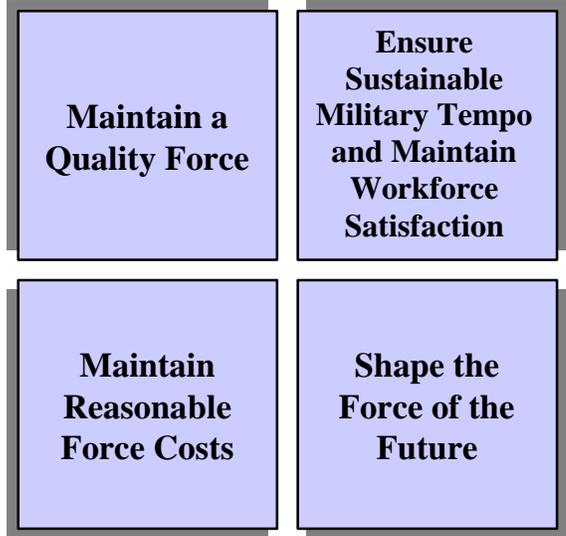


Force Management Risk

Providing a trained and ready force is the leading *business* of the Department of Defense. We must employ the tools of modern commerce to better manage our military and civilian workforce—more flexible compensation packages, contemporary recruiting techniques, improved training.

We must guarantee the working and living conditions that will enable our people to perform at their best. We must take care of the future—seek out or create the skilled workforce demanded of a 21st century military force. And finally,

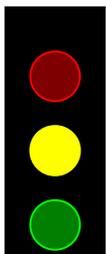


We must forge a new compact with war-fighters and those who support them, one that honors their service, understands their needs, and encourages them to make national defense a life-long career.

Secretary Rumsfeld, September 10, 2001

The Secretary's performance priority for overall force management risk in FY 2004 is *Manning the Force* to meet the needs of the global war on terrorism.

MAINTAIN A QUALITY WORKFORCE



It is hard to imagine a more challenging set of circumstances for a human capital manager than that experienced by military personnel specialists in the Department of Defense since September 11, 2001. Nearly 300,000 Reserve Component members have been mobilized over the past two years for on-going contingency operations. Another 40,000 Reserve Component members volunteered to be activated to support ongoing operations.

Throughout the year, the military departments carefully analyzed data on recruiting and retention, overall force levels, and inventories

of certain critical skills. To support current and pending contingencies, most found it necessary to impose some level of moratorium on retirements or separations. This maintained high levels of readiness in heavily employed units with special skills, such as special operations, pilots, and intelligence analysts.

At the same time, the tempo of international crises struck a chord with our nation's young people—recruiting programs performed strongly and large numbers of already serving military personnel elected to extend their periods of service. Even though the President waived limits on aggregate force levels due to our national emergency, the military departments worked hard to meet mission requirements within budgeted ceilings, trying to keep force costs at reasonable levels.

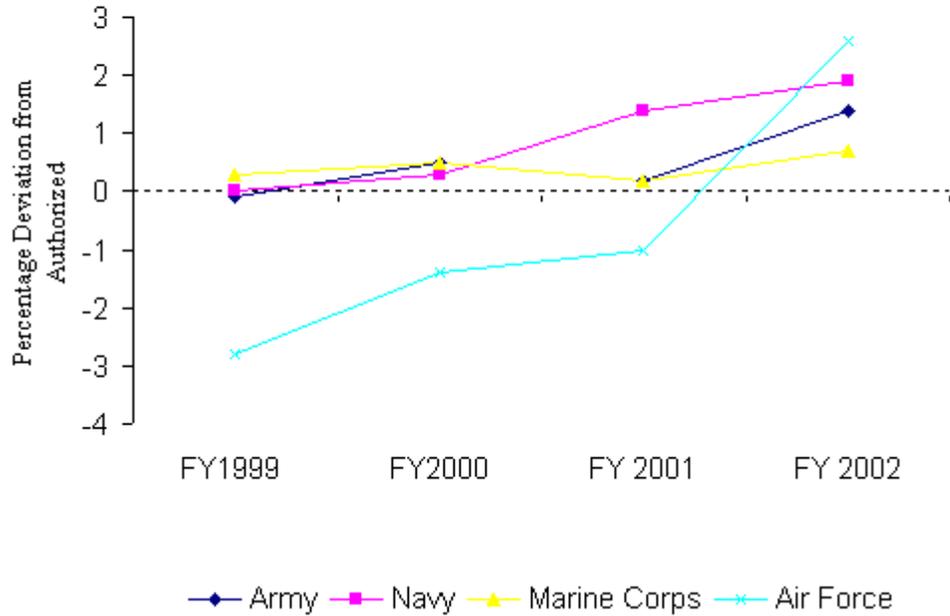
The lessons of this past year reinforced the fact that the demands on our military forces can change dramatically from month to month, day to day. Good measures of force quality and size are indispensable to our ability to guarantee we always have the right number of skilled people in place *throughout the year*, ready to handle each crisis as it comes.

Further, as the nation continues to face the new and varied defense challenges of the 21st Century, military personnel skills must evolve to match these challenges. Our performance metrics include efforts to define and capture both critical skill levels and the levels of experience needed to keep the force performing at top standards.

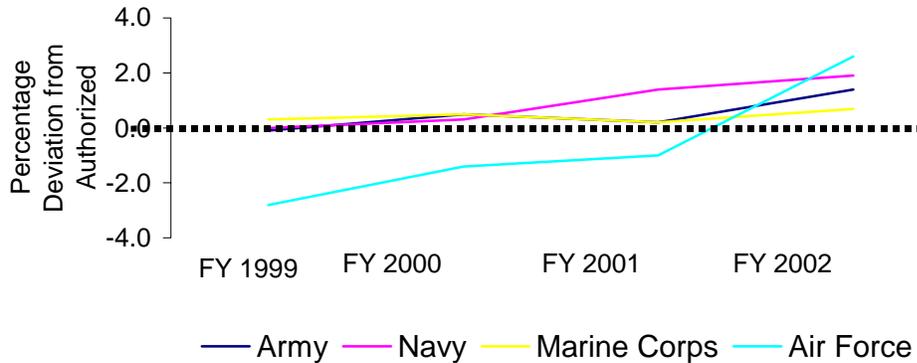
Maintain Manning Levels of Military Forces

Each year, Congress authorizes funds that the military departments must use only to maintain specific numbers of skilled service members, called “end strength.” Services are compelled to budget and recruit, retain, or release members to match those authorized end strength numbers by the end of the fiscal year. However, if he determines it to be in the national interest, the Secretary of Defense has the authority to increase the Active and Reserve Component end strength by 2 percent. For a large service like the Army, this means as many as 14,400 more Active Component and 11,100 more Reserve Component soldiers than provided for in the budget.

**Actual vs. Authorized FY 1999-2002
Active Component**



**Active Component
Actual vs. Authorized FY 1999-2002**



In the past, the military departments reported on whether they met their authorized end strength only once a year, on September 30. Therefore, it was possible that at other times during the year, force levels were higher or lower than authorized. A higher end strength

means funds intended for other activities, like training, must be used instead for personnel expenses. Too few people could mean that some military units may not have enough skilled personnel for their missions, or must draw personnel from other sources, negatively affecting other unit's missions.

