MODIFYING THE TERMINATION DATE

FOR

GI BILL EDUCATIONAL BENEFITS

Statement of

Neil M. Singer

Congressional Budget Office

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Mr. Chairman, it is my pleasure to appear before your Committee today to present the results of the Congressional Budget Office's analysis of one of the provisions of S. 2747, the proposed Veterans' Education and Employment Amendments of 1982. Accompanying me are Mr. Dan Huck and Mr. Edward Shephard.

This bill proposes several adjustments and improvements in veterans' employment, vocational rehabilitation, and education programs. My comments will be limited to Sec. 104(a) of the bill, which would modify the current December 31, 1989 termination date for GI Bill educational benefits by permitting members separating from active duty after that date to use benefits over an eight-year period, provided that use of the benefits begins within two years after separation.

As you know, this Committee requested that the CBO undertake a study of the costs and manpower effects of various proposals to modify or repeal the GI Bill's termination date. In brief, our analysis indicates that the provisions of Sec. 104(a) would result in a very modest reduction in separations among career servicemembers who might otherwise leave to use their GI Bill benefits before the 1989 termination date. Sec. 104(a) would also generate some small, near-term budgetary savings in the form of lower GI Bill expenditures. The long-term costs of the bill would be large, however, and an equivalent improvement in near-term retention could be obtained much more cheaply by using other incentives, such as pay raises or reenlistment bonuses.

CURRENT LAW AND THE GOALS OF SEC. 104(a) ON MANPOWER RETENTION

With the passage of P.L. 94-502, the Veterans' Education and Employment Assistance Act of 1976, the Congress terminated the Vietnam-era GI Bill for new recruits entering active duty on or after January 1, 1977. The Act also established December 31, 1989, as the closing date for all training under the Vietnam-era GI Bill, following precedents regarding termination of benefits set by the World War II and Korean War GI Bills. At present, all servicemembers with six years or more of service--about 40 percent of today's force--have earned benefits under the Vietnam-era GI Bill.

The Administration's support for modifying the GI Bill termination date stems from a concern that many current career servicemembers might leave service prematurely to take advantage of the benefits before the 1989 expiration date. This prospect could undermine efforts to overcome persistent shortages of senior enlisted personnel, which became a problem largely because of the high separation rates of career members between 1976 and 1980. The large military pay raises of 1981-1982, coupled with the unfavorable state of the civilian economy, have raised reenlistment rates in all the services to record high peacetime levels.

Nonetheless, shortages in selected but critical categories will probably persist for the next several years, especially in the Navy and Air Force, in which the requirements for these skilled career personnel are likely to grow.

The Congress and the Defense Department have already addressed these projected shortages with various other retention incentives; these include pay raises targeted to senior ranks, expanded reenlistment bonuses, and enhanced specialty pays for aviators, sailors, and submariners. Modification of the GI Bill termination date can be viewed as a similar incentive to encourage the retention of senior servicemembers. Like the effects of pay raises, but unlike those of bonuses and specialty pays, the effects of modifying the 1989 termination date unfortunately would not be confined to the skill areas and specialties in which career manpower shortages currently exist or are projected to develop.

PROJECTED EFFECTS OF SEC. 104(a)

The Congressional Budget Office's analysis indicates that extension of the 1989 termination date would have only a small impact on projected separations among enlisted members eligible for GI Bill benefits. The CBO estimates that, between now and the end of 1987, modification of the termination date as prescribed in Sec. 104(a) would result in the retention of approximately 1,300 members--in all skills and services--who would otherwise leave active duty. This change would represent a reduction of only about one-half of one percent in the 220,000 projected separations by enlisted members eligible for GI Bill benefits, most of whom will leave service for reasons unrelated to their use of the GI Bill. In other words, by 1987, the extension of benefits in Sec. 104(a) would increase by only one-tenth of one percent the projected career enlisted force of more than 1 million. If benefit levels were adjusted automatically (that is, indexed) to keep pace with inflation, the reduction in separations would still be only 2,700 members, or 1.2 percent. Moreover, Sec. 104(a) would actually increase post-1987 separations, as I will discuss shortly.

Method of the CBO Analysis

The CBO analysis rests on the premise that career servicemembers' retention depends on their valuations of anticipated future benefits. In evaluating future benefits, the methodology adjusts for the lower value that people place on deferred income in comparison to current income--that is, future benefits are discounted. This approach, which seems intuitively sensible, has been validated empirically, and it is now used by the Defense Department, the CBO, and other analysts in virtually all evaluations of military manpower policy. Since the current law termination date eliminates the anticipated future benefits of post-1989 use of the GI Bill, it should decrease the likelihood that members will reenlist. Thus, the termination date should encourage at least some members to separate from service prematurely--that is, earlier than they would have chosen if the termination date had not been in effect--in order to use their earned benefits.

Several reasons explain why the CBO estimates that only a few such premature separations will occur. One is the powerful influence that potential retirement benefits exert on career retention. The expected gains from remaining on active duty for at least 20 years and thus becoming eligible for retirement pay far outweigh the value of educational benefits. A second factor minimizing the impact of the termination date is that, historically, older servicemembers have used educational benefits at lower rates than have those who leave after just one or two terms (three to six years) of service. Thus, the loss that senior members anticipate from forfeiting their earned benefits is diminished by the lower probability of those benefits' being used.

