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PERSONNEL AND
READINESS

MAR 15 2004

The Honorable Duncan Hunter
Chairman
Committee on Armed Services
U.S. House of Representatives
Washington, DC 20515

Dear Mr. Chairman:

Enclosed is a Department of Defense Report on the Review of Compensation for Reserve Personnel requested by Senate Report 107-151, p. 328, which accompanied the National Defense Authorization Act for Fiscal Year 2003.

The review examined the extent to which personnel and compensation policies and statutes, including the retirement system, appropriately address the demands placed on guard and reserve personnel. At the Committee's request, the review also focused on reserve service requirements for retirement and the sufficiency of the Reserve Montgomery GI Bill and Reserve Survivor Benefit Plan programs.

The Department looks forward to continued partnership with Congress in enacting meaningful reforms in Reserve Compensation. We are thankful for your consideration in these paramount issues.

Sincerely,

Charles S. Abell
Principal Deputy

Enclosure:
As stated

cc:
The Honorable Ike Skelton
Ranking Member

DEPARTMENT OF DEFENSE

REPORT TO CONGRESS

RESERVE PERSONNEL

COMPENSATION PROGRAM REVIEW

OFFICE OF THE UNDER SECRETARY OF DEFENSE
FOR PERSONNEL AND READINESS

March 15, 2004

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INTRODUCTION

As requested in Senate Report 107-151 that accompanied the National Defense Authorization Act for Fiscal Year 2003, the Department conducted a comprehensive review of compensation for reserve personnel. The committee report—in calling for this review—noted the following:

> The committee recognizes that the contributions of the reserve components have greatly increased in the past decade. In particular, there are certain mission-critical skills and units among reserve forces that have been recalled for contingency operations, placing stress upon the members and their families. The role of reserves is so integral in the total force that military operations involving major, extended missions are required to include reserve participation.
>
> The committee is concerned that the pay and benefits of reserve personnel must appropriately compensate them for their service. Today's total force concept, which relies heavily on National Guard and Reserve forces for both day-to-day and contingency operations, differs from that envisioned by the designers of the reserve compensation and retirement system more than a half-century ago. Accordingly, the committee directs the Secretary of Defense to conduct a reserve personnel compensation review aimed at determining the extent to which personnel and compensation policies and statutes, including the retirement system that defers eligibility for retired pay to age 60, appropriately address the demands placed on guard and reserve personnel. Other topics that should be reviewed include the number of years of reserve service needed to qualify for retirement and the comparability and sufficiency of the Reserve Montgomery GI Bill and Reserve Survivor Benefit Plan programs. The Secretary should report the results of this review to the Committees on Armed Services of the Senate and the House of Representatives no later than August 1, 2003.

This review is timely since the Department is in the midst of a fundamental transformation of its strategy, policies and forces. Rather than a requirements-based force, the Department is transforming into a capabilities-based force, which will better position the Department to respond to a broader spectrum of current, emerging and future challenges.

Transformation of the Reserve components was the subject of the Department's recently released report on *Reserve Component Contributions to National Defense*. This report set the framework for enhancing military service in the 21st century by calling for greater flexibility for members to more easily transition between the Active and Reserve components and to vary their level of participation, which may change from full-time duty to simply being available in the event of total mobilization. This important new construct requires modifying the statutes and policies governing military personnel in order to permit service members to vary

their participation as their circumstances change. The compensation system must be able to support the Department's human resources strategy for the 21st century and to implement the "continuum of service" construct envisioned in the *Reserve Component Contributions to National Defense.*

Implementation of the continuum of service envisioned in the report is accomplished through five main objectives as depicted in figure 1.

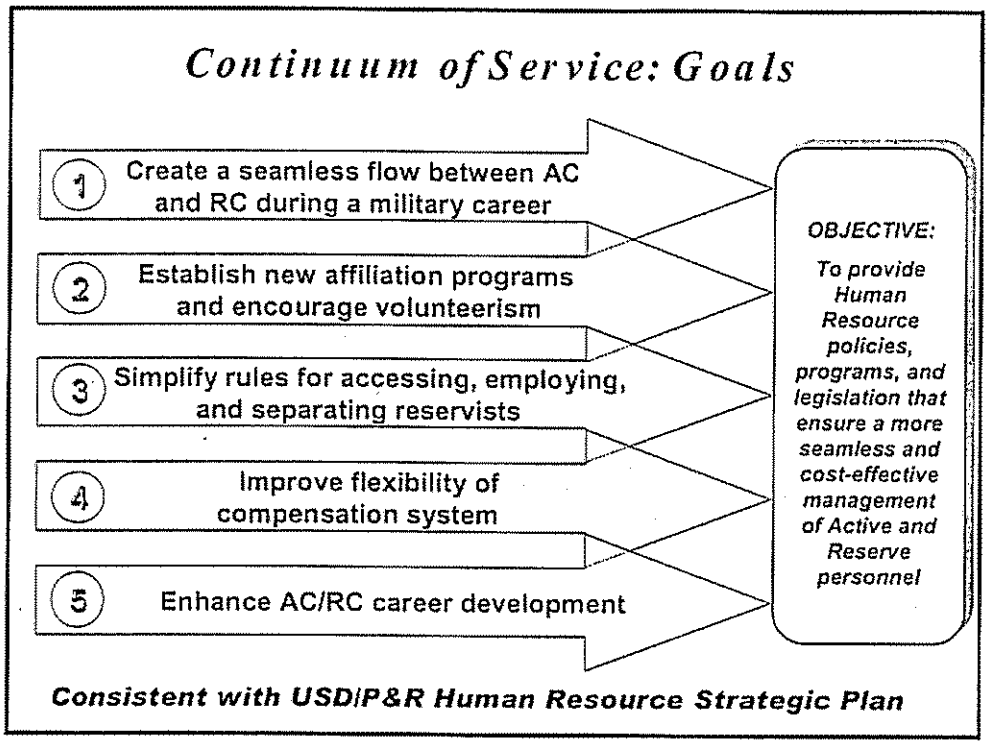

Figure 1

While one of the five objectives directly calls for appropriate changes to the compensation system, achieving the other objectives can be influenced through the compensation system to varying degrees. This objective does not require, nor are the needs of the Department best served by having, a rigid system of compensation that is identical for everyone. But the system must be fair—this is one of the principles of compensation. Compensation for inactive duty—which permits a Reserve component member to be paid the equivalent of two days of basic pay for at least eight hours of inactive duty but does not authorize payment of allowances—is a classic example of how the compensation systems for active duty and reserve service differ.

This will be the first review of all elements of reserve compensation since the 1988 report of the Sixth Quadrennial Review of Military Compensation, which focused exclusively on pay and benefits of Reserve component members. Two subsequent studies have reviewed some aspects of reserve compensation, but not the entire spectrum of compensation issues. The findings of those studies were reported in:

- the 2001 Parity of Pay and Benefits Report, which reviewed perceived inequities for Reservists serving on active duty pay, and
- the Ninth Quadrennial Review of Military Compensation, which reviewed special and incentive pays, and the housing allowance for Reserve component members on active duty or full-time National Guard duty for less than 140 days.

This is also the first review undertaken during a major mobilization of the Ready Reserve and provides a unique opportunity to evaluate issues that were not previously contemplated; and study elements of compensation that may appear inadequate given the increased use of Reserve component members in the daily operations of the Department.

It is in this context that the Department approached the review called for in Senate Report 107-151. This review was conducted from five different perspectives to determine what changes might be appropriate to support the goals of the continuum of service. The functional areas studied in this review include:

- Compensation issues related to mobilization
- Compensation issues related to service while on active duty, and in the case of the National Guard, also when performing full-time National Guard duty
- Compensation related to performing duty in an inactive duty status
- Compensation needed to support recruiting and retention
- The reserve retirement system

The issues reviewed under each area were developed from topics specifically stated in the Senate report; issues previously studied in the 2001 Parity of Pay and Benefits report and the 9th Quadrennial Review of Military Compensation report; topics of special interest to the Services and Reserve components, and issues known to be of interest to various stakeholders. The findings of this review are provided in the following report. No legislative proposals accompany this report even though some findings suggest legislation may be an appropriate solution.

Some legislative initiatives are currently being considered for the Department's Fiscal Year 2005 omnibus legislative program and others may be vetted for possible submission in subsequent years, pending the outcome of further analysis and planned studies.

Special And Incentive Pays

Historically, the first special and incentive pays were intended to provide enlistment and reenlistment incentives. The first special and incentive pays adopted in the twentieth century were intended to compensate members exposed to conditions more hazardous than those experienced by the average member of the armed forces during peacetime. As a matter of fairness and equity, Reserve component members who are in skill areas for which a special or incentive pay is authorized for active duty members should be eligible for that pay. Some special and incentive pays have always included Reserve component members as part of the eligible population, while others added Guard and Reserve personnel performing inactive duty training as an eligible population sometime after the pay was first established. However, there are a few incentive pays for which Reserve component members are eligible only when they are on active duty, but not when performing inactive duty. While bonuses are paid regardless of the member's duty status, incentive pays are paid only when the member is in a duty status. Therefore, Reservists are paid these incentive pays under the 1/30th rule; however, this may not provide sufficient incentive to attract Reservists into a particular career field or skill area.

With respect to bonuses, the recent increases in the maximum amount for the enlisted accession bonus and enlisted retention bonus are being used extensively to meet critical skill shortfalls within the Selected Reserve. Bonuses are a cost effective tool for targeting particular skills that are critically short, but the current limitations within some existing authorities and absence of authority in other cases may be limiting the Reserve components from addressing all manning shortfalls.

In reviewing special and incentive pays, and bonus authorities, areas were identified in which providing greater flexibility would allow the component to act positively to avoid potential problems and respond quickly to emerging problems. The following sections describe in greater detail incentive pays and bonuses, and provide several alternatives that would strengthen incentive programs in order to help the Reserve components meet their manpower needs in the 21st century.

The Purpose of Special and Incentive Pays

Special and incentive pays and their stated purposes fall into two main categories. The first category compensates members who are exposed to conditions more hazardous than those experienced by the average member during peacetime.

Examples of duties in this category include: parachute jumping, demolition duty, and duty on the flight deck of an aircraft carrier.

The second category is intended to induce members to acquire a particular skill or volunteer for certain career fields that would otherwise experience manning shortfalls. Examples of skills or career fields in this category include: foreign language proficiency, aviation, and enlisted leadership positions such as first sergeants and command chief master sergeants.

While some incentive pays originated with the purpose of compensating for hazard, they have evolved over time to career incentive pays. Examples of this change in purpose are found in Aviation Career Incentive Pay and Career Enlisted Flyers Incentive Pay.

THE 1/30TH RULE

The method for paying special and incentive pays authorized for eligible Reserve component members is generally governed by the 1/30th rule. That is, the member is entitled to 1/30th of the monthly pay for each day of duty or each period of inactive duty performed. It should be noted that the 1/30th rule also applies to basic pay. While the rule applies equally to active and reserve members, it is more apparent to Reserve component members because of the frequency with which they move in and out of a duty status. There is one exception to the 1/30th rule—that is hostile fire/imminent danger pay. Active and Reserve component members receive the full monthly payment if they serve even one day in the specified zone during the month, and Reserve component members receive the full monthly payment regardless of any change in their duty status.