Beginning this year, we will audit personnel levels quarterly, so small variances can be identified and addressed quickly. This should better rationalize force costs and lessen the risk that some units are not fully ready to respond in a crisis. Quarterly audits will also help us build more detailed trend information, allowing us to do more insightful, predictive analysis of the relationships among funding, force levels, and unit readiness.

Meet Military Recruiting Goals

QUALITY BENCHMARKS

It is not enough to bring the required number of people into the force: every service member must be able to perform his or her duties expertly. Over the years, we have found that educational achievement and general aptitude are reliable predictors of whether persons who apply to join the military will be able to perform to expected standards.

Recruits with a high school diploma are more likely to complete their initial term of service than either non-graduates or recruits with alternative high school credentials. Aptitude is a separate indicator of quality, and we measure it using the Armed Forces Qualification Test (AFQT), a subset of the Armed Services Vocational Aptitude Battery (ASVAB), which reflects math and verbal ability.

Individuals who score at or above average (a score of 50 or higher) on the AFQT are easier to train and have superior job performance relative to recruits with lower AFQT scores.

Individuals are classified into categories according to AFQT scores so that those scoring 50 or above are in AFQT Score Categories I, II, and IIIA (Cat I-III A).

Quality benchmarks for recruiting were established in 1992 based on a study conducted by the Department of Defense with oversight by

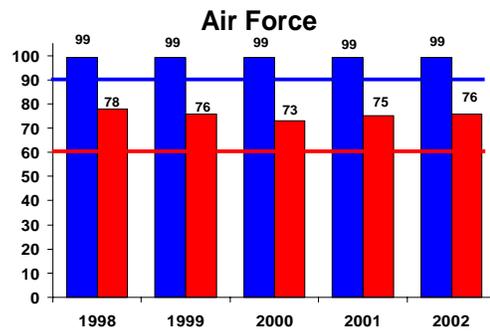
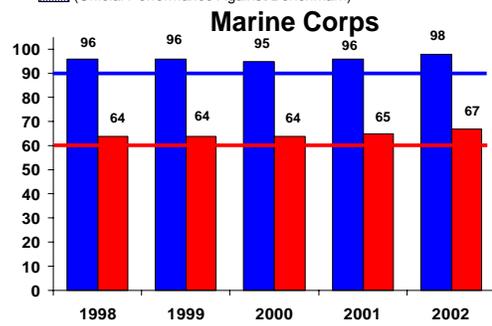
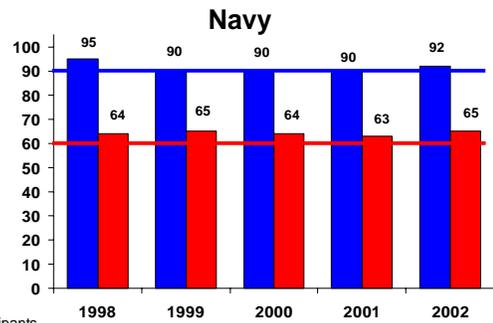
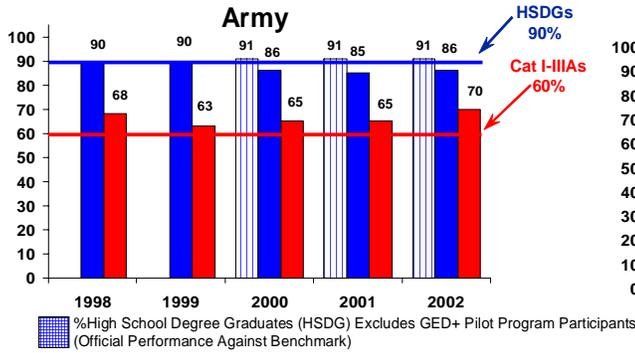
the National Academy of Sciences.¹ That study found it is cost effective to set quality benchmarks for recruiting that ensure at least 90 percent of non-prior service recruits are high school graduates (HSDG) and at least 60 percent have AFQT scores at or above 50 (Cat I-III A), with no more than 4 percent scoring between 10 and 30 on the AFQT.

Armed Forces Qualification Test (AFQT) Categories and Corresponding Percentile Score Ranges

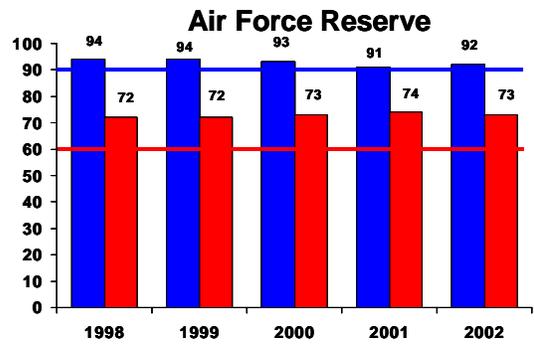
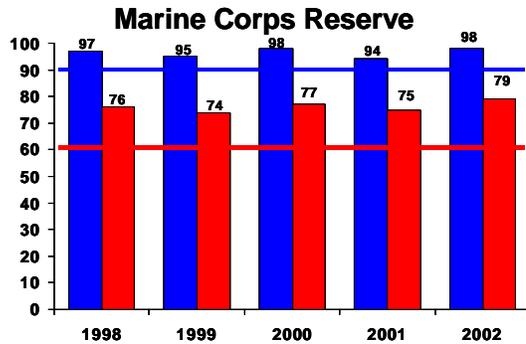
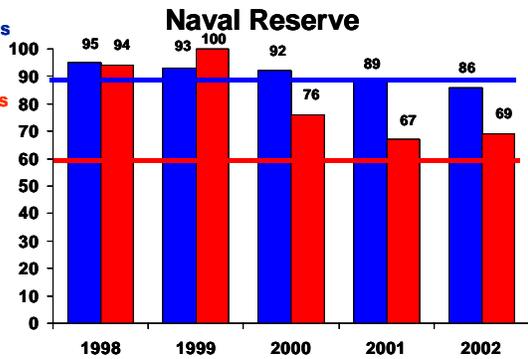
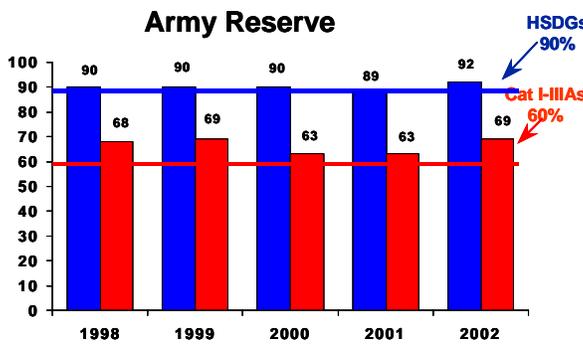
AFQT Category	Percentile Score Range
I	93–99
II	65–92
III A	50–64
III B	31–49
IV	10–30
V	1–9

