



Pilot with Task Force Medevac turns his back as UH-60 Black Hawk touches down at Eel River Conservation Camp in Redway, California, August 2015 (U.S. Army National Guard/Eddie Siguenza)

The Impact of Rising Compensation Costs on Force Structure

By Mark F. Cancian

The battle lines have been drawn: containing the growth of military personnel costs is either “a strategic imperative” or “breaking faith with those who have sacrificed so much.”¹ As

resources contract, the debate intensifies. Angry op-eds are exchanged, constituting the kind of high drama that attracts political and media attention.

Overlooked in this controversy are the adaptations that the Department of Defense (DOD) has already made to accommodate rising personnel costs. These are the same adaptations that businesses have made when faced with the

high costs of a core workforce: reduce the number of high-cost personnel, replace full-time labor with part-time, use outside contractors where possible, substitute capital for labor, and be ready to rebuild if the need arises. With the military, these adaptations have shaped force structure and, hence, strategy. As a result, the United States has built a technological force that cannot go to war without mobilizing Reserves and employing vast numbers of contractors. This in turn shapes responsiveness to threats, the forces employed, and the level of public involvement with the military and conflict. Yet these strategic shifts have been buried in the highly charged arguments about the level of compensation.

Rising Personnel Costs

That personnel costs have risen steeply is not disputed. Since 2001, pay per Active-duty Servicemember has grown over 80 percent in 2001 dollars (about

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50 percent in constant dollars).² Military pay has increased 40 percent more than civilian pay since 2000, and enlisted Servicemembers are now paid more than 90 percent of their civilian counterparts with comparable education and experience (officers earn more than 83 percent of their civilian counterparts).³ Retirement adds another \$26 billion a year, and non-cash benefits tack on \$39 billion, mostly for health care but also for quality of life programs such as child-care, schools, and adult education.⁴

These increased costs, often described as “unsustainable,” have caused widespread alarm. Top military and civilian leaders in the Pentagon and a broad array of think tanks have called for action to curtail personnel costs lest they crowd out readiness and modernization.⁵ The 2014 Quadrennial Defense Review makes compensation savings a major theme, so that funds are available “to sustain a healthy, ready and modern force into the future.”⁶

So far, these efforts have had little impact. Curtailing military pay or benefits during wartime is hard. Military pay raises continued even as government civilians endured 3 years of pay freezes, though the most recent raises in fiscal year (FY) 2014–2015 were constrained to 1 percent. Repeated Obama administration proposals to introduce higher fees for TRICARE, the military healthcare system, have mostly failed in the face of ferocious lobbying by military associations. An attempt to reduce the growth of military retirement costs as part of the FY 2014–2015 budget deal was repealed a month after it was enacted.

Indeed, just holding the line on new benefits is difficult. In the last year, DOD and Congress granted benefits to same-sex partners, expanded medical stipends and transition assistance programs, allowed single parents and pregnant women to enlist, and created a special TRICARE Prime enrollment process for remote eligibles. None of these expansions are necessarily wrong, but they are moving in the wrong direction if the desire is to contain personnel costs.

Faced with this dynamic, the government took the traditional path of

creating the Military Compensation and Retirement Modernization Commission. In January 2015, following extensive analyses and outreach, the commission presented a broad set of proposals for changes in health care, retirement, and benefits. Although congressional action is incomplete as of this writing, the House and Senate appear to have rejected most of the savings proposals but may modify the military retirement program to allow some benefits for personnel who leave before 20 years.

Adaptations and Their Effects

Critics of DOD efforts to reduce personnel costs argue that these expenditures have stayed constant over the last two decades and have not threatened modernization or readiness.⁷ This is true; the military personnel appropriations have varied within a narrow band from 22 percent to 30 percent of the DOD budget over the last 30 years (about 33 percent when healthcare costs are included). Concerns that personnel costs will hurt readiness and eventually “consume the entire defense budget”⁸ are, therefore, misplaced. However, this is not evidence of long-term fiscal sustainability, either. To accommodate higher personnel costs, DOD has made broad adaptations, which have had major strategic effects that are largely unrecognized.

