more difficult question is that of whether the new plan should be contributory. That since the benefit formula is similar to that of the civil service plan and since the civilian federal employee contributes 7% of his pay towards his cost, why should not his military counterpart? There are at least three reasons why he should not: first, to suggest a contribution would raise the spectre of a further erosion of benefits; second, the military constituency would request and secure a pay increase equal to the contribution; and third, on an actuarial basis the 7% contribution is quantitatively meaningless.
As to the commencement date of the annuity, the recommendations of
the Carter Commission are superb. As quoted in the epigraph of Chapter IV,
by delaying the commencement of old age annuities until age 55 at the earliest,
the quick "20 and out" pension has been effectively eliminated. This leaves
for consideration the two most difficult questions:

1. What is the obligation of the nation to the military retiree
   for the period between his actual retirement and the commencement of his annuity?

2. Can the nation, in the new climate of 5% - 9% inflation, continue
to protect the military retiree from the declining purchasing power of the
dollar?

The Deferred Compensation Trust Fund

The President's Commission introduced a new and very expensive trust
fund to be created for two purposes. First, it is intended to assist separated
personnel in their transition to civilian employment, and second to furnish a
source of income during the "blackout period" from date of separation to the
commencement of the old age military annuity beginning at the earliest at 55.13
While this feature is new, there has always been in effect a severance pay
for involuntarily separated officers which has provided substantial sums.14 The
Commission plan would extend this benefit to enlisted men.

A search of the available data bearing upon transitory benefits such
as the deferred compensation fund in the military plans of other states reveals
nothing of comparable scope or magnitude.15 Nor did the Commission in its full

13 Supra, Chapter 4. Table 4-3.

14 Supra, Chapter 4. Table 4-4.

report see fit to offer a citation to any precedent. The citizenry is thus left, should the Carter Commission recommendations be implemented, of providing benefits reaching higher than $150,000 for a departing officer in addition to a severance pay allowance of possibly more than $32,000. The Federal Republic of Germany, whose military retirement plan contains a maximum pension as a percentage of pay of 75%, has a separation allowance based on years of service times 3/4 pay.\textsuperscript{16}

<table>
<thead>
<tr>
<th>Years of Service</th>
<th>Allowance Times 3/4 Pay</th>
</tr>
</thead>
<tbody>
<tr>
<td>4 - 6</td>
<td>6 months</td>
</tr>
<tr>
<td>6 - 8</td>
<td>1 year</td>
</tr>
<tr>
<td>8 - 12</td>
<td>1 1/2 years</td>
</tr>
<tr>
<td>Over 12</td>
<td>3 years</td>
</tr>
</tbody>
</table>

Thus, our chief NATO ally pays at a maximum the sum equal to three times 3/4 annual pay as a transition benefit.\textsuperscript{17}

Canada pays a sum much lower. The Canadian model is a gratuity for under 10 years of service equal to 1/2 weekly salary times years of service. For service of 10 - 20 years, the gratuity consists of weekly salary times years of service.\textsuperscript{18} Of the eight states analyzed, six have some kind of transition allowance while the practice of Sweden is unknown. Again, the ideal plan would contain an equitable but not excessive allowance. Commission data reveal that some 85% of American military retirees require no more than 12 months to

\textsuperscript{16} Ibid.

\textsuperscript{17} Ibid.

\textsuperscript{18} Ibid. The Third Quadrennial Review contains voluminous but incomplete data for the military forces of U. S., U. K., Canada, Federal Republic of Germany, Sweden, Japan, France and Australia.
locate new work. If this is true the allowance of up to $182,000 for a transition of such short duration is excessive. Private industry gives to involuntarily separated wage earners perhaps two weeks' pay and executives no more than six months' salary. Clearly then the recommendations of the Carter Commission are excessive in this area. Such a fund was never postulated in any previous major reform package. The magnitude of the recommendations have no basis in either logic or equity.

Cost-of-Living Adjustments

The reader has been treated by now to an unambiguous position, a firmly taken stand on the question of the continuation of the CPI indexed cost-of-living adjustments for the American military. The Carter Commission, in recommending the continuation of this protection, did so briefly and succinctly with a very incomplete rationale. In a 205-page report, it devoted but 14 lines to the most expensive single component of the American military retirement plan; for even under the very modest inflation projection of 5%, some $292 billion will be paid out between 1975 and 2000 due to the CPI index tie-on to the military retirees alone.

The question is, what is the identity of the rationale, the moral or logical justification for the luxury of such a device for four million federal employees, divided approximately between the military and civilian civil service? There can be no question of the inequity for the one half of the American labor force who pays 98% of the military pension costs and who are themselves without private pension coverage of any description.