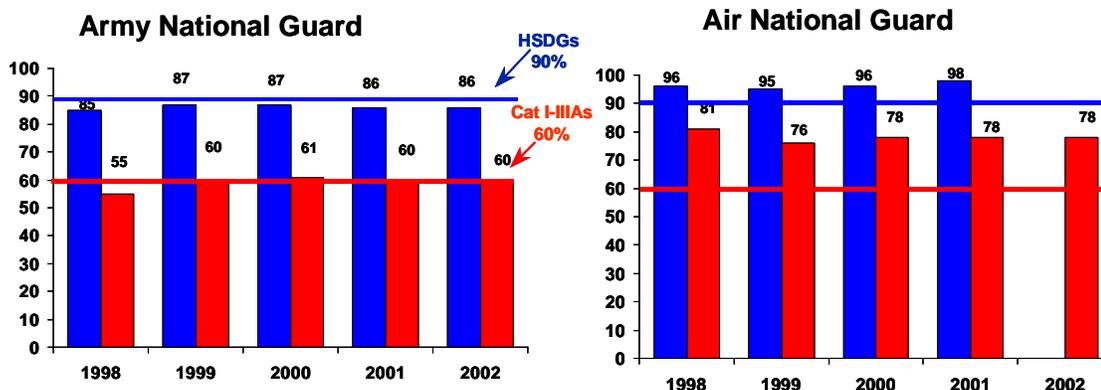
¹ These benchmarks were set by examining the relationship between costs associated with recruiting, training, attrition, and retention. They used as a standard the performance level obtained by the reference cohort of 1990 (the cohort that served in Operations Desert Shield and Desert Storm). Thus, they reflect the recruit quality levels necessary to minimize personnel and training costs while maintaining the performance standards met by the Desert Shield/Desert Storm cohort.

Quality Recruit Trends: 1998-2002



12





Notes: HSDGs are high school diploma graduates, our measure of educational achievement. Cat I-IIIAs are those scoring at or above 50 on the AFQT, our measure of aptitude. Cat IV percentages are not shown as the Services historically have no difficulty meeting the 4% limitation. FY 2002 Air National Guard data are not yet available.

CRITICAL SKILLS

Although the Department has met overall numeric and quality recruiting goals in the past few years, complete success requires a third variable: maintaining a sufficient and balanced level of critical skills when placing new recruits into military specialties. Each Service uses its own definition of “priority ratings” or “critical skills” to denote military specialties requiring particular emphasis by the recruiting command. In determining which military specialties become recruiting priorities, Services use factors such as degree of mission essentiality, career field manning level, number of entry-level vacancies, and recruiting difficulty (e.g., stringency of standards, unappealing nature of specialty).

However, the Department as a whole must identify critical skills based on military capabilities we need now and or will need in the future. That means that a shortage of a particular military skill area is not necessarily “critical.” For example, if we are short military administrative or personnel specialists, we may work more slowly or less efficiently, but we will get the job done. But if we are short linguists or communications specialists, we may be unable to deliver the intelligence analysis vital to maintain situational awareness on the battlefield, thus degrading a vital military capability.

The Department is developing a common definition for “critical skills.” With a common defense definition for recruiting “critical

skills,” we will be able to measure how well our recruiting and incentive programs work toward meeting critical skills needed for military capabilities and use this information to modify Department-wide recruitment strategies.

Meet Military Retention Goals

To successfully manage the overall force, we must balance the accession of new members with the retention of already trained and skilled personnel. For many skill categories, retention provides the best return on our investment in training and experience.

NUMERIC GOALS

The conventional way to measure successful retention (attrition for the Reserve Component) is to track progress toward a numeric goal—actually, one of two goals. The first goal is the overall number of service members retained in active or reserve duty in each military department. The second is the number of service members who elect to extend their commitments as a percentage of those eligible to re-enlist. Each service uses slightly different analysis methods, but in general retention targets are established by comparing how many new recruits are being brought on board with how many service members elect to remain in service.

Recruiting and retention goals are set annually, but are reviewed and reset (if necessary) throughout the year. This periodic feedback on the progress of our recruiting and retention efforts informs a range of decisions on force management strategies and resource allocations, such as retention bonuses.

CRITICAL SKILLS

Today, we identify critical skills for retention based on capabilities we need now and/or will need in the future. Each Service, to meet their own personnel requirements, defines what is a critical skill, usually shaped by historically chronic shortages in some specialties. The Department is working to develop a common definition of critical skills for retention to encourage, with bonuses and other incentives, individuals with scarce or highly technical skills to remain in the armed forces. We will then be able to measure how well our re-

tention and incentive programs work, and use that information to implement Department-wide strategies, while at the same time supporting our overall human resources strategy.

RETAIN BALANCED MIX OF SKILLS: EXPERIENCE AND GRADE

In light of the extraordinary challenges of the war on terrorism, we need to better understand how skill shortages or skill-level imbalances affect mission accomplishment. Our retention performance measures are moving beyond simple numeric goals. We want to guarantee we are keeping the right numbers of non-commissioned officers at the right grades and experience levels to fully meet mission needs. By the end of 2003, the common definition for critical skills will be established and each of the Services will be asked to establish a promotion-timing benchmark for the 10 most critical enlisted occupational specialties. This benchmark may be based on

Enlisted Recruiting Quantity Goals/Actual FY 1999-2004

Category	FY 1999 Actual	FY 2000 Actual	FY 2001 Actual	FY 2002 Target/Actual	FY 2003 Target	FY 2004 Target
Number of enlisted Active Component accessions	186,600	202,917	196,355	195,472/196,472	193,751	195,877
Number of enlisted Reserve Component accessions	140,070	152,702	141,023	139,846/147,129	141,450	144,728

Active Enlisted Retention Goals/Actual FY 1999-2004

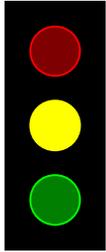
Service	FY 1999 Actual	FY 2000 Actual	FY 2001 ^a Actual	FY 2002 Goal/Actual	FY 2003 Goal	FY 2004 Projection
Army						
Initial	20,843	21,402	20,000	19,100/19,433	18,600	19,100
Mid-career	24,174	24,118	23,727	22,700/23,074	21,200	22,700
Career	26,130	25,791	21,255	15,000/15,700	17,200	15,000
Navy						
Initial	28.2%	29.6%	56.9%	57%/58.7%	56%	56%
Mid-career	43.8%	46.5%	68.2%	70%/74.5%	73%	73%
Career	53.3%	56.6%	85.0%	90%/87.4%	86%	86%
Marine Corps						
First term	23.8%	26.6%	6,144 ^b	5,900/6,050	6,022	5,962
Subsequent	56.5% ^c	63.4% ^c	5,900 ^b	5,784/7,258	6,172	5,628
Air Force						
First Term	48.7%	53.1%	56.1%	55%/72.1%	55%	55%
Mid-career	69.0%	69.7%	68.9%	75%/78.3%	75%	75%
Career	90.9%	90.8%	90.2%	95%/94.6%	95%	95%
^a In FY 2001, the Navy changed the way it calculated retention to exclude personnel who are ineligible to reenlist, so the percentage goal better reflected the number of people who chose to stay at a given reenlistment point. ^b In FY 2001, the Marines established numeric goals for retention and term goals for the first time. ^c FY 1999 and FY 2000 rates are from a previous program, and show achievements for 2 nd -term personnel. Definitions: Army: Mid-career: 7 to 10 years of service (YOS); career: 10 to 20 YOS. Navy: Mid-career: 6+ to 10 YOS; career: 10+ to 14 YOS. Air Force: Mid-career: 6 to 10 YOS; career: 10 to 14 YOS.						