Cut Expensive Personnel. The first adaptation is that, over time, DOD has cut the number of military personnel, particularly Active-duty troops, to fund higher individual compensation. For example, in 1994, \$130 billion (in FY 2014 dollars) paid 1,610,000 Active-duty personnel and 998,000 Guardsmen and Reservists. In 2014, \$137 billion paid 1,324,000 Active-duty personnel and 833,700 Guardsmen and Reservists. In other words, the same amount of money (slightly more, actually) was only enough to pay 450,000 fewer personnel. The Army and Marine Corps are particularly vulnerable because their budgets are so personnel-intensive (45 and 60 percent, respectively),⁹ but all Services are affected. Indeed, practically every budget-cutting concept proposed by a think tank or an

editorialist makes deep cuts to personnel. In one recent budget “wargame,” for example, four think tanks realigned force structure and acquisition programs to fit lower future budget levels. All four teams proposed deep cuts to personnel, reducing numbers by 150,000 to 300,000. This was, they argued, the “Willie Sutton principle” applied to defense budgeting: personnel are where the money is.¹⁰

Rely on Part-Timers. The second adaptation has been to rely more on lower cost part-timers—that is, the Guard and Reserves. Before the Vietnam War, the Guard and Reserves comprised only 26 percent of the total force; during the draft years, Active-duty personnel were readily available, so there was less need to rely on Reserves. With the end of the draft and the announcement of the Total Force policy in the early 1970s, the proportion began to rise. By the end of the Cold War, when the full cost of sustaining the all-volunteer force had been accommodated, Guard and Reserves comprised 36 percent of the total force. In FY 2015, the proportion rose to 39 percent.¹¹

To get a sense of what budget pressure might do to force structure in the future, suppose military personnel budgets hold constant (a best-case scenario for the next few years) but compensation increases at 2.5 percent per year (half the recent rate). That creates an annual bill of \$3.4 billion. To pay this bill out of the personnel appropriations, the Services would have to cut 23,000 Active-duty personnel a year or shift 32,000 positions from the Active to Reserve Component.¹² Historically, the Services have done a combination of the two and cut operations and modernization as well. Cutting Reserve personnel would also save some money but only about one-quarter what is saved by cutting Active personnel. To budgeteers, the financial gain is often not worth the political and strategic cost. As a result, the number of Reserve personnel has declined less; thus, their proportion has increased.

The shift from Active to Reserve personnel has a basis in strategy as threats have diminished and required timelines for deployments have lengthened. Less sophisticated threats and longer



Airmen of 919th Special Operations Security Forces Squadron practice building-clearing techniques during annual training at Camp Guernsey, Wyoming, August 2015 (U.S. Air Force/Sam King)

deployments allow Reserve units the time needed to mobilize, train, and deploy, so more of them can be used. The Guard and Reserves have also adapted by reconfiguring themselves from a “strategic” reserve to an “operational” one. Still, the shift has introduced a degree of strategic risk as the Nation relies on forces that are inherently less ready and harder to use. The disruption of civilian communities produced by deployment of Reservists may also make military force less usable (a good or bad thing, depending on one’s perspective).

A shift in power has followed the shift in personnel. In 2001, all Service Reserve chiefs received a third star to ensure their stronger participation in bureaucratic battles for resources and missions. In 2012, the Chief of the National Guard Bureaus received a fourth star and membership on the Joint Chiefs of Staff, establishing the Guard as a virtual fifth Service.

This dynamic of budget constraints and shifting power played out recently in the Air Force. In 2012, the Air Force proposed personnel cuts to both the Active and Reserve Components but more heavily to the Reserve. The Reserve Components, especially the Guard, working through their congressional supporters, had their cuts halted and a commission established “to undertake a comprehensive study of the structure of the Air Force . . . to best fulfill mission requirements in a manner consistent with available resources.”¹³ The commission, arguing both the ability of the Reserve Component to meet more mission requirements and the need to save money, proposed further realignment of missions from the Active to the Reserve Component so that the total force would shift from the present 69 percent Active/31 percent Reserve to 58 percent Active/42 percent Reserve.¹⁴ In

2015, Congress, concerned about similar tensions within the Army, created the National Commission on the Future of the U.S. Army. With the methodology used by the Air Force commission as a precedent, the commission could produce a similar result.