For many years, a number of Reservists have considered the 1/30th rule is unfair. They point out that they must meet the same qualification standards, maintain the same level of training and currency in the special skill, and are exposed to the same hazards associated with the duty as their active duty counterparts. Therefore, they argue that they should receive the full monthly incentive pay, whether or not they are in a duty status—thus they advocate eliminating the 1/30th rule. That argument has gained momentum over the past decade with the increased use of Reserve component members to perform day-to-day operations. But the merit of that argument must also be supported by the purpose of the special and incentive pays and the applicability of that purpose to the Reserve components.

PREVIOUS REVIEWS

Both the Sixth and Ninth Quadrennial Reviews of Military Compensation (QRMC) reviewed special and incentive pays.

Sixth Quadrennial Review of Military Compensation
In 1986, the Sixth QRMC was tasked to conduct a comprehensive review of the benefits and costs of all Reserve compensation programs—including an assessment of incentive pays. During unit visits by members of the Sixth QRMC, some Reservists addressed the 1/30th rule and expressed their dissatisfaction with the way the Aviation Career Incentive Pay program operates, believing that they should receive the same monthly rate of the incentive pay as their active duty counterparts. The Sixth QRMC found that this was not a new issue, but that it pointed to a fundamental misunderstanding regarding incentive pays. The Sixth QRMC stated that the primary purpose of incentive pays is not simply to compensate a member for undertaking occasional hazardous duties, but to serve as an incentive for undertaking a career that is, on a full-time basis, more hazardous than other service careers. Thus, they concluded that there was no compelling reason to change the 1/30th rule with respect to Aviation Career Incentive Pay, or other incentive pays.

Ninth Quadrennial Review of Military Compensation
In 1999, the Ninth QRMC revisited the issue of special and incentive pays in light of:

- DoD's Total Force policy that requires greater integration of the active and reserve forces,
- the role of the Reserve components, which has changed dramatically. They are no longer just a pre-trained manpower pool to be used in the event of full mobilization, but are now more fully integrated into missions that require less than full mobilization and are subject to more frequent call-ups, and
- recent significant changes in special and incentive pays.

The Ninth QRMC grouped special and incentive pays into three categories:

- Hazardous/hardship duty pays
- Career or skills retention pays with hazard
- Career or skills retention pays without hazard

The Ninth QRMC was unable to conclude whether or not the method of paying certain special and incentive pays to Reserve component members should be changed. They did state that there are some areas where a more consistent application of special and incentive pays for Reserve component and active component members might be considered. Thus, their primary recommendation was for further study.

However, they did express a special interest in Foreign Language Proficiency Pay (FLPP). They suggested that if the Services needed manning flexibility for their language skill requirements, then authorizing FLPP for Reservists who are not assigned to a billet that requires a language skill, but maintain proficiency in a foreign language on their own time might make sense. They further suggested that the pay should be at the same rate as that paid to active duty members who maintain proficiency in a foreign language.

CAREER INCENTIVE PAYS

In assessing the incentive pays intended to induce members to undertake a particular skill or career field, one must realize that the 1/30th rule reflects the member's career decision and compensates them accordingly. Those members who have chosen to undertake a full-time career are paid at the full monthly rate, while members who have elected to undertake military service on a part-time basis are paid proportionally to the amount of time they spend performing military service. Moreover, paying the incentive pay to the part-time force at the full-time rate would provide a much greater reward to those members who perform the least amount of duty and might actually serve as a disincentive for some members to perform any more than the minimum amount of part-time duty required.

However, there may be certain career positions that occasionally involve performing some function when the member is not in a duty status. Similarly, if it is desirable to have members with proficiency in a foreign language and the Reserve components can provide depth in a particular language, then it may be appropriate to provide an incentive for linguists at a rate greater than currently allowed under the 1/30th rule, particularly since this often requires the Reservist to maintain language proficiency on his or her own time rather than when in a duty status. In these types of situations, the 1/30th rule may not provide sufficient incentive to entice Reservists to serve in the career field or maintain the requisite proficiency level for skills such as language. But rather than changing the 1/30th rule, an alternative might be to establish a bonus that would enable the Reserve components to target specific shortfalls, which would avoid creating an expensive entitlement to address a very narrowly focused problem.

HAZARDOUS DUTY INCENTIVE PAYS

Similarly, Reservists who perform duty that involves hazard or danger have argued that they should be paid the incentive pay at the full monthly rate because they must meet the same qualification and proficiency standards and are exposed to the same hazards as their active duty counterparts. However, Reservists are only exposed to those hazards when they are on duty. Moreover, unless involuntarily called to active duty, Reservists volunteer for the duty they perform, and, as such, they control when and how frequently they will perform duty that may expose them to the hazard or danger. This is unlike their active duty counterparts who can be required to perform the hazardous duty at any time.

However, if there is a shortage of personnel to perform certain types of hazardous duty, then the 1/30th rule may not provide sufficient incentive to meet the manning needs. The same remedy of targeting specific shortfalls with a bonus could be applied to shortfalls in particular skill areas involving hazard.

IS THERE A PROBLEM?

This is the underlying question that must be answered before any change to the system is made. While both active duty and Reserve component members must maintain the same skill qualifications, there is no evidence that the Reserve components are experiencing shortages that would warrant a change to the current method of paying special and incentive pays. On average, Reservists perform the duty associated with the incentive pay less frequently than their active duty counterparts, even though they both maintain the same qualifications and meet the same proficiency requirements. Like their active duty counterparts, Reservists receive the incentive pay when they are in a duty status, whether or not they actually perform the duty associated with the particular incentive pay. Moreover, paying the full monthly incentive pay for part-time service may create an inequity between active and reserve compensation. Finally, the rationale stated for changing the 1/30th rule could apply equally to basic pay, which would result in a more costly and even greater inequity.

While there is no conclusive evidence that the Reserve components are experiencing shortages in critical skill areas and retention intentions appear positive thus far, the total effect of the mobilization in response to the Global War on Terrorism on the retention picture within the Services remains to be seen. The rigors of mobilization and the continued use of the Guard and Reserve may require additional incentives to retain acceptable levels within the Reserve components.

AN ALTERNATIVE APPROACH

Simply eliminating the 1/30th rule in order to pay Reserve component members the incentive pay at the full monthly rate would cost the Department nearly $171M annually as depicted in figure 2. Rather than changing the 1/30th rule when there is no evidence that this would solve a problem, a new authority providing the flexibility of a critical skills bonus, similar to the bonus available to the active force, may be a more cost effective and appropriate solution.

Cost to Pay Reservists Incentive Pays at the Full Monthly Rate

$M	HDIP	ACIP	CEFIP	Sub	Dive	SDAP	FLPP	TOTAL
ARNG	9.7	26.4	0.0	0.0	0.0	11.2	0.4	47.7
USAR	4.4	6.7	0.0	0.0	0.0	6.6	0.3	18.0
USNR	0.8	15.5	1.4	0.0	0.4	2.0	0.0	20.1
USMCR	0.1	2.5	0.1	0.0	0.0	0.0	0.0	2.7
ANG	5.6	27.4	4.2	0.0	0.0	3.0	0.2	40.4
USAFR	7.8	23.4	6.9	0.0	0.0	3.4	0.2	41.7
USCGR	0.0	0.0	0.0	0.0	0.0	0.2	0.0	0.2
TOTAL	28.4	112.5	12.6	0.0	0.4	26.4	1.1	170.8

HDIP	Hazardous Duty Incentive Pay (37 USC 301)
ACIP	Aviation Career Incentive Pay (37 USC 301a)
CEFIP	Career Enlisted Flyers Incentive Pay (37 USC 320)
Sub	Submarine Duty Incentive Pay (37 USC 301c)
Dive	Diving Duty Special Pay (37 USC 304)
SDAP	Special Duty Assignment Pay (37 USC 307)
FLPP	Foreign Language Proficiency Pay (37 USC 316)

Figure 2

An affordable alternative could be to use a combination of an incentive pay and a bonus, such as currently authorized for the aviation community. Using this community as a model, Reservists would continue to receive compensation for the career field or hazardous duty but could also be paid a critical skills bonus for those career fields or skill areas that require additional compensation to meet manning requirements.

This targeted approach is focused on particular needs of the Department and is much less expensive than authorizing special and incentive pays for all eligible Reservists at the full monthly rate. Moreover, a reserve critical skills bonus supports one of the five main goals of the continuum of service—improve flexibility of the compensation system.

Other Special Interest Items

FOREIGN LANGUAGE PROFICIENCY PAY (FLPP)

The Department has found that there are not sufficient personnel with proficiency in some foreign languages to effectively perform its mission. A critical element to meeting the demands for linguists is providing adequate monetary incentives. Overall, the current level of compensation has not provided sufficient incentive to maintain an adequate inventory of linguists to meet existing or projected requirements.

With compensation potentially inadequate within the active force, the application of the 1/30th rule for payment of foreign language proficiency pay to Reserve component members provides little, if any, incentive for them to maintain proficiency in a language skill, particularly since Reservists typically must maintain proficiency on their own time rather than when they are in a duty status.

The statutory limit on FLPP is $300 a month. DoD policy limits the pay to $200 for a career linguist who is qualified in one language. A career linguist who is proficient in more than one language is paid $300. A reserve career linguist qualified in one language receives $26.67 in foreign language proficiency pay for a drill weekend. If the Reservist is qualified in more than one language, the incentive is $40 per drill weekend. Foreign language proficiency pay for members who are not in a billet requiring a language skill starts at $50 per month. For a Reservist, this equates to only $6.67 per drill weekend for maintaining the minimum proficiency level. While having

a pool of Reserve component members proficient in a foreign language is part of the solution to the linguist shortage problem, it is obvious there is very little monetary incentive for Reservists to maintain proficiency in a language.

Among the alternatives being explored is establishing a Reserve Critical Skills Bonus paid as an annual or monthly payment following the member's annual proficiency recertification. Treating this incentive as a bonus rather than a pay would allow full payment to Reserve component members at a rate set by the Department. This approach, combined with other initiatives being considered, could provide the necessary monetary incentive for Guard and Reserve members to dedicate their time to maintaining or increasing their language proficiency, thus expanding the pool of linguists available to meet mission requirements.

INCENTIVE PAY FOR DUTY IN THE POLAR REGIONS

House Report 107-772 requested that the Department, while conducting this study, review the issue of payment of an incentive pay to Guard members who perform frequent and continuous duty on ski equipped aircraft operating in the polar regions. The General Accounting Office (GAO) conducted a similar review. GAO recommended that DoD assess certain factors in determining whether personnel performing polar duty should receive hazardous duty pay. Those factors included: the extreme working conditions that military personnel encounter while performing polar duty, the exposure of military personnel to potential medical hazards related to polar duty, and retention data for military personnel performing polar duty.

