



Congressional Budget Office

July 1, 2015

Analysis of Approaches to Reduce Federal Spending on Military Compensation

Western Economic Association, 90th Annual Conference

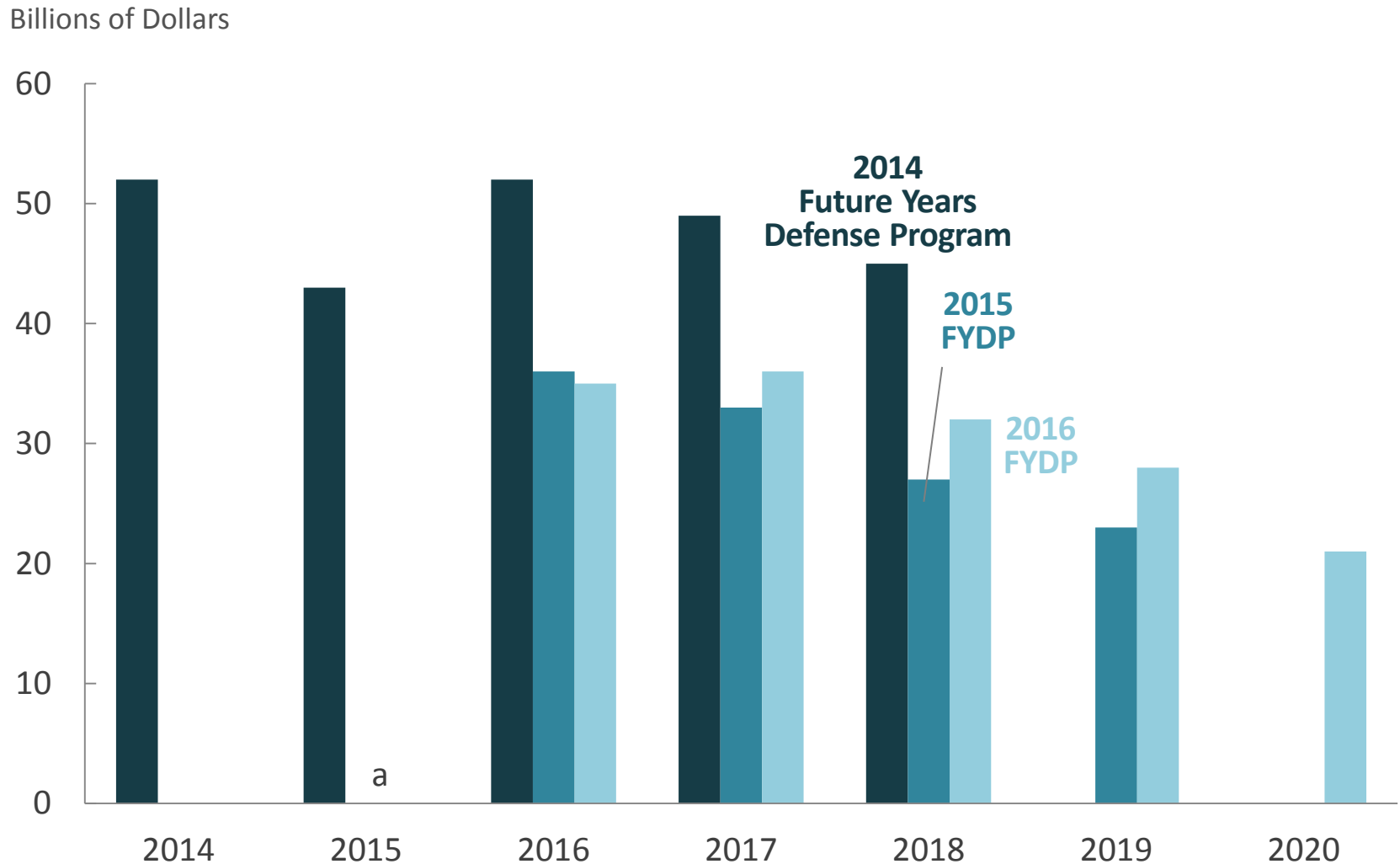
Carla Tighe Murray, Ph.D.

