

Making Defense Affordable

Cindy Williams



MISSION STATEMENT

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NOTE: This discussion paper is a proposal from the author. As emphasized in The Hamilton Project's original strategy paper, the Project was designed in part to provide a forum for leading thinkers across the nation to put forward innovative and potentially important economic policy ideas that share the Project's broad goals of promoting economic growth, broad-based participation in growth, and economic security. The authors are invited to express their own ideas in discussion papers, whether or not the Project's staff or advisory council agrees with the specific proposals. This discussion paper is offered in that spirit.

BROOKINGS

Abstract

The U.S. government faces a tough fiscal future. Absent significant changes to current taxation and spending policies, debt held by the public will mount within two decades to levels never before experienced by this country. The consequences for the American economy and for the nation's place in the world could be severe.

Unless overturned, the Budget Control Act (BCA) of 2011 will cut future non-war defense budgets by about 10 percent from previously planned levels. The cuts mandated by the BCA fall far short of bringing anticipated future deficits down to sustainable levels, however. As a result, non-war defense budgets seem likely to shrink even farther than the levels set under the BCA—even if the law is overturned during the coming year or two. A real decline of 16 percent or more relative to previously planned levels would be consistent with both the magnitude of the nation's structural fiscal problems and historical reductions to U.S. defense spending as wars end.

Efforts to reduce defense spending will be complicated by the fact that costs in some parts of the defense budget are growing significantly faster than inflation. This is particularly true in the areas of health care, pay, operation and maintenance, and equipment acquisition. If left unaddressed, that cost growth will eat into the funds available for military forces. This paper suggests a range of alternatives for curbing cost growth in those areas.

The paper also identifies two options for reshaping U.S. military forces in a way that would reduce future budgets while keeping a strong and ready military. It explores the capabilities of the forces under those options and the missions for which they would be suited.

Following the downsizing envisioned in either of the two proposed options, the U.S. military would still greatly outspend every other military in the world by a sizeable margin. The armed forces would be smaller than today's, but if the reductions are handled sensibly the forces will remain by far the best equipped, best trained, and best maintained in the world.

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Chapter 1: Introduction

The U.S. military is the strongest in the world by any useful measure. It is also by far the most costly. In 2010, the United States spent more on its armed forces than the next fourteen nations combined. U.S. defense spending accounted for more than 40 percent of total world military budgets (see figure 1).

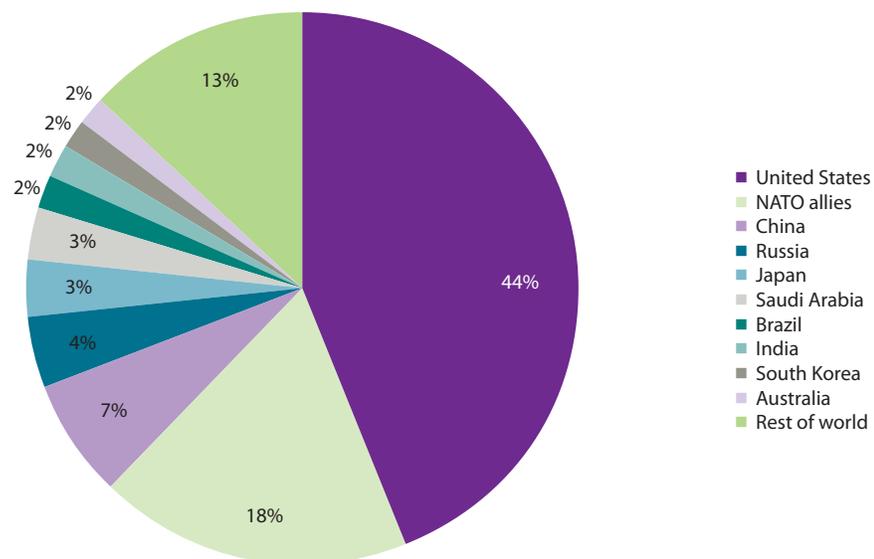
U.S. national defense is also well funded from a historical perspective.¹ In fiscal year (FY) 2010, defense spending was higher in real terms than at any time since World War II (see figure 2). Even excluding the costs of the wars in Iraq and Afghanistan, the defense budget in that peak year of funding was more than 40 percent higher than before 9/11.²

Since 2010, defense budgets have declined modestly as policymakers began to deal with the nation's fiscal situation. Nevertheless, U.S. national defense spending remains higher in real dollar terms than it ever was during the Cold War, and the U.S. defense establishment still outspends any other military by a factor of about six to one.

The U.S. government faces a tough fiscal future. If taxes do not rise from the levels established in the American Taxpayer Relief Act of 2012, and if federal spending continues on its current likely course, federal debt will grow to unsustainable levels over the coming years (American Taxpayer Relief Act of 2012).

In August 2011, President Obama signed the Budget Control Act (BCA) of 2011, which calls for significant reductions to federal spending, including funding for national defense, between FY 2012 and FY 2021 (BCA of 2011). Under the BCA, the total budget (including war spending) for national defense was set to shrink abruptly by about 8 percent on January 2, 2013 (Carter 2012). The American Taxpayer Relief Act pushed the implementation of the cutback to March 2013 and trimmed the size of the reduction required in FY 2013, but did not repeal the BCA. Unless the BCA is overturned, the total national defense budget will decline by a bit more than 6 percent from its planned level in FY 2013.³ The non-war portion of future national defense budgets will drop about 10

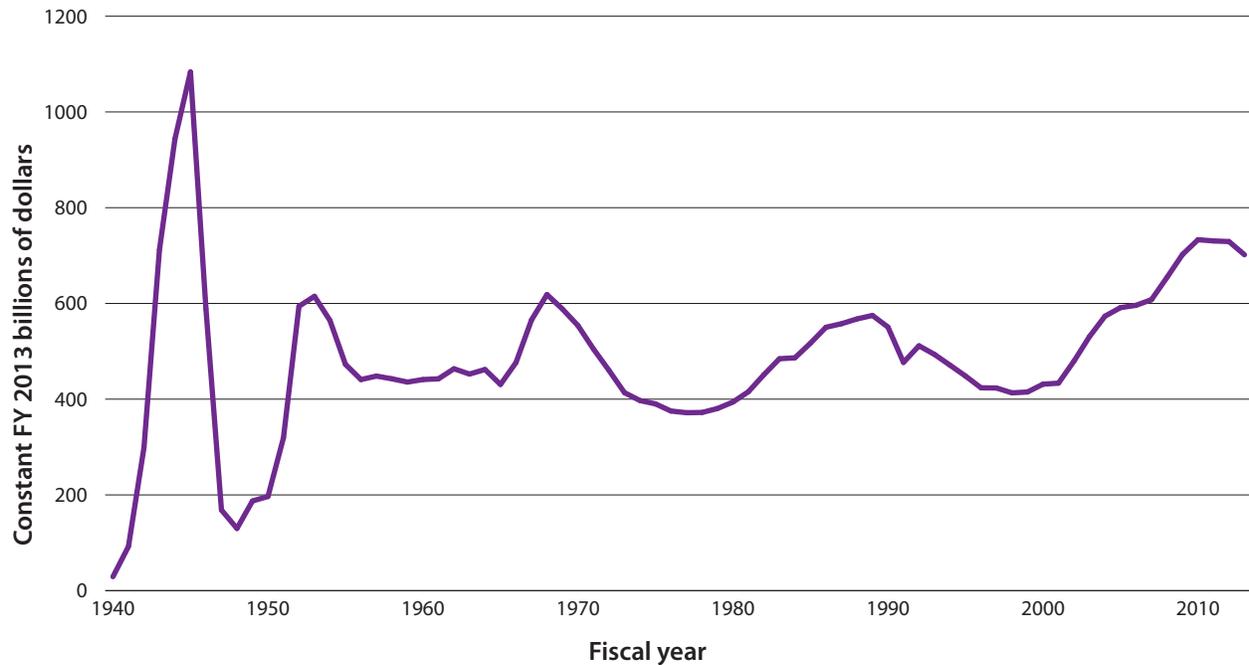
FIGURE 1.
World Defense Expenditures in 2010



Source: Author's graphic based on International Institute for Strategic Studies (2012).

FIGURE 2.

U.S. National Defense Outlays



Source: Author's graphic based on White House (2012, tab. 6.1).

percent from previously planned levels each year between FY 2014 and FY 2021.

Previous efforts to bring federal deficits under control relied heavily on cutbacks to defense spending. If history is a guide, policymakers will see such cutbacks as an important tool for reining in the debt in the future. Thus, whether or not the BCA stands, policymakers will likely choose to reduce non-war defense budgets over the next several years by at least the 10 percent stipulated in the Act. In fact, given the magnitude of the nation's fiscal problems, larger reductions may well be warranted.

The 10 percent reduction required by the BCA would return non-war defense spending in real terms just to its FY 2007 level. Even a 20 percent cut below the FY 2012 level would leave non-war defense spending above the FY 2001 level in real terms.

Unfortunately, however, a 2001-level defense budget will not buy the same amount of defense today as it did twelve years ago, because some categories of defense costs rose significantly faster than inflation during the past decade. This is particularly true in four areas of cost: military pay; health care for military personnel, families, and retirees; operation and maintenance of forces, equipment, and infrastructure; and the development and purchase of new weapon systems.⁴

If left unaddressed, those internal budget pressures will continue to erode the value of the defense dollar. The Congressional Budget Office (CBO) estimates that even if the Department of Defense (DoD) reduces its size, force structure, and weapons modernization programs as currently planned, its costs will continue to rise over the coming decade as military pay, health care, operation and maintenance, and weapons acquisition become more expensive (CBO 2012c). The growing costs will eat into the size of the military, the number of modern weapons it can afford, and the readiness of the force.

The DoD has grappled with rising costs for personnel and acquisition for years. In response, experts have offered numerous proposals for reforms. These include a fundamental overhaul of the military retirement system, broad changes to military compensation to expand the rewards to performance and increase the variability of pay among military occupations, a restructuring of health coverage for military retirees to look more like the system offered to federal civilians, and wholesale reform of the acquisition system (see, e.g., DoD 2008; Williams 2004). All of those reforms have the potential to save substantial amounts of money, yet little action has been taken, in large part because of political resistance to the proposed changes. This paper proposes a collection of seven more modest alternatives that avoid the more fractious political issues. Taken together,

the measures would avert a substantial fraction of the internal cost growth that the CBO projects.

Even if the growing internal costs can be restrained, defense budget reductions will translate into a smaller force and less-ambitious equipment programs. The cutbacks will restrict the missions that the armed forces are able to undertake at low or moderate levels of risk.

A more constrained mission set is arguably in order in any case. Since the end of the Cold War, policymakers on both sides of the political aisle have embraced an increasingly expansive collection of aims for U.S. foreign policy and security, with virtually no thought to cost. In addition to preparing for high-intensity warfare in major military operations, the aims include stopping the spread of nuclear weapons, ending civil wars, conducting stability and counterinsurgency operations, deposing dictators, and building market economies and democratic institutions.

Events of recent years provide a glimpse of the high costs of those expansive aims. The budgetary costs to date of the wars in Iraq and Afghanistan exceed \$1.4 trillion. More than 6,600 U.S. troops have died in combat in those countries, and another 50,000 have endured combat injuries. By some estimates, hundreds of thousands of service members and veterans suffer from posttraumatic stress disorder or traumatic brain injury. Many service members have been deployed multiple times and spent years away from their families.

Expansive security aims have also created problems for the military as an institution—particularly for the Army. The wars in Iraq and Afghanistan took a toll on the numbers and quality of recruits for the Army’s active and reserve components (Asch et al. 2010, 24–26). Multiple long deployments eroded Army retention (Hosek and Martorell 2009). In addition, the Army today has about 19,000 soldiers—enough to fill five brigades—who cannot be deployed, but who also cannot be separated from service until their medical status is adjudicated with the Department of Veterans Affairs (Bostick 2012, 15). For more than a decade, Army brigade-level training has focused almost exclusively on preparing for stabilization, postwar reconstruction, and counterinsurgency operations, leaving the service’s readiness for high-end maneuver warfare in doubt.⁵

The persistent, overactive use of the military can also create new foreign policy problems for the United States. For

example, today’s forward and active security strategy puts the United States and its military repeatedly and persistently into confrontation with the Arab and Muslim worlds and provides frequent ammunition for militant narratives about U.S. imperialist aims. It also incentivizes allies to free-ride or, worse, to “drive recklessly,” as Barry Posen puts it—exhibiting provocative international behavior in the belief that the United States will come to their rescue when that behavior gets them into trouble with their adversaries (Posen 2013). A more restrained strategy—one in which the United States intervenes much more sparingly in others’ conflicts and stops using the military to reshape other countries’ economic and governance structures—could ultimately make Americans more secure and our allies less risk-prone (Posen 2013).

With smart choices, the United States can retain a very strong military, fully ready, equipped, and capable of succeeding in an important range of missions, with budgets significantly smaller than today’s. Moreover, such a force can be better suited than today’s—both to the national security strategy currently envisioned by the DoD, and to a more restrained strategy.

This paper examines two options for reshaping military forces in a way that would reduce future budgets while keeping a strong and ready military:

- Option 4-1: Quickly reduce each military department’s non-war budget by 10 percent in real terms relative to the DoD’s FY 2013 plan; and
- Option 4-2: By FY 2015, reduce DoD non-war budgets by 16 percent in real terms relative to the department’s FY 2013 plan, with a strategic focus on forces for rebalancing toward Asia and the Pacific.

The paper is organized as follows: Chapter 2 looks at the fiscal pressures that are likely to push defense spending downward for the coming decade and the internal cost growth that will crowd out defense capability if left unchecked in an era of defense budget cutbacks. Chapter 3 examines measures that policymakers could undertake to avert that internal cost growth. Chapter 4 outlines the potential consequences for military force structure, equipment, and missions of Options 4-1 and 4-2. Chapter 5 addresses questions and concerns posed by the alternatives discussed in chapter 3 and the options proposed in chapter 4.

Chapter 2: A Time of Austerity

In FY 2012, the United States devoted about 4.6 percent of gross domestic product (GDP) to national defense (White House 2012, table 6.1). This includes the costs of the wars in Iraq and Afghanistan, which today account for about 0.5 percent of GDP.⁶ Some observers hold that the nation can afford indefinitely to devote 4–5 percent of GDP to defense.⁷

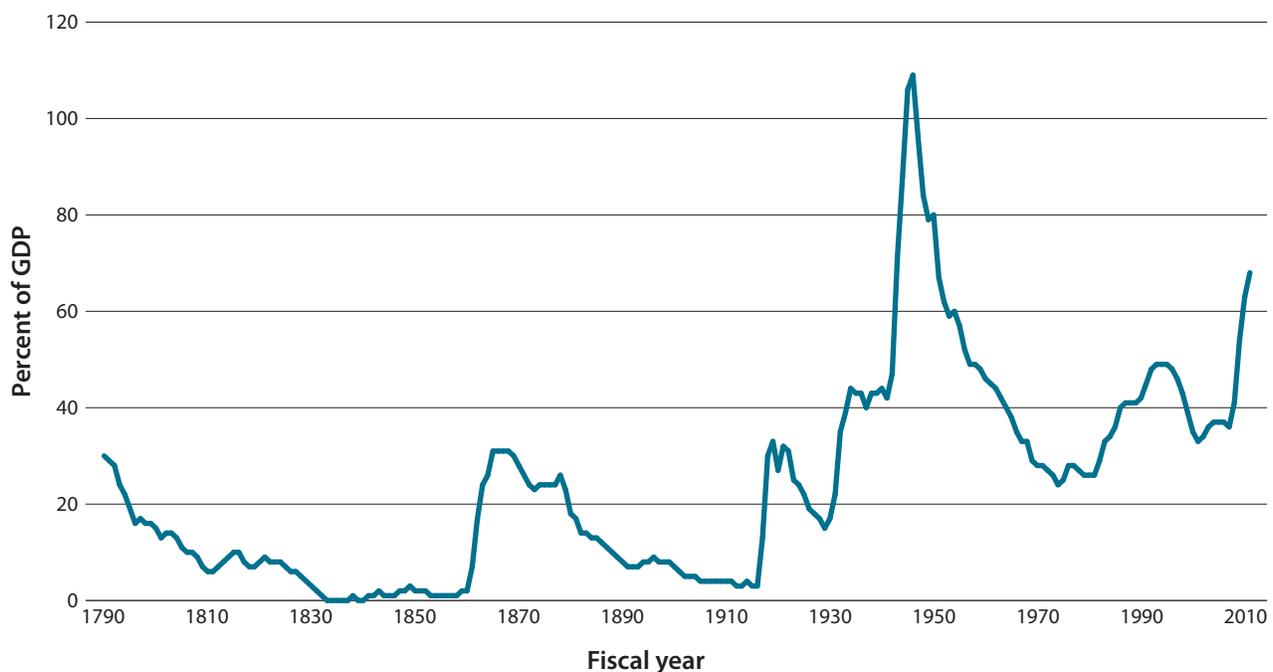
What share of GDP is affordable depends on a variety of factors, including public perceptions of threats to the nation's security as well as concerns over the nation's fiscal future. On the fiscal side, the share of GDP deemed affordable will depend on the level of taxation the public is willing to bear, the degree of debt-induced risk the nation's policymakers are willing to run, and choices about how much money should be devoted to other federal programs and activities. In the past, defense has been an important bill-payer for federal deficit reduction, particularly when efforts to narrow the gap between spending and revenues coincide with the ending of wars. This chapter looks at the nation's fiscal picture and past practice in an effort

to determine how much the United States might reasonably afford to spend on defense in the future. It also explores the internal challenges the DoD faces because of uncontrolled cost growth in important categories of its budget.