Section 615 of the FY 2004 National Defense Authorization Act added duty involving ski-equipped aircraft on Antarctica or the Arctic Icepack to the category list of duties that qualify for hazardous duty pay.

SELECTED RESERVE PERSONNEL ASSIGNED TO CERTAIN HIGH PRIORITY UNITS

Section 308d of title 37, U.S.C., authorizes a $10 per drill incentive for enlisted members of the Selected Reserve assigned to certain high priority units. Since the inception of this incentive, the Naval Reserve has used it to meet manning requirements on their Naval Reserve Force (NRF) ships. The Naval Reserve has used this incentive extensively to attract enlisted Naval Reservists to fill billets on NRF ships due to the homeporting limitation of NRF ships, coupled with the demanding nature of the shipboard assignment.

The Navy believes that expanding eligibility to include officers would enable them to also attract officers to serve in billets in these high priority units that are typically located far from where members reside. The other Reserve components also expressed an interest in using this authority to address shortfalls in critical units, but like the Navy, would like to be able to use this incentive for the officer corps as well. Finally, as part of the deliberations concerning this incentive, it was suggested that the limited amount currently authorized for this incentive may not be sufficient. However, no data was provided to build the business case for increasing the amount of the incentive pay. But, the idea of expanding the eligibility criteria for this incentive to include officers has merit.

Bonuses

While bonuses have been effective in attracting and retaining enlisted Reservists in skills that are critically short, the retention bonus in particular is very restrictive. Officers, with the exception of those officers in the health professions, are only eligible for an affiliation bonus, which provides only a nominal incentive for agreeing to affiliate with the Guard or Reserve. Several options exist to help the components meet manpower and skill shortfalls. One alternative might be to expand the eligibility criteria of the current enlisted retention bonus to include officers. Another option might be to request specific bonus authorities for particular officer skill shortages. A third alternative might be to consolidate various bonus authorities into a single bonus—much like the critical skills retention bonus that is now available for active duty personnel.

SELECTED RESERVE OFFICER AFFILIATION BONUS

One of the most significant officer recruiting challenges the Reserve components face, particularly in the Marine Corps Reserve, is the ability to man units with qualified company grade officers. The Marine Corps Reserve recruits most of their officers from the ranks of officers who have first served on active duty. While this practice has provided the Marine Corps Reserve with trained officers who have proven experience, knowledge and leadership abilities, a smaller active duty force has reduced the number of officers available to affiliate with the Marine Corps Reserve. As a result, the Marine Corps Reserve in particular now has a shortage of company grade officers (Second Lieutenant to Captain). The Marine Corps Reserve is exploring methods to increase accessions of company grade officers through recruiting efforts, command focus that emphasizes reserve affiliation upon leaving active duty, the use of the affiliation bonus for Reserve officers, and Reserve officer commissioning programs for qualified enlisted Selected Reserve Marines. The shortage of officers with prior active duty experience is similarly acute in the other Reserve components.

The affiliation bonus under section 308e of title 37, U.S.C., is currently available only to members with a remaining military service obligation. Moreover, the incentive is limited to a payment of only $50 per month for up to 18 months. While the affiliation bonus can be used for most company grade officers, it is not a tool that can be applied to officers who have completed their military service obligation or who do not have a reserve service obligation when they separate from active duty. Additionally, the amount authorized does not appear to be sufficient to induce qualified officers to affiliate with the Guard or Reserve.

An alternative that is currently being explored is establishing an accession/ affiliation bonus for officers who agree to serve in the Selected Reserve. This bonus would be targeted at occupational specialties and units that are critically undermanned and provide an incentive sufficient to help correct these readiness shortfalls. Since this would be a discretionary authority, it could provide an economic solution to the company grade officer-manning problem.

CRITICAL SKILLS BONUS

Public Law 106-398 provided a broad authority for a retention bonus for officer and enlisted personnel in critical skill areas who agree to serve on active duty. The bonus may be paid more than once, with a maximum of $200,000 for the member during the course of his or her career. This bonus enables the Services to react quickly to emerging or potential skill shortages, and is an effective retention tool.

In contrast, the bonus authority available to the Reserve components to address manning and critical shortfalls in the Selected Reserve is limited. The Selected Reserve enlistment bonus provides for a bonus of up to $8,000 for an individual who agrees to serve in the Selected Reserve. The bonus for reenlistment in the Selected Reserve provides for a maximum payment of $5,000 for a six-year reenlistment or a total of $4,500 for two back-to-back three-year reenlistments. A Reservist who reenlists for six years with a bonus is not eligible for subsequent reenlistment bonuses, and a Reservist who fails to immediately reenlist at the completion of the first three-year bonus obligation, or has completed the second three-year enlistment, is not eligible for additional reenlistment bonuses. Finally the bonus is limited to enlisted members with less than 14 years of total military service. The prior service enlistment bonus operates under the same restrictions as the reenlistment bonus, except the amounts were recently increased to $8,000 and $7,500 respectively. While the Reserve components use these valuable tools to help them meet Selected Reserve manning requirements, some statutory limitations constrain the ability of the Reserve components to meet certain mission critical skill shortages. Moreover, the only bonus available for officers, with the exception of officers in certain health care professions, is the affiliation bonus.

Authorizing a critical skills bonus for members of the Selected Reserve would enable the components to respond quickly to projected shortages and react quickly to emerging manpower and skill shortages. While the active duty bonus targets retention, a similar Selected Reserve bonus could target affiliation with a unit or position in the Selected Reserve, as well as provide a retention incentive for remaining in a critically undermanned skill in the Selected Reserve. This may be a more cost-effective approach of addressing shortages than eliminating the 1/30th rule.

Examples of where this type of bonus authority could be effectively applied today in the Selected Reserve include medical corpsmen, pararescue, linguists, civil affairs and flight engineers. Similarly, there are also critical skills in the officer corps that are short or projected to be short. Critical officer skill shortages exist in intelligence specialties and engineers. An example of a foreseeable shortage is in the Nurse Corps. While current staffing is sufficient, there is a growing national shortage of nurses, which, in the not too distant future, is projected to affect manning in the Reserve components. Also, there are other highly technical skill areas in which the military is having difficulty retaining members, such as information technology (IT). The Reserve components are an ideal place for IT professionals since it allows them to pursue their desire for a civilian career while still serving their country.

The current bonus authorities fulfill certain niche needs. However, consolidating the existing bonus authorities into a single, flexible bonus for service in the Selected Reserve may enable the components to quickly and effectively address emerging manning shortfalls.

Montgomery GI Bill

As a topic specifically identified for study, the Montgomery GI Bill for the Selected Reserve (MGIB–SR) was reviewed to determine if the educational assistance provided under this program is meeting the needs of the Reserve components, particularly in light of the increased use of the Guard and Reserve over the past 13 years. An issue that is often raised is the comparison of the level of benefits provided under the MGIB–SR to the level of benefits available to members who are eligible for educational assistance under the Montgomery GI Bill for active duty members. This has become a more prominent issue because of the significant increases in the educational benefit levels recently authorized for the active duty Montgomery GI Bill program. Since the benefit levels for the MGIB–SR have increased only at the rate specified in law, the question has been asked about the need for additional, corresponding increases in the benefit levels for participants in the Montgomery GI Bill for the Selected Reserve. But ultimately the question must be: is the Montgomery GI Bill for the Selected Reserve meeting the needs of the Reserve components at the current benefit levels? To answer that question, one must first be familiar with the two programs.

The Two Montgomery GI Bill Programs

Service members can qualify for educational assistance through two Montgomery GI Bill Programs—one based on active service and another based on continued service in the Selected Reserve. The program for active duty service members is codified in chapter 30 of title 38, United States Code (U.S.C.), and provides benefits for members who elect to participate in the program by contributing $1,200 through basic pay reductions during the first twelve months of active duty, and serve continuously on active duty for at least three years in the case of a member whose obligated period of active duty is for three years or more, or in the case of a member whose obligated period of active duty is for less than three years, serving continuously on active duty for at least two years. When either of these requirements has been met, the member is then eligible to use MGIB benefits. With some exceptions, the member is eligible to use the educational benefits up to 10 years after the member was last discharged or released from active duty.

These requirements illustrate the primary purpose of the active duty program, which is to provide educational assistance for members readjusting to civilian life after they separate from military service, and to enhance and make service in the armed forces attractive—a recruiting tool. Both programs also have a feature designed to assist the Services in filling critical skill area shortfalls by providing

benefits that are in addition to the basic MGIB benefits for service members who agree to enlist or reenlist in a skill designated as critically undermanned. This benefit payment is known as a "kicker." Finally, in a recent enhancement, the active duty program offers the opportunity for a service member to make an additional contribution of up to $600 for a maximum additional benefit amount of $5,400. With the exception of the kicker benefit, the Montgomery GI Bill program for active duty service is funded and administered by the Department of Veterans Affairs as a veteran's benefit.

In contrast, the Montgomery GI Bill Program for the Selected Reserve is codified in chapter 1606 of title 10, U.S.C., and provides education benefits to members who agree to serve for at least six years in the Selected Reserve. Unlike participants in the active duty program, the member is not required to contribute to the program and can begin using benefits immediately upon completion of initial skill training. Like the active duty program, the MGIB-SR also offers a kicker for members who agree to serve in a critically undermanned skill. Guard and Reserve members remain eligible for benefits for up to 14 years provided they continue to serve in the Selected Reserve. For Reservists who participate in the Selected Reserve kicker program, the reservist must serve in a critical skill or unit during the initial six-year service obligation. After completing the initial six-year service obligation in the critical skill or unit, the reservist retains eligibility for the kicker benefit regardless of specialty or unit assignment. However, the reservist must remain eligible for the MGIB-SR basic benefit in order to receive the kicker benefit. These requirements illustrate that the Montgomery GI Bill program for the Selected Reserve serves both as a recruiting incentive and a powerful retention program because of the requirement for the member to continue to participate in the Selected Reserve in order to use the benefit.

Benefit Levels

At the inception of the Selected Reserve Program in July 1985, the relationship of Selected Reserve benefits to those provided under the program for active duty service was 47 percent. That is, the benefit level for a full-time student under the Selected Reserve program was 47 percent of the benefit level for a full-time student who earned benefits under the active duty program. This relationship was maintained, within two percentage points until November 2000, when Congress significantly increased the benefits provided under the active duty program. The rapid increase in the benefit levels for the active duty program benefits, with no corresponding increase in the Selected Reserve program, has dramatically changed the benefit relationship between the two programs. By October 2003, the benefit level for the Selected Reserve program is projected to be 28 percent of the benefit level provided under the active duty program.

Cost to Restore the Benefit Relationship Between the Two Programs

Consideration has been given to restoring the historical benefit relation between the two Montgomery GI Bill programs. The Department projects that an increase in educational assistance benefits for the Montgomery GI Bill for the Selected Reserve to approximately 48 percent of the active duty benefit level would increase utilization of the program by 28 percent in 2004 and up to 95 percent by 2013, depending on the Reserve component. The combination of higher benefit payments and increased utilization would increase outlays by $154M in Fiscal Year 2005 and total $5B through Fiscal Year 2014.