Substitute Capital and Outside Support. DOD adaptations go beyond the personnel accounts. A further adaptation is the classic substitution of capital for labor. Businesses have done this as labor costs have risen (note the large number of robots in modern factories), and DOD has done the same. Unmanned aerial vehicles (UAVs), for example, now constitute a large proportion of the aviation inventory. Expensive new equipment such as the Navy’s *Ford*-class carrier is justified in part by reduced personnel requirements. Over time, procurement spending per Servicemember has increased, from \$37,000 in 1994 to

\$71,000 in FY 2014 (all in FY 2014 constant dollars).¹⁵ More broadly, the U.S. Armed Forces are more capital-intensive than the militaries of other countries. U.S. equipment spending runs about 25 percent of the total budget; our North Atlantic Treaty Organization (NATO) Allies are only at 14 percent (as NATO measures equipment spending).¹⁶

This approach has had some success. The liberation of Kuwait in 1991 and the overthrow of Saddam Hussein in 2003 were accomplished quickly and with few casualties. But the insurgencies in Iraq and Afghanistan could not be subdued despite the application of unprecedented levels of technology, from UAVs and sensors to long-range strike and the Internet battlefield. There is a whole literature exploring the impact of technology on warfare, and the U.S. focus on technology has roots beyond just the high cost of personnel—for example, in a democracy’s concern about casualties and a national fascination with technology. Nevertheless, the military is not exempt from the laws of microeconomics; high personnel costs drive organizations to substitute capital for labor.

Substituting capital for labor has had other limits, as the Navy and Air Force found out in the 2000s. Coming out of the procurement holiday in the 1990s and not getting procurement money in war funding as the Army was able to do, the Navy and Air Force needed a way to recapitalize. Even as the Army and Marine Corps were expanding, the Navy and Air Force cut personnel, planning to put the savings into modernization. Because of rising personnel costs, however, the savings went instead into expanded personnel compensation and benefits.

Another adaptation has been the expanded use of contractors both at home and on the battlefield, which shifts higher cost and permanent military personnel out of routine support functions. During the Iraq War, for instance, Americans and commentators were surprised to learn that contractors were the largest “coalition” partner. At the height of the war in 2007, there were 165,000 troops in country and the same number

of contractors (U.S., third-country nationals, and locals) supporting the war effort.¹⁷ This growth mirrored expanded use of contractors at home where many base functions, and some headquarters functions, had been turned over to outsiders. There were solid strategic reasons for both. Contractors at home and on the battlefield took over routine tasks that did not require military personnel, such as food service and base maintenance. When the war or task ended, the contractors could easily be discharged. This paralleled the practice in business of focusing core personnel on core tasks and contracting other tasks out.

But this new reliance on contractors raised a host of concerns. Initially, these concerns were focused on financial issues—waste and unethical business practices. They prompted congressional hearings, new contracting structures, and a major investigating commission, the Commission on Wartime Contracting in Iraq and Afghanistan.

On a deeper level, many commentators worried about the strategic effects of depending on for-profit entities in national security. At home, contractors seemed to have taken over inherently governmental functions such as intelligence analysis and writing military doctrine. Overseas, the widespread and unprecedented use of contractors, particularly as they moved out of support roles and into the direct application of violence, raised concerns about “conduct[ing] wars with less political debate . . . undermining the legitimacy of counterinsurgency efforts and damaging the perceived morality of the war effort.” Indeed, some observers worried that contractors “endanger the basic tenets of the military profession” by blurring the line between civilians and military.¹⁸ Despite these concerns, the rising cost of military personnel and their declining numbers will push force planners to rely even more on contractors in the future.

Expand in Wartime. The final adaptation has been the need to rapidly expand the force in wartime because the peacetime force would be too small to handle large conflicts. This approach was remarkably successful in Iraq and

Afghanistan, where the Army and Marine Corps were able to quickly add over 100,000 personnel during an increasingly unpopular war and without resorting to conscription. The risk is in timing—making the difficult political decision to expand when needed. The Iraq expansion did not begin until the end of 2006. It should have started years earlier before the force was strained by repeated deployments, but it took several years for the political apparatus to acknowledge so publicly that the wars would be long and hard. Thus, future force structures might only be viable if an early decision could be made to expand them. The Army is at greatest risk here, followed closely by the Marine Corps. Without rapid expansion, these Services will be stretched on the battlefield and stressed by long and frequent deployments.