FEDERAL FISCAL CHALLENGES

U.S. federal debt held by the public expanded between 2001 and 2008, fueled by the tax cuts that Congress passed in 2001 and 2002, an economic downturn early in the decade, and the costs of two long wars. Following the financial crisis of 2008, that expansion accelerated. In FY 2009, federal revenues covered only 60 percent of federal outlays (White House 2012, table 1.2). As late as FY 2012, the government still had to borrow 35 cents of every dollar it spent. The accumulating annual deficits pushed debt held by the public from 40 percent of GDP in 2008 to about 70 percent of GDP in 2012. Federal debt as a share of GDP today is larger than at any point in U.S. history, with the exception of World War II (see figure 3).

FIGURE 3.
Federal Debt Held by the Public



Source: CBO (2012a, fig. 1-5).

The economic downturn that began in 2008 explains part of the recent growth in the debt. Economic slowdowns typically make it harder to balance the budget: tax revenues shrink because many workers are unemployed or underemployed, and claims on federal benefits rise. In the recent downturn, the bank and automotive bailouts also drew on federal coffers, as did measures to stimulate the economy.

Not all of the rise in debt can be blamed on the weak economy, however. Much of the debt held by the public today is related to a structural imbalance between federal spending and revenues. Since the late 1960s, federal revenues have failed to keep up with spending in most years (see figure 4). On average between 1966 and 2012, tax receipts lagged outlays by nearly 2.9 percent of GDP. Absent serious policy changes, fiscal imbalances will persist even after nationwide employment rates and growth rates improve.

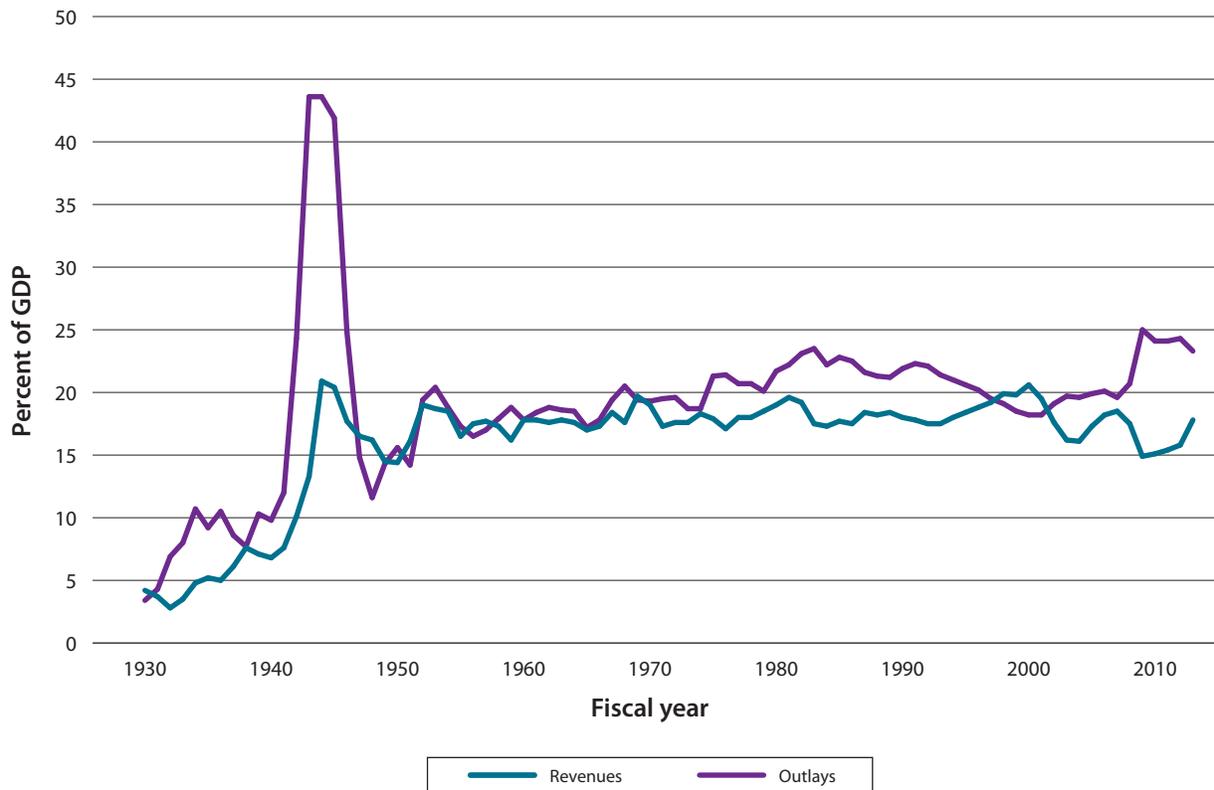
The CBO estimates that unless policies change dramatically, total federal spending (including interest payments) will grow from 23 percent of GDP today to nearly 36 percent of GDP twenty-five years from now—a level unseen since World War II (CBO 2012a, 12).⁸ Much of the budget expansion will result from growth in the costs of Social Security and of Medicare, Medicaid, and other health-care programs as more baby

boomers retire and the underlying costs of health care grow faster than the economy.

Several policy changes called for in law would bring some of that future spending under control. The biggest of these is the next round of cuts to defense and domestic programs under the BCA—starting with the automatic sequestration now scheduled for March 2013 and extending through FY 2021. The CBO’s current-policy scenario considers policies—rather than laws—as they stand today, and thus ignores the budget cuts that these laws will impose if they are allowed to stand.

Absent changes in tax policy, federal revenues will fall far short of keeping up with rising budgets. The CBO calculated in June 2012 that, under tax policies as they stood in 2012, revenues would rise to 18.5 percent of GDP in 2037—only about half of the 36 percent of GDP anticipated on the spending side. The American Taxpayer Relief Act of 2012 will increase revenues modestly, but annual deficits will still be substantial. Even with the tax rise established by the Act, federal debt held by the public would hit 100 percent of GDP in the next twelve years. Within about fifteen years, it would climb to the 109 percent that marked the highest point in U.S. history during World War II. Before 2040, debt would rise to 200 percent of GDP. Moreover, rather than leveling off or declining as it did

FIGURE 4.
Revenues and Outlays as a Share of GDP



Source: Author’s graphic based on White House (2012, tab. 1.2).

at the end of World War II, debt would continue to build (CBO 2012a, 19).⁹

Debt at that level is unsustainable from fiscal and economic points of view. Even if interest rates stayed below 4 percent—a most unlikely outcome—interest payments on the public debt would rise to 8 percent of GDP. That is well above the historical average of 2 percent and more than one-third of the share of GDP typically held by the total federal budget. More likely, however, interest rates would rise as creditors concerned over the possibility of default demanded higher yields.¹⁰ Should interest rates rise to 10 percent—a situation that the United States has experienced in the past—then federal interest payments alone could reach 20 percent of GDP before 2040, larger than the average size of the entire noninterest budget during the past fifty years.

How much money the nation spends on defense in future years will depend in part on how policymakers deal with the fiscal issues that face the nation.

In addition to pushing interest rates higher, such a large debt would risk crowding out investment in productive activities that promote economic growth. Perhaps most troubling, a debt of that size would limit the flexibility the nation's leaders have in dealing with future economic or financial crises. If banks are on the brink of failure and federal debt already exceeds the size of the economy, adding to the debt to pay for a bailout or a stimulus package will be even harder than it was the last time. Yet the very size of the debt could also cause creditors to lose confidence in the government's ability to make good on its debts, thus sparking a rapid rise in interest rates that would make borrowing unaffordable and lead to a fiscal crisis.

Before the American Taxpayer Relief Act passed, the CBO estimated that avoiding an unsustainable level of debt would require policymakers to shift at least 4.8 percent of GDP into taxes or out of spending—or to adopt some combination of

higher taxes and lower spending that result each year in a 4.8 percent narrowing of the anticipated imbalance between spending and revenues (CBO 2012a, 20).¹¹ The fiscal shift would have to begin in FY 2013, and to operate for at least twenty-five years (CBO 2012a, 20). Moreover, with every year of delay, the amount of money to be shifted into taxes or out of spending will rise. For example, if policymakers do not address the problem before FY 2015, then the size of the annual changes required will grow to 5.2 percent of GDP (CBO 2012a, 20).

The American Taxpayer Relief Act adds less than 0.4 percent of GDP to the revenue side of that equation. Thus, even with the revenue increases of that Act, policymakers must still shift more than 4.8 percent of GDP from one side of the ledger to the other by FY 2015 to put the federal government on a sustainable fiscal path.

The nation's political leaders generally agree that fiscal changes are needed, but they continue to disagree over how future shifts should be apportioned between higher taxes and lower spending. To the extent that spending is to be cut, they disagree over which areas of the budget are ripe for reductions. In the absence of agreement on those issues, they might find an easy mark in the national defense budget.

DEFENSE AS A BILL-PAYER FOR DEFICIT REDUCTION

Some observers argue that defense spending should not drop below 4 or 5 percent of GDP. Others argue that addressing the nation's fiscal problems and improving long-term economic prospects will require a significant reduction in the share of the economy that goes to defense and security (see, e.g., Mandelbaum 2010). How much money the nation spends on defense in future years will depend in part on how policymakers deal with the fiscal issues that face the nation.

In the past, U.S. spending for national defense fell rapidly at the conclusion of wars, as figure 2 suggests. Accumulating the funds needed to fight a big war can require borrowing significant sums of money, and defense reductions are an obvious choice for policymakers looking to shrink deficits and debt. As the Cold War ended, for example, the administration and Congress agreed to reduce defense spending by about one-third in real terms. Defense became the main bill-payer in a major deficit reduction effort that began in 1986, a few years before the Soviet Union collapsed. (A rapidly growing

economy and growing tax receipts also played important roles in that effort.)

The BCA itself offers another illustration of the ease with which policymakers turn to the defense budget as a bill-payer for deficit reduction. That law called for two rounds of fiscal shifts. The first round required cuts from defense and nondefense discretionary spending, to narrow anticipated budget deficits over a ten-year period by about \$1 trillion; it had no effect on entitlements or taxes.¹² The second round called for a congressional supercommittee to recommend specific tax increases, entitlement cuts, and discretionary cuts that would shave another \$1.2 trillion from the debt anticipated in FY 2021. When the supercommittee failed in its charge, taxes were held completely harmless, and almost all of the budget cuts fell on the discretionary accounts. One-half of the second round of cuts are now scheduled to come through reductions to defense.

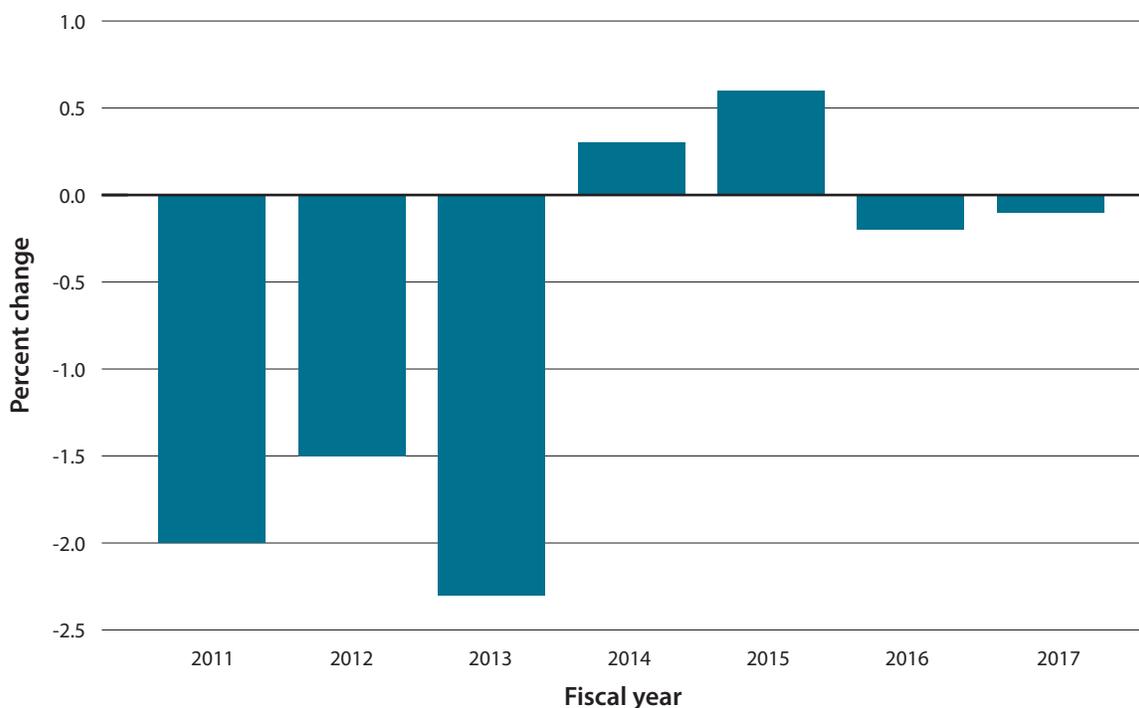
Policymakers on both sides of the political aisle argue that they never intended for the automatic defense cuts to take place; rather, they hoped that the threat of those cuts would inspire the supercommittee to reach compromise on a broader menu of deficit-reduction measures. Nevertheless, because lawmakers could not come to terms on a “grand bargain” that would address discretionary spending, entitlements, and

taxes together, defense and other discretionary spending are now scheduled to pay most of the BCA’s bills.

Defense spending is also an easy mark for deficit reduction because it is so high by historical standards. Non-war budgets for national defense rose by about 50 percent in real terms between FY 1998 and FY 2010. They declined by 3.5 percent in real terms between FY 2010 and FY 2012. The president’s budget request for FY 2013 would reduce the non-war budget by another 2.3 percent in real terms, bringing total defense cuts between 2010 and 2013 to about 6 percent based on the president’s FY 2013 plan (see figure 5). Budgets to fund the wars also rose rapidly during the past decade, but have since declined; war budgets are scheduled to drop further as combat troops leave Afghanistan.