Should the Benefit Level be Increased?

While the Department acknowledges that the cost to obtain a post-secondary education has increased, the benefit level provided under the Montgomery GI Bill for the Selected Reserve is sufficient to meet the current recruiting and retention needs of the Reserve components. Thus, the Department has not requested, nor can it justify increasing benefit levels beyond those already established in law for the MGIB–SR program.

However, the Department continues to closely monitor recruiting and retention trends within each Reserve component and conducts surveys to help predict the retention intentions of Reservists, particularly with the surge in employment of Guard and Reserve members to support the Global War on Terrorism. If early warning indicators show that recruiting and retention are becoming a problem and it appears that increasing the MGIB-SR benefit levels will help sustain recruiting and retention at the desired levels, increases in the benefit level may be considered.

Mobilized Reservists and the Active Duty Program

As part of the MGIB review, the Department examined the active duty program from the perspective of mobilized Reservists possibly gaining eligibility for program benefits for active duty service. As previously described, a member has met the active duty service requirement if his or her initial period of active duty is for less than three years and the member serves at least two years of continuous active duty. The law also allows a member who is discharged or released from active duty for the convenience of Government, and has completed at least 20 months of active duty, or for other specified reasons, to qualify for active duty program benefits. It should be noted however, that the same period of service cannot be used to gain eligibility for both programs. Therefore, reservists who are still within their initial six-year MGIB-SR service obligation while mobilized and enroll in the MGIB active duty program must obligate for additional service in the Selected Reserve in order to retain eligibility for benefits under the MGIB-SR program.

The law also provides for in-service enrollment in the active duty Montgomery GI Bill program for a member who has previously not made a Montgomery GI Bill program election. To qualify under this provision, the member must complete at least two years of continuous active duty. The member may then receive educational assistance provided he or she continues to serve on active duty or participates satisfactorily in the Selected Reserve.

To minimize the impact of mobilization on Guard and Reserve members, the Department established a policy to use Reserve component personnel only as long as mission requirements dictate. This judicious use policy results in some Reservists being released short of meeting the active duty Montgomery GI Bill program eligibility requirements. But because the mobilized Reservist is not serving on his or her initial period of active duty, the 20-month exception does not apply, and there is no similar 20-month exception under the in-service provision.

There may be several alternatives that could provide mobilized Reservists with the opportunity to attain eligibility for the active duty (or an active duty-like) benefit. One might be to provide a 20-month exception under the in-service program. Judicious use of Guard and Reserve members is a valid and appropriate principle. So a second option might be to allow Guard and Reserve members to use cumulative periods of active duty served in support of a contingency operation to gain eligibility for the active duty MGIB program. A third alternative may be to recognize that the way the Guard and Reserve are being used does not necessarily fit the program parameters of the current active duty program and a hybrid benefit, with its own eligibility criteria and benefit level, may be in order.

Before pursuing any of these alternatives, consultation with the Department of Veterans Affairs (DVA) is required. Any program changes must be thoroughly assessed to determine policy implications and funding impacts. The Department plans to enter into a dialog with DVA to consider these options and others that may be more appropriate and effective.

Housing Allowance

Basic Allowance For Housing (BAH)

Regular military compensation (RMC) consists of basic pay, basic allowance for housing, basic allowance for subsistence and the Federal tax advantage accruing from allowances since they are not subject to Federal income tax. In reviewing the elements of RMC, the only component of that compensation with a marked disparity between the entitlements for Regular members and Reserve component members is found in the basic allowance for housing.

Evolution of the Housing Allowance

Prior to 1980, members who were not provided government quarters received a Basic Allowance for Quarters (BAQ). This allowance was paid at a specified rate based on (1) the member's pay grade and (2) whether or not the member had dependents. There was no distinction between an active duty member and a Reserve component member performing active duty. Whether the Reservist was on active duty for a week or a month, the Reservist received the same housing allowance as an active duty member. Even in 1980, when the Variable Housing Allowance (VHA) was first established to provide an additional allowance to members who resided in high cost of living areas, Reservists were eligible for VHA regardless of the number of days they served on active duty. However, the statute that authorized VHA was amended in 1983 to authorize VHA for Reserve component members only when they were on active duty for 140 days or more. This change was based on several factors, but primarily it was a cost savings measure for the Federal Government. The assumptions at the time were that:

- Reservists usually perform their duties close to their home,
- Reservists rarely experienced a financial loss for duty periods of less than 140 days, and
- the majority of training schools for reservists were 20 weeks or less.

CONVERSION TO A SINGLE HOUSING ALLOWANCE

In 1998, BAQ and VHA were combined into a single entitlement—Basic Allowance for Housing—to achieve efficiency and equity. Efficiency was gained by having adjustments to the housing allowance tied to the cost of housing, rather than the percent of the annual adjustment to basic pay. Equity was achieved by making the portion of the housing cost paid by the member (the absorption or out-of-pocket costs) uniform regardless of the service member's duty location.

BAH AND THE 140-DAY THRESHOLD

When the law was amended to authorize a single housing allowance, the 140-day VHA threshold was retained with respect to payment of the new allowance for Reserve component members. Under current law, the Secretary of Defense has the authority to establish the housing allowance rate for Reserve component members who are on active duty for less than 140 days, unless the call to active duty is in support of a contingency operation. The housing allowance that is authorized is essentially the old BAQ rate, which is adjusted annually. This allowance is commonly known as BAH II. When compared to the average BAH rate for all grades, with or without dependents, the average BAH II rate is currently about $400 per month less.

There is one exception to the 140-day threshold that was enacted by section 633 Public Law 102-190, Dec 5, 1991, 105 STAT. 1380 (National Defense Authorization Act for Fiscal Years 1992 and 1993) in response to the mobilization of Reserve component members for the Persian Gulf War. This exception authorized payment of VHA for a Reserve component member under a call or order to active duty in support of a contingency operation. When the BAQ and VHA provisions were combined to provide for BAH, a similar exception was included in the amendments to permit Reserve component members on active duty in support of a contingency operation to be paid BAH, rather than BAH II, regardless of the number of days specified in their orders.

When the 140-day threshold was established 20 years ago, Reservists were employed in a significantly different manner than they are today. Over the past decade, Reserve component members have become an integral part of most operations and missions, and are often called upon to serve on active duty for varying lengths of time. But, cost is still the dominant consideration with respect to the housing allowance paid to Reservists. The Department projects that it would cost $93M annually to reduce the BAH II threshold to 30 days. To completely eliminate the 140-day threshold, it would cost $162M annually. Ideally, as a matter of equity, we would eliminate the 140-day threshold and simply pay Reservists BAH, but the Department would need to fund such a change and balance this goal

against other competing requirements. Reducing the threshold for payment of BAH, rather than BAH II, to no more than 30 days may be a more viable option.

BAH AND THE RESERVIST WITHOUT DEPENDENTS

Reserve component members without dependents are not authorized a housing allowance if they are provided government quarters while serving on active duty. This is appropriate if they have been authorized to move their household goods at government expense. But because Reservists are typically ordered to active duty for short periods, it is not practical for them to move out of an apartment or house, or sell their house since they will be returning to that residence shortly. Reservists without dependents are essentially in the same position as Reservists with dependents who are provided temporary government quarters for the member at their temporary duty location. They both must maintain their civilian residence, but only the Reservist with dependents receives a housing allowance. However, there is one exception. Reserve component members without dependents who are ordered to active duty in support of a contingency operation may not be denied a housing allowance if they are responsible for rent or mortgage payments. This is an appropriate exception and prevents them from absorbing their entire housing expense out-of-pocket. It may be appropriate to extend this exception to Reservists without dependents who are serving on active duty other than in support of a contingency operation and not authorized to move at government expense. The Department will consider if an amendment to the governing statute to address this situation is appropriate as part of the next Unified Legislation and Budgeting cycle.

HOUSING FOR MOBILIZED RESERVISTS

The mobilization of Reserve component members often means assigning them to a duty location away from where they normally reside. Recognizing the temporary nature of mobilization (even though it may be for up to 24 months), the Department's mobilization personnel and pay policy specifies retaining Reservists in a temporary duty status—rather than issuing permanent change of station orders—unless a permanent change of station is more advantageous to the Department and the member. Typically, Reservists do not move their families when they are mobilized since the vast majority of mobilized Guard and Reserve members will return to the location where they resided before the mobilization. Moreover, they do not want to uproot their families. Thus, retaining the member in a temporary duty status is appropriate. To help cover the additional expenses of living away from their permanent residence—lodging, meals and incidental expenses—Reservists are entitled to per-diem if they are in a temporary duty status.

Unlike the mobilization for the Persian Gulf War and subsequent Presidential call-ups where Reservists generally served for about 180 days, Reservists serving in support of the Global War on Terrorism are generally serving for one year with a few extended into a second year. The Global War on Terrorism is expected to continue for several years and the Department anticipates that Guard and Reserve members will continue to be called upon to support this effort. Per-diem, especially for housing, can be costly to the Services for these extended periods of temporary duty.

There are several possible options that may help to minimize the cost to the government. First, when commands know that they will be augmented with mobilized Reservists, they can contract for lodging if quarters are not available on the post or base. The command may be able to procure housing at cheaper rates than if the individual is required to find his or her own living accommodations, which would save the government money. Another option is to obtain lodging on a weekly or monthly basis at a cost below the maximum daily lodging rate.

A third option may be to modify the authority found in section 403(d) of title 37, United States Code, which authorizes a family separation housing allowance. This section authorizes a housing allowance at the rate for members without dependents for the area where the member is assigned, if the member is on permanent duty and is not authorized to move his or her dependents at government expense. This provision could be applied to mobilized Reservists with dependents if they are issued permanent change of station orders. Expanding the authority to include Reserve component members without dependents who are called to active duty in support of a contingency operation is another alternative.

A related issue was resolved with passage of Section 635 of The National Defense Authorization Act for Fiscal Year 2004. This section provides the Secretary of the Military Department may reimburse a member, who has been ordered to temporary duty for more than 30 days, for their lodging expenses while in a leave status. This will particularly benefit Reservists on extended temporary duty who accrue considerable leave and often want to take that leave to return home to be with family and friends, and attend to personal affairs. Until passage of the Act, Reservists who were not willing to move out of their temporary quarters had to absorb the full cost of this lodging while on leave.

Inactive Duty Compensation

The recent Department of Defense report on *Reserve Component Contributions to National Defense* called for a paradigm change that would facilitate participation of Reserve component members at varying levels and make it easier for the combatant commanders and Services to employ Guard and Reserve members. One aspect of the continuum of service concept focuses extensively on the individual and how to make it easier for service members to vary their level of participation—creating a seamless flow between the Active and Reserve components, and facilitating varying levels of participation. Another aspect of the continuum of service is to simplify the rules for accessing, employing and separating Reservists. The current system of duty statuses for employing Reserve component members is ineffective and does not support either of these continuum of service goals. There are 32 different duty statuses and each Service has variations of those 32 duty statuses, which only adds to the confusion.