20 Ibid., p. 66.
Largely because of the generous inflationary adjustments to current wages and salaries of the federal establishment plus the automatic adjustments to both the military and civilian retirement community in the area, Washington has become the highest per capita income city in the nation. It has a household income of $28,000 per year. One fourth of the total work force of the area is federally employed with an average income of $20,000. It has been estimated that due to the complex manner in which federal pay has been based on the idea of "comparability", there is now a federal wage advantage of as much as 20%.

If there are to be savings from the ultimate modification of the military retirement there must be a reduction or curtailment of benefits. Most of the alternates illustrated in Tables 4-1 and 4-2 project savings only far into the future and relatively small sums until the turn of the century. It is difficult and perhaps even inequitable to cut or curtail benefits for those personnel who presently are in the force or on the retired rolls. While this is true of most of the types of benefits present in a retirement plan it should not be germane to the decoupling of the CPI index from the pensions of either military or civilian civil service retirees. What was merely unwise in the era of 3% annual inflation is highly dangerous in times of 9% inflation. It is the magnitude and manner of this type of inflation protection that is unique.

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21 There is evidence of public resentment directed at both the opulence and power of the federal bureaucracy and ostentatiousness of Washington. For example, Harpers magazine recently devoted its cover story to the wealth of the capital city. (Tom Bethell, "The Wealth of Washington," Harpers, June 1978, p. 48) See especially a superb discussion of the inequity of the percentage principle in inflationary wage increases for the federal civil servant in Newsweek, "Our Unfair Pay Raises," March 13, 1978, p. 19. There, author Paul E. Mullinax argues for a flat amount principle as did military retiree Everett H. Clark in Exhibit III of the Appendix, as a more equitable and economical manner to compensate for inflation.
In the last analysis, however, no one should without qualification predict the future course of a sensitive political issue such as military pension reform. It was thought, for example, that Congress would address the issue during the second session of 1977. However, the Congress had been flooded with legislation introduced by an over zealous executive branch. As mentioned earlier, it was in April of 1977 that Congressman Les Aspin introduced his "trial balloon" in a floor motion and it was noted at that time that the Joint Chiefs of Staff had privately urged the subcommittee members to delay pension reform for another year because of critical morale problems and the threat of military unionization. It is now possible, however, that more serious events have overtaken pension reform, namely the state of the All-Volunteer Army itself. The reader has noticed the secondary theme, implicitly and explicitly expressed throughout this thesis, that the future of the AVF is clouded and that its days are numbered. There is a distinct possibility that the Joint Chiefs have understated the deterioration of the service arms and that the armed forces cannot in the immediate future survive simultaneously a radical reorganization accompanied by a complete or partial return to the draft -- and a revision of the military pension system.22 It is not a pleasant thought.

22On June 25, Senator Harry Byrd, ranking member of the Senate Armed Services Committee, released a statement to the principal newspapers of Virginia. This news release coincided with completion of the last half of the final chapter of the author's thesis. Senator Byrd stated that he is now experiencing grave doubts as to the viability of the AVF -- citing rising manpower costs, high cost of recruitment, excessive attrition, etc. The sense of his article was to the effect that alternatives to the AVF were being investigated and that the possibility exists that a return to the draft or some form of national services would be necessitated. (Senator Harry F. Byrd, Jr., "Volunteerism Isn't Working," Richmond Times Dispatch, June 25, 1978, Sec. G, p. 7.)
APPENDIX
EXHIBIT I

1570 love Point Dr.
Salt Lake City, Utah 84117

Clarke-
Read your article in CIV Journal
1st Act 77.
Retired USAF Major (23 years Active
Duty - No National Guard Time), C.C.C., Self-
Employed, etc.

If you approach the "Military Pension
System" as the Defined Compensation
System it is, it fully taxable, your Article
becomes sick.

We have earned & flew for lower
Rate of Pay, Hoping to hire (I had 3 wars)
& draw the Defined Compensation Allowed!
So, I take issue with your Article,
cause if The Vocation of Test Flying, etc. was
desirable, non Civilians could volunteer.

Sincerely

[Signature]

Maj. Jack B. Stowers
1590 Lone Peak Drive
Salt Lake City, Utah 84117
Mr. Shelton Clarke, Jr.  
The Home Life Insurance Company  
253 Broadway  
New York, New York 10007  

12 October 1977  

Dear Mr. Clarke:

Your excellent article entitled, "The United States Military Pension System - To Halt A Runaway," appearing in the October 1977 issue of C.L.U., was most interesting to me for two reasons: (1) I am a Military Retiree and (2) I am a Professional Life Underwriter.

In June 1963, I retired from USAF with twenty-seven years service with the rank of Major. Sixty days prior to my retirement the Congress made a major change in the Military Retirement Law. That drastic change as of now reduces by $4,800.00 my annual annuity. That drastic reduction of benefits occurred at the end of a long career during a period when the WWII personnel hump was retiring. To place that drastic reduction of benefits in sharp focus, a Chief Master Sergeant with the same length of service retiring today receives benefits equal to mine. If the Cost of Living Index had not been included in the Act of 1963, my annuity would be about equal to a Buck Sergeant retiring today.