Labor Economics versus Moral Obligations

Why can we not just settle on an objective formula for compensation that avoids these tough structural tradeoffs? The reason is that there are fundamentally different views on the nature and purpose of compensation. On one side are the labor economists—that is, people who argue that compensation should be set at a level adequate to recruit and retain the numbers and quality of personnel an organization needs. Cindy Williams, formerly an economist at the Congressional Budget Office, came to symbolize this approach when she testified in 1995 that all objective measures of compensation fairness were badly flawed and that, ultimately, “in a volunteer environment, the best indication of how well the military can compete as an employer is the overall picture of the services’ success in recruiting and retention.”¹⁹ Therefore, military compensation could be assessed like other occupations and vary based on the state of recruiting, retention, and the economy. When unemployment is low and the force is expanding, compensation needs to rise to be competitive. Thus, compensation grew rapidly in the 2000s. However, when the force is shrinking (as it is today), compensa-

tion can decline. This view also held that compensation should be adjusted for personnel quality, with higher skilled personnel paid more than lower skilled personnel as happens in the broader economy.

On the other side are those who argue that there is a moral obligation to pay workers a “fair” wage. This view has roots as diverse as Karl Marx’s socialism and Catholic social teaching, from Pope Leo XIII in the 19th century to Pope Francis today (“Not paying a just [wage], focusing exclusively on financial statements . . . goes against God”).²⁰ Applied to the military, this approach argues that the Nation owes generous compensation to the 1 percent who serve on behalf of all. The military is not a job; it is a calling or a profession (to use the words of Charles Moskos, the late dean of military sociologists), and it deserves compensation on a moral basis, not an economic one.²¹ This perspective is also egalitarian; all those who serve should be honored and treated equally, consistent with the rank structure. These arguments often take a moral tone. As General Gordon Sullivan, USA (Ret.), head of the Association of the U.S. Army, stated, cuts to compensation “demonize our troops as unworthy of the benefits they receive while ignoring the challenges, sacrifices, and hardships military personnel and their families face.”²²

The debate is not limited to the military. It has parallels at universities regarding payment of a living wage for low-skilled workers and in national debates about the level of the minimum wage. It does mean, however, that agreement on military compensation has been elusive. What one side regards as “reasonable adjustments,” the other side regards as “betraying a commitment.”

Some commentators have proposed conscription as a way out of this conundrum of high costs and adverse strategic consequences. Conscription seems to offer lower costs, abundant personnel, and a feeling that “everyone is in this together.” In fact, experience from the Vietnam War indicates that of these goals, only abundant personnel are likely achievable and even then at a high cost to



New Jersey National Guard Soldier from 50th Infantry Brigade Combat Team launches RQ-11 Raven unmanned aerial vehicle during joint exercise, Warren Grove Gunnery Range, New Jersey, June 2015 (U.S. Air National Guard/Matt Hecht)

morale, effectiveness, and public regard. Whatever conscription’s benefits might be, however, politicians, the military leadership, and the American people all oppose its reinstitution. Therefore, little more needs to be said about it as a solution.

The Strategic Dimension

So the debate continues. Many commentators complain about the structural trends. Rachel Maddow criticizes “relying on a pop-up army . . . of greasy, lawless contractors.” Andrew Bacevich laments “the large gap between the military and society.” Bernard Rostker warns about the risks in overreliance on “unready” Reservists.²³ These concerns may or may not have merit, but they are essentially irrelevant. Unless the approach toward military compensation changes, the prospect is more of the same—a shrinking force, greater reliance on Reservists, contractors as a permanent element of the military force structure, capital substituting for labor, and rapid force expansion when wartime demands exceed what the peacetime force can handle.