Selected Reserve Enlisted Attrition Ceilings/Actual FY 1999-2004

Selected Reserve Component	FY 1999 Actual	FY 2000 Actual	FY 2001 Actual	FY 2002 Ceiling/Actual	FY 2003 Ceiling	FY 2004 Projected
Army National Guard	18.5	18.0	20.0	18.0/20.6	18.0	18.0
Army Reserve	27.2	29.4	27.4	28.6/24.6	28.6	28.6
Naval Reserve	29.8	27.1	27.6	36.0/26.5	36.0	36.0
Marine Corps Reserve	30.5	28.4	26.4	30.0/26.0	30.0	30.0
Air National Guard	11.7	11.0	9.6	12.0/7.3	12.0	12.0
Air Force Reserve	14.2	13.9	13.4	18.0/8.7	18.0	18.0
Note: All numbers are percentages and represent total losses divided by average strength.						

time-in-service, promotion points, or other factors. Once established, service benchmarks will allow us to better manage retention and promotions, avoid promotion bottlenecks, and allocate the right mix of experienced senior enlisted across the force.

ENSURE SUSTAINABLE MILITARY TEMPO AND MAINTAIN WORKFORCE SATISFACTION



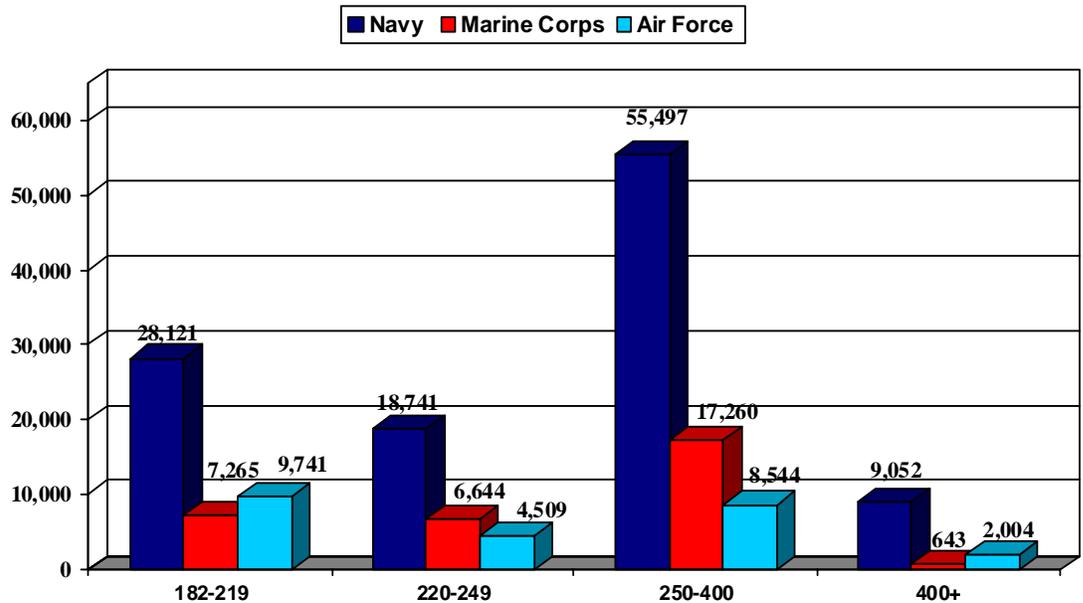
The military lifestyle presents special challenges to family life. Overseas tours away from support networks, frequent moves that disrupt a spouse's career or a child's school routine, and long separations from family members test the strength of our military families every day. The Secretary is committed to providing a high quality of life for those who serve and for their families. The Department's Social Compact (<http://mfrc.calib.com/socialcompact>) confirms our commitment to the highest standards for health care, housing, and support during family separations, as well as to meet the changing expectations of a new generation of military service members, such as increased spouse employment and career opportunity.

Of particular concern is how the time a service member must spend away from home station affects his or her family. Accordingly, we monitor where, why, and how frequently our military units deploy. This information is helping us build force management tools to more evenly distribute workload among those occupational skill groups called upon most often in times of crisis.

Ensure Sustainable Military TEMPO

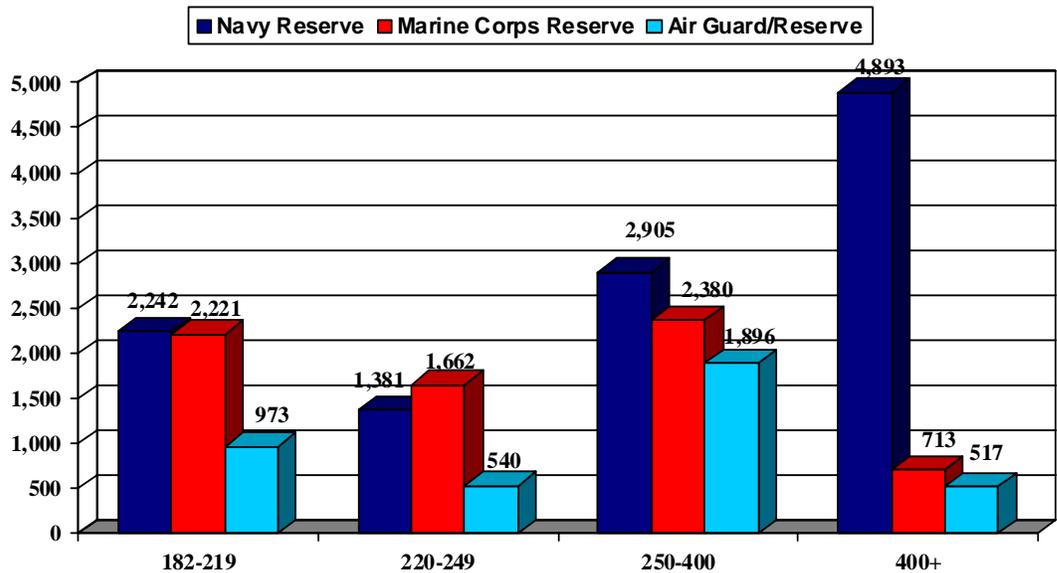
Operational tempo is the number of days a military unit or individual service member operates away from home station. Traditionally, each military service measured tempo rates for training, professional military education, peacekeeping missions, humanitarian relief efforts, planned force rotations, and other military missions differently. For example, some services did not count time spent in school as deployment; others tracked only the movement of entire units, not individuals. However it is clear – whatever the reason for the absence – time away from home station affects families (who must endure separations) and unit members left behind (who must pick up the slack).

Active Component—Members Deployed More Than 182 Days
(as of 2nd Quarter, 2003)



Note: Army data will be available in October 2003.

Reserve Component—Members Deployed More Than 182 Days
(as of 2nd Quarter, 2003)



Note: Army FY 2003 data will be available in October 2003.