Unless overturned, the sequestration procedures of the BCA will cut a bit more than 6 percent from the total national defense budget in March 2013.¹³ If the BCA stands, non-war defense budgets between 2014 and 2022 will be about 10 percent lower in real terms than the president’s budget for FY 2013, and about 13 percent lower than the FY 2012 budget. The BCA would thus return the national defense non-war budget to its FY 2007 level in real terms (see figure 6).¹⁴

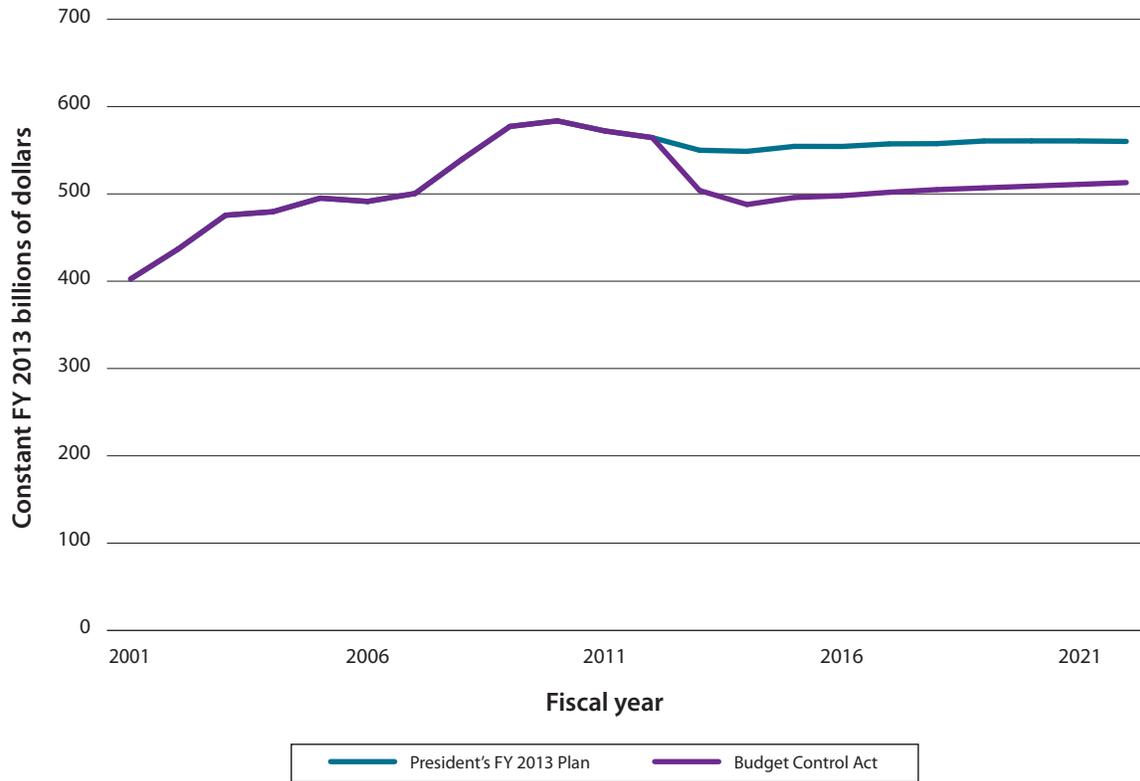
FIGURE 5.
Annual Real Change in Department of Defense Non-War Budget, President’s FY 2013 Plan



Source: Author’s graphic based on Office of the Under Secretary of Defense (Comptroller) (2012, “Fact Sheet: The Defense Budget, February”).

FIGURE 6.

National Defense Budget Authority under Budget Control Act



Source: Author's calculations based on American Taxpayer Relief Act of 2012; BCA of 2011; Office of the Under Secretary of Defense (Comptroller) (2012); Office of the Under Secretary of Defense (Comptroller)/Chief Financial Officer (2012).

Note: Figures for FY 2013 assume the allocation to non-war budget of the entire national defense sequestration cut.

To explore what level of defense spending policymakers might find affordable in the future, consider the fiscal finding discussed earlier: if taxation and spending policies do not change substantially before 2015, then leaders looking to put the federal debt on a sustainable path would have to shift 4.8 percent of GDP permanently into revenues or out of budgets. One way to shift that much money would be to raise tax rates significantly above the levels set by the American Taxpayer Relief Act—or reform tax policies enough to add that much to the revenue side of the ledger each year. Such a move would quickly bring revenues to more than 23 percent of GDP, however—significantly higher than the United States has experienced, at least since the 1930s. In the current antitax political climate, such a move seems highly unlikely. On the other hand, that move would allow the defense budget to stay at its FY 2012 level in real terms (including war funds) for a decade.

Alternatively, the president and Congress could decide to close the remaining gap entirely through budget cuts. One way to do this would be a “proportional cuts” plan. This plan would distribute the 4.8 percent of GDP in such a way that defense, nondefense discretionary, and mandatory programs

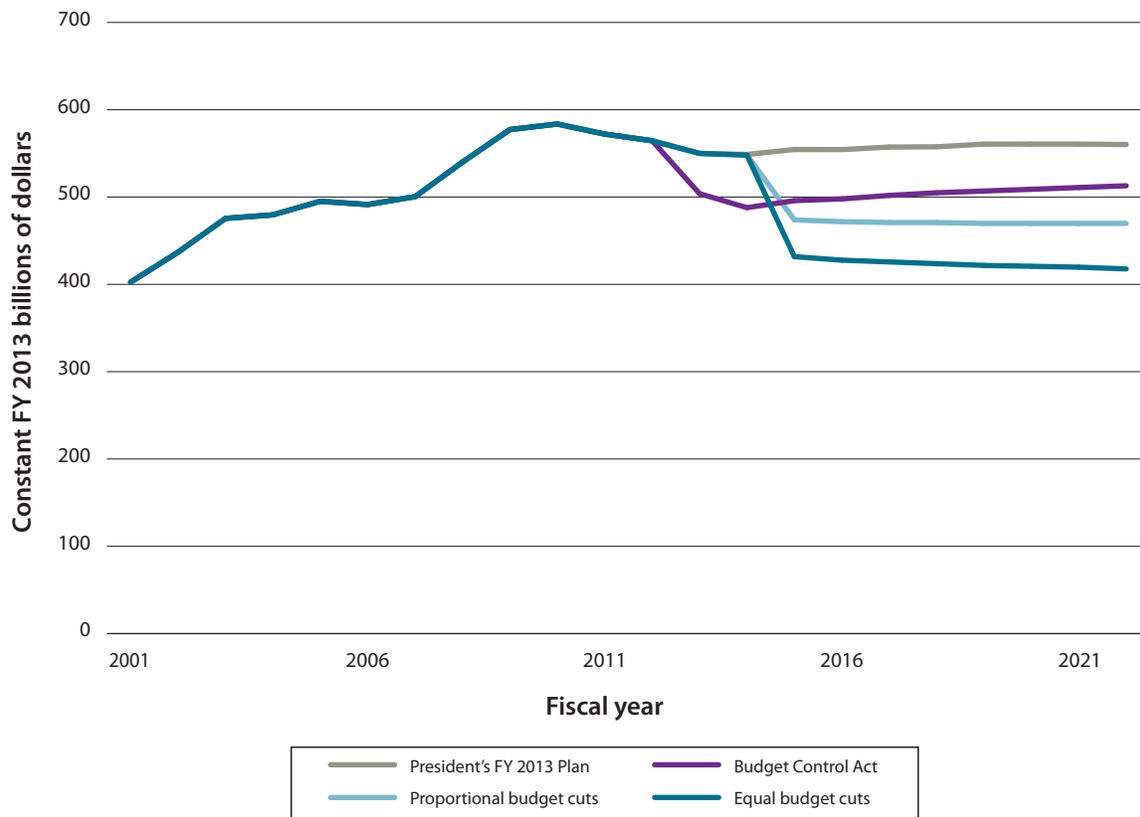
are each hit in proportion to the shares they hold in the FY 2012 budget.

In that case, total defense spending (which includes any money for wars) would be reduced by a bit less than 1 percent of GDP, relative to its levels in the CBO's current-policy estimate. Nondefense discretionary programs would be cut by about the same amount, and mandatory programs, including the major entitlements like Social Security, Medicare, and Medicaid, would together contribute a bit less than 3 percent of GDP. If policymakers cannot agree to a rise in revenues beyond those established by the American Taxpayer Relief Act, then this would seem a fair allocation of the pain of budget reductions. The non-war budget for national defense would be about 16 percent below the level envisioned in the president's FY 2013 plan.¹⁵

Another possibility is that the nation's leaders will strike a compromise by raising taxes as well as cutting budgets, beginning in FY 2015. One way to do this would be through an “equal cuts” plan, spreading the 4.8 percent pain equally among four categories: national defense activities, nondefense

FIGURE 7.

National Defense Budget Authority under BCA and More Sustainable Plans



Sources: For president's FY 2013 Plan and BCA: author's calculations based on American Taxpayer Relief Act of 2012; BCA of 2011; Office of the Under Secretary of Defense (Comptroller) (2012); and Office of the Under Secretary of Defense (Comptroller)/Chief Financial Officer 2012. Figures for FY 2013 assume the allocation to non-war budget of the entire national defense sequestration cut.

For Proportional Budget Cuts and Equal Budget Cuts: author's calculations.

discretionary programs, mandatory spending, and tax revenues. This would reduce defense budgets by about 1.2 percent of GDP relative to the CBO's current-policy estimate. Compared with the administration's plan for FY 2013, that allocation of the fiscal pain would translate into a 24 percent cut to non-war defense spending in real terms.¹⁶

In the context of history and current politics, both the proportional-cuts plan and the equal-cuts plan seem plausible. Figure 7 illustrates how the defense budget might look under those two plans, as compared with the president's FY 2013 plan and the path that national defense would take under the BCA as adjusted by the American Taxpayer Relief Act. As the figure reflects, either plan would reduce defense more deeply than the BCA. The proportional-cuts plan would return non-war defense spending to about its FY 2003 level in real terms. The equal-cuts plan would take the non-war defense budget to a level a bit higher than before September 11, 2001.

Chapter 4 looks at how the military might be restructured to bring defense budgets down to the BCA level, or to effect the deeper reductions of the proportional-cuts plan.

PRESSURES INSIDE THE DEFENSE BUDGET

Between FY 2000 and FY 2010, the DoD added about 57,000 active-duty military personnel to its rolls, expanding the size of the force by less than 4 percent.¹⁷ Yet non-war defense budgets rose over the same period by more than 40 percent. Some of that rise can be explained by the added people and by deliberate decisions to increase investment in new military equipment. But a significant share of budget growth within the DoD resulted from four factors that the department found increasingly difficult to control:

1. Growth in health care costs for military personnel, families, and retirees;
2. Rising costs of civilian pay, military pay, and military allowances;
3. Rising costs in other areas of operation and maintenance; and
4. Unplanned growth in the costs to develop and purchase new equipment.

Rising costs in those four areas were again a challenge to the DoD as it developed its plan for the FY 2013 budget. That plan would reduce the size of the active-duty force by about 7 percent, trim the Guard and Reserve, eliminate 18 percent of the Army's active-duty combat brigades, and defer some investment in equipment—all to cut only about 2 percent from the budget in real terms (Office of the Under Secretary of Defense [Comptroller]/Chief Financial Officer 2012).

Despite those cutbacks to forces and new equipment, the CBO estimates that the DoD will not be able to achieve the 2 percent budget reduction. Rather, the CBO finds that DoD budgets between FY 2013 and FY 2017 would need to be 4.7 percent higher—on average, some FY 2013 \$25 billion more annually—than the department's proposed budget for FY 2013 to FY 2017. By FY 2022, the DoD would face an annual shortfall of some \$52 billion (constant FY 2013 dollars)—again because of the growing costs of health care, pay, operation and maintenance, and new equipment.

Unless such internal cost growth can be contained, it will crowd out spending for military capability as budgets shrink or remain steady. In a time of austerity, getting a handle on these growing internal costs will be crucial for the DoD, regardless of the national security strategy the nation's leaders ultimately decide to pursue. Chapter 3 offers a variety of proposals for avoiding cost growth in the four areas.

The end of the wars in Iraq and Afghanistan offers the nation and the DoD an opportunity to reassess the size and shape of the military as well as the way it should be equipped and trained in the future. By making smart choices in those areas and limiting excess cost growth, U.S. leaders can shape a very strong and well-equipped military despite significant budget reductions.

Chapter 3: Taking Control of the Defense Budget

This chapter examines some of the reasons behind the growing costs of military health care, military pay, operation and maintenance, and weapons acquisition during the coming decade. It proposes seven alternatives to avert some of the costs in each of those areas, and ends with a section on implementation.¹⁸

REINING IN THE COSTS OF MILITARY HEALTH CARE

Health care is the fastest-growing element of the defense budget. In FY 2012, the DoD spent some \$53 billion to cover the health care of active-duty service members and their families, military retirees, and retirees' families and survivors.¹⁹ That is more than double what the department spent on military health care in FY 2000. Absent changes in policy, military health costs will rise by at least 25 percent in real terms during the coming five years (CBO 2012c, 17). The CBO calculates that costs for the system will nearly double within the next two decades (CBO 2012c, 21).

In part, the rapid rise in costs of the military health-care system reflects the growing costs of health care in the rest of America. But for the military system, three other factors explain much of the recent growth.

The first factor is a major expansion of benefits for military retirees who qualify for Medicare (typically those who are sixty-five or older). In 2000, Congress authorized the Tricare for Life program, which provides wraparound coverage for those retirees and their Medicare-eligible dependent family members and survivors. The DoD established an accrual account to recognize the future costs of those benefits for service members currently in the force. By 2012, that account added nearly \$10 billion to the department's health-care bill.

The second factor is that the share of health-care costs borne by military retirees is extremely low in relation to the share typically paid in the private sector. Medicare-eligible military retirees currently pay no premium whatsoever for the wrap-around coverage of Tricare for Life. Retirees not yet eligible for Medicare can choose among three so-called Tricare plans. The least expensive plan charges no premium to members; the most expensive plan has a premium of about \$40 per month for family coverage. This stands in sharp contrast to typical premiums for health coverage in the private sector, which

can easily run to ten times that much. Moreover, Tricare premiums did not rise at all between the mid-1990s, when the Tricare system was established, and 2012, yet the premiums paid by employees in the civilian sector grew rapidly during that period.

Most of the military retirees who are not yet eligible for Medicare are employed in the civilian workforce and have access to other health coverage. Before 1995, a large fraction of those younger military retirees chose the health coverage offered by their post-military employers or by a spouse's employer, even though they were eligible for coverage by the military system. That changed during the past fifteen years, however. For most retirees, the very low cost of Tricare relative to the options available to them in the civilian workforce attracted them to choose the military system. As a result, a significant share of the health-care costs for military retirees and their families shifted out of the civilian sector and into the DoD.

A third factor that pushed up defense health care costs faster than those in the civilian world is the low copayments charged under Tricare and Tricare for Life for medical services and prescription drugs. Copayments can cause the members of an insurance plan to think twice about doctors' visits, treatments, or prescriptions that might not be needed. Indeed, individuals in the military system utilize significantly more health care than those who are insured by other employers.²⁰

Policymakers could reduce some of the cost growth stemming from that third factor simply by increasing the copayments charged for prescription drugs provided under the Tricare and Tricare for Life plans. One plan proposed by the CBO would charge \$3 for generic drugs and \$9 for brand-name drugs provided through the military's own pharmacies. For prescription drugs purchased in other locations or through the mail, the plan would raise copays on a one-month supply from \$3 to \$15 for generic versions, or to as much as \$45 for medicines that are not included in the Tricare formulary (CBO 2011a, 82). Active-duty service members would not be affected; their prescriptions would still be filled with no copay, as they are today. The CBO estimates that increasing participants' drug copayments in this way could save the DoD about \$1.3 billion on average each year over the coming decade (CBO 2011a, 82).

To temper the cost growth arising from the second and third factors, the DoD and two successive administrations proposed repeatedly to adjust member premiums and copayments to levels closer to those paid in civilian health-care programs. In its FY 2013 budget request, the DoD again outlined a range of measures that would begin to curb its future health-care bills. These include the following:

- Impose a premium for Medicare-eligible retirees and family members who use the Tricare for Life program.
- For retirees who are not yet eligible for Medicare, raise the premium imposed on the Tricare plan that already requires members to pay a monthly fee, and impose new premiums on the plans that currently do not charge a premium.
- Increase deductibles paid by retirees and their families and survivors.
- For retirees and for family members of those currently serving, increase the copayments charged for prescription drugs (Office of the Under Secretary of Defense [Comptroller]/Chief Financial Officer 2012, 5-3).

