



RESEARCH SUMMARY

Analysis of a Salary-Based Pay System for the QRMC

The Institute for Defense Analyses (IDA) investigated the implications of a change to a single-salary system for military compensation. IDA found that such a system would likely increase total costs to the Department of Defense (DOD), reduce retention and have little effect on military readiness. Also, military personnel were not in favor of a change.

The DOD is required by law to review military compensation policy every four years. For the 13th Quadrennial Review of Military Compensation (QRMC), the U.S. president directed the Secretary of Defense to compare how a change from the current military compensation system to an alternative single-pay, salary-based structure would affect military readiness, personnel recruitment and personnel retention. The current system includes substantial tax-free benefits, particularly the basic allowance for housing. Prior studies suggested that a salary system, entirely subject to taxes, would make the system more comparable to the civilian sector and thus, in a sense, more fair.

The QRMC asked IDA to provide the fact-finding, analytic tools and analysis necessary to

assess how such a system would affect service members' earnings and behavior, as well as the readiness, cost and tax revenue implications. An IDA research team including economists Nancy Huff and Stanley Horowitz first modeled the after-tax income effects of transitioning to a military compensation system that would combine basic pay, housing and subsistence allowances into a single, taxable "salary." Team members paid particular attention to how the change would affect personnel in different pay grades. The team then used econometric models to estimate the likely responses of service members to changes in after-tax income and

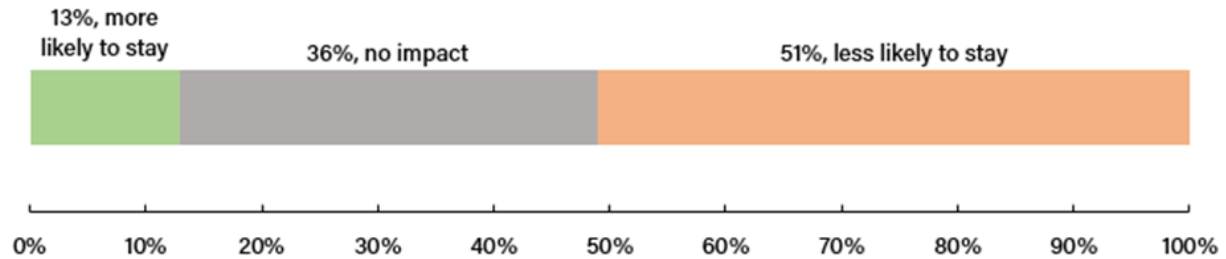
IDA

June 2024 | Product 3001654

Would you support or oppose a change to a single-salary system of compensation?



Would such a change make you more or less likely to stay in the military?



conducted focus group sessions with active and reserve members of every military department.

Analysis found that a salary system that increased base pay by the same proportion for all personnel would adversely affect those in lower pay grades because the tax-free allowances make-up a larger fraction of their take-home pay. A more tailored salary system could eliminate this effect. Junior enlisted personnel who live in barracks and receive no housing allowance would benefit from a salary system.

As recommended by congressional guidance, IDA looked at effects of a salary system that holds cost to the federal government constant and found that it would increase total costs to the DOD by more than \$9 billion. From a government-wide perspective, the costs would be offset by additional federal tax revenue. It would also collectively reduce service members' take-home pay by roughly \$600 million because of additional state taxes.

Further analysis indicated that career retention would likely decline while accessions for enlisted personnel might improve. Implementing the proposed single-salary system would introduce

substantial additional complexity and generate little, if any, benefit to readiness. Moreover, a salary system is likely to encounter substantial resistance from current military service members. Focus groups and surveys revealed that service members are generally opposed to a salary system — they think the current system is “fair enough.” After contemplating these findings, the DOD did not recommend transition to a single-salary system.

This summary is based on [IDA Document D-13204](#).



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IDA-managed federally funded research and development center. She holds a doctorate in economics from Clemson University. Her fields of expertise span labor economics, game theory and industrial organization. Stanley A. Horowitz (shorowit@ida.org), a member of CARD's research staff, holds a master's degree in economics from the University of Chicago.