Senior Analyst, National Security Division

This presentation provides information published in *Cost Estimate for S. 1376, National Defense Authorization Act for Fiscal Year 2016* (June 2015), www.cbo.gov/publication/50266; *Long-Term Implications of the 2015 Future Years Defense Program* (November 2014), www.cbo.gov/publication/49483; *Growth in DoD's Budget from 2000 to 2014* (November 2014), www.cbo.gov/publication/49764; *Options for Reducing the Deficit: 2015 to 2024* (November 2014), www.cbo.gov/budget-options/2014; and *Costs of Military Pay and Benefits in the Defense Budget* (November 2012), www.cbo.gov/publication/43574.

Most years, the Department of Defense (DoD) has projected that the costs of its plans would exceed funding caps for discretionary funding set in the Budget Control Act of 2011.

Amounts by Which DoD's Projections of Costs Exceeded the Caps

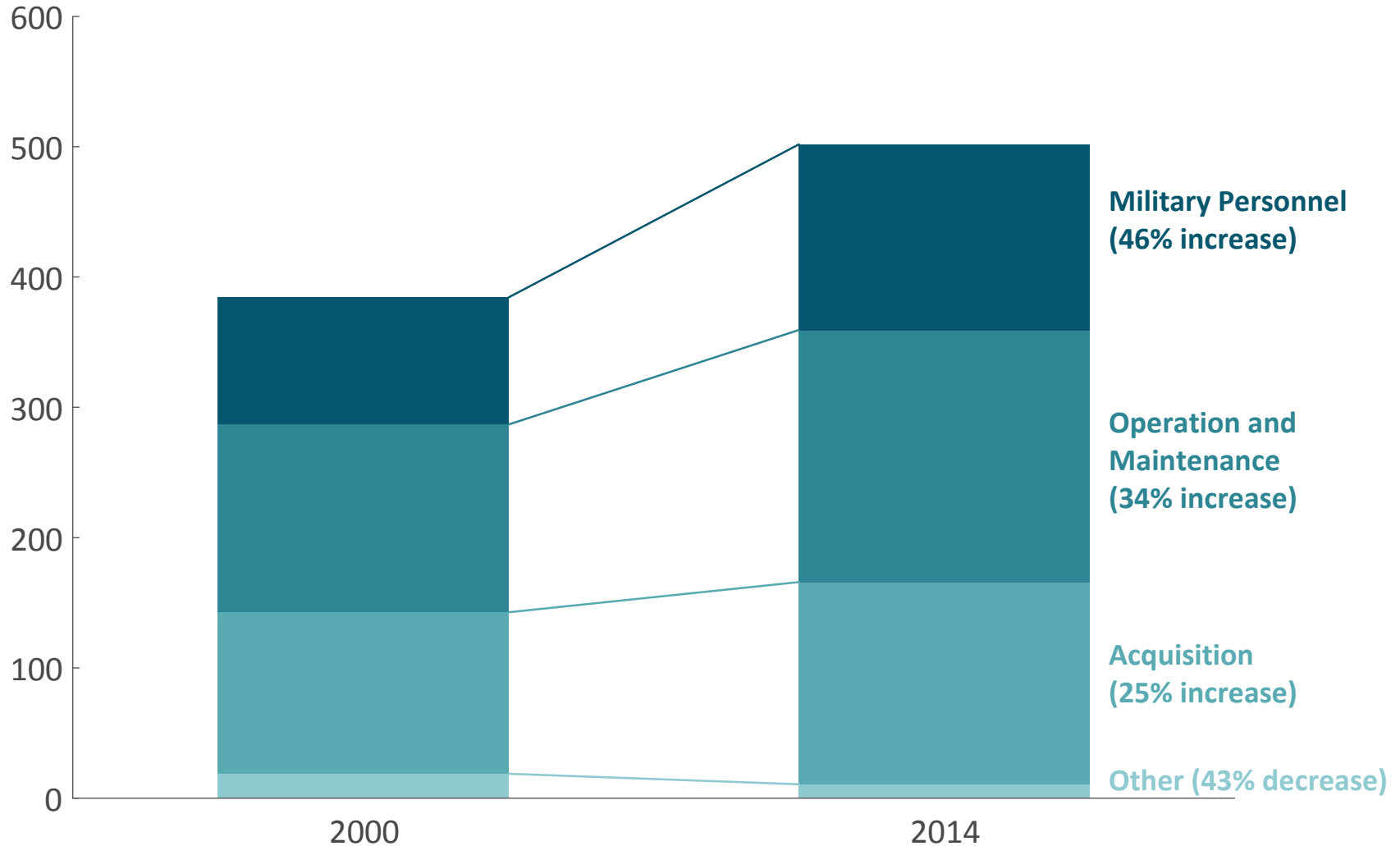


a. For 2015, DoD requested \$496 billion in its base budget in the 2015 FYDP, which equaled the cap set by the Budget Control Act for that year. Funds for overseas contingency operations are not subject to the caps and are not shown here.

The appropriation for Military Personnel (which includes pay and benefits) has been one of the major growth areas in the defense budget.

The Department of Defense's Base Budget, Adjusted for Inflation, Fiscal Years 2000 and 2014