In its proposal, the DoD specifically exempts from higher payments the survivors of service members who died on active duty, as well as service members who retired for medical reasons (Office of the Under Secretary of Defense [Comptroller]/Chief Financial Officer 2012, 5-3). The department estimates that its proposal would save \$1.8 billion in FY 2013 alone (Office of the Under Secretary of Defense [Comptroller]/Chief Financial Officer 2012, 5-3). The CBO finds that the measures proposed by the DoD would significantly slow the growth of military health care spending between FY 2013 and FY 2022; by 2022, the DoD's proposal would avert as much as \$17 billion in annual spending (CBO 2012c, 21).

Unfortunately, Congress rejected most of the DoD's proposal in the National Defense Authorization Act for FY 2013.

Alternative 3-1 would accept the changes to cost sharing arrangements that the DoD proposed in the FY 2013 president's budget, saving an average of more than \$10 billion annually over the coming decade, and \$17 billion in FY 2022.

This alternative would save the DoD some money simply by reducing the share of military health-care costs borne by the government. More important, it would bring the share borne by most military retirees closer to what they would pay for coverage through other plans, thus encouraging them to consider the other choices available to them. It would also raise individuals' out-of-pocket expenses, thus discouraging the overutilization of health-care goods and services that the department faces today.

A more dramatic change would be to exclude retirees and their family members or survivors entirely from Tricare's most expensive plan, and to charge a premium for the other two plans, similar to what federal civilians pay for their plans.²¹ The CBO estimates that this choice could save the DoD more than \$11 billion annually over the coming decade (CBO 2011a, 81).

AVERTING COST GROWTH FOR MILITARY CASH COMPENSATION AND RETIREMENT PAY

Between 1998 and 2012, military basic pay grew significantly faster than pay in the private sector and 62 percent faster than the consumer price index.²² Compared with price inflation across the GDP, it grew even faster.

Proponents of across-the-board military pay raises that exceed inflation argued that military pay lost ground relative to pay in the private sector in the years that followed two double-digit military pay increases granted during the Carter and Reagan administrations. But twelve years of across-the-board raises to military pay that exceed wage growth in the private sector restored the relationship that held between military pay and private-sector pay following those two extraordinary pay raises (Murray 2010, 6). Moreover, if one considers the full amount of military cash compensation—that is, the cash allowances for food and housing (and the tax advantage that accrues to service members because those allowances are not taxed) in addition to basic pay—military personnel are now paid far better in relation to their private-sector counterparts than they were after the two exceptional pay raises of the early 1980s (Murray 2010, 6).

Limit military pay raises.

For the first few years after 1998, the DoD requested what it considered to be catch-up raises, and Congress granted them. Beginning in the mid-2000s, however, the department requested across-the-board pay raises at the level of private-sector wage growth each year. Contrary to those requests, Congress granted raises in excess of private-sector wage growth through FY 2010. In its FY 2013 plan, the DoD requested basic pay raises for FY 2013 and FY 2014 that are consistent with the rise in wages in the civilian world. For FY 2015 through FY 2017, the department signaled its intention to request raises below both the GDP deflator and the civilian benchmark.²³ The law currently requires military pay to rise annually consistent with the civilian benchmark, however. Unless Congress accepts a serious slowdown in military pay growth, military pay raises will continue to crowd out spending for other military activities.

It is critically important that policymakers ensure that military personnel are compensated fairly for their service. Moreover, cash pay is a crucial tool for recruiting and retaining the high-quality volunteers the armed services need. The above-

inflation increases to cash pay beginning in the late 1990s probably helped the services attract and keep the troops who saw the nation through the wars in Iraq and Afghanistan.

With the wars winding down and a weak economy, however, military recruiting and retention are excellent. The downsizing expected under the president's budget for FY 2013 will make it even easier to meet the services' expectations for numbers and quality of personnel. Moreover, service members' cash pay today stands well above the seventy-fifth percentile of private-sector pay for workers with similar levels of education and years of experience. At the entry level for both enlisted personnel and officers, cash pay falls at about the ninetieth percentile, compared with that of similarly educated, entry-level civilian workers.²⁴ An end to above-inflation pay raises is warranted and will not weaken the armed forces.

The DoD, working with the administration and Congress, has a range of options for restraining the rising costs of military pay. The most extreme choice is to freeze pay—that is, offer no pay raise at all—for one or more years, as lawmakers did with civilian pay in 2011 and 2012. Freezing military pay for three years beginning in 2014 would save the DoD about \$8.5 billion on average between FY 2014 and FY 2022, compared with offering raises equivalent to the rise in private-sector pay for each of those three years. Alternatively, policymakers might choose to trim pay raises for several years to keep up with some, but not all, of the annual rise in pay outside of the military. Holding military pay raises at one-half percentage point below the rise in the civilian employment cost index for the years from 2014 to 2017 could save the DoD some \$1.5 billion on average each year between FY 2014 and FY 2022.

Alternative 3-2 recommended in this paper falls between those alternatives. Rather than raising military pay annually to reflect pay growth in the private sector, this alternative would limit military pay raises to the level of GDP inflation every year for four years, beginning in 2014—a difference of about 1.9 percentage points for each pay raise. On average over the decade, the alternative would save \$5.6 billion a year compared with a plan that holds raises to the full level of the civilian wage benchmark each year. In FY 2022, it would avert about \$6.7 billion (FY 2013 dollars) relative to the CBO's estimates of defense internal cost growth.²⁵

Encourage more service members to leave before retirement.

The DoD devotes a larger share of its compensation dollar to retiree benefits than other government organizations, and a far larger share than private-sector firms. The military retirement system differs greatly from typical plans in the private sector. Members generally do not vest in the plan until they complete twenty years of service, compared with a maximum of five years to vesting under most civilian plans. After the twenty-

year point, members can retire with a generous defined benefit—a lifetime monthly pension that begins immediately upon retirement. This “cliff vesting” encourages many service members to remain in service for more years than either they or their service personnel managers might prefer—and then to depart shortly after reaching the twenty-year point.

In the past, several studies sponsored by the DoD and others have called for reforms of the military compensation and retirement systems to put more of the compensation dollar into immediate cash pay and to reduce the distortions caused by cliff vesting (see, e.g., Asch, Johnson, and Warner, 1998; DoD 2008, vol. 2; Williams 2004). Such reform has the potential to save the DoD billions of dollars annually (Defense Business Board, 2011; DoD, 2008, vol. 2).

In its FY 2013 budget plan, the DoD announced that it would establish a new commission to make recommendations for retirement system reform. Such recommendations have been roundly rejected by policymakers in the past, however. Even if the DoD and the service chiefs request substantial reform of the system, lawmakers may not agree. Moreover, the department's experience with a modest retirement change adopted in the 1980s makes clear how easy it can be to overturn such reforms before they even begin to pay off.²⁶

Nevertheless, the armed services on their own might be in a position to undertake cost-saving changes that could result in a stronger force overall. Today, about 15 percent of enlisted personnel and nearly one-half of officers serve long enough to become eligible to retire with an immediate pension and an extremely generous health-care plan. Many of those individuals are needed to fill positions that require significant levels of experience. On the other hand, too many remain in service well beyond the point where their added years of experience pay off in improved performance in the tasks they handle.

The Marine Corps encourages most of its enlisted personnel and many of its officers to depart after a relatively short period of service.²⁷

Under **Alternative 3-3**, all of the armed services would reduce over time the pool of service members who serve until retirement by 30 percent. The services have a variety of measures available to help make such a shift. These include early counseling of new service members (a measure widely used in the Marine Corps), adjustment and enforcement of up-or-out gates, and narrowing of promotion standards. Over time, these measures would lead to a younger force and could improve force management at every level.²⁸

The alternative would save money by reducing funds the services must set aside in accrual accounts to recognize the future costs of military pensions for those currently in service.

Over the longer term, it could greatly slow the growing costs of health care and other benefits for retirees. The alternative would impose somewhat higher costs for recruiting and initial training, because more recruits would be needed to make up for the shorter periods of service. It would also require larger budgets for the involuntary separation pay that service members receive when up-or-out rules require them to leave before they are eligible to retire. In the net, the alternative might save as much as \$2.5 billion on average over the next ten years, and \$5 billion in FY 2022. Substantially greater savings would be realized beyond the decade as fewer new retirees enter the retiree health-care plan.

Reduce military housing allowances.

Service members receive a cash allowance to offset the costs of housing. Until the past decade, that allowance was meant to offset about 85 percent of service members' costs to rent appropriate housing on the open market. Those who lived in housing provided by the government did not receive the allowance.

Early in the decade of 2000, Congress passed legislation to close the gap between service members' housing allowance and their rental costs. Today, the housing allowance is set by region to reflect the full price of housing considered appropriate for service members, depending on their rank and family status.

When Congress made that decision, the DoD owned and operated a substantial stock of housing, most of it on military bases. About 30 percent of military families lived in government housing. Because the government is not an efficient landlord, however, the government's cost was considerably higher than the size of the housing allowance or the cost of housing outside the military base. Moreover, the government housing stock—much of it built during the 1950s—was aging. On the other hand, living in military housing typically left service members better off financially, because the housing allowance they would receive if living off-post covered only 85 percent of their costs. As a result, most military bases ran long waiting lists for their housing.

At the time, advocates of raising housing allowances argued that if the allowance was set equal to the cost of procuring housing from the private sector, service members would choose against the on-base housing in favor of living off-base. Over time, the DoD could divest itself of much of the aging housing, and turn more of its attention to its core responsibilities (see, e.g., CBO 1993).

Instead, the DoD undertook a major initiative to revitalize the housing on military bases, but to turn the responsibility for building and maintaining the new quarters over to contractors in the private sector. As an incentive for contractors to keep the costs affordable, the department executed agreements

to ensure the housing units are kept at nearly 100 percent occupancy rates for decades.

As experts anticipated, service members are far less interested in living on-base now that their housing allowances cover the full costs of living on the outside. Waiting lines for the on-base units have largely dried up. The DoD, under obligation to the contractors to keep the housing full, increasingly turns to non-active-duty personnel to live in the on-base units. Reservists, government civilians, retirees, and members of the general community are now recruited to live in the on-base quarters.

Alternative 3-4 would reduce military housing allowances to reflect 90 percent, rather than 100 percent, of the price of appropriate housing provided by the private sector outside of the military base. Under this alternative, the DoD might still be obliged to pay its housing contractors who rent units to service members at the full price of housing outside the base. Even under that assumption, the alternative would save the DoD about \$1.4 billion annually over the decade. (Alternatively, returning the allowance to cover 85 percent of rental costs, as was the case before 2000, would save as much as \$2.1 billion annually; setting it at 95 percent of the price of appropriate housing outside the military base would save about \$900 million each year.) Smaller housing allowances also would again make housing on-base look more attractive to service members from a financial point of view, and thus likely would begin to restore the military character of on-base neighborhoods.

TAKING CONTROL OF OPERATION AND MAINTENANCE BUDGETS

For decades, per-troop spending for operation and maintenance in the DoD has grown in real terms by an average of 2.5 percent a year (see Daggett 2009, 8).²⁹ Some of that growth may have been unavoidable, but much of it was due to deliberate policy choices that pushed such spending upward.

For example, during the late 1950s and early 1960s, the expansion of family-friendly infrastructure on military bases translated into permanently higher costs for installation upkeep. The 1970s saw the transition from conscripts to the all-volunteer force. The shift to volunteers added to maintenance costs for training facilities and office space as the armed services looked for ways to offset some of the negative features of military life. The late 1980s and early 1990s saw a significant expansion of military missions, including new requirements for base environmental cleanup, drug interdiction, nuclear threat reduction with states of the former Soviet Union, and treaty verification. More recently, the shift of significant workload from uniformed personnel to DoD civilians and contractors pushed activities out of military personnel accounts and into the operation and maintenance title (Williams 2010).

Rising per-troop costs for operation and maintenance have been so persistent that some experts now treat them as unavoidable—a sort of law of physics. For example, the CBO’s estimates of future cost growth in the DoD assume that non-war operation and maintenance spending outside of the military health accounts will continue to grow faster than inflation, despite the department’s planned cutback of more than 100,000 troops (CBO 2012c, 7, 17). Persistent cost growth should be avoidable, however, if policymakers eschew burdening the DoD with new responsibilities and tighten the reins in key areas.

Limit pay raises for defense civilians.

Pay for the civilian workforce comprises more than one-third of the DoD’s operation and maintenance budget. Between 1998 and 2009, civilian pay raises generally kept pace with those for uniformed personnel.³⁰ In 2010, civilian raises fell behind those for the military, and civilians experienced a pay freeze in 2011 and 2012. Nevertheless, the earlier raises meant that defense civilian workers today are substantially better off relative to their counterparts in the private sector than they were in 1998.

The plan put forward by the DoD with its FY 2013 budget would increase civilian pay at the same rate as military pay from 2014 until 2017. Like military pay, civilian pay would not keep up with wage growth in the private sector for several years. Given the recent freeze on civilian pay, however, Congress might be tempted to revert to the practice of the previous decade and raise pay for those workers consistent with wage growth in the private sector. Such a move would add billions of dollars to defense budgets. The CBO’s estimates of defense internal cost growth assume that Congress will not resist that temptation (CBO 2012c, 20).

As with military pay, decision makers might consider a range of options for bringing this area of cost growth under control. One choice would be a return to pay freezes. Holding civilian pay rates at their 2013 levels during 2014, 2015, and 2016 would save the DoD roughly \$7 billion on average each year between FY 2014 and FY 2022. Alternatively, the rise in pay for government civilians could be limited for four years to a level that is one-half of a percentage point below the rise in pay across the private sector. That measure could save the DoD about \$1.2 billion on average every year between FY 2014 and FY 2022, compared with offering raises at the level of the employment cost index every year. As with military pay, the alternative suggested in this paper takes the middle ground.

Under **Alternative 3-5**, across-the-board pay raises for federal civilian workers—including those in the DoD—would be limited to the rate of GDP inflation for four years, beginning in 2014. This alternative would avert an average of \$4.6 billion

of the internal cost growth the CBO anticipates annually for the DoD and \$5.5 billion in costs during FY 2022.

Combine the military’s grocery and retail stores and end the commissary subsidy.

The DoD operates a commissary system to sell groceries on military installations; it also operates three separate base exchange systems that sell retail goods.³¹ Taxpayers subsidize the commissary system with about \$1.3 billion in the defense budget each year. Other subsidies include the tax-free status of commissary and exchange purchases as well as the real estate and buildings that house the stores (CBO 1997; CBO 2011a, 84). The DoD’s grocery and retail systems aim to provide goods and services to service members and retirees at lower prices than they would pay in civilian grocery or department stores. Beneficiaries of the grocery and retail benefits often complain that they can get better prices by watching for sales or going to big-box stores outside the base, however.

By combining the grocery system and the three retail systems and ending the \$1.3 billion subsidy to the commissaries, the DoD would save about \$1.5 billion a year on average during the coming decade.³²

Alternative 3-6 would take those actions, and in addition would offset service members’ increased grocery costs through cash allowances for active-duty members of \$400 per year on average.³³ The alternative would not offset the added costs for retirees, who make up more than one-half of eligible beneficiaries of the commissary and retail benefit. This alternative would save about \$900 million a year on average during the decade, and about \$1.3 billion in FY 2022 (CBO 2011a, 84).

REINING IN WEAPONS COST GROWTH

The cost to develop and purchase new military systems typically doubles or even triples from one generation to the next as designers incorporate new technologies and expand capabilities. In the past, individual weapon systems have also experienced substantial growth between the first formal estimates of their costs and the actual costs to deliver them. This is true for research and development work, as well as for production.