In October 2001, lawmakers clearly stated their view — *a day away is a day away*. Accordingly, we track and report the number of days an

individual service member spends away from home station against a congressionally mandated ceiling of no more than 400 days away from home station over 24 consecutive months. At the 400-day/24-month mark, each deployed service member is paid a “high-deployment” per diem.

Although payment of the high-deployment per diem has been suspended during the current national emergency, each military service is still collecting data on individual deployment. The Army has fielded a web-based application to make it easier for units to post data to a central database; the Navy also intends to field a web-based solution sometime in the future. The task of creating a complete and accurate data system across all services is a difficult and expensive process, and we expect validation and verification to continue throughout 2003.

Also in 2003, the Chairman of the Joint Chiefs of Staff, working with combatant commanders and the military departments, will establish a Global Joint Forces Rotation Policy. This policy will set steady-state levels of air, land and naval presence in critical regions throughout the world, allowing us to synchronize deployments of forces worldwide and thus better manage tempo levels.

Monitor Commitment to Military Lifestyle

Perhaps the best predictor of whether service members will chose to continue their military career is their commitment—and that of their spouses—to the military lifestyle. To better understand this phenomenon, we have begun work on a measurable index modeled after research routinely used by the private sector to monitor employee commitment. These factors may differ by spouse or family member, but include pay raises, moves, deployments or family separations, influence on a spouse’s career, effect on a child’s education, time with family, or promotion opportunity.

Last summer, we conducted focus groups at four military installations to ask service members and spouses what they thought were the main reasons they wanted to stay or leave military life. We are now analyzing that data and constructing a standard tool we will use to survey our military population. By FY 2005, we hope to validate an index that will provide insight into factors influencing the

commitment to military service over time. Because the commitment of both member and spouse are important to maintaining an all-volunteer force, we also will develop a complementary index of spousal commitment to the military.

Quality of Life Social Compact Improvement Index

In keeping with the American standard of living, the new generation of military recruits has aspirations and expectations for quality of life services and access to health care, education, and living conditions that are very different from the conscript force of the past. Like their civilian counterparts, today's military families rely on two incomes to maintain their desired standard of living; some 60 percent of the force has some family responsibility.

Accordingly, the Department of Defense Social Compact lays out a 20-year strategic plan for ensuring our performance goals for quality of life keep pace with the changing expectations of the American workforce. This plan will address the needs of the two-thirds of military families living off the installation, as well as the needs of the Reserve Components.

Last year, we asked teams of experts to review each area covered by the compact and update functional performance goals. This year we will establish achievable performance targets for each area, and identify measures we can use to evaluate progress toward achievement. Once established, these metrics will be reported annually. In combination with the commitment index and relevant cost factors, this Social Compact Improvement Index will provide a comprehensive perspective from which the Department can make informed interventions and adjustments to the programs considered necessary to sustain a dedicated and satisfied military workforce.

Department of Defense Social Compact

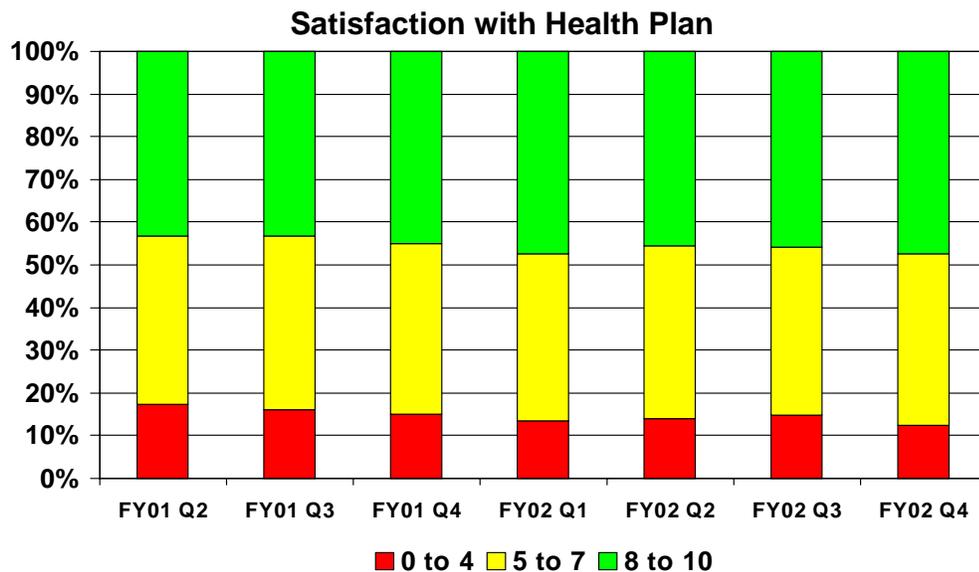
Where We Started		Where We Are Headed	
High-school graduate force	→	Expanded post-secondary education opportunities for a more educated force	
On-base "company town" mentality	→	Development of less base-centric programs for the two-thirds of the population that live off base	
Family separation with little support	→	24/7 toll-free Family Assistance Support	
Few dual-career families and more stay-at-home spouses	→	Increased attention to the dual income norm	
Less frequent Reserve Component mobilization	→	Enhanced family programs to accommodate increased Reserve deployments	
Internet access not readily available	→	Increased service delivery through technology	
Less complex financial world	→	Initiate financial readiness training	
Disparate service cultures	→	Parity of QoL service delivery and more joint (multi-service) installations Policies reflect all-volunteer force with family responsibilities	

Satisfaction with Military Health Care

Each year, we ask a sample of our 8 million eligible beneficiaries to rate their experiences with the Military Health Care system by answering the following question:

Use any number from 0 to 10 where zero is the worst health plan possible, and 10 is the best health plan possible. How would you rate your health plan now?

We consider beneficiaries who rate our health plan as 8, 9, or 10 to be “satisfied.” In FY 2002, 46 percent of those surveyed indicated they were satisfied with their care, exceeding our performance target for FY 2002. This year, we have established a “stretch” performance target of about 56 percent satisfaction—or as adjusted to match the civilian benchmark, based on the most recent National Consumer Assessment of Health Plans Survey Database.



Source: Health Care Survey of DoD Beneficiaries

We also measure satisfaction with access to appointments and with service provided during appointments, based on a monthly Customer Satisfaction Survey of beneficiaries who had an outpatient

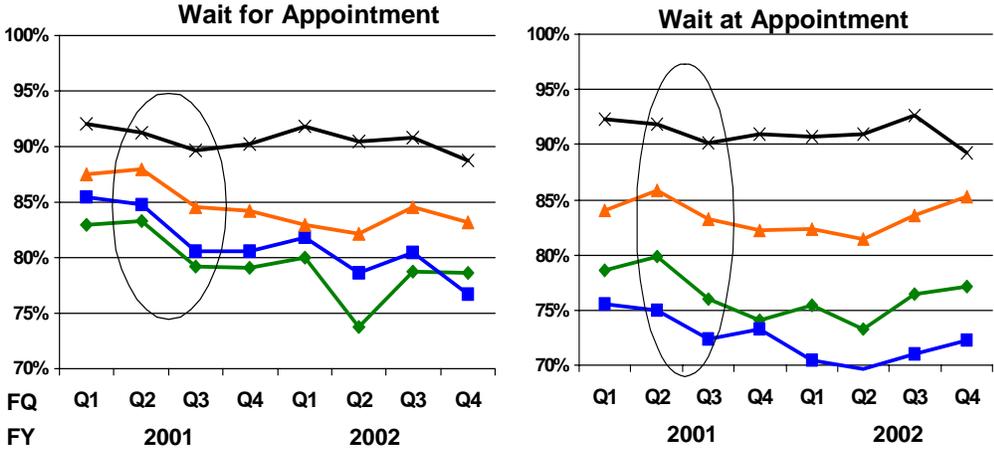
medical visit at a military hospital or clinic during the previous month.