In their simplest form, the duty statuses can be divided into three categories: active duty, inactive duty and full-time National Guard duty. This is unlike the Active component, which has one duty status—active duty. One objective for implementing the continuum of service is to streamline the duty status system. Full-time National Guard duty is the most appropriate and effective way for members of the Army National Guard and Air National Guard to prepare for their federal missions and must be retained. However, a fundamental change could be made by transitioning to more of an active duty system for federal duty performed by all Reserve component members. This is not to say that inactive duty does not have a place in the reserve duty system. Virtual training and virtual duty are ideally suited for inactive duty. That is, training performed by the member through distributed learning or when the member performs defense missions, but is not under direct military control or supervision—telecommuting. But the traditional drill weekend could just as easily and just as effectively be performed in an active duty status. This would eliminate the perception, and often the reality, of the Reserve force as nothing more than an hourly workforce—work four hours and get paid, or work in hourly increments over the course of several days or weeks until four hours has been accumulated and receive pay for the equivalent of one drill.

The Origin of Inactive Duty

Inactive duty can be traced back to the Militia Act of 1792 (May 8, 1792), which established the Uniformed Militia. The Act prescribed that all male citizens between the ages of 18 and 45 were effectively enrolled in the militia and were required to appear, properly armed and equipped, whenever called out to exercise or into service.

The National Defense Act of 1916 authorized for the first time the use of federal funds for payment of inactive duty training, and the Act of June 4, 1920, first set the rate of "drill pay" at 1/30th of basic pay for drills of not less than 1½ hours. However, there is no evidence that Congress intended to equate the pay for one drill to one day's pay.

In 1930, following a ruling by the Comptroller General that multiple drills in a single day were permissible, the Navy amended regulations to permit as many as three drills to be performed in a single day. But the Judge Advocate of the Army held for many years that it was legally objectionable to pay more than one drill in a single calendar day. The debate over multiple drills was settled by the Career Compensation Act of 1949, after the Army raised the issue of multiple drills during testimony and proposed language that would make it absolutely clear that no more than 1/30th of one month's pay could be paid for drills performed in a single day. The bill was initially amended accordingly, but three days later the amendment was rescinded after further discussion, including a joint Navy-Air Force memorandum urging the committee not to adopt the amendment.

A DoD policy directive of May 2, 1955, authorized multiple drills of not less than 4 hours within one calendar day. That directive was revised on May 5, 1956, to limit multiple drills to two per day. Today, the law specifies that in order to be compensated for inactive duty, at least two hours of duty must be performed. The DoD Directive on this subject specifies that a minimum of four hours of duty must be performed in order to receive compensation. However, both the law and DoD policy are silent on the issue of requiring the duty to be performed in the same calendar day in order to receive compensation.

AN ACTIVE DUTY SYSTEM

Transitioning to a system in which—like active duty members—a day of duty is a day of duty would make it much easier to employ Guard and Reserve members. It would also help reduce the frustration experienced by combatant commanders when they want to employ Reserve component members. However, such a change should not be undertaken if it means reducing the level of compensation and retirement credit Reservists receive under the current systems. As part of this review, the Department developed several alternatives that might make such a transition possible. This concept is still in the developmental stages, and further, detailed analysis is needed to compare all aspects of Reserve service under a predominately active duty system versus the current active duty-inactive duty system. Also, further study is needed to uncover any possible unintended consequences.

But this concept does have some merit in that it may provide an opportunity to eliminate or at least reduce some concerns with the current compensation system. The goal is to operate under an active duty system, but retain the level of compensation Reservists currently receive when performing inactive duty. There are two approaches that could be taken to transition from an inactive duty system—maintain the same level of gross pay or maintain the same level of net pay. Why the two approaches? Compensation for inactive duty is all taxable income, while allowances paid as part of the active duty pay system are not taxable. This means that a member on active duty pays less in income tax and less is withheld from his or her pay for the Federal Insurance Contributions Act (FICA), thus increasing net pay.

THE TAX ADVANTAGE

Regardless of which alternative is used, there is some tax advantage gained or savings accrued to the government because allowances are not taxable income. The tax advantages could be used to offset the travel entitlement that would likely result from transforming to an active duty system. Under the gross pay concept, the only tax advantage realized is from the reduced FICA contributions by the Department since the allowances are not subject to FICA. Under the net pay model, a greater tax advantage is realized because of the reduced FICA contributions required from the employer and employee as well as the advantage from the housing and subsistence allowances, which are not subject to income tax. Here is how each alternative might work.

GROSS PAY ALTERNATIVE

Under the gross pay alternative, the Reservist's gross pay would remain the same. The difference in the gross pay for one day of active duty—pay and allowances, and two drill periods—the equivalent of two days of basic pay, would be made up with an incentive-type pay. The incentive pay would be an entitlement, essentially for Reserve participation, that would maintain the Reservist at the same level of gross pay the Reservist received for performing two drills. The net effect for the Reservist is a pay raise. Since the allowances are not taxed, a larger portion of the gross pay goes to the Reservist in their take-home pay. But this alternative provides very limited funds that could be applied to a possible new travel entitlement. The only tax advantage realized is from the employer FICA that is not paid on the allowance portion of the pay. The charts below (figures 3 and 4) provide two examples that depict the effect of the gross pay concept, showing its effect on both gross pay and net pay.

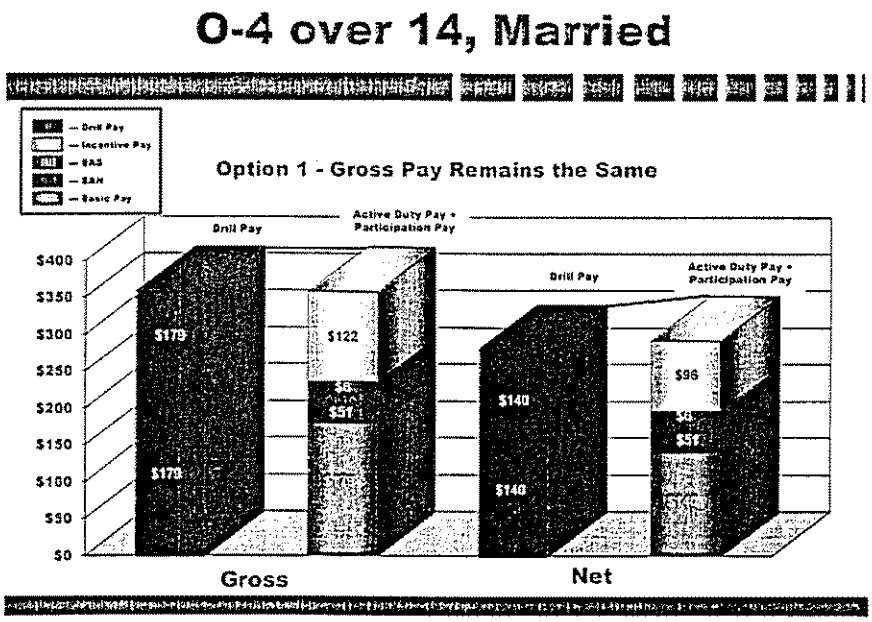

Figure 3

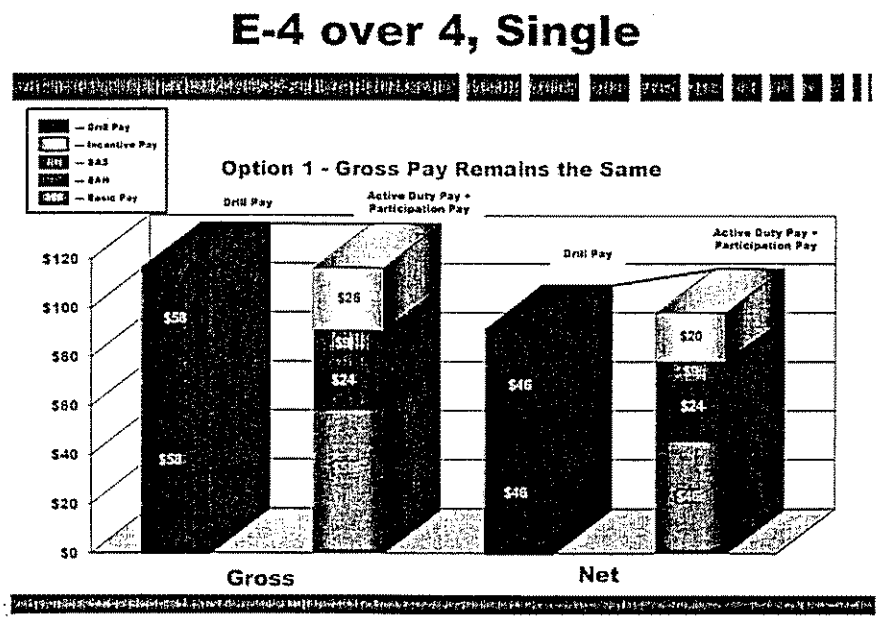

Figure 4

NET PAY ALTERNATIVE

Under this alternative, the Reservist's net pay under the active duty system would remain the same as his or her net pay under the drill system. This results in an increase in funds that could be applied to a possible new travel entitlement under the active duty system. The tax advantage is realized from the non-taxable allowances and reduced employer and employee FICA payments. In this alternative, the gross pay is less, reflecting the greater tax advantage of this option. While the income tax savings depend on the tax bracket of the individual, there are savings in all cases. The charts below (figures 5 and 6) depict the same two examples used previously, but use the net pay model, and demonstrate the effect on both gross pay and net pay. Although these charts reflect that the net pay under the active duty system and the drill system are equal, most members will actually realize an increase in net pay—unless the Reservist has no significant outside income and resides in a state with no state income tax—since most would likely be in a higher tax bracket than assumed here and tax savings based on state income tax have not been factored into the calculation.