Billions of 2014 Dollars

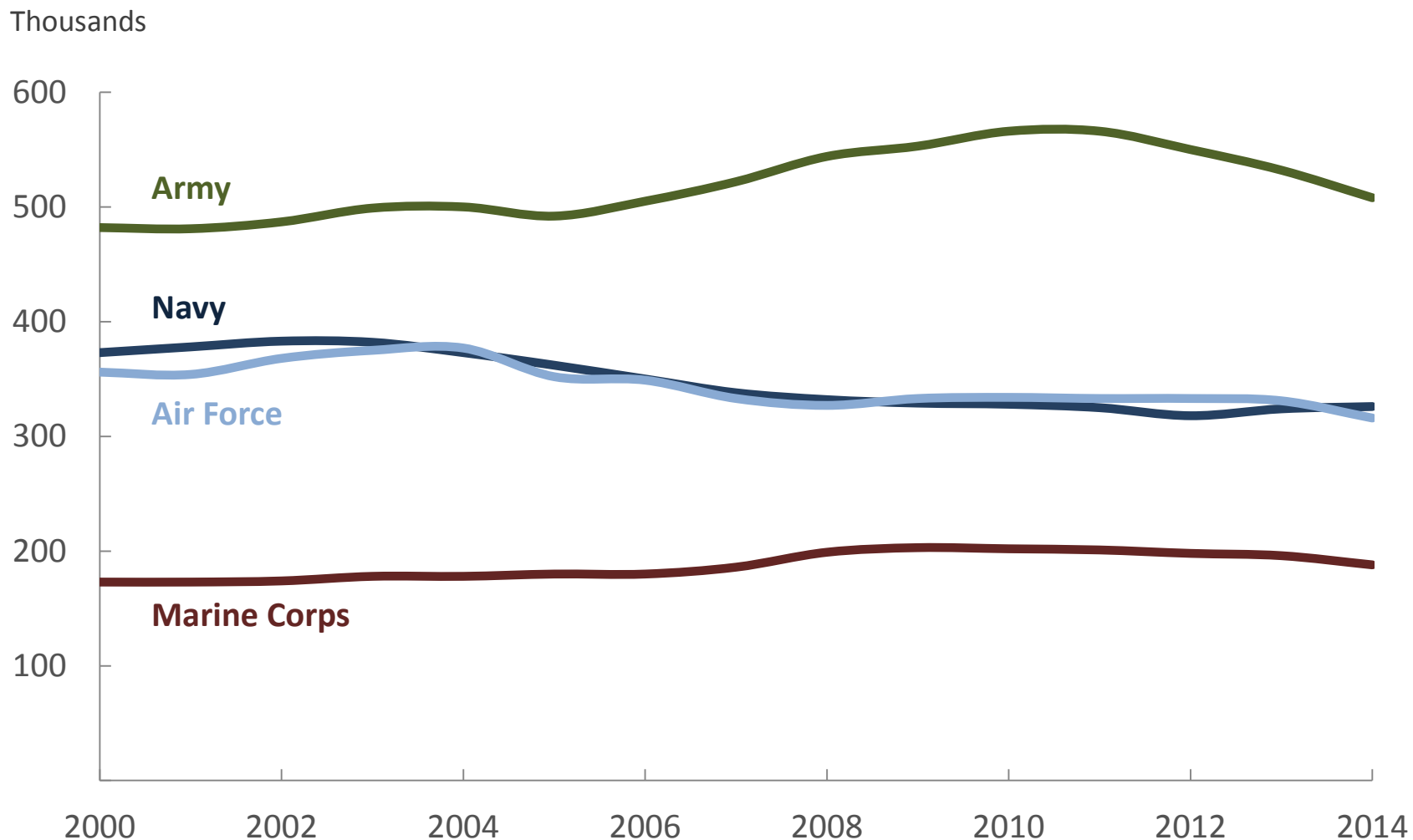


Growth in the appropriation for Military Personnel is even more striking because active end strength has declined slightly since 2000.

War-related increases in the end strength of the Army and Marine Corps were offset by reductions in the Navy and Air Force.

DoD's total end strength fell by 3.3 percent, from 1.38 million in 2000 to 1.34 million in 2014.

The Services' Active End Strength



Note: End strength is the number of personnel on the rolls as of the final day of the fiscal year.

A significant amount of military compensation is in the form of noncash or deferred benefits.

The Composition of Military Compensation in the President's 2016 Budget Request

Billions of 2016 Dollars

Cash		Noncash/Deferred Compensation	
Basic Pay	52.3	Health Care	32.9