Results obtained during FY 2002 indicated that overall satisfaction was shaped mainly by how easy it was to make an appointment, and how long the beneficiary had to wait for an appointment.

Accordingly, we have initiated two improvement programs:

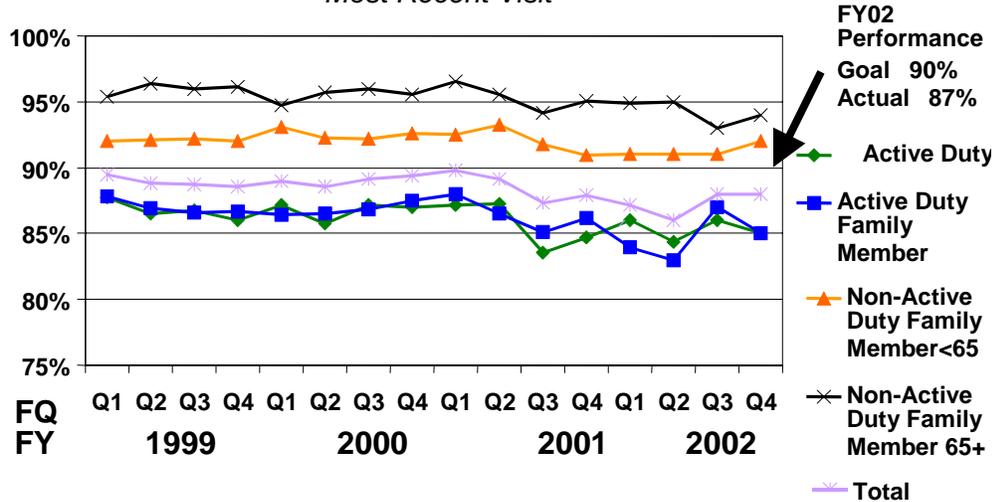
- *TRICARE Online* allows prime enrollees to schedule a visit with their primary care manager via the Internet, instead of having to call for an appointment.
- *Open Access* allows prime enrollees to call military treatment facilities directly for same-day appointments.

Components of Satisfaction



Overall Satisfaction with Care

Most Recent Visit



Source: Customer Satisfaction Survey (as of Jan. 2003).

MAINTAIN REASONABLE FORCE COSTS



The term “force cost” typically refers to military pay and allowances. However, a much broader pricing strategy is needed to fully capture all the force-related activities that combine to drive overall labor costs in the Department of Defense.

Over the past year, we have devised several new metrics to capture the *per capita* costs of quality of life programs and health care per enrollee, as well as costs of recruiting and retaining civilian personnel. A pilot project being led by the Business Initiatives Council is exploring ways to quantify the cost of contracted personnel within the Army, with the goal of developing a methodology that can be applied across all the military services.

Over the long term, we plan to build a suite of metrics that will fully describe military compensation by comparing the education and experience of the defense workforce to the private sector. This will provide insights into how compensation affects retention, allowing a more fully developed picture of what it will cost to ensure the nation has the quality personnel it needs – now and in the future.

COST PER ENLISTED SERVICE MEMBER THROUGH BASIC TRAINING

Each year, we enlist about 340,000 new recruits (195,000 for the Active Component and 145,000 for the Reserve Component). Most of these young men and women are destined to fill entry-level billets: enlisted soldiers, sailors, airmen, and Marines who will serve in those jobs for a few years, then return to civilian life or advance to positions in the military that require more skill and experience. This cycle of recruit, train, and replace is a major cost driver for force management.

Two factors combine to provide a rudimentary indicator of the price of replenishing the total force over time: (1) the average annual cost to recruit one new service member and (2) the cost to complete basic training per service member.

Recruiting expenses include pay and other personnel compensation for the recruiting staff, enlistment bonuses offered to new members, college fund programs, advertising, and general support. Training covers the costs of the supporting infrastructure (manpower, equipment, facilities) needed to indoctrinate recruits into military culture, raise their standards of physical conditioning, and instruct them in basic military skills.

Historically, we have found that the cost-per-recruit has increased annually, while the cost of basic training has remained relatively stable. Unlike training costs, recruiting costs vary with economic conditions, national or local unemployment rates, or the level of interest among young people in serving their country.

Military Personnel Costs

In FY 2003, we made three major improvements to the cost-basis of military compensation.

- We added \$1.9 billion over the FY 2002-enacted level for a 4.1 percent across-the-board pay increase.
- We added \$0.3 billion to narrow the pay comparability with the civilian sector.

- We reduced the average service member's out-of-pocket housing expenses from 11.3 to 7.5 percent for FY 2003, on a glide path to cut of out-of-pocket expenses to zero by FY 2005.

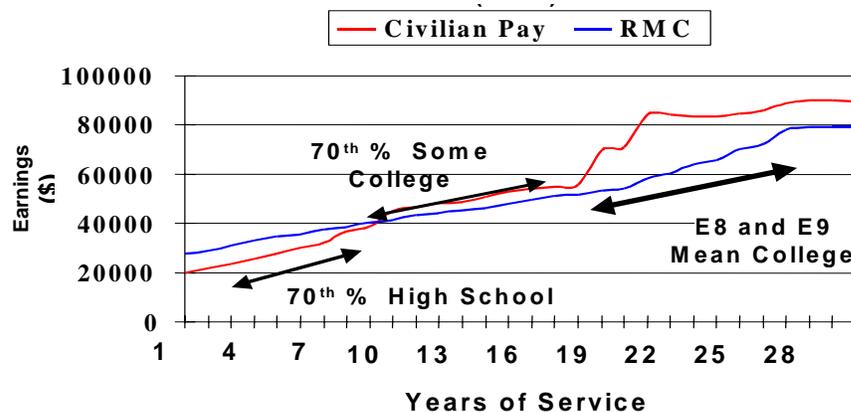
Improved pay and benefits signal our commitment to our defense workforce. However, we still do not know exactly what compensation thresholds or benefits have the most influence on a service member's decision to join or remain in the armed services. Therefore, we are researching new metrics to help us better understand the complex relationships between military compensation and other force management factors.

RATIO OF MILITARY TO CIVILIAN COMPENSATION BY YEARS OF SERVICE.

For years we have debated how to compare military compensation with the civilian sector. Though a seemingly straightforward task, such comparisons are complicated and can be misleading.

After extended study, the 9th Quadrennial Review of Military Compensation recommended that the pay of enlisted service members in their first 10 years of military service be compared with 70th percentile of earnings of all high school graduates. When enlisted compensation fell below the 70th percentile, recruiting and retention problems appeared. (It is generally very costly, both in terms of dollars and experience mix, to correct recruiting and retention shortfalls after the fact.) After 10 years of service, the compensation of senior enlisted members is compared to civilians with some college education.