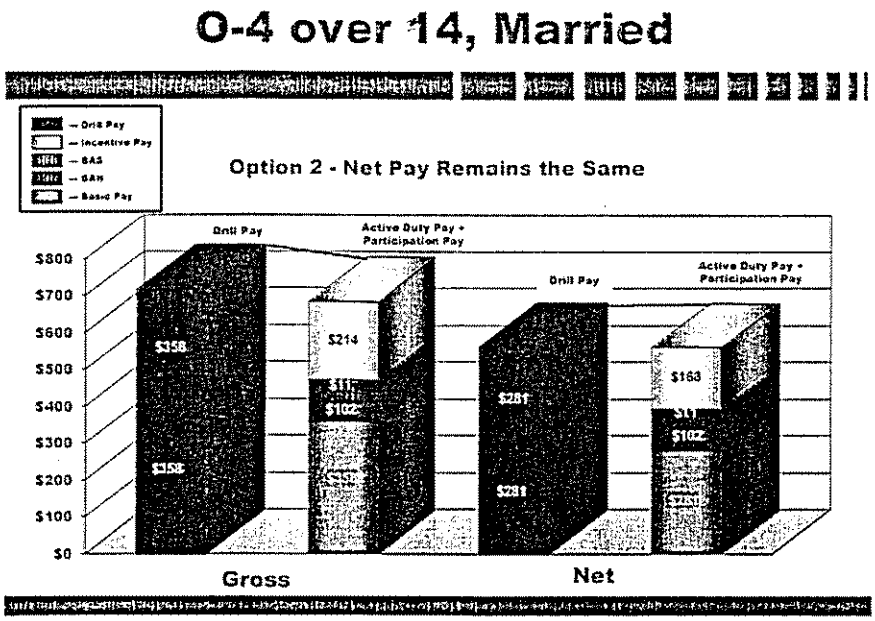

Figure 5

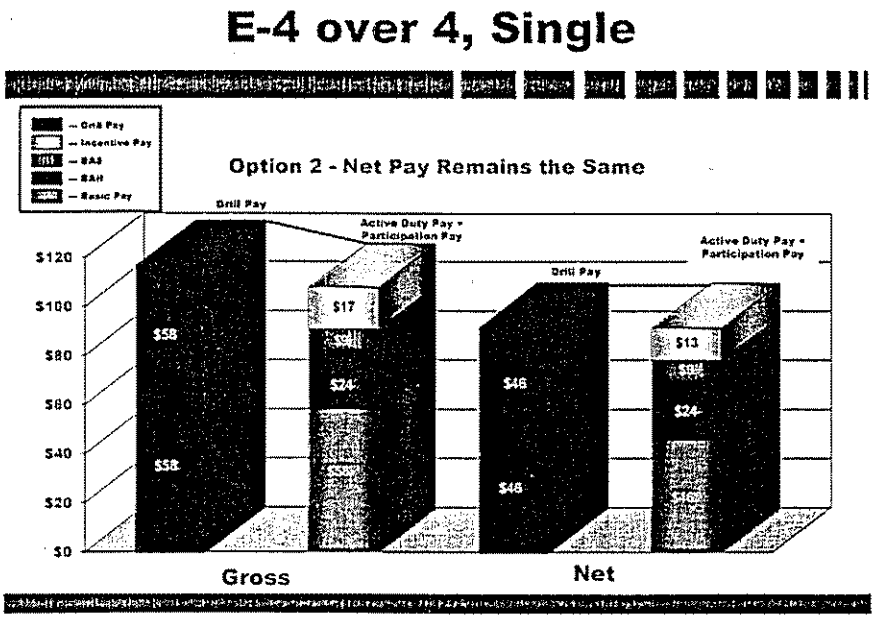

Figure 6

LEVERAGING THE TAX ADVANTAGE

As previously stated, the tax advantage can be applied to pay for the travel entitlement that would likely result from transitioning to an active duty system. This could also set the stage for addressing other compensation inequities such as BAH II, the housing allowance paid to Reservists on active duty for less than 140 days. But, it should be noted that the tax advantages under this concept do not yield enough savings to effect changes in all areas where there may be inequities.

Aside from implementing changes to inactive duty in order to possibly provide reimbursement for travel to the drill site, Congress has introduced Bills in the past that would restore the pre-1986 tax deductions for expenses associated with reserve duty. While the Department defers to the Department of Treasury on such matters, the Department has not objected to those Bills.

THE NEXT STEP

There are still many details that must be studied before the Department pursues a change of this magnitude. But there are clearly benefits that can be reaped from such a change. While this concept is still in the developmental stages, it supports several goals of the continuum of service concept and warrants further study. Including a discussion of this concept in this report is intended to open a dialog on possible changes of this nature. It also makes clear the Department's motivation is not to reap savings at the expense of Reservists, but rather to maintain the same level of compensation while transitioning to a compensation system that parallels the active duty system and returns the savings to Reservists by correcting other compensation inequities.

Income Protection

Income protection or replacement of "lost income" has again surfaced as an issue with the mobilization of large numbers of Guard and Reserve members for the Global War on Terrorism. Recent survey data reveals that just over one third of mobilized Reservists experience a reduction in total family income. For those families that do experience a reduction in total family income, about 75 percent reported their monthly reduction in income is $2,000 or less. Although the Department has been mobilizing Guard and Reserve members almost continuously since 1995, income loss has not been a major issue until the most recent mobilizations. Most likely, this is because the call-ups preceding the most recent mobilization have been relatively small and generally for a more limited duration. This allowed for a more tailored mobilization process, which could accommodate the needs and circumstances of individual Reservists. But the fact that involuntary call-ups have been routinely taking place for over twelve years should have alerted Reservists to the potential for being mobilized and the need to plan accordingly.

This issue first surfaced during the 1991 Persian Gulf War when nearly two-thirds of the 250,000 Reservists mobilized for Operations Desert Shield and Desert Storm reportedly suffered economic loss as a result of one or more of the following:

- Military pay being less than civilian income
- Additional expenses incurred by the member and his/her family as a result of activation
- In some cases, continuing loss of income after release from active duty due to erosion of a civilian business or professional practice

Following the Persian Gulf War, the Department addressed this problem by proposing and Congress passing the Ready Reserve Mobilization Income Insurance Program. This program, which became effective on October 1, 1996, was designed as a voluntary, self-funded insurance program that would provide a measure of economic security to Reservists while mobilized. However, the program experienced difficulties from the beginning because of excessive adverse selection that resulted in an immediate demand for benefit payments and minimal funds from which to pay those claims. Because of the immediate insolvency of the program and other design flaws, the program was terminated in November 1998. While there has been periodic interest by private insurance companies to develop an income protection plan for mobilized Reservists, that interest waned following the terrorist attacks of September 11th and the subsequent mobilization of a significant number of Reservists.

The decrease in the number of Reservists who now may experience a loss of income when mobilized compared to the 1991 Persian Gulf War period may—to some degree—be attributed to the significant increases in military pay authorized by Congress in recent years. Other factors that may also help offset differences between military pay and allowances and civilian income include contingency authorities enacted after the Persian Gulf War and policies established by the Department. These changes include:

- Paying the housing allowance based on the location where the Reservist maintains his or her primary residence rather than the duty location
- Authorizing Reservists without dependents a housing allowance even though they are provided government quarters, if the Reservist is still responsible for rent or mortgage payments
- Retaining mobilized Reservists in a temporary duty status, thus entitling them to per diem to help offset expenses associated with being away from home

Also, in order to promote the judicious and prudent use of the Reserve components, the Department is undertaking a series of actions to rebalance the force. One goal of the force rebalancing initiative is to limit the involuntary mobilization of Reservists to not more than one year every six years. This will provide greater predictability for Guard and Reserve members.

While the rebalancing initiative will enable Reservists to better prepare financially for the possibility of mobilization, there will continue to be some Reservists whose military income will be less than their civilian income. In studying this issue, three different approaches that might address the reduction in income experienced by some Reservists were examined.

- The first approach emphasizes financial planning through improved education and training.
- The second approach deals with providing some form of income replacement or subsidy.
- The third approach presents a debt management alternative.

FINANCIAL PLANNING

Just as we require Reservists to prepare a "family care" plan that can be invoked upon mobilization, a financial plan in the event of mobilization is equally important. Providing the training and tools to develop such a plan would help Reservists realistically assess the possible impact that mobilization might have on their financial situation. This approach, combined with a greater degree of predictability with respect to mobilization from a rebalanced force would enable Guard and Reserve members to be better prepared financially for mobilization.

INCOME REPLACEMENT

This approach would—to some degree—make up the difference in earnings. The Ready Reserve Mobilization Income Insurance Program is an example of this approach. If a program could be developed that is fiscally sound, this would be a preferred option under this approach. Another obvious alternative under this approach is for the Department to simply make up the difference between a Reservist's military pay and civilian pay. But, to simply increase the level of direct compensation for Reservists, would send the message to the full-time force that the nation places greater value on its part-time force and is willing to compensate them at a higher rate than the full-time force. An alternative that recognizes the additional burden of deployment for both active duty members and mobilized Reservists is more in keeping with the total force concept. The per diem allowance for lengthy or numerous deployments is a vehicle that could be used, with modifications that were offered by the Department and are currently being considered by the Congress. This would help to address the hardships associated with mobilization and deployment of Reservists, just as it addresses the hardship of deployment for active duty members.

DEBT MANAGEMENT

This approach might use the Servicemembers Civil Relief Act concept as a model. Under this approach, a Reservist who has been involuntarily mobilized and is experiencing difficulty meeting his or her debt payments because of an involuntary call to active duty would have legal standing to negotiate with his or her creditors to adjust payments or possibly defer debt payments during the period of mobilization. The debt period could be extended to equal the period of deferment—a thirty-year loan would in effect become a thirty-one year loan if the Reservist was mobilized for a year. Expanding this concept beyond just personal debt, to also apply to business debts, might be a very attractive and valuable option for Reservists who own a small business or who are in private practice.

THE NEXT STEP

While there have been media reports about mobilized Reservists whose military income is less than their civilian income and Congressional interest in this issue, it does not appear to be significantly affecting retention. Surveys of recently mobilized Reservists suggest that there is only a two-point variance in retention intentions when compared to historical retention rates. Most Reservists want to contribute to the national defense and are willing to maintain their Guard or Reserve affiliation if they are given meaningful work and used only as long as required, even when their circumstances while mobilized are not ideal. Many Reservists also consider the overall benefits of military service when making a decision about continuing to serve in the Guard or Reserve. These factors include: education benefits, commissary and exchange privileges, access to morale, welfare and recreation facilities, and, upon entitlement to retired pay, healthcare benefits for life for themselves and their dependents.

We do not want to repeat the mistakes of the Ready Reserve Mobilization Income Insurance Program and need to assess the various approaches that have been presented in much greater detail. Factors beyond the pure arithmetic calculation of military income versus civilian income need to be considered. Special attention also must be focused on Reservists who are most at risk—those who own a small business or are in private practice. Therefore, before the Department takes any action or makes any recommendations regarding income loss, we plan to contract for an independent, in-depth study on this topic.

Reserve Component Survivor Benefit Plan

As a required topic for this report, the Department studied the Reserve Component Survivor Benefit Plan (RC-SBP). Specifically, the Department looked at the comparability of the RC-SBP program with the Uniformed Services Survivor Benefit Plan (SBP) for members retiring from active duty. The Department also reviewed the overall sufficiency of the RC-SBP.

The SBP applies to Uniformed Services personnel serving on active duty and to Reserve component members upon becoming entitled to retired pay at age 60, unless the member made a previous election to provide an annuity through RC-SBP. Reserve component members must make an RC-SPB election after receiving notification that they have attained eligibility to receive retired pay at age 60, even though they may continue to serve in the Guard or Reserve. This is unlike members who retire from active duty, who do not make an election until the time of their retirement.