And that is the element missing in discussions about military compensation. It is about more than what military

personnel deserve or whether the costs are “affordable.” It is about the adaptations the military establishment has made to accommodate the higher personnel costs. These adaptations have had profound strategic effects—effects that no Quadrennial Defense Review or strategy document discusses. The key strategic decision, then, is whether the military structure that the compensation structure produces supports the strategy the Nation wants, with risks and costs that are acceptable. The United States has backed into the existing structure without a lot of thought. As compensation discussions renew, the debate going forward ought to be broadened to include these strategic effects. JFQ

Notes

¹ “Strategic Imperative,” from Posture Statement of General Martin E. Dempsey, Chairman of the Joint Chiefs of Staff, Senate Armed Services Committee, Fiscal Year 2015 Department of Defense Budget, March 5, 2014, available at <www.armed-services.senate.gov/download/dempsey_03-05-14>; Steve Strobbridge, “Spare Us the ‘Keeping Faith’ Blather,” *MOAA.org*, March 15, 2012, available at <www.moaa.org/main_article.aspx?id=9412>.

² Robert Hale, Testimony to the Senate

Armed Services Committee, March 28, 2012, available at <www.defense.gov/news/newsarticle.aspx?id=67743>. Calculations vary depending on treatment of accruals for TRICARE and retirement, the mobilization of Reservists, and personnel costs in war funding, but all methods show large cost increases.

³ Comparison with civilian compensation from *Report of the Eleventh Quadrennial Review of Military Compensation (QRMC), Main Report* (Washington, DC: Department of Defense [DOD], June 2012), 31. The increase of 40 percent compared to civilian compensation has been cited repeatedly by DOD; for example, see Secretary of Defense Chuck Hagel, *FY 2015 Budget Preview*, February 24, 2014.

⁴ *Interim Report of the Military Compensation and Retirement Modernization Commission* (Washington, DC: Military Compensation and Retirement Modernization Commission, June 2014), 15, § 6.2. DOD costs only.

⁵ For example, on June 3, 2012, 25 experts from 10 think tanks wrote an open letter to senior Members of Congress and the Secretary of Defense recommended “curb[ing] the growth in military compensation costs, as well as reductions to bases and shrinking the civilian workforce.” The think tanks spanned the ideological spectrum from the libertarian Cato Institute to the liberal Center for American Progress to the conservative American Enterprise Institute. For a sample of individual statements, see Leon E. Panetta, Testimony before the Defense Subcommittee of the Senate Appropriations Committee, June 13, 2012; Robert Gates, Remarks at the Eisenhower Center, Abilene, KS, May 8, 2010, which included his famous comment, “Health-care costs are eating the Defense Department alive,” available at <www.defense.gov/speeches/speech.aspx?speechid=1467>; Chuck Hagel, “FY15 Budget Preview,” The Pentagon, February 24, 2014, available at <www.defense.gov/Speeches/Speech.aspx?SpeechID=1831>; Dempsey.

⁶ *Quadrennial Defense Review 2014* (Washington, DC: DOD, March 4, 2014), 39, 48–51.

⁷ The Military Officers Association of America did the original analysis, which has been picked up by many others. See, for example, *A Bargain, Not a Liability* (Alexandria, VA: Military Officers Association of America, 2014), 3. This calculation excludes non-cash benefits and veterans’ benefits, both of which have increased steeply in recent years.

⁸ For example, David R. Segal and Lawrence J. Korb, “Manning and Financing the Twenty-First Century All-Volunteer Force,” in *The Modern American Military*, ed. David M. Kennedy (New York: Oxford University Press, 2013), 127; Paul K. MacDonald and Joseph M. Parent, “The Banality of Retrenchment,” *ForeignAffairs.com*, March 9, 2014, available at <www.foreignaffairs.com/articles/usa/2014-03-09/banality-retrenchment>.

⁹ Military personnel appropriation as a percentage of total service FY14 budget. Excludes war funding (overseas contingency operations funding). Total personnel compensation, with health care and benefits, is substantially larger. The Marine Corps percentage is unusually high because its aviation procurement and operations are mostly funded by Navy appropriations.

¹⁰ *Joint Think Tank Event: Alternatives to the QDR and FY15 Defense Budget, Comparison Across Teams* (Washington, DC: Center for Strategic and Budgetary Analysis, February 5, 2014), available at <www.csbaonline.org/2014/01/28/joint-think-tank-event-alternatives-to-the-qdr-and-fy15-defense-budget/>. The teams were from the Center for Strategic and Budgetary Assessments, Center for Strategic and International Studies, Center for a New American Security, and American Enterprise Institute. Willie Sutton was a bank robber who apocryphally stated that he robbed banks “because that’s where the money is.”