Housing and Subsistence Allowances	24.3	Retirement Accrual	16.4
Other Types of Pay and Allowances	15.9	Retiree Health Accrual	6.2
		Schools	3.1
		Family Housing	1.4
Total	92.5	Commissaries	1.2
		Other (Including child care, family support, and fitness centers)	3.5
		Total	64.7

Note: Data exclude the funding requested for overseas contingency operations (OCO). Veterans' benefits are omitted because they are not part of DoD's budget.

Four Options to Reduce Spending on Military Compensation

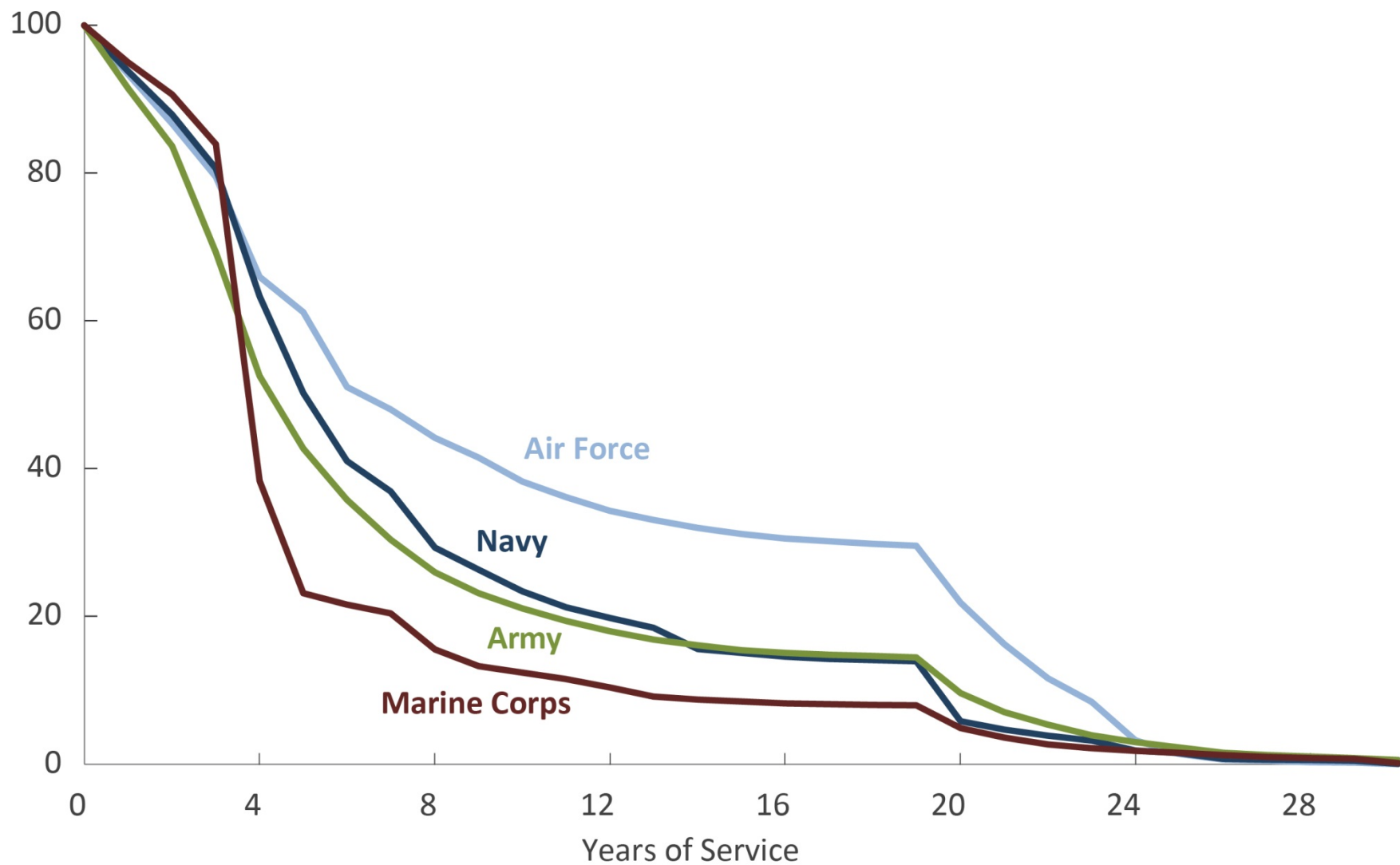
Option	Reductions in Outlays Over a 10-Year Period
1. Cap Increases in Basic Pay for Military Service Members	\$25 billion
2. Replace Some Military Personnel With Civilian Employees	\$19 billion
3. Increase TRICARE Cost Sharing for Retirees	\$20 billion to \$71 billion
4. Eliminate Concurrent Receipt for Disabled Veterans	\$108 billion