Some of the cost growth within a weapons program can be attributed to slowdowns in production imposed for budgetary reasons. A production plant sized to deliver forty aircraft per year typically operates less efficiently if the number built drops to twenty-four, and the learning that can reduce costs on the shop floor over time occurs more slowly. But much of the cost growth experienced by weapons programs occurs because cost estimates are too low to begin with; technologies or designs are immature or are misunderstood at early points in the

acquisition cycle when mistakes can still be avoided; designs are flawed or not sufficiently detailed—or some combination of those factors. When budgets are tight, such unplanned cost growth can lead to a troubling cycle: as costs per unit rise, the number of units purchased must be trimmed, leading to further cost growth because of shop floor inefficiencies and forgone learning.

The decade of 2000 witnessed an explosion of uncontrolled cost growth in major defense systems. Perhaps the most egregious was the Army's Future Combat System—actually a collection of systems—that was meant to replace the Army's ground combat vehicles with weapons that were much lighter, easier to transport, more maneuverable on the battlefield, and better connected through information technologies than those of the past. The Army spent tens of billions of dollars on the system before finally accepting what experts had said early in the program: the technologies the Army hoped to incorporate into it were not ready for prime time. Even if the system could be built, it would take vastly longer and cost far more than initially estimated (see, e.g., CBO 2006).

In recent years, lawmakers passed legislation meant to tighten and enforce the DoD's acquisition procedures and rules. Laws passed in 2008 and 2009 established organizational changes related to cost estimation and developmental testing inside the DoD and put in place new procedures for enforcing existing laws against going forward with systems whose costs grow well beyond initial estimates (Duncan Hunter National Defense Authorization Act 2008; Weapon Systems Acquisition Reform Act of 2009, 2009). The DoD also rewrote and tightened its own acquisition rules and vowed to enforce those rules more rigorously in future.

For a short period, the new measures seemed to work. For example, the Government Accountability Office (GAO) reported for three years in a row that program managers had more of the key knowledge they needed as systems moved from one step in the acquisition cycle to the next than in past programs (GAO 2012, 3). But by 2012, GAO found significant continued cost growth among the major weapons programs. Nearly one-half of all the programs GAO examined in 2012 experienced per-unit cost growth unrelated to quantity changes during 2011. Only about four in ten programs were within 10 percent of cost estimates put forward five years earlier and within 15 percent of their initial estimates (GAO 2012, 15–16).

The office also identified a range of serious problems that, if left unaddressed, will likely push weapons costs even higher (GAO 2012). For example, of the eight major programs that the DoD allowed to pass from one acquisition phase to the next during 2011, only one demonstrated that enough knowledge had been accumulated to warrant proceeding (GAO 2012, 3).

Systems continue to move into the development phase before key technologies are demonstrated in realistic environments. They continue to progress with immature designs, and to start into production before their program offices establish that manufacturing processes are well in hand (GAO 2012, 19–25). In addition, a number of systems—most notably the F-35 Joint Strike Fighter—are well into the production phase, even though their developmental testing is not complete and they still face significant challenges in research and development (GAO 2012, 10). Such so-called program concurrency invites expensive redesign and rebuilding after units are produced, and runs counter to existing regulations. The DoD is still lax in enforcing its own rules. Unless things change, weapon costs will continue to rise.

Alternative 3-7 would require the DoD to enforce its own acquisition procedures and to cancel systems facing estimated cost growth in excess of 10 percent over a period of five years. If tighter enforcement could avert even one-half of the cost growth that the CBO anticipates for weapons not yet in production, annual savings relative to the CBO's picture of defense internal cost growth could be as much as \$6 billion on average and \$10 billion in FY 2022.

IMPLEMENTING THE ALTERNATIVES

Implementing all of the alternatives discussed in this chapter could save the DoD more than \$30 billion on average between FY 2013 and FY 2022 (see table 1). By FY 2022, annual savings would be about \$47 billion (FY 2013 constant dollars). These alternatives would go a long way toward restraining the internal cost growth that otherwise will eat into the defense dollar. This section discusses the politics of change and explores the steps that will be needed to implement them.

Alternatives 3-1 to 3-6 affect military and civilian pay and military benefits. Implementing them will require congressional action in most cases and congressional cooperation in all.

Spending for pay and benefits grew so unremittingly during the past fifteen years that slowing such spending's growth may seem impossible. Two factors arguably fueled most of the growth: rapidly rising defense budgets, and the wars in Iraq and Afghanistan. In contrast, today's fiscal crisis and the imminent end of the wars open the window to change.

In 1998, the call for rapid growth in pay and expanded retirement benefits came not from the secretary of defense or from Congress, but from the service chiefs (see, e.g., Shelton 1998). The chiefs argued that the quality of military recruits was in decline and there were difficulties in staffing some military career fields. Their request came against the backdrop of intense national debate regarding how best to spend the \$4 trillion in surpluses that budget analysts anticipated would

TABLE 1.

Alternatives to Slow Internal Growth in Department of Defense

	FY 2013 billions of dollars	
	Average annual savings	FY 2022 savings
Alternative 3-1, health care	10	17
Alternative 3-2, limit military pay raises	5.6	6.7
Alternative 3-3, encourage early separation	2.5	5
Alternative 3-4, housing allowance	1.4	1.4
Alternative 3-5, limit civilian pay raises	4.6	5.5
Alternative 3-6, consolidate retail activities and end commissary subsidy	0.9	1.3
Alternative 3-7, slow growth in weapons costs	6	10
Total	31	46.9

Source: Author's calculations based on multiple sources. See text related to individual alternatives.

accrue over a decade under extant taxation and budgetary policies. Federal coffers were flush, and anything seemed possible. The administration and Congress found the chiefs' call persuasive. The wars in Afghanistan and Iraq reinforced concerns over pay and benefits. Pay rose rapidly, and new benefits were added almost every year for a time.

By 2007, however, uniformed and civilian defense leaders had grown worried that mounting personnel budgets were eating into the funds they needed to sustain crucial military capability. The DoD and successive administrations requested a slowdown in across-the-board pay raises and began an effort to adjust the cost-sharing arrangements for military retiree health care. Congress rejected those proposals.

Today, the situation is different. The wars are close to an end, recruiting and retention are better than ever, and the federal government faces rising debt, instead of rising surpluses, for as far as the eye can see. For DoD pay and benefits, the environment looks more like the belt-tightening period that began in the mid-1980s—when Congress shrank the military retirement plan and cut military pay raises below those in the private sector—than like the expansive period that began in 1998.³⁴

To implement Alternative 3-1 and slow the rapidly growing costs of military health care, the DoD should again request the changes it proposed in its FY 2013 budget. In an era of fiscal restraint, Congress should include the relevant changes in the National Defense Authorization Act.

Health care for military retirees can be considered as one piece of the nation's overall health-care puzzle. As such, it can be considered by Congress in conjunction with other

deliberations about federal spending on health care for the elderly. In fact, one element of Alternative 3-1—the establishment of a premium for Tricare for Life coverage for Medicare-eligible military retirees—falls with Medicare and other entitlements on the mandatory side of the federal budget; it can be handled in Congress through the expedited procedures of the budget reconciliation process.

Alternative 3-2 to limit the size of military pay raises for a period of four years also requires congressional action. Between 2000 and 2010, lawmakers granted pay raises well above inflation, even in years when the DoD requested smaller raises. More recently, however, Congress has granted raises consistent with wage growth in the private sector. To implement Alternative 3-2, the DoD should request a military pay raise consistent with GDP inflation. Congress should honor that request in the National Defense Authorization Act.

Under Alternative 3-3, the military services would encourage more uniformed personnel to depart well before becoming eligible to retire. The alternative addresses the rising cost of retiree benefits by creating fewer retirees—thus avoiding the politics of limiting benefits or raising costs for individual retirees.

To a large extent, the choice of how many individuals to retain is the purview of the services. To implement this alternative, the personnel chiefs of each service should craft plans for reducing the number of individuals who serve until retirement while ensuring appropriate staffing by rank and career field. The service chiefs and the secretaries of the military departments, in consultation with the secretary of defense and appropriate congressional committees, should make the

necessary adjustments to up-or-out gates and promotion rates to put those plans into operation.

Realizing Alternative 3-4 with a reduction in the share of local market housing prices represented in the military housing allowance will require cooperation between the secretary of defense and Congress. Current law calls for housing allowances to pay the full cost for rank-appropriate housing on the local rental market. Implementation of the alternative requires Congress to rewrite that legislation. The secretary of defense should outline a plan for phasing in the lowered allowances, and request that Congress rewrite the legislation to put the plan into effect. Congress should include the needed language in the National Defense Authorization Act, and should mark the military personnel accounts in future authorization and appropriation legislation to reflect the change.

The number of civilians working in the DoD grew rapidly during the wars in Iraq and Afghanistan. Alternative 3-5 would limit across-the-board pay raises for those employees for four years. The 801,000 defense civilians are part of the wider workforce of federal civilians, and requests for their pay raises rest with the White House. The secretary of defense should work with the Office of Management and Budget and the Office of Personnel Management to develop the request for

the president's annual budget. Congress should enact the pay raises, which will be set to match those of military personnel.

Alternative 3-6 would combine the grocery and retail systems of the DoD, end the commissary subsidy, and provide a grocery allowance to active-duty service members. Implementing the alternative will require the DoD to request authority to reorganize the grocery and retail systems. The secretary of defense should also request that Congress end the commissary subsidy and authorize the new grocery offset benefit for serving troops. Congress should make those changes in the National Defense Authorization Act and reflect them in future appropriations.

None of these alternatives will be easy to implement. All of them are likely to face political hurdles from important constituencies, including interest groups representing military personnel, military retirees, and veterans.³⁵ Adopting them will require the firm commitment and leadership of the uniformed military, the secretary of defense, the White House, and Congress. Absent such reforms, however, the U.S. military faces a decade of erosion in size and capability as it struggles to adapt to lower budgets in the face of mounting internal costs.

Chapter 4: Options to Reduce Forces

The alternatives considered in chapter 3 can stem the DoD's internal cost growth and thus help that department hew to a budget that rises each year for inflation. They will not push defense spending below the FY 2012 level in real terms, however. Reducing defense budgets in line with the BCA or decreasing them more deeply will likely require cutbacks to force structure.

Significant changes in force structure can be beneficial regardless of budget concerns. The past two decades gave ample evidence of the perils of a national security strategy that sees virtually any conflict around the globe as a vital interest for the United States and that aims to remake the rest of the world in America's image. A growing number of experts argue that a more restrained strategy would reap important benefits that go well beyond defense contributions to a brighter fiscal future (see, e.g., Bacevich 2010, particularly the prescriptive final chapter; Friedman 2010; Gholz, Press, and Sapolsky 1997; Mandelbaum 2010; Posen 2013).

In January 2012, the White House and the DoD together unveiled a new security strategy that establishes priorities for the future (White House and DoD 2012). The strategy still leans forward and is a far cry from restraint. Nevertheless, the document outlines a more focused and selective approach to national security than that of recent years. In his transmittal letter accompanying the document, Secretary of Defense Leon Panetta describes the United States as being at a "strategic turning point after a decade of war."

With the war in Iraq behind us and combat operations in Afghanistan winding down, the document prescribes a greater focus of the military effort toward Asia and the Pacific region. It suggests that in the future rising powers like China will pursue a wide range of means to thwart the ability of the U.S. military to operate effectively in distant theaters—what the DoD calls the "anti-access/area denial challenge." The White House/DoD document sees building the capacity to

operate around the globe, despite those anti-access and area denial problems, as a top priority for the armed forces (White House and DoD 2012, 4–6). The new strategy puts the types of military operations of the past decade—stability operations, counterinsurgency, and humanitarian operations—at the bottom of the list of future military concerns.³⁶ A strategy of restraint would similarly focus attention more squarely on the potential for conflict among great or rising powers—and thus on China (Eugene Gholz, Daryl G. Press, and Benjamin Valentino, "Time to Offshore Our Troops," *New York Times*, December 12, 2006; Posen 2007; Sapolsky et al. 2009).

China's population and geographic area are immense. Many observers believe that a war involving that country would be fought largely at sea and in the air. Thus, the future missions that the DoD embraced in January 2012 would seem to require

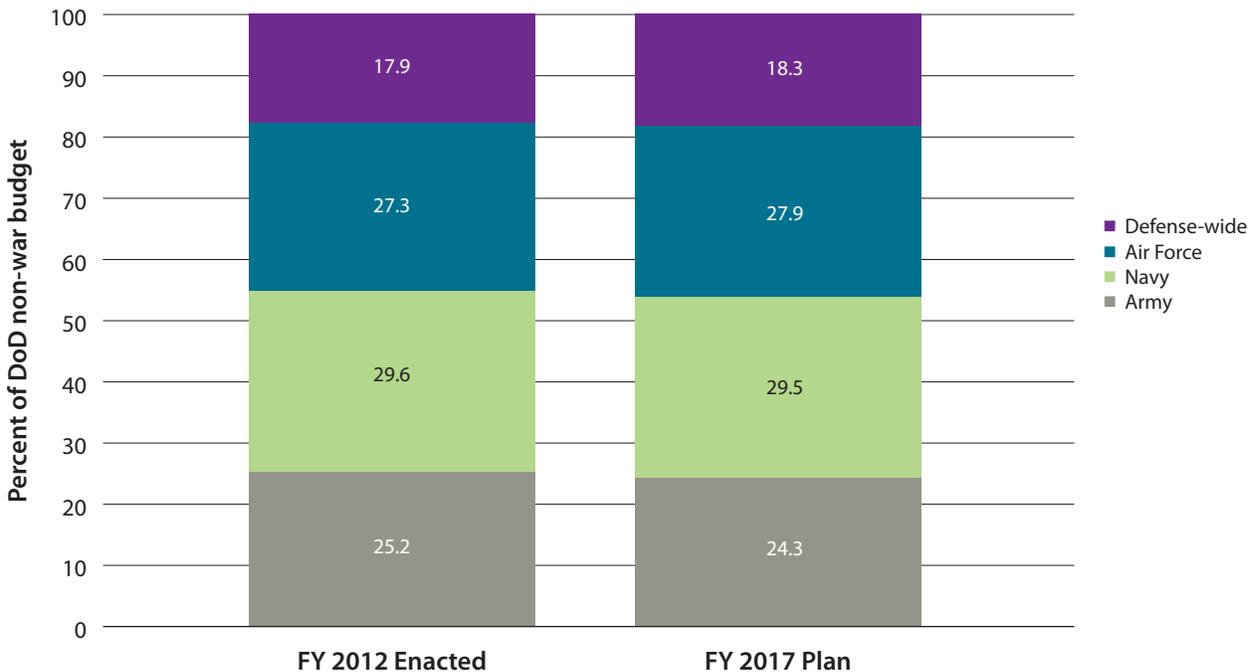
How any budget cutbacks are distributed among the services will determine the future shape and capabilities of the military.

relatively more of the Navy and to some extent the Air Force, and comparatively less of the Army than the boots-on-the-ground wars of the past decade.

How any budget cutbacks are distributed among the services will determine the future shape and capabilities of the military. It will have important implications for the missions the armed forces can conduct effectively.

FIGURE 8.

Shares of the Department of Defense Non-War Budget Devoted to Each Military Department, FY 2017 versus FY 2012



Source: Author's calculations based on Office of the Under Secretary of Defense (Comptroller) (2012, tab. 6-26.)

Yet the budget plan the DoD submitted in February 2012 does not reflect a significant shift in relative resources away from the Army and into the sea and air services. Even by FY 2017—well after combat operations in Afghanistan are meant to end—the plan would shift less than 1 percent of the DoD's funds away from the Army (see figure 8). The Navy would hold virtually the same share of the budget as in FY 2012, while the Air Force would gain a few tenths of a percentage point. The defense-wide accounts that capture department spending that falls outside the services would also gain a small share.³⁷

The decision not to shift resources significantly among the military departments reflects a long-standing practice of the DoD. At least since the middle of the Cold War, the share of defense spending allocated to each service has barely budged. Even when presidents or secretaries of defense enter office imagining that they will shift resources among the services, they leave office not having done so.

Thus, even if the next secretary of defense believes that such a shift is warranted, he or she may not be able to implement it. The options offered in this chapter consider how the armed forces might look in the future under two conditions: either the share of defense spending devoted to each military department remains about where it is in FY 2012, or budget shares are shifted to reflect an increase in the relative relevance

of maritime forces in a strategic shift toward Asia and the Pacific.