¹¹ Office of the Under Secretary of Defense (Comptroller)/Chief Financial Officer, *United States Department of Defense Fiscal Year 2015 Budget Request Overview* (Washington, DC: DOD, March 2014), A2, A3.

¹² Author calculation using data from FY14 DOD budget materials and Eleventh QRMC. This calculation is consistent with a detailed Active/Reserve Component cost comparison conducted by the Reserve Forces Policy Board, *Eliminating Major Gaps in DOD Data on the Fully Burdened and Life-Cycle Cost of Military Personnel: Cost Estimates Should Be Mandated by Policy* (Washington, DC: Reserve Forces Policy Board, January 7, 2013), 5. The study calculated that “the [Reserve Component] per capita cost ranges from 22% to 32% of their [Active Component] counterparts’ per capita costs, depending on which cost elements are included.”

¹³ *National Defense Authorization Act for Fiscal Year 2013*, Public Law 112-239, January 2, 2013, Subtitle G, § 363 (a)(1).

¹⁴ *Report to the President and Congress of the United States* (Washington, DC: National Commission on the Structure of the Air Force, January 30, 2014), 36.

¹⁵ Office of the Secretary of Defense (Comptroller), *National Defense Budget Estimates for FY 2014*, May 2013, tables 6-8, 7-5, available at <comptroller.defense.gov/Portals/.../defbudget/fy2014/FY14_Green_Book.pdf>. Excludes war funding.

¹⁶ Calculated from data in *Financial and Economic Data Relating to NATO Defense* (Brussels: NATO Public Diplomacy, February 24, 2014).

¹⁷ Moshe Schwartz and Jennifer Church, *Department of Defense’s Use of Contractors to Support Military Operations: Background, Analysis and Issues for Congress*, R43074 (Washington, DC: Congressional Research Service, May 17, 2013), 25. For an expanded discussion

of contractors on the battlefield, see Mark F. Cancian, “Contractors: The New Element of Military Force Structure,” *Parameters* (Autumn 2008), 61–77.

¹⁸ Strategic concerns from T.X. Hammes, “Private Contractors in Conflict Zones: The Good, the Bad, and the Strategic Impact,” *Joint Force Quarterly* 60 (1st Quarter 2011), 26–32; Gary Schaub, Jr., and Volker Franke, “Contractors as Military Professionals?” *Parameters* (Winter 2009/2010), 101.

¹⁹ Cindy Williams, Testimony on Military Pay before the Senate Armed Services Committee (Washington, DC: Congressional Budget Office, March 16, 1995), 14. This testimony hit the Internet as an example of attacks on military benefits and made Dr. Williams well known.

²⁰ Karl Marx, *Critique of the Gotha Programme* (1875); Pope Leo XIII, *Rerum Novarum (Rights and Duties of Capital and Labor)*, 1891; Pope Francis, “Speech to Workers in Cagniliarca, Sardinia,” September 23, 2013, cited in John Coleman, “Pope Francis on the Dignity of Labor,” *America Magazine*, November 20, 2013, available at <<http://americamagazine.org/content/all-things-/pope-francis-dignity-labor>>.

²¹ Charles C. Moskos, Jr., “The All-Volunteer Military: Calling, Profession, or Occupation?” *Parameters* (Winter 2010/2011), 23–31.

²² Gordon Sullivan, “Don’t Cut Troops’ Pay and Benefits,” letter to the editor, *Washington Post*, January 6, 2014.

²³ Rachel Maddow, *Adrift: The Unmooring of American Power* (New York: Crown Publishing, 2012), 186–187; Andrew J. Bacevich, *The Limits of Power: The End of American Exceptionalism* (New York: Metropolitan Books, 2008), 122–123, 131, 152–156; Bernard Rostker, *Rightsizing the Force: Lessons for the Current Drawdown of American Military Personnel* (Washington, DC: Center for a New American Security, June 2013), 5–11.