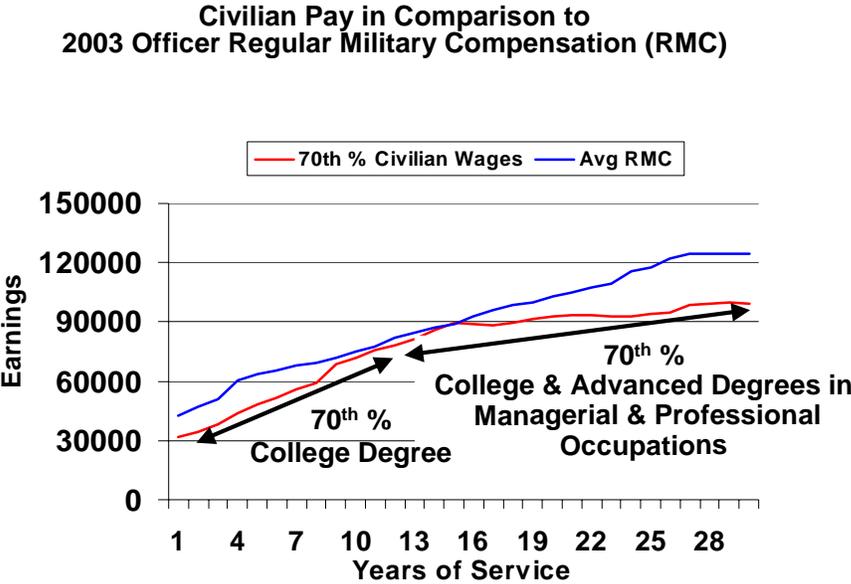
Civilian Pay in Comparison to 2003 Enlisted Regular Military Compensation (RMC)



Note: Regular military compensation (RMC) is the total of basic pay, the housing and subsistence allowances, and the resulting tax advantages (allowances are not subject to Federal income tax).

For officers in their first 12 years of service, the commission recommended that military pay be compared to civilians with college degrees. After 12 years of service, officer compensation is compared to the pay of civilians with college and advanced degrees in managerial and professional occupations.

Although somewhat complicated, these metrics provide meaningful insights into the relationship between military and civilian sector compensation, and help us structure a military compensation system that allows us to compete in the open marketplace for high quality talent.



Civilian Personnel Compensation

Civilian compensation is the combined total of basic pay, premium pay (overtime, locality, special skill), employee benefits (retirement, health), and leave earned and used. We routinely collect detailed data on civilian compensation. Although a useful indicator of overall compensation trends for civilians, this metric cannot be used to evaluate how funds spent for recruitment or other employment incentives contribute to the overall quality of the civilian workforce.

Civilian force costs (Current Year \$000)	FY 1999 Actual ^a	FY 2000 Actual ^a	FY 2001 Actual ^b	FY 2002 Projected ^c	FY 2003 Projected ^c	FY 2004 Projected Output ^c
Total	40,107,638	40,464,205	42,258,733	44,867,063	46,167,420	46,851,293
Basic pay	30,637,396	31,029,482	31,887,999	33,376,576	34,409,122	34,853,540
Premium pay	1,816,501	1,733,466	1,985,502	2,347,501	2,144,505	2,148,222
Benefit pay	7,344,625	7,507,789	8,066,742	8,822,937	9,245,600	9,515,435
Separation pay	309,116	193,468	318,490	320,049	368,193	334,096

^a FY 1999 to FY 2000 from OPM data sources.
^b FY 2001 from DoD Component summary of PB FY 2003 .
^c FY 2001 through FY 2004 from DoD Component Summary of PB FY 2004-2005.

Unpaid Compensation: Community Quality of Life (QoL) Per Capita Cost Metric

Other performance measures tell us that QoL factors – the “unpaid” compensation we provide our military members and their families – is a strong contributor to overall workforce satisfaction. Consequently, we are researching new metrics that will help us isolate and evaluate investments in QoL services. By FY 2005, we hope to be able to begin tracking average QoL investments per active duty member, and the relationship between budget levels and progress being made by individual military departments toward our overall performance goals for QoL standards. It will also help us explore the relationship between QoL programs, their impact upon commitment to the military lifestyle, and costs.

The Military Health Care System Meets Key Performance Goals

Military medical care is the primary method of providing the health care benefit to our active duty members, retirees, and their families. We will spend more than \$26.4 billion in FY 2004 to provide health support for a full range of military operations and sustaining the well-being of all of those entrusted to our care.

Over the past two years, we have made fundamental changes in how we think about managing medical benefits and readiness. The revamping of the military health system begins with the new Managed Care Support Contracts, which will establish incentives for bringing patients back into our Military Treatment Facilities (MTFs).

The goal is to increase the productivity at the MTFs and redirect more individuals from purchased care to the MTF.

We also are refining how we think about and measure medical readiness by researching new metrics to monitor medical readiness at both the unit-level and for individual service members. The Defense Health Program will implement these new measures by setting rigorous goals in its annual performance contracts.

We already have some indicators—including the first two metrics described below—that offer insights into the complex relationships between *providing* and *managing* quality health care. In addition, we are developing an indicator to track medical costs per enrollee.

OUTPATIENT MARKET SHARE

Outpatient visits represent the majority of contacts between the military health system and its more than 8 million beneficiaries. Accordingly, our outpatient market-share metric looks at how much of the care is delivered in Military Treatment Facilities (MTFs) vice being purchased in the private sector. Since providing medical services during wartime carries a large fixed cost, our goal is to use our organic resources in the most efficient and effective manner during peacetime. Over the next couple of years, we intend to stabilize and recover market share around the MTFs by increasing the productivity of the staff.

PRIMARY CARE PROVIDER PRODUCTIVITY

The performance of a Health Maintenance Organization (HMO) correlates directly to the quality of the primary care it delivers. Not only is the HMO primary caregiver often the first medical professional the beneficiary sees, he or she is responsible for delivering most of the preventive care that keeps beneficiaries healthy and away from more costly specialty care.

To capture the complexity of care for the medical encounter and the resources consumed, we use a performance indicator called a “Relative Value Unit (RVU).” The RVU concept was developed by the Centers for Medicare and Medicaid Services, and approximates physician resources expended during a medical encounter. For example: a patient returning to a doctor’s office with a simple problem

may score only 0.17 RVUs, while an arthroscopy surgery of the knee is rated at 16.00RVUs.

The average RVU per primary care provider in the Department of Defense during FY 2002 was 13.6 per day. For FY 2003 and FY 2004, we have set “stretch” goals of greater than or equal to 14.5 and 15.5, respectively. While there is no direct comparison available to the private sector, the American Medical Group Association found that family medicine practices averaged 3,808 RVU’s per provider per year. This equates to approximately 18.5 RVU’s per provider per day, which will be our goal in 2007, as we increase by 1 RVU per provider per day until 18.5 is achieved.