The next two sections of this chapter consider two options:

- Option 4-1: Quickly reduce each military department's non-war budget by 10 percent in real terms relative to the DoD's FY 2013 plan; and
- Option 4-2: By FY 2015, reduce DoD non-war budgets by 16 percent in real terms relative to the DoD's FY 2013 plan, with a strategic focus on forces for rebalancing toward Asia and the Pacific.

The chapter ends with a brief discussion of implementation.

OPTION 4-1: DISTRIBUTE THE BCA REDUCTIONS PROPORTIONATELY AMONG THE MILITARY DEPARTMENTS

This section explores how the armed forces might be sized, shaped, and equipped if the DoD and other national defense players are required to reduce budgets in conformance with the BCA, and if the budgets of the military departments are reduced proportionately, as is past practice. It examines the implications of Option 4-1 for the missions that the U.S. military would be positioned to conduct in the future.

As discussed in chapter 2, the BCA would decrease the defense non-war budget by about 10 percent compared with the plan submitted to Congress with the president's FY 2013 budget request. This represents a cut of about 13 percent in real terms relative to the FY 2012 non-war budget. Under this option, the Army, Department of the Navy, and Air Force non-war budgets would each fall by 13 percent in real terms from their levels in FY 2012.³⁸ (This assumes that an equivalent reduction can be made to the defense-wide budget that falls outside of any of the services. One of the biggest drivers of that budget is military health care. If health costs can be curbed as suggested in chapter 3, then this is a fairly realistic assumption. If not, however, each service will likely find itself with less money than this option supposes.)

Implementing the reductions to personnel levels and force structure outlined in this section in a methodical way would take more than a year. To accommodate an orderly downsizing, Congress might wish to stipulate a less abrupt budgetary cutback than the one-year drop called for under the BCA. Alternatively, the services may find it necessary to hold back on some investment or sustainment programs while reducing personnel and force levels between FY 2013 and FY 2015.

Changes to the Army

The plan put forward by the DoD with its budget request for FY 2013 would reduce the size of the combat Army from forty-five to thirty-seven maneuver brigades. Option 4-1 would eliminate an additional five combat brigades from the active-duty Army, leaving the service's active component with thirty-two brigades. The active-duty Army would shrink from 562,000 soldiers in FY 2012 to 430,000 troops.³⁹ The Army's reserve component would not be reduced appreciably.⁴⁰

The Army canceled its most expensive equipment investment programs in recent years, leaving the service with a lean non-war budget for research and development and for procurement of new equipment. Under this plan, equipment purchases would be slowed to match the new anticipated size of the Army, but no procurement program would be canceled. The Army will likely find, however, that it cannot afford an expensive replacement for its Bradley Fighting Vehicle, and that a program that upgrades and refurbishes existing Bradleys makes more sense.

Unfortunately, a sizeable fraction of troops in the Army today cannot be deployed to any war, in many cases for medical reasons. In 2012, some 19,000 soldiers could neither deploy nor be released from service because their disability cases were tied up in a lengthy process of adjudication that involves the individual, the Army, and the Department of Veterans Affairs (VA) (Bostick 2012, 15). The Army and the VA are working to speed the process, but in the meantime, five brigades worth

of soldiers are missing from deployable units (Bostick 2012, 15). The future capacity and effectiveness of the Army depends on resolving these cases. In both of the options outlined in this chapter, I assume that the large majority of these cases can be brought to closure, and the soldiers either separated or returned to fighting units, within a year or two of the end of combat operations in Afghanistan.

With the 430,000 troops of Option 4-1, the active-duty Army would be about 12 percent smaller than it was in 2001. It would still be able to engage with NATO allies and to provide a deterring presence on the Korean Peninsula, as the DoD currently plans. It would also be highly capable of and ready for missions at the lower end of the conflict spectrum, including humanitarian operations, smaller peacekeeping operations, and disaster relief.

In addition, the Army would be fully capable of conducting an operation of the combined size of Iraq and Afghanistan that lasted for a year or so. Alternatively, it could continue its presence missions in Europe and Asia while conducting two operations on the level of the Persian Gulf War of 1991, each aimed at halting an enemy attack. With participation from the Marine Corps and the Guard and Reserve, U.S. armed forces would still have the capacity to win decisively in one of those wars—that is, march to the enemy's capital, plant the flag there, and remain to occupy the territory for a period. Like the force currently planned by the DoD, however, the U.S. military would no longer be large enough to carry out “win and hold” operations in two places at the same time.

Like the force the DoD envisioned in its FY 2013 budget request, this Army would be significantly more stretched than it was during the height of the wars in Iraq and Afghanistan to maintain the needed rotations if wars of that size lasted for several years. If policymakers again commit to a war or combination of wars requiring as many as 200,000 ground troops for years at a time, the Army would have to be expanded.⁴¹

Changes to the Navy and Marine Corps

The U.S. Navy has a fleet of 284 warships today. It hopes over the coming decades to expand the fleet to more than 300 ships (O'Rourke 2012, 9). The Marine Corps has three Marine Expeditionary Forces (MEFs), with three active-duty divisions and one reserve division.

For decades, the Navy has persistently built fewer ships than its plans called for. Part of the reason for this is persistent, unplanned growth in the costs of its ships. Another factor is that the Navy makes long-term shipbuilding plans under the assumption that future budgets will be significantly larger than past ones—or that the service itself will be able to devote a larger share of its budget to shipbuilding than it has in the past. For

TABLE 2.

Navy Ships under Options 4-1 and 4-2

Ship Type	Number of Ships		
	Navy plan for 2032	Option 4-1	Option 4-2
Aircraft Carrier	11	9	8
Surface Combatants and Mine Countermeasures	135	115	90
Attack Submarines and SSGNs	45	38	44
Ballistic Missile Submarines	10	8	10
Amphibious Warfare Ships	32	27	30
Combat Logistics and Support Ships	62	53	53
Total Ships	295	250	235

Source: O'Rourke (2012, 9); and author's calculations.

example, the Navy's FY 2013 shipbuilding plan assumes that it will be able to spend about 10 percent more on ship construction and conversion during the coming decade than on average over the past three decades—despite the budget constraints already in place in the DoD's FY 2013 plan. Between 2023 and 2032, the service assumes its shipbuilding funds will outstrip those of past decades by 35 percent (CBO 2012b, 11).

Under Option 4-1, the Navy could afford to build and operate a fleet of about 250 ships. Sized at this level, the Navy could match its shipbuilding program more realistically to its future budget. The number of active-duty sailors and Marines would decline from 528,000 in FY 2012 to 462,000 (leaving about 294,000 sailors in the Navy and 168,000 Marines).

Of course, how many ships the Navy can afford depends upon how much each ship costs to build and operate. The new Littoral Combat Ship (LCS) is smaller than the service's other warships, and its crew capacity is severely limited. In 2010, the Navy agreed (subject to congressional appropriations) to purchase twenty LCSs from two shipbuilders over a period of several years, at prices significantly lower than cost experts had predicted (CBO 2012b, 24). The Navy also expects that the costs to operate the new ships will be lower than for previous ships. If all of its ships were LCSs, the Navy could afford far more than 300 ships, even at reduced budgets. On the other hand, if they were all aircraft carriers, it could not afford nearly as many.

This option assumes that the Navy would retain ships in the new plan in proportion to their numbers in the Navy's current plan for two decades from now. Table 2 illustrates the number of ships of each type the Navy would have under the two options outlined in this chapter, compared with the number in the Navy's plan for FY 2032.

The Option 4-1 fleet would eliminate two aircraft carriers and their associated air wings, keeping a total of nine carriers and eight air wings, in contrast with eleven carriers and ten air wings under the Navy's current plan. The Navy already plans to operate a ten-carrier fleet during FY 2013 and FY 2014, and the DoD has indicated that the risk of that carrier fleet is acceptable in the context of today's presence missions, the ongoing war in Afghanistan, and other potential near-term operations (DoD 2010, 45–47). With nine carriers and the surface fleet proposed in this option, the Navy would likely give up the goal of keeping a carrier in the Mediterranean or the Atlantic for much of every year. It could still keep the surface elements of one carrier battle group based in Japan and another carrier group operating full time in the Indian Ocean. In addition, the fleet would retain the capacity to surge at least three more carrier groups within about one month.

The option falls short of the number of attack submarines the Navy might need to support all of its carrier battle groups and conduct the other operations expected of them. It also deepens a shortfall that already exists in the number of amphibious warfare ships the Marine Corps would like to support its expeditionary operations (CBO 2011b, 9).

Option 4-1 reduces the number of nuclear ballistic-missile-carrying submarines (SSBNs)—the most secure and survivable leg of the nation's nuclear triad of submarines, long-range bombers, and intercontinental ballistic missiles (ICBMs).

The DoD's FY 2013 plan would remove about 20,000 Marines from the Marine Corps between FY 2012 and FY 2017. It also calls for the elimination of four active-duty and one reserve Marine infantry battalion as well as several tactical air and artillery units. The Marine Corps is required by law to retain at least three active-duty divisions, but the DoD has significant

leeway regarding how the divisions are configured. This option would trim Marine Corps force structure consistent with reducing the service by another 14,000 Marines.

Changes to the Air Force

The Air Force today has sixty combat-coded tactical air squadrons between its active and reserve components.⁴² Under the plan put forward with the FY 2013 budget, the service intends to shed six of them, leaving fifty-four squadrons (Department of the Air Force 2012, 3). Option 4-1 would quickly eliminate another seven squadrons, leaving the service with forty-seven squadrons, with about 960 fighter and attack planes. The option assumes proportional reductions to other elements of the service's force structure, including airlift and air refueling, surveillance aircraft, long-range bombers, ICBMs, and space operations units. Active-duty end strength would drop rapidly to about 290,000 airmen, compared with some 329,000 airmen in the FY 2013 plan.

During the past two decades, the capability of the Air Force to deliver weapons precisely on targets has grown markedly, despite cutbacks in the size of the tactical force. The same period witnessed the growth of a fleet of unmanned aerial vehicles that increasingly took on combat as well as surveillance and communications roles. Both the 2010 *Quadrennial Defense Review* and the January 2012 strategy update note that the advanced technologies incorporated in present and future systems mean that the service can do more than before with fewer aircraft (DoD 2010; White House and DoD, 2012).

Moreover, the tactical Air Force today is greatly oversized for the wars it was called upon to fight in recent years, including the onset of operations in Afghanistan in 2001, support for the initial invasion of Iraq in 2003, and the air war over Libya in 2011. With their short ranges and land basing, Air Force tactical aircraft are arguably not well suited to wars that pose significant anti-access challenges—as even a near-term war against China might. On the other hand, Air Force fighters and attack aircraft would be of great use in wars against an enemy like Iran or Syria. Those countries' air defenses are significant, but defeating them and establishing control of the air would by no means require the Air Force to be sized at the level envisioned in the FY 2013 budget. The further reduction suggested in this option will leave the Air Force fully capable of fighting effectively in two wars where land basing is not under serious challenge.

The drawdown of Air Force mobility and tanker assets discussed here could pose a problem for the other services, however. The Air Force plan for FY 2013 calls for the elimination of 150 such aircraft—about 15 percent of the fleet—during the coming five years. The Army is already concerned that Air Force airlift resources will not meet its needs in a rapidly

unfolding ground war. Assuming the service is constrained to a proportional share of budget cuts at the BCA level, a better choice for the DoD overall might well be for the service to shed more tactical units and retain a larger share of its other fleets.

Reductions under this option would trim the ICBM force consistent with the other cuts to the service. The Air Force has argued in the past that such a reduction is inefficient; eliminating a few tens of missiles does nothing to reduce the costs of command and control, infrastructure, and upkeep that drive spending for the fleet. Achieving sizeable savings would require the elimination of the entire force.

Changes to intelligence funding and defense agencies

Intelligence spending reportedly makes up a significant fraction of the DoD budget. By some estimates, as much as 85 percent of the \$80 billion total intelligence budget for FY 2012 fell somewhere in the defense budget. Much of it is believed to reside in the budgets of the military departments. Option 4-1 rapidly reduces intelligence spending in the DoD by 10 percent relative to its FY 2013 plan, consistent with cutbacks to the military departments.

Beginning in 1998, the nation's intelligence spending rose more sharply than the overall military budget, more than doubling in real terms between 1998 and 2010.⁴³ Intelligence budgets have since declined modestly. The president's FY 2013 budget called for another 12 percent reduction in real terms, to about \$72 billion. This option would bring intelligence spending to a level about 80 percent higher in real terms than it held in 1998.

The option would also trim the budgets of the independent defense agencies by a total of 10 percent relative to the president's FY 2013 plan. (Some of those agencies, such as the Defense Intelligence Agency, the National Geospatial-Intelligence Agency, the National Security Agency, and the National Reconnaissance Office, are part of the intelligence community and included in the discussion of intelligence spending in the paragraph above; their budgets would not be cut twice.) Nonintelligence agencies in this group include support agencies like the Defense Logistics Agency and the Defense Contract Audit Administration as well as agencies whose main roles are technology development or acquisition, such as the Missile Defense Agency and the Defense Advanced Research Projects Agency. In this option's spirit of proportional budget reductions, each agency's budget would be reduced by 10 percent—though in reality the DoD could choose to offset smaller cuts to some agencies with larger cuts to others.

In addition, some of the agencies in place today can be eliminated in the coming years. These include the Office of the Special Inspector General for Iraq Reconstruction and the Office of the Special Inspector General for Afghanistan Reconstruction.

OPTION 4-2: CUT BUDGETS BY 16 PERCENT WHILE REBALANCING TOWARD ASIA AND THE PACIFIC

Option 4-2 would size, shape, and equip the armed forces to emphasize future missions in Asia and the Pacific, while reducing annual defense budgets in real terms by 16 percent from the president's request for FY 2013. For the total defense budget, the option reflects the proportional-cuts path for deficit reduction described in chapter 2. For the military departments, it reflects the strategic rebalancing toward future operations in Asia and the Pacific that the DoD outlined in its January 2012 strategy update. This section examines the forces that might result and the missions they would be able to conduct in the future.

In keeping with the strategic rebalancing, this option adjusts force structure to emphasize the maritime wars that seem more

from which to build quickly should the service be required to expand in the future.

The Army is the most manpower-intensive of the armed services. By reducing that service more deeply than the others, Option 4-2 would also help to curtail the growing costs of military pay and benefits.

Like Option 4-1, this option trims the Army's procurement programs consistent with the new force structure, but does not require the Army to cancel key development or procurement programs. As in the previous option, however, the service might find its new combat vehicle program to be overly expensive, and choose instead to refurbish and upgrade existing Bradley Fighting Vehicles, or alternatively to produce an upgraded version.

With the 370,000 troops of Option 4-2, the Army would be about 25 percent smaller than it was in 2001. Consistent with the rebalancing toward Asia, the service would remove most of its permanent presence from Europe. It could still retain a small presence on the Korean Peninsula. In keeping with the rebalancing strategy (and consistent with a more restrained foreign policy), the Army should no longer be the tool of first resort for solving problems around the globe. Rather, the service should focus on preparing to fight a major war in situations where core U.S. interests come under serious challenge. The service would still be highly capable of and ready for missions at the lower end of the conflict spectrum, including humanitarian operations, smaller peacekeeping operations, and disaster relief—but political leaders would have to understand that using it routinely in those roles would eat into its capacity to fight in a big war.

With participation of the Guard and Reserve, the Army would be fully capable of conducting an operation of the combined size of Iraq and Afghanistan that lasted for a year or so. Alternatively, it could conduct one and possibly two operations aimed at defending against an enemy invasion of a distant country. With participation from the Marine Corps and the Guard and Reserve, U.S. armed forces would still have the capacity to win decisively in one of those wars. Like the force currently planned by the DoD, however, the U.S. military would no longer be large enough to carry out “win and hold” operations in two places at the same time.