Note: Estimates were prepared in November 2013 and spanned the 2014–2023 period.

Reforming military retirement is another approach to reducing spending.

The current defined benefit system pays benefits equal to 50 percent of the average of the 36 highest months of basic pay (often called high-3), but only to the 17 percent of enlisted members (or 50 percent of officers) who reach 20 years of service.

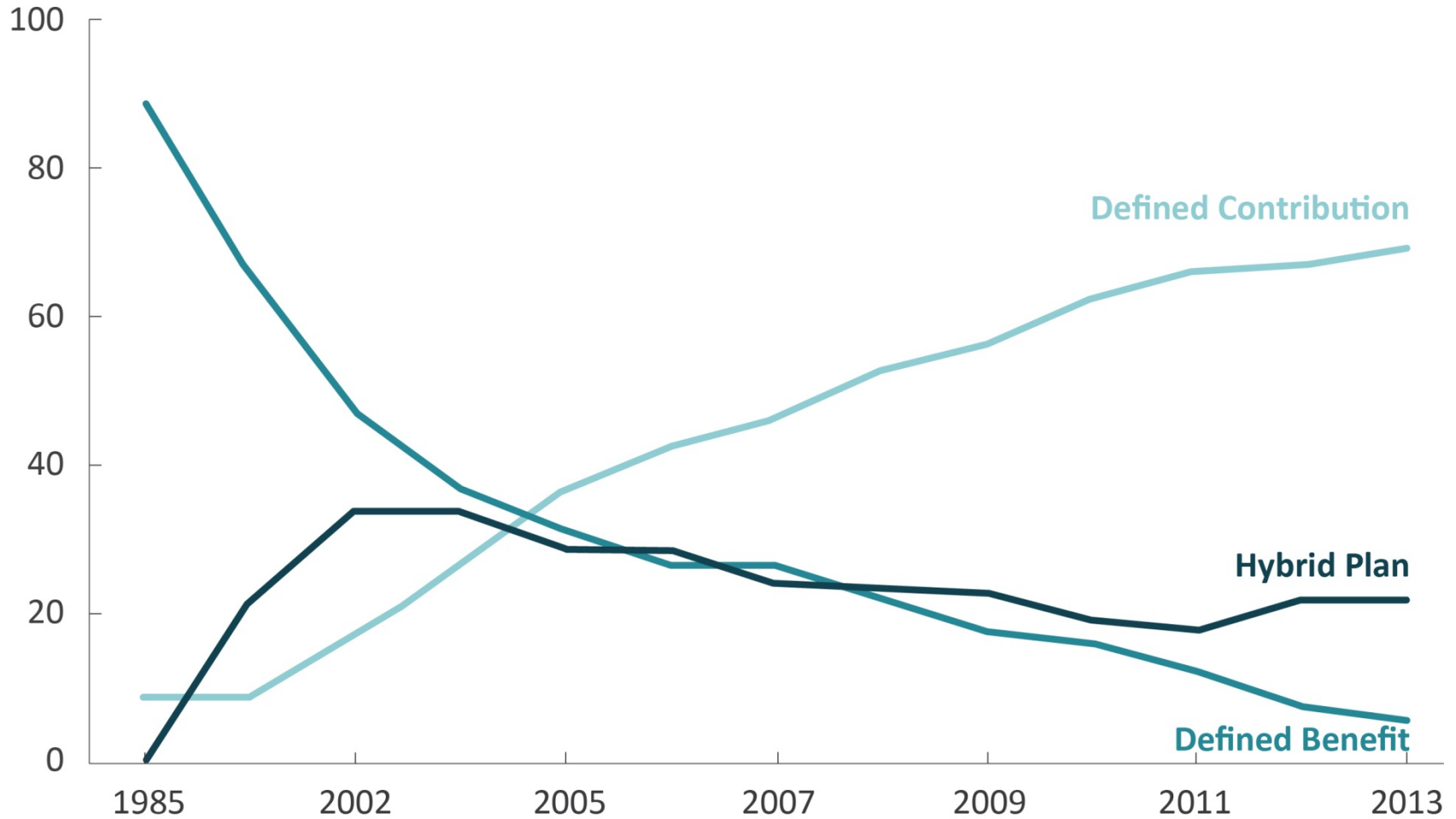
Percentage Remaining in the Military as Years of Service Increase



In industry, the trend has been away from the defined benefit plans and toward defined contribution plans, typically with employer matching (like the Thrift Savings Plan) or hybrid plans.

Types of Retirement Plans in Industry

Percentage of Fortune 100 Companies



Source: Military Compensation and Retirement Modernization Commission.

Key Provisions in the Senate-Passed Version of the National Defense Authorization Act for Fiscal Year 2016 (H.R. 1735)

Provision	Description
Reduce the Defined Benefit	<p>The multiplier decreases (so service members retire at 40% rather than 50% of high-3 basic pay).</p> <p>Retirees may choose a lump-sum in place of all or part of a retirement annuity until age 67.</p>