Will the Pension Reform Act of 1974 permit a Pension Plan which has been effect for twenty-seven years to make drastic reductions in benefits the year a large number of covered personnel are scheduled to retire? Would the Congress even consider drastic reductions in Social Security Benefits the year an extremely large number of citizens retire? I do not think so. Should the people of the United States be less fair with their Military Personnel who have Borne the Battle?

You are aware of the fact that for the past several years the Military Retiree has lost significant benefits.

It seems to me that Retired Military Personnel deserve to be able to plan with confidence for their golden years without having to worry about more benefits being taken from them on a month to month basis.
Mr. Shelton Clarke, Jr. - continued -

Would you please take the time to explain to me how you propose to deal with the problem of the Pre 1964 Military Retiree? I will be most grateful for your thoughts on that problem.

Sincerely,

Robert L. Dunn

P.S. If a Military Retiree pays more in Federal Income taxes than he receives in a Military Annuity, is he really costing his fellow citizens anything? It would be interesting to know the total amount of Federal and State Income Taxes paid by all Military Retirees. If you deducted that amount from the total cost of the program, wouldn't you really have the true cost of the Military Retirement Program?

CF:
C.L.U. Journal
Letters to the Editor

Cost-of-Living Raises: Windfall or Pittance

To the Editor:

As a citizen I am disturbed by the spread of the cost-of-living adjustment (COLA) into labor unions and now into the salaries of judges, top officials of the executive branch and probably Congressmen.

Although benefiting from it myself as a military retiree, I have become convinced that it is essentially a giveaway program which dispenses too much to those who don't need it and not enough to those who do.

The application of percentage increases in the Consumer Price Index (C.P.I.) across Federal pay scales, high and low, is an undeserved and excessive windfall for the above-average and an unfair pittance at the lower end.

A 5 percent increase in the C.P.I. would raise a Congressional salary by $186 a month, enough to pay for all groceries and basic needs, not just the inflationary extra, but would give the $150 Social Security beneficiary only $7.50, not even enough for one filling of the gas tank of his jalopy, if he owns one.

The fact is that the C.P.I. has a reverse relationship to salary level, and the tragedy is that when each is expressed in percentage it is easy to slide into the assumption that the more pay you get and spend, the more compensation you need to stay caught up.

This is nonsense! Who says the affluent need it?

What needs to be said, and loudly, is that any cost-of-living adjustment should be a flat rate across the board because the low end needs it and the high end can well afford to have it that way.

The present discriminating and unbalanced adjustments are highly inflationary in themselves. Labor Bureau statistics quoted by The Times last July gave COLA figures veering from 22 cents an hour to $1.05; that's from $8.80 to $42 a week of forty hours, a ridiculous indication of the kind of economic football the device has become.

In my own case, I have been glad to get these raises. But enough is enough, and I don't believe the generals really need their giant increases while the sergeants have to scramble for post-retirement jobs or go on relief.

At a guess, a flat increase of about $20 a month would be ample for everybody to cover their actual needs after a 5 percent C.P.I. rise. Anything above that is just money thrown out to people who don't need it.

Everett H. Clark

Tunkhannock, Pa., Sept. 12, 1976
SELECT BIBLIOGRAPHY

The following bibliography is select in the sense that it lists those sources that contributed measurably to the foregoing narrative. With one exception, these primary sources were written within the last two years. The cited works are not large numerically. However, the books, reports, papers and studies which comprise them were carefully chosen. As of the time when it became necessary to "close down" the research for this theses it was felt that the most authoritative collection of source material had been assembled. That time came in April 1978 when the Report of the President's Commission on Military Compensation was released.

Contrary to the normal procedure, this brief section is listed in the order of direct, meaningful and inspirational utility to the author.


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BIOGRAPHY

L. Shelton Clarke, Jr. was born at Petersburg, Virginia on July 25, 1922. He attended Hampden Sydney College from 1940-1942 and the University of Virginia from 1945 to 1947. He received his J.D. degree from the University of Richmond Law School in 1950. He has been engaged in employee benefit and insurance planning since that date. He is a member of the Virginia Bar. He practiced law from 1969 to 1971. He is an instructor in the Advanced Pension Planning Course of the Graduate School of Financial Sciences of the American College of Chartered Life Underwriters. He testified before the Retirement Incomes Subcommittee of the Committee on Aging in the U.S. Senate in 1965 and before the President's Commission on Military Compensation in 1977.

Mr. Clarke is a veteran of World War II. He flew a tour of duty over Germany during the air offensive of 1944-45 as a B-17 crew member. During the Korean War he was a heavy weapons platoon leader in the Virginia Infantry National Guard. He is a graduate of the Fort Benning Infantry School.