This Army would not be able to sustain the needed rotations for a long war similar to the combined effort in Iraq and

...the service should focus on preparing to fight a major war in situations where core U.S. interests come under serious challenge.

likely in Asia and the Pacific region. It reduces the Army more sharply than the other services. In the Air Force, it reduces the short-range, land-based tactical air forces that would be particularly vulnerable to anti-access/area denial challenges in the region, and sizes them to provide battlefield support to a smaller Army. The option favors naval forces, particularly those that would be most useful in a maritime war against a rising power in Asia.

Changes to the Army

Option 4-2 reduces the Army's budget by 20 percent compared with the president's request for FY 2013. It eliminates eleven brigades from the active Army, in addition to the eight brigades the service plans to cut under its current plan. The result is an active-duty Army of twenty-six maneuver brigades and about 370,000 soldiers. The option retains the Army National Guard and Reserve at their currently planned sizes, providing a base

Afghanistan. If policymakers again commit to a war or combination of wars requiring as many as 200,000 ground troops for years at a time, they would need to grow a significantly larger Army.

Changes to the Navy and Marine Corps

This option would reduce the Department of the Navy budget by 10 percent relative to the FY 2013 plan—the same as in Option 4-1. Consistent with the rebalancing strategy, it makes changes within the naval force to prepare it better for a blue-water fight in an access-challenged environment. Like Option 4-1, this option keeps a Navy of about 294,000 sailors and a Marine Corps of about 168,000 Marines.

With 235 ships, Option 4-2 retains a fleet that is smaller than that of Option 4-1, but better matched to anticipated missions and also better organized to make full use of the capabilities of each element. It reduces the carrier fleet from nine ships in Option 4-1 to eight ships. It reduces the number of LCSs from fifty-five ships in the current plan to thirty, but retains enough large surface combat ships to support fully the remaining carriers. It builds relatively more nuclear-powered attack submarines (SSNs) than Option 4-1, retaining a fleet of forty-four of those ships for the longer term. It also restores three of the amphibious warfare ships eliminated under the first option, bringing the number of ships supporting the Marine Corps to thirty.

As in Option 4-1, this eight-carrier Navy would abandon the goal of keeping a carrier in the Mediterranean or the Atlantic for much of every year. It could still keep one carrier battle group based in Japan and one operating full time in the Indian Ocean. In addition, the fleet would retain the capacity to surge at least two more carrier groups within about one month, with the potential for a third within two or three months.

The larger attack submarine fleet of this option is better suited to support in full the remaining carrier battle groups and conduct other operations that will be crucial in an access-challenged environment. The option also sizes the amphibious fleet to match the expeditionary needs of the Marine Corps more closely (CBO 2011b, 9).

Option 4-2 retains a fleet of ten nuclear SSBNs—two more than the previous option. The larger fleet recognizes the crucial role of this leg of the triad in nuclear deterrence and offsets the elimination of the ICBM force proposed in the discussion of the Air Force below. This option retains a Marine Corps sized as for the previous option.

Changes to the Air Force

Option 4-2 reduces Air Force spending by 18 percent in real terms, relative to the president's budget request for FY 2013. It retains an active-duty component of about 267,000 airmen.

Compared with the president's FY 2013 plan, Option 4-2 would eliminate twelve fighter and attack squadrons, leaving the service with forty-two squadrons, with about 850 fighter and attack planes. The option would make smaller cuts to the airlift, air refueling, and surveillance fleets that would provide important support during a major war in an access-challenged environment. Under this plan, Air Force mobility and tanker assets would be better matched to meet the needs of the Army.

The resulting land-based tactical fleet would be well matched to provide close air support to the smaller Army of this option. It would also retain 150 F-22s capable of air-to-air operations against highly capable enemy fighters in a challenging air defense environment. Programs aimed at developing that aircraft's ability to bomb targets on the ground would be ended.

This option would outfit the Air Force with relatively more long-range bombers than Option 4-1. It would preserve Air Force plans to build its new bomber, but drop expectations for stealth and focus the research and development program on developing an affordable plane that can be equipped with nuclear as well as conventional payloads. The new bomber would be designed to carry significant numbers of cruise missiles in addition to precision-guided bombs, and thus be well suited to standoff operations in an access-challenged environment.

The reductions and reshaping suggested in this option will result in an Air Force fully capable of supporting ground operations in a major war where land basing is not under serious challenge. Together with the air assets of the Navy and Marine Corps, the service will be better positioned to suppress enemy air defenses, establish and sustain control of the airspace, and conduct important air-to-ground missions even when access is challenged.

This option would retain vital space operations elements. It would wholly eliminate the ICBM force. The elimination of more vulnerable ICBMs would be offset by the Navy's retention of a relatively larger fleet of secure and survivable SSBNs, and by the new Air Force bomber.

Changes to intelligence funding and defense agencies

Option 4-2 reduces intelligence spending in the DoD by 16 percent relative to the FY 2013 plan. This would still leave intelligence spending at a level about 62 percent higher in real terms than in 1998. The option would also trim the budgets of the independent defense agencies by a total of 16 percent relative to the president's FY 2013 plan (with care not to assess the intelligence agencies twice).

A smaller force, better suited to the future

Compared with the president's plan for FY 2013, Option 4-2 effects a further shift in emphasis toward those naval and air

TABLE 3.

Comparison of Options

	FY 2012 Force	Planned Force	Option 4-1	Option 4-2
Active Army Brigades	45	37	32	26
Active Army End Strength	562,000	490,000	430,000	370,000
Navy Ships	284	300+	250	235
Active Navy End Strength	325,700	319,500	294,000	294,000
Active Marine Corps Divisions	3	3	2+	2+
Active Marine End Strength	202,100	182,100	168,000	168,000
Air Force Tactical Squadrons	60	54	47	42
Active Air Force End Strength	332,800	328,600	290,000	267,000
Total Active End Strength	1,422,600	1,320,200	1,182,000	1,099,000

Sources: CBO (2012b); DoD (2010); Office of the Under Secretary of Defense (Comptroller) (2012); Office of the Under Secretary of Defense (Comptroller)/Chief Financial Officer (2012); White House and Department of Defense (2012); and author's calculations.

forces that are likely to contribute more to fights in Asia and the Pacific. The option devotes a larger share of the defense budget to the Department of the Navy and a smaller share of that budget to the Army than either the FY 2012 budget or the president's plan for the future. It trims the share held by the Air Force.

The option results in a military significantly smaller than today's, but one that is shaped more in keeping with the missions currently envisioned by the DoD. Forces under the option are deliberately less ready to undertake a long counterinsurgency war. This military should not be called upon routinely to settle problems around the globe that are not directly tied to U.S. vital interests. If it is, there is a risk that it will not be ready to fight and win the major wars for which it is shaped.

Nevertheless, the force retains the capability to win decisively in a major theater war, while conducting a smaller operation elsewhere. Even under this option, the United States will retain by far the most powerful military in the world well beyond the decade under consideration in this report.

A STRONG, HIGHLY CAPABLE FORCE

Table 3 summarizes the force structures considered in this chapter and compares them with the current force and the force planned by the DoD. The two options represent paths that are significantly different. Option 4-1 is budget-driven, in that it makes proportional spending cuts across the services to reduce the total defense budget by 10 percent from the FY 2013 plan. Option 4-2 makes deeper budget cuts, but specifically preserves and enhances forces that are likely to contribute the most to the operations the DoD envisions for the future.

Compared with today's forces or the president's FY 2013 plan, both options raise the level of risk for some future missions and should be understood by policymakers as foreclosing others. The second option in particular fits well with a substantially more restrained foreign policy than that of the past decade.

Nevertheless, under either of the options proposed here, the United States will retain the strongest, best-funded, best-equipped, and best-trained armed force in the world, with significant operational and strategic depth provided by a sizeable and well-equipped reserve component.

Under either option, the force will be fully capable of winning decisively in one major theater war, while helping an ally defend against attack in about the same timeframe. Units will be highly ready to deploy to a distant theater. The Navy will sustain significant presence in areas of high interest. Leaders will be able to send multiple ground-force brigades to conduct humanitarian or peacekeeping missions far from home. But neither force will be able to sustain itself in a long, sizeable occupation or counterinsurgency operation without drawing heavily on the Guard and Reserve and without a significant military buildup.

IMPLEMENTING THE OPTIONS

Options 4-1 and 4-2 would both save significant sums relative to the FY 2013 plan. The legislation required to implement Option 4-1 is arguably already in place, in the form of the BCA of 2011. Even if Congress averts the sequestration now scheduled for March 2013, the BCA calls for about a 10 percent reduction relative to the president's FY 2013 plan in FY 2014 to FY 2021.

To implement Option 4-1, the secretary of defense would prepare fiscal guidance that reduces the budget of each military department by the same percentage. The secretary also should issue policy guidance outlining any specific expectations for service programs. The service chiefs and secretaries of the military departments will develop their plans and budgets accordingly. As in other situations, Congress will offer adjustments among programs and activities through authorization and appropriation acts; legislators will want to avoid appropriations above the annual BCA levels for national defense, however, which would trigger sequestration.

Current law restricts the DoD's freedom to cut back in some areas. For example, the Navy is required to retain at least eleven aircraft carriers, and the Marine Corps must keep at least three active-duty divisions. If DoD budgets are to be reduced consistent with levels under the BCA, then Congress will need to reconsider such laws in light of the smaller appropriations.

It could take two or more years for the services to complete in a methodical way the personnel and force structure reductions suggested under this option. To accommodate an orderly process, Congress may want to adjust the slope of the BCA cutbacks to make them less abrupt. Alternatively, the armed services might find it necessary to hold back on some investment and sustainment programs to achieve some of the savings needed between FY 2013 and FY 2015.

Option 4-2 makes deeper reductions than the BCA calls for, and does not distribute those reductions proportionately among the services. Both the depth of the reductions and their disproportionate allocation make implementation more complex and magnify the importance of communication and partnership between the DoD and the services, and between the DoD and Congress.

The decision to undertake a 16 percent reduction might well begin in a future fiscal bargain between Congress and the president. If so, lawmakers would likely stipulate the reduction in a new law—similar to the BCA—and also incorporate it into the annual budget resolution. The secretary of defense would then have little leeway as to the size of the total DoD request. There would be leeway regarding the distribution of cutbacks among the services. The secretary of defense would provide fiscal and policy guidance to the DoD's components consistent with the shifts in missions, budget share, and forces outlined in Option 4-2.

Making the guidance stick will require early discussions between the secretary and the service chiefs and also with Congress, which in the past has looked unfavorably on changes to service budget shares. Finally, implementation of this option will require Congress to reflect the changed realities in annual authorization and appropriation acts.

Chapter 5: Questions and Concerns

The policy alternatives and options proposed in this report will be met with objections from a variety of quarters. This chapter discusses five areas of concern raised by critics in the past:

1. Reductions in military spending would result in a military too weak to defend the nation.
2. Policymakers will continue to reach for the military tool regardless of articulated strategy.
3. The personnel-related alternatives of chapter 3 would break faith with service members and retirees who served honorably and sacrificed for their country.
4. Reductions in equipment investment would harm the industrial base.
5. Congress will not support the needed changes.

The following subsections treat those concerns in turn.

1. REDUCTIONS IN MILITARY SPENDING WOULD RESULT IN A MILITARY TOO WEAK TO DEFEND THE NATION.

Critics of reduced military spending argue that preserving U.S. power requires spending more, not less, on defense. Some even favor the establishment of a floor—generally 4 percent—on the share of the economy to be devoted to defense. Assuming that the economy grows faster than inflation, this of course would translate into a significant rise in real defense spending over the course of a decade.

Proponents of that view generally hope that steadily growing U.S. military budgets—and the fierce and technological armed forces they underpin—will dissuade rising powers even from entering the competition by building up their militaries.⁴⁴

In fact, the opposite is more likely true. Trying to hold U.S. defense spending at 4 percent of GDP will make it harder for the United States to deal with fiscal and economic realities that must be addressed; it will ultimately weaken the nation. The better choice is to make this the decade of fiscal and economic improvement.

The global economic picture makes it highly unlikely that rising powers can be held from entering the competition for military power in any case. From an economic point of view, the world is arguably multipolar already. China's GDP is rising rapidly, despite the current slowdown in that country. The CIA estimates that China had three-quarters of the GDP of the United States in 2011.⁴⁵ The GDPs of India and Brazil are also large and rising quickly. It is likely only a matter of time before multipolarity extends to the military sphere as well. That being the case, the United States would be wise during the coming decade to develop the tools and adopt the posture needed to advance its interests and achieve security when other nations do compete for military power.

Moreover, even at lower levels of defense spending, the United States will retain the strongest armed forces in the world for decades. China's military spending today is less than 20 percent of the U.S. non-war defense budget (International Institute for Strategic Studies 2012, 467–473). Even if that country could outspend the United States on defense two decades from now—a questionable hypothesis—it could take many years to build up the sort of military power the United States will still enjoy, assuming that we can get and keep our economic house in order. Russia's military spending is less than 12 percent of that of the United States, and trends for that country are generally downward (International Institute for Strategic Studies 2012, 467–473). All of the other big military spenders in the world are U.S. allies.

2. POLICYMAKERS WILL CONTINUE TO REACH FOR THE MILITARY TOOL REGARDLESS OF ARTICULATED STRATEGY.

Some observers fear that, regardless of articulated strategy, policymakers will not be able to resist the temptation to get the United States involved in foreign interventions, including long counterinsurgency and stability operations. Once the military is committed, the mission will expand until every last soldier and Marine has boots on the ground in theater.

The record of the past two decades provides ample evidence that leaders seriously underestimate the likely cost and duration of wars before undertaking them. Uniformed leaders are also right to worry that political leaders might plunge the

military into wars even when uniformed leaders counsel a more cautious approach.

On the other hand, the past two decades also provide future policymakers with important evidence of the problems and costs inherent in overuse and overextension of the military. A smaller military focused more tightly on missions in Asia and the Pacific could reinforce that evidence in the minds of future policymakers.

3. THE PERSONNEL-RELATED ALTERNATIVES OF CHAPTER 3 WOULD BREAK FAITH WITH SERVICE MEMBERS AND RETIREES WHO SERVED HONORABLY AND SACRIFICED FOR THEIR COUNTRY.

The men and women who volunteer to serve in uniform make big sacrifices on behalf of their country. They do so in the understanding that they will be paid well for their service and that their health needs will be met. Those who serve long enough to become eligible to retire, do so in the expectation of a generous pension and quality health care for life. With the nation still at war, some will argue that the personnel-related proposals of chapter 3 would short-change the members and retirees who have given their country so much. On the contrary, the dramatic expansion of service member and retiree compensation since 1998 means that pay and benefits for those who serve will still be very generous, even after the rapid spending growth is slowed.

The changes to health-care cost sharing proposed in Alternative 3-1 specifically exclude the survivors of service members who sacrificed their lives. They also exclude service members who retire because of medical disabilities incurred while in service. Nevertheless, opponents of the alternative will argue that any health-care cost borne by military retirees breaks a promise of “free health care for life” for those who serve until retirement.

That argument makes no sense. Health care for military retirees was never absolutely free. Since the inception of Medicare in the mid-1960s, retirees over the age of sixty-five and their survivors were covered by Medicare and expected to use that system as their first choice. They were permitted to use medical services in military hospitals and clinics on a space-available basis. But even then, costs were often imposed in the form of wait times. More important, the growing share of health-care costs borne by individuals not in the military system should serve as a signal that all is not as it once was. Health-care costs have grown dramatically. Military retirees should not be the only people in America unaffected by that growth.

Service members’ immediate pay grew handsomely for more than a decade. The raises already granted will not be overturned. In fact, under Alternative 3-2 troops would continue to receive pay raises that keep pace with inflation.

Alternative 3-4 would trim the housing allowance, but the alternative could be phased in over time to ameliorate the impact on the pocketbooks of those who continue to live outside of military housing.

Chapter 3 deliberately avoids changes to the structure of the military retirement system. Instead, Alternative 3-3 encourages the services to reduce the fraction of troops who stay in service long enough to become eligible to retire. The alternative would permit the services to retain relatively more personnel in military career fields that benefit the most from experience, and separate more people in career fields where the payoff to experience is smaller.