The influence of time also plays an important role in estimating the effects of the termination date. Sec. 104(a) would permit use of benefits as late as the year 2014 for members who entered service in 1976. The discounted value today of these deferred benefits is far less than their projected nominal value. CBO's analysis used conservative discount rates to limit the weight of this factor. We also tried to mitigate the effects of time by analyzing a case in which GI Bill benefits would be indexed to inflation. Although benefits are not now indexed, in the past they generally have been raised on an ad hoc basis to preserve their real value.

The CBO estimates that an indexed program would produce about 2,700 fewer pre-1988 separations, but at much higher cost than an unindexed extension.

Cost Savings Projections

Modification of the termination date, with benefits either indexed or not, will lead to a deferral of the use of GI Bill benefits by members who are dissuaded from separating prematurely. The short-run savings caused by this deferral, however, are greatly outweighed by the long-term use of GI Bill benefits by servicemembers whose eligibility otherwise would end in 1989. The marginal reduction in enlisted separations that would result from extending the termination date would yield cumulative savings of approximately $14 million in GI Bill benefit outlays between fiscal years 1983 and 1989. These short-run savings would vary from $300,000 in fiscal year 1983 to a maximum of nearly $3 million in fiscal year 1988. The CBO estimates, however, that the proposed extension would increase cumulative post-1989 outlays by approximately $725 million. If benefits were indexed to the inflation rate, cumulative fiscal year 1983-1989 savings would be $38 million, but post-1989 total outlays would increase by $2.8 billion. (All these cost estimates are in nominal dollars, using CBO's baseline inflation projections.)

COST COMPARISON WITH OTHER RETENTION INCENTIVES

Extension of the termination date for GI Bill benefits seems a quite expensive way to improve career enlisted manning. The CBO estimates that the cost per additional servicemember would be approximately $550,000 for an unindexed program or $1 million if benefits were indexed. These costs are so high because most of the potential users of post-1989 benefits would remain in service even if their eligibility were terminated. Annual across-the-board pay raises of one-tenth of one percent between 1983 and 1987 could produce the same 1,300-member reduction in premature separations as the Sec. 104(a) extension, but at a cost of only $218 million in contrast to $725 million. Selective reenlistment bonuses would be even more efficient, at a cost of $40 to $120 million (depending on members' length of service) to reduce premature separations by the same 1,300.

Bonuses would also be more efficient, because they would retain the skilled personnel whom the services need most. In contrast, extending the availability of GI Bill benefits beyond 1989 would be of equal value to all servicemembers. Therefore, many of the estimated 1,300 members who would remain in service rather than separate prematurely would probably be in skills in which the services do not project manning shortages. In terms of ameliorating the services' manpower problems in critical skills, therefore, the Sec. 104(a) extension would be even less efficient than shown by our calculations.

A further difficulty with the proposed extension is that it would only defer, not eliminate, the incentive for members to separate from service to use their GI Bill benefits. The CBO estimates that, under Sec. 104(a), the services would experience 470 more separations between 1988 and 1990 than would occur under current law. These additional more distant separations would partially offset the near-term (pre-1987) manpower gains that Sec. 104(a) would achieve.

Despite the high relative cost of reducing premature separations by modifying the GI Bill termination date, considerations of equity might still make the extension desirable. Survey data and anecdotal information suggest that senior servicemembers are very sensitive to the appearance of inequity posed by the 1989 date. Nearly all persons who have served in the military during the last four decades have been eligible for GI Bill benefits. Yet today's career members, who have served longer than most, will lose their benefits because of a change in law made during their term of service. This issue of equity may counterbalance the high long-term costs of Sec. 104(a).

The CBO's analysis of this fairness issue suggests other ways in which the separation incentive of the 1989 termination date could be alleviated. One approach would be to offer those active-duty members who have earned GI Bill benefits the right to receive in cash part of the value of their entitlement (say, 25 percent) in return for at least one additional reenlistment and forfeiture of rights to future training. Such a "cash out" would be less selective and therefore more costly than current reenlistment bonuses. But it would confer offsetting savings in the form of bonus cost reductions, would improve career manning in the short run, and would eliminate the long-run incentive for members to separate to use their GI Bill benefits.

A more complex alternative would be to offer senior members the option to transfer their GI Bill (chapter 34) entitlement to the Veterans' Educational Assistance Program (chapter 32) now in effect. Although the basic benefits under the chapter 32 program are substantially less valuable to members than GI Bill benefits, the Defense Department is authorized to provide supplemental benefits, called "kickers," to encourage recruitment and retention. At present, the department uses kickers only for recruiting, but there is no bar to extending these benefits to senior personnel in shortage skills at the department's discretion. An advantage to this approach is that "kickers" could be targeted toward critical personnel and thus could be more efficient than any across-the-board incentives such as those provided under Sec. 104(a). A disadvantage, however, is that the eventual incentive to separate in order to use educational benefits would persist.

Mr. Chairman, this concludes my prepared statement. Mr. Huck, Mr. Shephard, and I will be pleased to answer any questions you may have.