The Advent of RC-SPB

Prior to 1978, Reserve component members did not have the opportunity to protect an eligible beneficiary in the event of the member's death prior to becoming entitled to retired pay upon attaining 60 years of age. RC-SBP benefits were first enacted by Public Law 95-397, the Uniformed Services Survivors Benefits Amendments, September 30, 1978. The fundamental design of this plan was to provide an opportunity for members with 20 qualifying years of service for a Reserve retirement to purchase protection for an eligible beneficiary in the event of death prior to reaching age 60 with the resulting entitlement to retired pay, and automatic protection under SBP. A member currently chooses from three options during the 90-day period immediately following notification of eligibility to receive retired pay at age 60:

a) Decline participation and wait until age 60 with the opportunity to then make an election to participate in SBP (if the member dies prior to reaching age 60, no survivor annuity is payable)

b) Elect to provide an annuity to an eligible beneficiary, which begins at either age 60, if the member dies before age 60, or on the date of death, whichever is later

c) Provide an immediate annuity which is payable to an eligible beneficiary upon death of the member

No RC-SBP premiums are paid by the member prior to receipt of retired pay. However, the member and annuitant share the cost of coverage for that period of coverage in the form of an actuarial reduction in both the retired pay while the member is living and the annuity that is paid to the eligible beneficiary.

ACTIVE DUTY DEATH BENEFIT

Historically, the Plans that covered active duty and Reserve component members were very similar in design and administration. That is, until enactment of section 642 of the National Defense Authorization Act for Fiscal Year 2002 (Public Law 107-107, 115 STAT. 1151), which amended section 1448 of title 10, United States Code (U.S.C.), to provide an immediate SBP annuity to the surviving spouse of a member who dies in the line of duty while serving on active duty, regardless of the member's years of service. That member is considered to have retired with a 100 percent disability rating, therefore maximizing the annuity for the surviving spouse.

While the SBP for active duty death benefit covers Guard and Reserve members who die in the line of duty while serving on either active duty or full-time National Guard duty, it does not provide an annuity to the surviving spouse of a Reserve component member who dies while performing inactive duty. This problem was addressed by Congress in section 644 of the National Defense Authorization Act for Fiscal Year 2004 (P.L. 108-136), which amended section 1448(f) of title 10 of the U.S. Code to provide a death benefit for the surviving spouse of a reservist who dies while performing inactive duty training. This new provision certainly recognized that an inequity existed and now provides a benefit to the surviving spouse of a reservist who was not covered under the active duty death benefit. However, a difference still exists in the method for calculating the annuity. The active duty death benefit treats the deceased member as totally disabled at the time of death and uses this as the basis for calculating the annuity for the surviving spouse. The new RC inactive duty death benefit converts the member's total points into years of service to form the basis for calculating the annuity for the surviving spouse. The net effect is that in the vast majority of situations, the annuity provided to the surviving spouse of the reservist who dies while performing inactive duty training will be much smaller than the annuity that would have been provided if the same member had died on active duty. Moreover, if the death is considered sudden (e.g. heart attack) or caused by a job related accident (e.g. accident in the motor pool), the annuity payments will be completely offset by payments from the Department of Veterans Affairs (VA) under the Dependency and Indemnity Compensation (DIC) program in almost all cases.

HIGH 36 MONTH AVERAGE

The change in law to provide an active duty death benefit also revealed a likely defect in the statute with respect to the method of calculating the high 36-month average under section 1407 of title 10, U.S.C., for Reserve component members who are retired with a disability under sections 1201 or 1202 of title 10.

The method required to determine the high 36-months for retired pay purposes affects Reserve component members with a Date of Initial Entry into Military Service on or after September 8, 1980. The law specifies that "active service" as defined in 10 U.S.C. 101(d)(3) must be used when computing this average. "Active service" is defined as "service on active duty or full-time National Guard duty." To compute the high-36 month average for a Reserve component member, only periods of actual active service (annual training, active duty for training, etc.) can be used to determine the average. No inactive duty time can be included in determining the high 36-month average. Because of the periodic nature of reserve service, the computation for most Reservists would reach back years, well beyond the most recent 36 months. Figure 7 compares the active duty death benefit annuity payable to the surviving spouse of a Reserve component major on active duty to the active duty death benefit annuity payable to the surviving spouse of an active duty major using the high 36-month calculation currently required by law.

It appears that this may be an unintended consequence when the law was enacted, since the two other provisions of law requiring the computation of the high-36 for Reserve component members (retirement under chapter 1223, and nonregular service disability retirements under section 1204 or 1205 of title 10) both treat Reservists as if they were on active duty and entitled to pay during the most recent 36 months as a member. This is a much more equitable method to compute the high 36 months, which should also apply to Reservists retiring because of a disability under section 1201 or 1202.

Example of a major currently serving in the Army Reserve

- His only active duty has been annual training and short tours of active duty for training. (Data on the left are the major's ACTUAL periods of active duty).
- His DIEMS is July 17, 1981, therefore he is under the high 36-month retirement system.
- For the purposes of this example, this major was called to active duty on April 30, 2003, and died in the line of duty on May 1, 2003, while serving on active duty.
- The computation on the left shows the active duty death benefit annuity for his spouse under current law.
- The computation on the right shows the active duty death benefit annuity for the spouse of regular officer.

High three computation under 10 U.S.C. section 1407(c)

YEAR	ACTIVE DUTY DAYS	PAY GRADE YEARS OF SERVICE	MONTHLY ACTIVE DUTY PAY	AMOUNT OF PAY
2002	12	O-4/20	5,310.60	2,124.24
2001	5	O-4/20	4,986.60	831.10
2000	11	O-4/19	4,785.90	1,754.83
2000	4	O-3/19	4,139.10	551.88
2000	12	O-3/18	4,139.10	1,655.64
1999	12	O-3/18	3,949.50	1,579.80
1999	28	O-3/17	3,949.50	3,686.20
1998	15	O-3/16	3,812.40	1,906.20
1997	12	O-3/16	3,708.60	1,483.44
1997	5	O-3/15	3,708.60	618.10
1996	102	O-3/15	3,600.60	12,242.04
1996	29	O-3/14	3,600.60	3,480.58
1995	15	O-3/13	3,432.00	1,716.00
1994	13	O-3/12	3,345.00	1,449.50
1993	12	O-2/12	2,488.20	995.28
1993	6	O-2/11	2,488.20	497.64
1992	14	O-2/10	2,399.40	1,119.72
1991	181	O-2/09	2,302.80	13,893.56
1990	59	O-2/09	2,212.20	4,350.66
1990	96	O-2/08	2,212.20	7,079.04
1989	70	O-2/08	2,135.40	4,982.60
1989	14	O-2/07	2,135.40	996.52
1989	212	O-1/07	1,684.50	11,903.80
1988	105	O-1/07	1,618.20	5,663.70
1988	36	O-1/06	1,618.20	1,941.84

1080	TOTAL ACTIVE DUTY DAYS
TOTAL PAY	88,503.91
HIGH-THREE AVG	2,458.44

High three computation under 10 U.S.C. section 1407(d)

YEAR	NUMBER OF MONTHS	PAY GRADE YEARS OF SERVICE	MONTHLY ACTIVE DUTY PAY	AMOUNT OF PAY
2003	4	O-4/21	5,528.40	22,113.60
2002	12	O-4/20	5,310.60	63,727.20
2001	7	O-4/20	4,986.60	34,906.20
2001	5	O-4/19	4,986.60	24,933.00
2000	4.34	O-4/19	4,785.90	20,770.81
2000	3.66	O-3/18	4,139.10	15,149.11

36	TOTAL MONTHS
TOTAL PAY	181,599.91
HIGH-THREE AVG	5,044.44

Surviving spouse of an RC member

Spouse AD Death SBP Annuity	
Member's high 36 BP	$2,458.44
Retired Pay Factor	75%
Spouse Annuity Factor	55%
Monthly SPB Annuity	$1,014.11

Surviving spouse of an AC member

Spouse AD Death SBP Annuity	
Member's high 36 BP	$5,044.44
Retired Pay Factor	75%
Spouse Annuity Factor	55%
Monthly SPB Annuity	$2,080.83

Figure 7

Reserve Retirement

Members of the National Guard and Reserve are making significant contributions to protect national interests as reflected by the increased reliance on Reserve component personnel under the Department's total force policy. This change in the employment of the Reserve component started with the 1991 mobilization for the Persian Gulf War. Integrating the Reserve components into daily military operations and mobilizing Reservists to support contingency operations has heightened awareness of differences in compensation and benefits. One of the most noticeable differences is the age at which Reservists are eligible to receive retired pay. Unlike active duty members who receive retired pay immediately upon retirement, Reservists who retire with a non-regular retirement must wait until they reach age 60.

The committee specifically asked the Department to review this issue. A review of the reserve retirement system is particularly important and timely because of the changing role of the Reserve components. A review by the Department is also prudent since there have been a number of bills introduced in Congress that would, using somewhat different approaches, reduce the age at which reserve retirees could begin receiving retired pay.

There are two aspects that must be considered in any change to the reserve retirement system. The first, and most important, is the potential impact on force management, and second, the cost. Changing the reserve retirement system to allow members to receive retired pay earlier, without a complete understanding of how such changes would affect the behavior of members with respect to retention, may lead to unintended negative consequences for Reservists, the Department, or the Federal government.

Legislative Proposals

Several bills that would amend the age requirement for receipt of retired pay for Reservists have been introduced in the House and Senate.

- The first approach would have the reserve retirement system mirror the active duty system by allowing Reservists to receive retired pay immediately upon retirement after completing 20 qualifying years of service.
- The second approach would lower the retirement age from 60 to 55.

- The third approach would reduce the retirement age in one-year increments for every two years of additional service beyond 20 years. There are two variations of this third approach. One would reduce the age no lower than 55, while the second approach would reduce the age requirement no lower than 53.

PURPOSE OF THE RETIREMENT SYSTEMS

In order to help shape the discussion of possible changes to the reserve retirement system, it would be useful to first understand the purpose for the regular and reserve retirement systems.

Regular Retirement: To ensure that (1) the choice of career service in the armed forces is competitive with reasonably available alternatives, (2) promotion opportunities are kept open for young and able members, (3) some measure of economic security is made available to members after retirement from career military service, and (4) a pool of experienced personnel exists who are subject to recall to active duty during time of war or national emergency.

Reserve Retirement: To provide an incentive for qualified personnel to retain membership and continue training in the Reserve components and thereby provide a pool of skilled, trained, and readily available manpower to augment active duty forces in times of national emergency.

It is easy to see how recruiting (making the choice of military service competitive), keeping promotion opportunities available (retention/force management), and having a pool of experienced personnel available for recall are applicable to the Guard and Reserve in today's environment. But not as obvious may be the economic security aspect. However, there is a connection. While it may not be as significant for Reservists as it is for active duty members, we cannot overlook the fact that most members of the Selected Reserve rely on their reserve pay as part of their family income. And just like active duty members, Reservists experience a reduction in family income when they retire from the Guard or Reserve. While providing an immediate annuity would be costly and might be counterproductive to good force management, a cost neutral alternative that would allow Reservists to receive an immediate or earlier reduced annuity may help some bridge this gap.

Any changes to the retirement systems should be supported by a cost benefit analysis, which provides evidence that revising the reserve retirement system will enhance force management (recruiting, retention and promotion). Moreover, any changes to the system should be the most cost effective to achieve force management objectives and address specific military problems, particularly when such changes would increase the cost to the Department and the Federal government.

FORCE MANAGEMENT

The Department's ability to shape the force is particularly important in the debate about lowering the retirement age for Reservists.