Finally, in time of war it is not easy to restrain pay and benefits for those who serve. But the way to honor the service of those who contributed so much is not to avoid the changes that must be made if the DoD is to live within its means during the coming decade. Rather, the solution is to stop asking the nearly impossible of the nation’s men and women in uniform. This means not reaching for them as the first tool of foreign policy; not entering into long wars that demand that individuals must deploy to difficult and uncertain missions two, three, four, or even five times in the course of a few years; not routinely recalling reservists who had reason to believe their service obligations were behind them; and not requiring individuals to remain in service for months after they become eligible to leave.⁴⁶

4. REDUCTIONS IN EQUIPMENT INVESTMENT WOULD HARM THE INDUSTRIAL BASE.

Recommendations for reduced defense spending often include the wholesale cancellation or deferral of multiple equipment programs (see, e.g., Domenici-Rivlin Debt Reduction Task Force 2010; Korb and Pemberton 2011; National Commission on Fiscal Responsibility and Reform [the Simpson-Bowles Commission] 2010; and Sustainable Defense Task Force 2010). Such cancellations may run the risk of closing production lines and ending research and development programs that the services count on to preserve a healthy industrial base.

The changes proposed in Options 4-1 and 4-2 generally avoid that risk. Rather than cancelling acquisition programs or forgoing them altogether, both options reduce production consistent with the elimination of force structure. The savings estimates also assume that the services will choose to cut back on research and development programs that no longer fit with their expectations for the future.

5. CONGRESS WILL NOT SUPPORT THE NEEDED CHANGES.

Beginning with the National Defense Authorization Act of 2000, lawmakers repeatedly expanded pay and benefits for

military personnel and retirees—even when the expansion was not requested by the DoD and, in some cases, even when the DoD’s leaders advised against it. Congress also continued to support military development and procurement programs in the face of substantial cost overruns and schedule slips. One might thus conclude that lawmakers will oppose many of the changes suggested in this paper.

On the other hand, three important factors may change the calculus on Capitol Hill. The first is the imminent end of the wars in Iraq and Afghanistan, which will ease the disproportionate burden carried by military personnel and their families. The second is the troubling fiscal picture, which

propels the consideration of tradeoffs and efficiencies in every area of expenditure.

The third factor is the sentiment of the service chiefs and the uniformed military. In today’s fiscal environment, the service chiefs support changes that would rein in the growth of personnel and acquisition costs to free up money for force structure, readiness, and modernization. During the coming year or two, uniformed and civilian defense leaders can play an important role in helping Congress to make the changes that will be necessary to put the DoD on a sound footing for the longer term.

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Endnotes

1. The federal budget function designated “national defense” includes spending by the Department of Defense, the atomic energy programs that provide nuclear weapons and environmental cleanup of the nuclear weapons establishment in the Department of Energy, and smaller defense-related programs in other agencies.
2. As a share of GDP, however, national defense spending is significantly lower than during the Cold War.
3. The DoD will have some leeway in allocating the FY 2013 reduction between war and non-war activities. If the allocation favors spending for the wars, then the non-war portion of the FY 2013 budget could drop by more than 8 percent relative to the president’s plan of February 2012.
4. Operation and maintenance is one of the defense appropriation titles. It includes a broad range of activities related to the readiness of the forces—for example, the purchase of fuel and spare parts for operating equipment. It also includes most of the department’s spending for training, for the upkeep of equipment and facilities, and for administrative activities like handling the payroll. The lion’s share of the department’s military health care bills are paid through the operation and maintenance title, as are most of the department’s civilian workers.
5. “To again become masters of combined arms maneuver will require revitalizing home-station training, modernizing the Army’s training centers and preparing our soldiers to confront enemies equipped with the most advanced weaponry” (Secretary of Defense Leon Panetta, as quoted in Chris Carroll, “Army Must Maintain Conventional Warfare Skills, Panetta Says,” *Stripes Central*, October 12, 2011; see also Gentile 2010).
6. Author’s calculation, based on Office of Management and Budget (OMB) 2012, table 2; and DoD 2011, table “FY 2012 OCO Request: Total Obligational Authority, Budget Authority, and Outlays by Appropriation.”
7. During the past decade, several former senior military officers argued that non-war defense spending should rise to a level of 4 percent of GDP and be held there, citing that share of the economy as both necessary for a strong defense and affordable over a long period. The same view was espoused by policy analysts at the Heritage Foundation and the American Enterprise Institute. More recently, Martin Feldstein (2011) argued that any figure short of 5 percent of GDP is affordable.
8. The estimate reflects CBO’s extended alternative fiscal scenario, which assumed that tax rates remain at their 2012 levels and that the second round of BCA budget cuts do not take place.
9. I have adjusted the years by which debt will exceed specific levels to reflect the modest narrowing of future deficits under the American Taxpayer Relief Act of 2012.
10. Some analysts argue that rising debt levels are less likely to push interest rates up than in previous decades because of the position of the U.S. dollar as the world’s reserve currency and the large fraction of the public debt that now is held by foreign governments. Briefly, they hold that foreign creditors with vast holdings of dollars accumulated by selling goods and services in the United States really have no other good place to put their money. Recent problems in euro-zone economies reinforce this point of view. So does the fact that interest rates today are at a historical low point, even though U.S. federal debt is at a post–World War II high point. Nevertheless, most economists would agree that running a debt that approaches twice the size of the economy is risky business.
11. The estimate assumes that the BCA cuts currently scheduled to begin in March 2013 are ultimately rescinded. If the BCA stands, then its cuts will shrink the fiscal shift required to achieve sustainability by about 0.5 percent of GDP.
12. Discretionary activities are those whose funding depends on appropriations each year. Mandatory programs are those whose funding is determined by extant law; they include entitlements like Social Security, Medicare, and Medicaid.
13. Although not included in the budget limits and cuts imposed by the BCA, war funds will be included in the FY 2013 sequester calculation. Because the DoD executes its war and non-war funds together, however, leaders will have some leeway in allocating the reductions between the two categories. If war funding is kept off limits from the sequestration cuts, then the cutback to the FY 2013 non-war national defense budget will amount to more than 8 percent.
14. The figure reflects adjustments to the BCA levels in FY 2013 and FY 2014 called for under the American Taxpayer Relief Act.
15. CBO’s scenario begins with total defense spending in FY 2012, including the funds for wars. It assumes that under current policies total defense spending would rise to account for inflation every year between FY 2012 and FY 2022. The scenarios outlined here assume that spending for wars would taper off gradually over the course of the decade. Under this plan, non-war national defense spending would be about 18 percent in real terms below the FY 2012 non-war budget as enacted. It would be about 20 percent in real terms below the peak non-war defense budget of FY 2010.
16. Relative to the enacted national defense base budget for FY 2012, this would be about a 27 percent real reduction. It would represent about a 30 percent real cut to defense spending relative to the peak defense budget of FY 2010.
17. The Army and Marine Corps added about 113,000 troops, while the Navy and Air Force dropped about 67,000. Full-time Guard and Reserve positions grew by about 11,000 (Office of the Under Secretary of Defense (Comptroller) 2012, table 7-5).
18. The options suggested here are by no means the only ones available to policy makers. A more ambitious path would be to reverse the entitlements granted during the past fifteen years, including Tricare for Life, concurrent receipt of military retired pay and veterans’ disability compensation, the elimination of the Social Security offset for surviving spouses of deceased military retirees, and expanded Tricare benefits for reservists.
19. Military retirees are distinct from other veterans; they generally have served for twenty years or more, thus becoming eligible for an immediate pension and for other benefits, including health care. The military health system also covers some eligible reservists and their families. There are about 9.6 million total eligible beneficiaries, though not all of them use the military coverage (Office of the Under Secretary of Defense (Comptroller)/Chief Financial Officer 2012, 5-2). Today there are about 1.9 million retirees receiving retired pay (DoD 2012, 18).
20. For example, for Tricare Prime, the military plan that operates like a health maintenance organization (HMO), utilization rates for inpatient services were 78 percent higher than in civilian HMOs in FY 2011 (Bannick 2012, 62).
21. This is one of the options considered by CBO; see CBO (2011a, 81). The most expensive plan, called Tricare Prime, operates like an HMO. The other two plans are Tricare Standard, a fee-for-service plan; and Tricare Extra, a preferred-provider plan.
22. Author’s calculation based on Bureau of Labor Statistics data and Office of the Under Secretary of Defense (Comptroller) (2012, chap. 5).
23. Pay raises planned under the FY 2013 budget request are 1.7 percent for 2013 and 2014, 0.5 percent for 2015, 1.0 percent for 2016, and 1.5 percent for 2017.

24. For military officers, the civilian comparison group is college-educated workers. For enlisted members, the DoD changed the civilian comparison group in recent years from workers with a high school diploma to those with one year of college (see, e.g., Murray 2010, 4).
25. Author's calculation based on data from Office of the Under Secretary of Defense (Comptroller) (2012, table 6-2); and CBO (2012c, 19). The calculation assumes a total base in 2013 of about \$76 billion, and forgone raises of 1.9 percent each year from 2014 to 2017.
26. The so-called Redux reform would have trimmed retired pay for those entering service after 1986. The reform was largely overturned in less than two decades, before those who entered after 1986 began to retire.
27. The Corps typically retains fewer than 40 percent of enlisted Marines on active duty beyond the first four years (CBO, 2012d, 26).
28. Opponents of the option may argue that reducing the fraction of long-serving individuals will harm the distribution of service members among the ranks. That should not be the case, however. The Army, Navy, and Air Force today reenlist a significantly larger fraction of service members as their first terms end than in 1987, when the department was still flush with Reagan-era budgets and the rank distribution was arguably in good shape (see Office of the Under Secretary of Defense [Personnel and Readiness], 2012, table D-32).
29. The estimate reflects annual operation and maintenance spending per active-duty troop, adjusted for inflation.
30. The exceptions were in 2002 to 2004, when military personnel with certain ranks and time in service received larger raises (see Office of the Under Secretary of Defense [Comptroller], 2012, table 5-12).
31. The Army and Air Force share a single exchange service; the Navy and Marine Corps each has its own.
32. Author's calculation based on CBO (2011a, 84).
33. As CBO suggests, the allowance might be higher for service members at lower ranks and lower for those who earn more (CBO 2011a, 84).
34. For the pay raises as they relate to the employment cost index, see CBO (1999, 11).
35. For a discussion of the political obstacles surrounding the reform of military personnel systems and how to overcome them, see Punaro (2004, 265–288).
36. While the document is not explicit about whether the list of missions it offers is meant to be in priority order, much of the official discussion on its release suggested that the order in which missions appear on the list is meant to reflect their priority.
37. The Air Force argues that its actual spending power is significantly less than the 27 or 28 percent of DoD spending reflected here. Indeed, in FY 2012, nearly \$34 billion—about 21 percent of the total Air Force (non-war and war) budget—falls into a category that the service describes as “non-blue” or “pass-through funding.” This category includes spending for intelligence agencies like the CIA, whose funding resides largely inside the DoD but is not controlled or managed by the department. It also includes funding for health-care accounts that the Air Force does not control. For a discussion of the non-blue budget, see Hebert (2010). For the purposes of this chapter, the actual share of defense spending devoted to each military department does not matter; the question is whether that share rises or falls in future budgets. In fact, Air Force non-blue funds rose between FY 1990 and FY 2012 from 17.4 percent to 20.6 percent of the service's total budget, indicating a shift out of service-controlled accounts in the Air Force budget of about 1 percent of the total defense budget. This rise in non-blue funding may thus have caused the Air Force to suffer a small decrease in the share of the defense budget that it actually controls, relative to the other services. On the other hand, the other military departments are also affected by pass-through accounts, and it is possible that those accounts also grew disproportionately during the past two decades. What we can say is that if the Air Force-controlled budget has suffered disproportionately in comparison with the budgets of the Army or Navy, the damage since 1990 is no more than 1 percent of the total defense budget. The author is most grateful to the Air Force directorate for Public Affairs and the Office of the Air Force Comptroller, which provided data on Air Force blue and non-blue spending since FY 1990.
38. The Department of the Navy includes the Navy and the Marine Corps.
39. The force structure and personnel estimates in this chapter are based on the author's calculations and reflect the relationships among reductions to total defense spending, service operation and maintenance spending, force structure, and personnel during the post-Cold War drawdown.
40. This assumption is made for three reasons. First, after years of significant contributions to the wars in Iraq and Afghanistan, the Guard and Reserve are arguably better equipped and better trained than they have been for decades. Scrapping the strides at this point would make little sense. Second, the reserve component can serve as a hedge in the event that more ground forces are needed during the coming decade than are available in the active component. Finally, downsizing the reserve component—particularly the Army National Guard—has been nearly impossible for political reasons in the past.
41. In the event of a large war with significant warning time, or a long war that requires persistent rotation of units into theater, policymakers could choose to restore the draft or to conduct a more limited call-up of conscripts through the Selective Service System. They also could alter rotation policies, either by requiring units and individuals to remain longer in theater or by reducing the amount of time they spend at their home bases between deployments.
42. Combat-coded squadrons are those not held solely for training purposes.
43. In 1998, the director of the CIA disclosed a total intelligence budget of \$26.7 billion in current dollars, which is about \$37 billion in FY 2013 dollars. In recent years, the director of national intelligence has routinely released total figures for intelligence spending. In 2013 dollars, the FY 2010 intelligence budget came to nearly \$85 billion. The figures discussed here include spending attributed to the wars in Iraq and Afghanistan.
44. The *DoD Quadrennial Defense Review Report 2006* (DoD 2006) espoused a range of technological advances, including persistent surveillance and precisely targeted conventional missiles carried on submarines, to help “shape the choices of countries at strategic crossroads” (DoD 2006, 6). For an outsider view of the elements and cost of a grand strategy of primacy, see Posen and Ross (1996/7).
45. Purchasing power parity estimate; CIA argues that this is the best estimate. The exchange rate estimate puts China's GDP at about one-half the size of U.S. GDP (CIA 2012).
46. These points are made in Sustainable Defense Task Force (2010, 25).

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Highlights

Cindy Williams of the Massachusetts Institute of Technology proposes reining in the costs of military health care, averting cost growth for military cash compensation and retirement pay, taking control of operation and maintenance budgets, and controlling weapons cost growth. In addition to these internal cost measures, she suggests downsizing and restructuring the armed forces.

The Proposal

I. Take control of internal costs

- Change the structure of cost-sharing for military health care by imposing a premium for Medicare-eligible retirees and family members, raising Tricare premiums, increasing deductibles, and increasing copayments. This proposal specifically exempts service members who retire for medical reasons and the survivors of service members who die on active duty.
- Limit both military and civilian pay raises to the rate of GDP inflation for the next four years.
- Reduce military housing allowances to reflect 90 percent rather than 100 percent of the price of private-sector housing.
- Implement a combination of measures aimed at lowering the fraction of military personnel who remain in service until retirement. Measures might include early career counseling, adjustment and enforcement of up-or-out gates, and narrowing of promotion standards.
- Streamline the DoD's retail establishment by combining the commissary and base exchange systems, eliminating the \$1.3 billion annual commissary subsidy, and offsetting increased costs through cash allowances for active-duty members.
- Enforce existing acquisition rules and cancel systems that incur cost growth in excess of 10 percent over a period of five years.

II. Strategically reduce the size of the force

- To bring defense budgets into line with or below the levels mandated by the BCA, the DoD will need to make significant cuts to force structure. How the cuts are distributed among the armed services will determine the shape of the future force and the missions for which it is best suited. Williams considers two options. The first is to reduce defense budgets in line with the BCA and to distribute the cuts proportionately among the military departments. The second option is to reduce defense budgets in real terms by 16 percent from the president's request for FY 2013, but to spread the cuts unevenly among the military departments so as to create a force more suited to future operations in Asia and the Pacific.

Benefits

Williams' suggestions for controlling internal costs will allow the DoD to save an average of \$31 billion annually over the next decade, thus potentially holding the line against cost growth above inflation. In addition to these savings, the DoD can cut the budget below today's levels by downsizing and reshaping the forces in line with strategic aims. This will result in a force that is better suited to core missions of the future and fully capable of protecting national security.



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