MEDICAL COST PER ENROLLEE

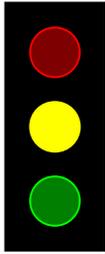
Several years ago, we consolidated our health care delivery under our TRICARE management activity, and began reforming how we purchased care from the private sector.

To gauge the progress of those initiatives, we are developing an indicator that will track how well the Military Health System manages care for those individuals who have chosen to enroll in a HMO-type of benefit. The medical cost per enrollee will capture three major management issues:

- How efficiently care is provided.
- How effectively enrollee demand is managed.
- How well the Military Treatment Facility determines which care should be directly provided by the MTF facility versus being purchased from a Managed Care Support Contractor.

Using the information from this measure (plus intermediate products), we will be able to assess at the overall efficiency of the Military Health System.

SHAPE THE FORCE OF THE FUTURE



The global war on terrorism has demonstrated that we need a force that is trained and prepared to meet future asymmetric threats and international challenges. Clearly, *status quo* personnel management will not suffice. Yet our personnel management policies, procedures, and practices are still based on Cold War models derived from the experiences of World War II mass mobilization.

Today we need to critically evaluate how we can shape the force of the future. We need modern personnel systems, a way to better use the Reserve Component, and a return of our warfighters to warfighting roles. We need to identify and fill critical skills needed to optimize new technology and new ways of doing business. We need to rapidly transform how we train the force.

This is dramatic, unprecedented change, and a tremendous challenge. Initially, our major focus will be to maintain the momentum of the research, pilot tests, studies of corporate systems, and experimental activities meant to discover “best practices” that are adaptable to the Department of Defense. At the same time, we must look hard at our internal processes and make tough decisions. For example, we must delineate core and non-core functions within the Department and decide the appropriate fate of non-core functions.

Define and Meet Core Divestiture Requirements

Once we decide what activities are “core” to the defense mission, we need to make sure the right people are doing those jobs. We need a well-grounded plan to reallocate personnel resources – military and civilian – to improve our warfighting capability. We also need to update policies and processes within the Reserve Component to bind it more strongly to the Active Component, by applying lessons-learned from our comprehensive review of *Reserve Component Contributions to National Defense*, and measure our progress. (See www.defenselink.mil/ra/documents/annualreports/rcompfinal.pdf.)

Meet Civilian Workforce Management Objectives

**“The current system is not agile enough...The civil service system has the right values, but its processes are outdated...We need to have a compensation system that is responsive to the market and to performance...
...We cannot succeed with today’s system.”**
Dr. David Chu
Under Secretary of Defense for Personnel and Readiness

The Department of Defense civilian workforce comprises approximately 50 percent of the total government workforce. The skill and dedication of this workforce are key to the effectiveness of our military force. Yet our civilian workforce has gotten older, and many individuals are reaching retirement age. Advancing science and technology have resulted in a skill imbalance in some cases.

Our Human Resource Strategic Plan (www.dod.mil/prhome) lays out the way ahead for recruiting and managing an excellent modern workforce. We will monitor our progress, with a special focus on two key objectives: (1) reducing the time required to fill civilian vacancies and (2) identifying and filling positions defined as critical skills. We have to attract bright young people to join us, while at the same time creating the challenge and rewards that will encourage our best talent to stay with government service.

The Department must change the way it *manages* civilian personnel. The “one-size-fits-all” Government-wide civilian personnel system no longer responds well to the Department’s national security mission. Accordingly, we are working to establish a National Security Personnel System (NSPS). Much like the new personnel policies in place at the Department of Homeland Security, NSPS would give us the flexibility to modernize our personnel management system while continuing to preserve merit principles, respect Veterans’ Preference, and maintain union involvement.

The design of the NSPS is based on over 20 years of experience in operating personnel demonstration projects and alternative personnel systems. Key features include:

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- Shifting civilian employees from the general schedule pay system to a pay-band system.
 - Replacing automatic annual pay increases with a pay-for-performance system.
 - Streamlined hiring authority.
 - Special pay authorities to bring specialists and retirees on board for special projects.

Meet Military Personnel Requirements of a Transformed Force

As we have done for the civilian workforce, we have also created a Military Human Resource Strategic Plan, which sets achievable goals for near-, mid-, and long-term implementation. Inherently flexible, this strategy is designed to rapidly adjust to changing requirements. Some 42 research efforts have been or are being undertaken to support this plan. The most promising study recommendations would provide the President and Secretary of Defense greater flexibility in managing job tenure and career length for general and flag officers. Over the long term, we intend to use the data collected from these many research efforts to design and implement optimal career patterns and service obligations for the force as a whole. Future critical skills, such as information operations, language and foreign area expertise, and space operations will be defined, and progress toward meeting the resulting need will be monitored.

Reserve Component personnel management is being modernized as well. The Reserve Components provide a link between the military and the civilian sector of American society. To take full advantage of that link requires a personnel management system that offers greater flexibility in accessing and managing individuals throughout a military career, that may span both active and reserve service – or across a “continuum of service.” This means simplifying the rules for employing Reserve Component members, creating conditions that enhance volunteerism, allowing for varying levels of Reserve participation and facilitating seamless flow of personnel from active to reserve and reserve to active over the course of a military career.

Additionally, Reserve Component members bring diverse civilian skills and experience to the military beyond what is available in the regular component. Managing within a continuum of service can help to attain and retain skills that are hard to acquire and maintain in the military to include those in innovative technologies. It will provide opportunities to establish new and innovative affiliation programs and defense partnerships with industry for individuals willing to support military forces.

Management Initiatives

IMPROVE FLEXIBILITY THROUGH A NEW APPROACH TO MANAGING PERSONNEL
<ul style="list-style-type: none"> • Structure management to provide varying levels of participation – a “Continuum of Service.”
<ul style="list-style-type: none"> • Modify force management and compensation policies to support the “Continuum of Service” concept.
<ul style="list-style-type: none"> • Streamline the manner in which members are placed on military duty by reducing the number of duty statuses.
<ul style="list-style-type: none"> • Implement innovative management techniques to include new management programs and auxiliaries for special skill sets, and design and test new affiliation programs.
<ul style="list-style-type: none"> • Reduce dependence on involuntary mobilization of Reserve Component members needed early in an operation through expanded use of volunteerism.
ENHANCE CAPABILITY BY REBALANCING THE TOTAL FORCE
<ul style="list-style-type: none"> • Move early-deploying Reserve Component forces later in the deployment plans and later-deploying Active Component forces with the same capabilities forward in the deployment plans.
<ul style="list-style-type: none"> • Increase “high-demand” capability in the active structure, the reserve structure, or both.
<ul style="list-style-type: none"> • Expand the use of reach-back to reduce footprint in theater through virtual connectivity.
<ul style="list-style-type: none"> • Expand Reserve Component augmentation of certain Active Component capabilities to increase platform performance.
<ul style="list-style-type: none"> • Rebalance capabilities by building more active structure when all other possibilities have been exhausted.

Adopting a new availability and service paradigm as the basis for managing Active and Reserve forces would allow individuals to change levels of participation with greater ease and better leverage the Department’s investment in training and education to meet operational requirements. Greater reliance on Reserve volunteers can reduce burdens of involuntary mobilization, active personnel opera-

tions tempo and repetitive activations and deployments among traditional reservists.