Immediate annuity

The proposals that would provide an immediate annuity could certainly have a positive effect on promotion opportunity for the more junior force. But there might well be a very strong financial incentive for Reservists to retire immediately upon becoming retirement eligible resulting in an unintended loss of experienced personnel. This is particularly true for members who joined the Guard or Reserve after having served for four, or five, or more years on active duty. There is a point at which some members may actually earn more by retiring than if they continue to serve in the Guard or Reserve. The result could be increased recruiting requirements and training costs.

Age 55 annuity

Currently, there is no evidence that the proposals that call for lowering the retirement age to 55 will help shape the force. Most Reservists, who would immediately benefit from such a change, are already retired. However, a change to the system that would serve as a retention incentive for the mid-career force at the point that they make the critical decision whether to stay or get out clearly has merit. Further study is required to determine the effect of simply lowering the retirement age on the retention decision of the mid-career force.

Earlier annuity for additional years of service

The proposals that gradually reduce the retirement age for additional years of service have certain merit and philosophically support the continuum of service concept, but further study is required. While it may serve as a retention incentive, it might also negatively affect promotion opportunities of mid-career personnel. Additionally, changes in the laws governing mandatory separation of officers must also be reviewed in conjunction with this approach. The

proposals that provide retired pay at age 55 for those with 30 years of service would only benefit colonels, Navy captains, general and flag officers, and depending on service policy, some senior enlisted members. The proposals that would further reduce receipt of retired pay to age 53 for those with 34 years of service would, with rare exceptions, only benefit general and flag officers. To make this reward for additional service equitable for all Reserve component members, the current "up or out" statutes should be reviewed, possibly providing the Services with more flexibility.

COST

Immediate annuity

The Department estimates that providing an immediate annuity to Reservists would increase cost to the retired accrual account by $1.6B in the first year and $18B over the next 10 years. Outlays from the United States Treasury are projected to be $3B in the first year and $31B over 10 years. There is also an increase in the cost to the Defense Health Program because of the increase in eligible beneficiaries. It is estimated that the cost would be $650M in the first year rising to $9B over 10 years.

Age 55 annuity

The Department's estimated cost to lower the age requirement to 55 would be $600M in the first year and nearly $6.6B over the next 10 years. In addition, outlays from the United States Treasury are projected to be $1.4B in the first year with total outlays for the first 10 years projected to reach $14B. The increased cost to the Defense Health Program because of the additional eligible beneficiaries is projected to be $300M in the first year, with the 10-year cost reaching nearly $4B.

Earlier annuity for additional years of service

The Department does not have a model that would help predict the behavior of the reserve force to the changes in the reserve retirement system that would provide an earlier annuity based on additional qualifying years of service. Absent such an analytical tool, developing an accurate cost estimate is extremely difficult. As described below, the Department has contracted for the development of the analytical tools that will determine the effect that various changes to the reserve retirement system might have on the force. This will enable the Department to project potential costs.

INDEPENDENT CONTRACTED STUDY

To fully determine the effects any changes to the reserve retirement system would have on the force, the Department needs a model that will help predict the behavior of the force to possible changes. The Department has contracted with RAND, a Federally Funded Research and Development Center, to conduct a detailed study of the reserve retirement system, which includes the requirement to develop such a model. RAND has completed the first year of a two-year study of the reserve retirement system. Not only will the study provide the analytical tools to predict behavior, it will also evaluate various options that include providing retired pay at an earlier age. But absent the appropriate analysis, caution must be exercised in making any changes to the reserve retirement system. Even with a cost neutral change to the system, it would be prudent to be able to first predict the effects on the force to determine if force management is enhanced.

EARLIER RETIREMENT FOR CONTINGENCY SERVICE

While the Department would like to proceed with caution with respect to any changes to the reserve retirement system, one alternative that is worth considering might be to reduce the age for receipt of retired pay by one year for each year a Guard and Reserve member has been called to duty in support of a contingency operation. Under this approach, Guard and Reserve members would receive a month for month reduction in the retirement age requirement for each month served in support of a contingency operation. For example, a Reservist who has been mobilized or served voluntarily to support the Global War on Terrorism for one year would be able to receive retired pay at age 59. And a Reservist who has been extended or volunteers for a second year would be eligible to receive retired pay at age 58, if the member completes the second year.

However, care must be taken that changes to the retirement system are equitable across the force and do not disadvantage Reservists who have committed to and completed a career in the Guard or Reserve but may not have been mobilized during their career. To offer an enhanced retirement for only those who have been mobilized may be viewed as an inequity by those who have neither been mobilized nor served voluntarily in support of a contingency operation simply because they are in a skill area that was not required for those operations.

Further study is needed to determine the effect on the force and project the cost of this option. An analysis of this concept will be included in the on-going study of the reserve retirement system.

SUMMARY – THE NEXT STEPS

The Department of Defense's recently released report on *Reserve Component Contributions to National Defense* established as one of five goals to improve flexibility of the compensation system. This report has identified a number of areas where improvements in compensation and benefits provided to Reserve component members may be appropriate that would provide the flexibility envisioned in the Reserve Contributions report. There are five possible courses of action associated with the findings contained in this report. The first is to complete independent, contracted studies that are either underway or will be initiated in Fiscal Year 2004. The second is to further develop the business case that would support possible legislative changes. The third is to develop potential policy changes where the Secretary of Defense or the Secretaries of the Military Departments have the authority to make such changes. The fourth is to work with other federal agencies involving programs with shared responsibilities. The fifth, and the most challenging aspect associated with most of the options described in this report, is to identify the resources necessary to fund an increase in the level of compensation.

No legislative proposals accompany this report even though some findings suggest legislation may be an appropriate solution. Some legislative initiatives are currently being considered for the Department's Fiscal Year 2005 omnibus legislative program and others may be vetted for possible submission in subsequent years, pending the outcome of further analysis and planned studies. The following paragraphs briefly summarize the findings and possible options the Department will consider with respect to each subject in this report.

SPECIAL AND INCENTIVE PAYS

While this study found that the 1/30th rule is appropriate and does not warrant a change, it was also determined that an additional, targeted incentive is warranted. The active duty critical skills retention bonus provides a model that could be a very effective tool in the Reserve components. A flexible bonus authority could also replace the Selected Reserve reenlistment bonus and the prior service enlistment bonus. Moreover, providing a bonus authority that includes both officers and enlisted members would provide the Services with the flexibility to target current and projected manning shortfalls in all areas. As such, the Department will develop a business case for creating a Selected Reserve Critical Skills Bonus. If the results provide sufficient justification, the Department will consider a legislative initiative for the next Unified Legislation and Budgeting cycle.

The Department also reviewed the appropriateness of a special pay for duty involving ski-equipped aircraft on Antarctica or the Arctic Icepack and the findings of a recent GAO report on this subject. Section 615 of the National Defense Authorization Act for Fiscal Year 2004, added this duty to the list of duties which qualify for hazardous duty incentive pay.

Finally, the Department will consider the benefits vs. costs of expanding the authority under section 308d of title 37, United States Code, to include officers. This authority provides an incentive for enlisted Reservists assigned to certain high priority units, and may be an equally useful and cost effective tool to fill officer billets in designated units.

MONTGOMERY GI BILL

The Department will continue to closely monitor the recruiting and retention trends in the Reserve components. If the components begin experiencing recruiting or retention problems that can be addressed with increases in the benefit levels provided under the Montgomery GI Bill for the Selected Reserve, the Department will review possible benefit increases and their potential merits, including the impact of restoring the historical relationship with the active duty MGIB benefits.

The current requirements to qualify for the Montgomery GI Bill for active duty service may not provide sufficient flexibility for Guard and Reserve members who have not previously had the opportunity to participate in that program, but are now serving more frequently and for longer periods on active duty. To address this issue, the Department will work with the Department of Veterans Affairs to consider possible changes that would provide Guard and Reserve members with an equitable opportunity to qualify for the active duty program.

HOUSING ALLOWANCE

The Secretary of Defense has the authority to establish the housing allowance rate for Reserve component members serving on active duty for less than 140 days. The primary concern with providing the same housing allowance rate for Reserve component members as active duty members, regardless of the duration of the period of active duty, has always been funding. But this disparity does not facilitate a seamless flow from Reserve to active duty, and the Department will review funding priorities and sources that could allow for a more reasonable threshold—possibly 30 days, or eliminate the threshold all together.

In conjunction with addressing the threshold issue, the Department will also consider legislation to address the apparent inequity experienced by Reservists without dependents who are provided government quarters but are still responsible for a housing expense during short periods of active duty.

To minimize the cost of housing mobilized Reservists on temporary duty away from their homes, the use of contract quarters should be considered to the extent practicable. The Department will further consider expansion of the family separation housing allowance authority to include Reservists who are called to active duty in support of a contingency operation.

INACTIVE DUTY COMPENSATION

The discussion of possibly converting to more of an active duty system for Reserve components may have merit. Such a conversion can be accomplished without reducing the level of compensation Reservists currently receive. In fact, there may be an opportunity with this type of change to actually fund some of the inequities identified in this report without decrementing funding in other programs. But further work is required and the Department continues to develop this concept.

INCOME PROTECTION

The reduction in income experienced by some mobilized Reservists is a challenging problem and any solutions must be carefully crafted. The Department will initiate an independent study of this issue, with the goal of finding balanced solutions. In the interim, the Department and the Services are attempting to provide Reservists with information to assist them in understanding the financial implications of mobilization and information on resources that are available to assist them while mobilized.

RESERVE COMPONENT SURVIVOR BENEFIT PLAN

While no significant shortfalls were identified with the Reserve Component Survivor Benefit Plan, two issues related to the active duty Survivor Benefit Plan were identified. Although a very positive step was recently taken to provide for the payment of an annuity to the spouse of a Reservist who dies in the line of duty while performing inactive duty, the first issue relates to what may be perceived an inequity in the basis used to calculate the annuity. The amount of the surviving spouse's annuity will be considerably less than if the Reservist had died on active

duty. There should be no distinction in the annuity provided to the spouse of a Reservist who dies in the line of duty—whether it is active duty or inactive duty. As such, the Department will consider an initiative to amend the appropriate statute as part of its Unified Legislation and Budgeting cycle.

The second issue involves computation of the annuity for a survivor of a Reserve member who dies in the line of duty while serving on active duty. The method of determining the high 36 months for calculating the retired pay of Reserve component members who retired because of a service connected disability under section 1201 or 1202 of title 10 is not consistent with the calculation used under other provisions of title 10 and can result in a significant reduction in the survivors' annuity. To correct this inequity, the Department will consider an initiative to amend the appropriate statute as part of its Unified Legislation and Budgeting cycle.

RESERVE RETIREMENT

Currently, the Department does not have the analytical tools that would allow us to predict how changes to the reserve retirement system would affect force management. To address this weakness, the Department has contracted a study that will develop an appropriate model that can predict how changes to the reserve retirement system will affect force management. The contract also calls for an assessment of various alternatives to the current reserve retirement system. Once this study is complete, the Department can determine what changes, if any, to the current system will support the Department's human resources requirement for the 21st century.