Add a Defined Contribution With Government Matching	<p>The government makes a standard contribution of 1% of basic pay on entry.</p> <p>For years of service 2 through 20, the government pays an additional matching contribution (1 for 1) up to 4% of basic pay.</p> <p>Funds are available to withdraw starting at age 59½ without tax penalty.</p>
Add Continuation Pay to Preserve the Current Force Structure	<p>Continuation pay begins at 12 years of service from 2.5 times monthly basic pay (active) or 0.5 times active-equivalent monthly basic pay (reserve).</p>
Allow Switching to the New System	<p>Active members who are currently serving may switch to the new system during a one-time opt-in period.</p>

CBO estimates show that the Senate-passed retirement proposal would increase the deficit but reduce DoD's spending over 10 years.

The Budgetary Effects of the Senate-Passed Proposal for Military Retirement (H.R. 1735)

Millions of Dollars

	Total, 2016–2025
Mandatory Outlays	
Annuity payments	-1,200
Lump-sum payments in lieu of annuity	3,320
Total	2,120
Revenues	-1,088
Net Effect on the Deficit of Change in Mandatory Outlays and Revenues	3,208
Discretionary Budget Authority	
Government contributions	13,030
Continuation payments	8,090
Accrual payments to the military retirement trust fund	-42,240
Net Change in DoD's Discretionary Budget Authority	-21,120